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Article — Digitized Version

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Intereconomics

Suggested Citation: Osterkamp, Rigmar (1990) : Is there a transfer of resources from developing to industrial countries?, Intereconomics, ISSN 0020-5346, Verlag Weltarchiv, Hamburg, Vol. 25, Iss. 5, pp. 242-247,
<https://doi.org/10.1007/BF02933656>

This Version is available at:

<https://hdl.handle.net/10419/140261>

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Is There a Transfer of Resources from Developing to Industrial Countries?

One of the arguments put forward to support the claim that an unfavourable world economic environment is impeding effective structural adjustment in developing countries is the premise that the flow of resources to indebted developing countries is not only insufficient but also declining and has actually been negative for some years. This leads to the demand for a politically guaranteed positive transfer of resources. Is this demand justified?

A country receives a "net inflow of resources" or a positive net resource transfer if and only if it receives more goods and services from the rest of the world than it supplies to other countries. The combined trade and services account – the current account, excluding transfer payments – is then in deficit. This deficit must be financed, which is only possible in one or more of the four following ways:

- ☐ Net borrowing abroad; the country's debt increases.
- ☐ Net inflow of direct investment from abroad (taking foreign investment into account); the debt remains unchanged.
- ☐ Receipt of transfer payments from foreign governments and non-governmental organisations; the debt remains unchanged.
- ☐ Self-financing through the net repatriation (liquidation) of foreign investments accumulated, for example, as a result of capital flight or through a reduction in foreign exchange reserves; the debt remains unchanged.

This is illustrated in Figures 1 to 4. Figures 1, 2 and 3 portray the case of a current account deficit, in other words a positive net resource transfer. Figure 4 shows a current account surplus and hence a negative net transfer of resources.

Apart from its political content, the demand for a net inflow of resources therefore also has purely logical implications, for if a country cannot or does not wish to

finance the inflow of resources by increasing its debt, it must have greater recourse to non-debt-creating flows – direct investment, transfer payments and the reversal of capital flight. Leaving pure transfer payments aside, in these circumstances the demand for a net inflow of resources is in effect a demand for action by the developing countries themselves, namely to improve conditions so that residents and foreigners will be prepared to invest and hold their assets in the country rather than abroad.

If this solution is considered impossible or inadequate, countries wishing to have a positive net transfer of resources must accept increased indebtedness, and a correspondingly higher future debt servicing burden. If neither an increase in the inflow of funds without a debt effect nor additional borrowing is an acceptable path, this logically means forgoing a net inflow of resources. In these circumstances it would then be pointless to make political demands for such a transfer; only a demand for increased development aid in the form of transfer payments would be admissible on logical grounds.

Many debtor countries do not even consider their debts to be excessive and would be prepared to finance a positive net transfer of resources by increasing their borrowing. The demand for a net inflow of resources therefore carries an implied demand on creditor countries to facilitate and tolerate continued growth in debt by granting additional credit. Such a demand would mean that the debtor countries were trying to achieve by political means what is not happening voluntarily and by market means.

This political demand is often justified on the grounds that a positive net transfer of resources to poor countries is normal and necessary and that an outflow is perverse and has to be avoided. It is true that countries with few

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Different Patterns of Resource Transfer

Figure 1
Net Inflow of Resources with Export Surplus

Exports	Imports
A	(Net) interest payments

A: Current account deficit and its external financing (net borrowing, net access to direct investment, transfer payments).

Figure 3
Net Inflow of Resources with Import Surplus

Exports	Imports
A	(Net) interest payments

A: As in Figure 1. Even when interest payments are set against A there remains a net inflow of resources.

Figure 2
Net Inflow of Resources with Export Surplus and Capital Flight

Exports	Imports
$\frac{A}{B}$	(Net) interest payments
	C

A: As in Figure 1
B = C: External financing to augment foreign exchange reserves, (reported) new investment abroad, (illegal) capital flight.
A + B: Total external financing, which exceeds the current account deficit (A).

Figure 4
Net Outflow of Resources

Exports	Imports
	(Net) interest payments
	D

D: Current account surplus that can be used to finance foreign lending and transfer payments, direct investment abroad, debt reduction, an increase in foreign exchange reserves and capital flight.

capital resources tend to be importers of capital over the long term, but this capital inflow comes about not because of the shortage of capital itself but because of the higher yields it makes possible, but even then only if higher yields are actually paid.

Analysis of the Current Account

As stated above, the current account (excluding transfer payments) tells us whether a country is an overall provider of resources to the rest of the world (current account surplus) or a recipient (deficit). Table 1 shows that the current account of the developing countries as a group was in deficit throughout the eighties with the exception of 1980. The developing countries therefore consistently received more goods and services than they provided. These deficits obviously include interest payments on loans raised

abroad. Until they are repaid, they constitute services to the recipient country, for which the interest payment is remuneration.

The current account deficits fluctuated very widely; they were high at the beginning of the eighties but then declined, not least as a result of economic policy efforts and structural adjustment programmes by debtