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Origin and Consequences of the Debt Crisis and Ways of Solving It

by Jürgen Westphalen, Hamburg*

In the 1970s Latin America accounted for a high, and constantly increasing, proportion of the total public foreign debt of all developing countries, reaching a share of 35 % by the end of the decade. In comparison, Latin America's share of the total GDP of the developing countries is around 20 %. The following article explains the specific causes of the debt crisis in Latin America and suggests some ways of overcoming it.

The total foreign indebtedness of Latin America (public and private debtors) amounted to US \$ 205 bn at the end of 1980, 269 bn at the end of 1981 and over 300 bn at the end of 1982. An increase of around 7 % was announced for 1983, i.e. a total indebtedness of US \$ 325-330 bn at the end of the year. These figures include some estimates since precise information is not available for the private foreign debts of some countries. At the end of 1982 the Latin American nations with the highest indebtedness were Brazil (83.2 bn), Mexico (approx. 83 bn), Argentina (38.7 bn) and Venezuela (33.1 bn). On that same date, the foreign debts of those 4 nations accounted for approximately 75 % of the foreign indebtedness of Latin America. Argentina's foreign indebtedness increased by 500 % between 1973 and 1982, Brazil's by more than 500 %, Venezuela's by 700 % and Mexico's by almost 900 %.

To avoid misleading conclusions, these absolute figures must be related to appropriate comparative data: for example, of 16 Latin American countries Brazil was the leader in terms of absolute indebtedness but held the much better position of 13th in terms of its total indebtedness as a percentage of the gross domestic product (GDP) and the 9th position in terms of its foreign indebtedness per capita, a good average situation. Table 1 shows the ranking of the four most indebted countries in absolute terms.

The remark that 75 % of Latin America's total debts can be attributed to these four countries also requires some qualification: if we allow for the fact that in 1982 that group of countries provided 78 % of Latin America's GDP, their share of the total indebtedness no longer seems excessive.

A comparison on the international level¹ shows that Latin America accounted for a high and, in the 1970s, a constantly increasing proportion of the total public foreign debt of all developing countries (1970-72: 28 %; 1975/76: 32.5 %; 1979/80: 35 %). Latin America's share of the total GDP of the developing countries is around 20 %. The comparatively heavy foreign indebtedness reflects Latin America's relatively high level of development and its correspondingly large capacity for indebtedness. The Latin American share of the servicing of all the developing nations' public foreign debts has undergone an even greater and, in the 1970s, rapid increase (1970-72: 38.3 %; 1975/76: 45 %; 1979/80: 50.6 %). These figures indicate the comparatively unfavourable debt structure of Latin America, i.e. the preponderance of the foreign loans taken up by Latin America at market conditions.

External Causes of Indebtedness

When discussing the causes of the indebtedness it is advisable to distinguish between internal and external causes and, in turn, to subdivide those two groups into the causes which can be remedied easily and in the short term and those requiring difficult and long-term remedies. As the proportion of external causes increases, the debtor nations' latitude for action is narrowed and the responsibility of the partner countries or international institutions becomes greater. The greater the proportion of causes with difficult and long-term remedies, the longer the debt crisis will last.

Amongst the external causes we must mention first and foremost the world recession which has become a

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¹ Banco Interamericano de Desarrollo: Deuda Pública Externa de los países latinoamericanos, Washington, July 1982.

Table 1

	absolute	% of GDP	per capita
Brazil	1	13	9
Mexico	2	10	6
Argentina	3	6	5
Venezuela	4	5	1

Table 2
Deterioration in the Terms of Trade

	1981 (1970 = 100)	1982	Deterioration 1981/1982 (in %)
Latin America: total	116	109	-6
Oil-exporting countries	241	211	-12
Other countries	68	65	-4

serious long-term crisis and has resulted in a marked impairment of Latin America's exports and economic growth.

The strong rise in oil prices in 1973/74 and 1979/80 was of crucial importance for the oil-importing countries. If, as the American economist William R. Cline² has done, we compare the actual oil imports of all non-oil-producing developing nations since 1973 with the sums which they would have had to pay for the imports if the oil price had risen no more than the wholesale price index in the USA, we find that an extra US \$ 260 bn was spent on oil imports between 1973 and 1982. On the other hand, we must bear in mind that the Latin American oil-exporting countries have benefited from this trend. In recent years, however, the deterioration in the terms of trade³ has been borne primarily by the oil-exporting countries (see Table 2).

The marked curbing of inflation combined with continuing high budgetary deficits in the USA, i.e. the conflict between a strict monetary policy and a more relaxed fiscal policy causing a dramatic rise in interest rates, also had a considerable impact. According to information supplied by the UN Economic Commission for Latin America (CEPAL), between 1976 and 1982 the

six-month LIBOR rate rose from 6.1 % to 14.3 % in nominal terms and from -2 % to 6 % in real terms. Loans taken up during periods of high inflation in the industrial nations (1974: 11.6 %; 1975: 10.2 %) and low or even negative real interest rates become an extremely heavy burden in times of reduced inflation and high real interest rates.

One particular feature of Latin America's foreign indebtedness in the 1970's was the disproportionate increase in the bank loans taken up at market conditions and the corresponding reduction of loans granted on "soft" conditions from public sources, that is to say from international financial institutions or from the industrial countries' capital aid. In 1970 45 % of Latin America's total public foreign debt derived from private sources but this had risen to 70 % by 1980; over the same period the share of private foreign banks increased from 20 % to 56 %. The proportion of foreign debts from public sources correspondingly fell from 55 % in 1970 to only 30 % in 1980; 24 % of Latin America's public foreign debts in 1970 and 17 % in 1980 originated from international financial institutions; 31 % in 1970 and 13 % in 1980 from the industrial countries' capital aid. One immediate result of this change in the structure of indebtedness is a marked deterioration in the composition of the debt-servicing which still consisted of one-third interest and two-thirds amortization payments in 1970 whereas by 1980 the interest/amortization ratio was 48:52.⁴

Finally, this list of external causes must include the psychological effects, one example being the impairment of the entire region's creditworthiness as a result of the "Mexico crisis" in the autumn of 1982.

Internal Causes

The internal causes of indebtedness include in particular incorrect decisions on economic and development policy. As G. Fels⁵ rightly states, to a large extent the increased indebtedness in recent years has ceased to parallel the investment operations in the debtor countries; instead, a continuation of former consumption patterns and an increasing waste of resources in the public sector can be observed. Serious consequences were also produced by the over-valuation of domestic currencies (e.g. in Chile and Mexico) which, although assisting the fight against inflation, curbed exports and increased imports, thus directly exacerbating the debt situation. Equally detrimental effects were caused by allowing irresponsibly high budget deficits as a result of a defective taxation system or inefficient collection of taxes and excessive state expenditure on salaries and

² W. R. Cline: *International Debt and the Stability of the World Economy*, Washington 1983, pp. 20f.

³ CEPAL: *Balance Preliminar de la Economía Latinoamericana en 1982. Notas sobre la Economía y el Desarrollo de América latina*, No. 373, January 1983.

⁴ Banco Interamericano de Desarrollo, op. cit.

⁵ G. Fels: *Die internationale Verschuldungskrise*, in: *Volkswirtschaftliche Korrespondenz der Adolf-Weber-Stiftung*, Munich, No. 7/1983.

Table 3
Total Foreign Debts of Latin America

(end of 1982)

Country	US\$bn	Country	% of GDP	Country	US\$ per capita
1) Brazil	83.2	1) Costa Rica	134.3	1) Venezuela	2253
2) Mexico	83.0	2) Nicaragua	118.0	2) Costa Rica	1760
3) Argentina	38.7	3) Bolivia ¹	107.3	3) Chile ¹	1454
4) Venezuela	33.1	4) Chile ¹	101.2	4) Uruguay ¹	1442
5) Chile ¹	16.1	5) Venezuela ¹	88.8	5) Argentina	1358
6) Columbia	9.8	6) Argentina	81.5	6) Mexico	1125
7) Peru	9.6	7) Uruguay	79.4	7) Nicaragua	1102
8) Ecuador	6.7	8) Honduras ¹	75.4	8) Ecuador	784
9) Uruguay	4.2	9) Ecuador	75.1	9) Brazil	668
10) Costa Rica	4.1	10) Mexico	59.1	10) Peru	554
11) Bolivia ¹	3.1	11) El Salvador	58.8	11) Bolivia ¹	522
12) Nicaragua	2.8	12) Peru	50.1	12) Honduras ¹	460
13) Honduras ¹	1.8	13) Brazil	43.6	13) Columbia	360
14) El Salvador	1.7	14) Columbia	39.1	14) Paraguay	359
15) Guatemala ²	1.5	15) Paraguay	31.4	15) El Salvador	330
16) Paraguay	1.2	16) Guatemala ²	18.4	16) Guatemala ²	205
Latin America	315.0	Latin America	58.6	Latin America	880

¹ 30. 6. 1983. ² 31. 3. 1983.

subsidies; in Mexico, for example, the deficit in the 1982 national budget was equivalent to 16.5 % of the GDP. In addition, many countries made serious errors in their debt management which, for example in Venezuela, allowed an extremely high proportion of short-term foreign debts to develop. In Mexico and Venezuela over-high exchange rates combined with maintained convertibility, unattractive domestic interest rates and a growing loss of confidence in the government, produced the conditions for a large-scale flight of capital. Inexpedient and inopportune development strategies were – and in some cases still are – applied in the majority of the debtor countries, such as too much emphasis on promoting industry with excessive protection for new industries, a lack of attention to agriculture causing an increasing reliance upon food imports, the expansion of inefficient state operations in the economy and – partially as a result of an incorrect assessment of future development potential and partially for reasons of national prestige – the implementation of extravagant projects.

The relative weighting of the external and internal causes varies from country to country. The fact that – irrespective of to some extent very different economic and financial policies – almost every Latin American country has been affected by the debt crisis induces CEPAL⁶ to draw the general conclusion that

⁶ CEPAL: La Crisis Mundial y América latina. Notas sobre la Economía y el Desarrollo de América latina, No. 378/379, June 1983.

⁷ W. R. Cline, op. cit., pp. 122, 65, 61f.

considerably more importance attaches to the external causes of indebtedness. This argument is also accepted by many experts outside Latin America who consider that the principal causes of the debt problem lie in the weak international economic climate. Thus William R. Cline⁷ describes the worldwide recession as the root cause of the international debt crisis. According to Cline's calculations, one percentage point of growth in the industrial nations has seven times the effect of a one percentage point drop in interest rates as regards the alleviation of the developing countries' burden of indebtedness. He concludes from this that, even if it is achieved at the cost of some increase in interest rates, any durable improvement in the industrial nations' economic growth would be beneficial to the debtor countries.

Although any marked reduction in oil prices would assist the oil-importing countries of Latin America, it would – contrary to widely-held opinion – be distinctly harmful to the solving of the problem of worldwide indebtedness because, according to Cline's calculations, the relief for the oil-importing countries would by no means offset the additional burden imposed upon the oil-exporting countries by the reduction of their export earnings.

In addition to the external causes, however, we should certainly not underestimate the considerable importance of the internal causes in some countries nor the extent of the "home-produced" problems of

indebtedness in Latin America. As regards the duration of the crisis, only a general statement can be made to the effect that many causes can certainly not be easily and quickly remedied; Latin America's debt crisis is therefore at least a problem for the 1980s, and perhaps for even longer.

Latin America's Need for Funds

CEPAL⁸ considers that in the medium term an annual minimum capital inflow of US \$ 35 bn to Latin America is essential if interest payments abroad are to be continued and the 1982 per capita income maintained. Although an inflow of US \$ 35 bn would be higher than in 1982 (16.6 bn), it would be well below the 1981 level (38.0 bn). Latin America's per capita income was US \$ 1,500 in 1982 which was 3.4 % below the previous year's figure. In the Federal Republic of Germany a gross national product of approximately US \$ 13,500 per inhabitant was achieved in 1981. So the development objectives on which CEPAL's estimates of Latin American needs are based are set at a very modest level; consequently, the minimum capital inflow can at best be sufficient only for a very limited period.

If the net interest payments are deducted from the net capital flow, we obtain the net transfer of resources. For quite a while to come Latin America will remain a net exporter of resources. According to the World Bank's calculations, Argentina and Brazil will not again achieve a positive net transfer of resources before 1993 and Chile and Mexico will have to wait until the mid-1990's. So until then those countries will have to remit net interest payments abroad which are in excess of the net inflow of capital from abroad. According to the World Bank's forecasts, the net outflow of resources will reach its peak in 1985 at US \$ 4.8 bn for Brazil, 10.3 bn for Mexico and 2.6 bn for Chile; Argentina has already passed the peak (US \$ 3.4 bn) in 1983.

The 1983 report of the Interamerican Development Bank (IDB)⁹ rightly states: "In the present economic climate the prospects of external financing are not very encouraging." According to information from the Bank for International Settlements (BIS), the foreign commercial banks' lending has recently shown a clear decline. The credits granted by the international financial institutions are subject to limits which cannot be extended to any marked extent unless the industrial nations are considerably more willing than hitherto to top up those institutions' funds with large sums. In 1965-70 the IDB's loans to Latin America accounted for about 25 % of the accumulated current account deficits of all

the Latin American countries whereas this represented only 11 % in 1975-80. Over the same period the share of the World Bank's loans to Latin America fell from 21 % to 12 % of the region's total current account deficit.¹⁰ Nor can Latin America have much hope of any noteworthy rise in the industrial nations' capital aid; the general principle is that, with a few exceptions, the newly industrialising countries receive no capital aid. Finally, scarcely any increase can be expected in private foreign direct investment in Latin America in the medium term. Although private foreign investment in Latin America did rise in absolute terms in the 1970s, this rise was by no means as great as the total inflow of capital from abroad: in 1971-73 it averaged US \$ 2.8 bn per annum or 24.5 % of the total inflow of capital, while in 1976-79 it was US \$ 4 bn or 17 % and in 1981 US \$ 7.3 bn or 16 %. Very serious efforts will be needed before private direct investment from abroad regains the level it achieved in the early 1970's.

At the end of the 1970s, foreign sources already contributed some 20 % of the funds for gross investment in Latin America. It will be extremely difficult to maintain this percentage in the coming years. Since any further relative increase of foreign bank loans is undesirable in view of its damaging effect upon the structure of debts and, in fact, bank loans will probably be reduced under present conditions, the main points at which measures for maintaining the inflow of funds can be applied are the multi- and bilateral public sources and, in the longer term, private foreign direct investment; but the attempts being made by international financial institutions in conjunction with foreign banks to develop new models of mixed financing also deserve attention.

Consequences of the Crisis

The debt crisis has an impact upon the Latin American debtor countries themselves, the foreign creditors and, possibly, the international financial system. The measures adopted by the debtor countries for overcoming the crisis have, almost without exception, produced unavoidable detrimental secondary effects. Since exporting has now become extremely difficult as a result of the unfavourable international economic climate, the attempts to achieve a surplus on current account are directed mainly towards imports. In 1982 Latin America's imports fell by almost 20 % while, according to initial calculations, the drop in 1983 was nearly 30 %. The latitude available for

⁹ Banco Interamericano de Desarrollo: Progreso Económico y Social en América latina. Informe 1983, Washington 1983, p. 152.

¹⁰ CEPAL: La Crisis Mundial . . . , op. cit.

⁸ CEPAL: La Crisis Mundial . . . , op. cit.

curbing imports varies from country to country but nowhere is it unlimited. The more liberal the former import policy, that is to say the more "surplus" goods have been imported, the greater the present latitude (e. g. in Chile, Mexico and Venezuela). To cite an example of the opposing trend, Brazil has applied a relatively cautious import policy for years but is heavily dependent upon imports of means of production and spare parts and accordingly has considerably less latitude for future import restrictions. Under these conditions any curb on imports means that the need for means of production and spares cannot be sufficiently met and this in turn may hold back or stop production and, in some circumstances, damage the export potential and lead to dismissals of the labour force. On the other hand, however, producers who are not dependent upon imports may benefit from the fact that the import curbs keep foreign competitors off the domestic markets.

As far as expenditure is concerned, the measures to reduce the budget deficits are intended to cut personnel and non-personnel costs, and subsidies. A reduction in personnel costs achieved by dismissals or by raising wages and salaries below the inflation rate causes a drop in the demand for consumer goods which in turn may lead to increasing unemployment and a growing social discontent and internal political instability. A reduction in non-personnel expenditure is achieved mainly by suspending or extending the duration of major projects, which may also have harmful effects upon the labour market and/or by retrenchment in the subsidies for production, exports or consumption. Any cuts in the aid for production usually involve dismissals of the labour force, and declining exports can prove counter-productive in view of the dependence upon foreign exchange earnings. A rise in the price of essential consumer goods, such as basic foods or petrol, also produces an additional burden – principally upon the poorest classes of the population.

As far as revenue is concerned, consolidation is effected by raising taxes and duties or by improving the collection of taxes; these measures, too, usually have an inhibiting effect upon production and/or consumption. The vital issue is that of the tolerance threshold of the broad stratum of the poor population in the individual debtor countries. In none of the Latin American debtor countries is it possible to say that austerity policy will not affect political stability.

As foreign indebtedness grows, the difficulties in satisfying the demand for capital from abroad also increase. Taken together, in all the non-oil-producing developing countries the ratio between interest payments and net new indebtedness¹¹ rose from 30 % in 1975-78 to 55 % in 1979-81 and 103 % in 1982. So in 1982 the new debts incurred were no longer sufficient to cover interest payments to foreign lenders. For most of the debtor nations this process will continue at least until 1986. The interest payment – net new indebtedness ratio in 1982 was 79 % in Mexico and Chile, 93 % in Brazil and 220 % in Argentina. Consequently, the new foreign borrowings leave nothing for capital investment or for creating a cushion of reserves in most of the debtor nations. These countries are caught up in a vicious circle of indebtedness in which new borrowings are constantly required simply to maintain the status quo.

From the point of view of the creditor nations Latin America's curb on imports means that their own exports to Latin America are restricted. As far as the German economy as a whole is concerned this has only a limited impact since in 1982 only 2.6 % of Germany's total exports went to Latin America.¹² But considerable losses of earnings on Latin American markets have already been suffered by some specific German firms. Other industrialised countries have been much harder hit by this development than the Federal Republic: in 1982 the drop in exports from the industrialised countries registered 46 % for Argentina, 42 % for Chile, 33 % for Mexico and 14 % for Brazil. The fall of US exports to Mexico from US \$ 17.8 bn in 1981 to US \$ 11.8 bn in 1982 has in itself destroyed an estimated 250,000 jobs in the USA. The World Bank estimates that more than 600,000 jobs have been lost in all the countries exporting to Latin America as a result of the decline in Latin American imports.

The debt situation still carries risks to the international financial system, risks which can derive particularly from the American banks which are deeply involved in Latin America. By the end of 1982 the nine largest US banks¹³ had granted developing and eastern bloc countries loans equivalent to almost 300 % of their capital. The loans to only five Latin American countries – Argentina, Brazil, Chile, Mexico and Venezuela – exceeded 160 % of their capital. The commitment of some US banks was well above this average: the loans granted to those five countries by the Chemical Bank were 170 % of its capital while the equivalent figures were 175 % for Citibank, 196 % for Crocker's National Bank and as much as 263 % for Manufacturers' Hanover Trust. If a large proportion of the debts deriving from their foreign

¹¹ W. R. Cline, *op. cit.*, p. 88.

¹² Deutsch-Südamerikanische Bank AG: Kurzbericht über Lateinamerika, No. 1/84, Hamburg 1984, p. 10.

¹³ W. R. Cline, *op. cit.*, p. 34.

credit operations proves impossible to collect and thus has to be written off, the banks in question would lose a considerable part of their net assets and, under the prevailing circumstances, that loss could hardly be absorbed by feeding in new capital; so the only solution would lie in large-scale credit reductions which could have very serious consequences for the national economy of the creditor country in question and also for the entire international financial system. Each successful rescheduling, each effective adjustment operation in a debtor nation and, above all, any measure which strengthens the prospects of durable economic growth in the industrialised countries does, however, help to forestall this risk.

Ways of Overcoming the Crisis

According to the prevalent opinion of experts both inside and outside Latin America, the debt crisis can be solved; the Latin American debtor countries are in various stages of illiquidity but are not insolvent. The solution of the crisis does, however, call for various major preconditions, particularly a worldwide permanent recovery of economic activity and intensive joint efforts to remedy the causes of the crisis by both the debtors and the creditors.

The majority of the Latin American countries have applied for the rescheduling of part of their foreign commitments, i.e. a reorganization of the debts with a view to extending their term. So far this ad hoc reaction to the debt crisis has had mainly very positive results thanks to the good cooperation between the debtor countries and the government agencies and central banks in the creditor nations, the foreign commercial banks and the international financial institutions with the IMF playing a particularly vital part in this success. The main aim of rescheduling is to extend unfulfillable short-term debt servicing commitments to the more distant future; so the main result is to gain time which must be used to develop and introduce a long-term design and solution which seem capable of remedying the causes of the crisis.

Proposals for global solutions of the debt problem have recently been increasingly introduced into the debate. The following can be cited as examples: converting lendings into capital (H. J. Krahnen); the sales of problematic loans to a supranational conversion agency which would arrange for them to be rescheduled into longer term loans with low interest rates (Peter Kenen); the conversion of bank credits into long-term low-interest loans under the management of the IMF (Schumer); rediscounting of the commercial

banks' problematic credits by the pertinent central banks (Peter Leslie), etc. etc. The justified objections to such proposed global solutions are, firstly, that they tackle only the acute problems but do not include any plans for the long-term re-establishment of the debtor countries' creditworthiness and, secondly, that after a global solution to the problem has been applied many commercial banks would probably see no further reason for granting credit to the debtor countries until they have considerably improved their economic situation, an achievement which would, however, be delayed much longer without new bank loans.

The Latin American countries themselves have on occasion suggested a special type of global solution in the form of a "debtor cartel" which would push ahead with the conclusion of general rescheduling agreements to the particular benefit of the smaller weaker debtor countries. But there is increasing support for the view that a debtor cartel would have damaging effects upon the creditworthiness of its members. CEPAL¹⁴ has recently expressed unequivocal opposition to this solution on the grounds that the situations of the debtor countries are so diverse "that it would be somewhat unrealistic and inexpedient to aim at a general rescheduling programme".

Until a convincing global model for solving it has been developed the debt problem will continue to be dealt with individually for each debtor country. Adjustment measures will have to be adopted in each country in keeping with its potential and its specific circumstances. In this respect the only possible general comment is that, in order to prevent or at any rate restrict any harmful side-effects of, for example, a reorganization of the budget or the re-establishment of realistic exchange rates, the necessary adjustment processes should be introduced as soon as possible before the growing foreign indebtedness has become a debt crisis. The general aim of the adjustment efforts is, firstly, to achieve less dependence upon foreign finance and, secondly, to improve the capacity for incurring debts. Important specific aims are, for example, to make the country in question more attractive to private foreign capital and to achieve increasing current account surpluses. When considering the prospects of export surpluses in the balance of trade, however, allowance must be made for the fact that any revival of economic activity in the industrial nations has only a blunted impact upon Latin America's exports since a considerable proportion of those exports already goes to other developing countries, mainly other Latin American countries. For example, other developing countries purchase 9 % of the total exports from

¹⁴ CEPAL: *La Crisis Mundial* . . . , op. cit.

Mexico, 30 % from Argentina and Peru and 38 % from Brazil.

Nearly every opinion expressed on the debt problem includes an urgent call to strengthen the IMF's position and increase its funds. At present, the IMF does not usually take action until the debtor country in question is suffering from a debt crisis. The rehabilitation costs would certainly be lower and the prospects of success greater if ways were found of making the IMF's advice and assistance effective at a much earlier stage. The IMF's usual conditionalities are generally considered justified and important but we often hear the criticism that more careful attention to the special potentials and requirements of the debtor country in question would be desirable in order as far as possible to obviate damaging effects upon economic growth, per capita incomes, social peace and political stability. CEPAL¹⁵ refers to the danger that if the IMF conditionalities are wrongly conceived or administered in the wrong dosis, their aims may be frustrated.

Need for New Concepts

The commercial banks are expected to continue their grants of new loans to the Latin American debtor countries. In this connection W. R. Cline¹⁶ refers to "involuntary lending" by those banks which already have commitments in the credit-seeking debtor country and thus an interest in continued debt-servicing payments and in a rapid solution of the crisis in that country. He considers that those banks have fallen into a "lender's trap" and vigorously opposes any global solution to the crisis which will let the banks off the hook.

The "involuntary lending" aspect must also be taken into consideration in the debate on the interest rates chargeable on rescheduled loans. CEPAL calls for market reductions in interest on the grounds that the country risk has been moderated after a rescheduling has been successfully concluded. (In this assessment, however, the risk immediately prior to the rescheduling has been wrongly applied as a yardstick while, generally speaking, the underlying credit and the corresponding agreement on interest rates were arranged at a much earlier period and in a completely different risk situation). Cline counters CEPAL's demand with the view that, on the one hand, in the interests of the debtor countries every possible incentive to grant further loans should still be given to the banks in their lender's trap but, on the other hand, increased interest rates may have a deterrent effect upon other countries as regards any precautionary but not yet urgent attempts to reschedule. Nevertheless, situations are conceivable in which the creditor banks are prepared to grant

concessions on interest rates in the belief that these could be an essential aid towards the recovery of the debtor country.

The industrialised countries are expected to increase their activities in order to move out of the present stagnant period. It appears that many politicians in those countries are not yet sufficiently aware of the vital importance of their economic and financial policies as elements for solving the worldwide debt crisis. This is virtually the only explanation of, for example, the striking contrast between the high sentiments expressed at the so-called economic summit in Williamsburg and the subsequent inadequate actions. The recovery prospects of the international economy seemed to have perceptibly improved around the end of 1983. Yet we should not overlook the fact that the driving-force behind the expansion in the USA derives mainly from the enormous increase in the budget deficit and can therefore last only for a limited period. The view which can sometimes be heard to the effect that the recovery process is already in operation in the industrialised countries and will become stronger of its own accord without any special outside assistance, could very soon prove to be fatally mistaken. Furthermore, the continuing uncertainty of a durable upswing in the industrialised countries and the certainty gained from historical experience that any such economic upswing will last only for a limited period should be a sufficient reason to develop new concepts which make it possible to overcome the debt crisis and achieve a long-term funding of the Third World's economic development even in periods of non-growth or only very slight growth.

CEPAL¹⁷ calls for a new range of mechanisms ("una nueva institucionalidad") for controlling the creation of international liquidity; in other words, it demands "a new Bretton Woods". There does, in fact, appear to be an urgent need for international funding to be adjusted in line with the changed circumstances and also for new sources and ways for supplying capital to the credit-seeking developing countries, new principles for employing capital, new facilities for controlling its employment and new forms of cooperation between international financial institutions and private commercial banks. But we must wait and see whether this requires a new range of mechanisms. Something would no doubt be gained by adapting the existing mechanisms, which have proved their worth over many decades, to the requirements of the 1980s and 1990s.

¹⁵ CEPAL: *Crisis y Deuda en América latina. Notas sobre la Economía y el Desarrollo de América latina*, No. 384, September 1983

¹⁶ W. R. Cline, *op. cit.*, pp. 73f.

¹⁷ CEPAL: *La Crisis Mundial* . . . , *op. cit.*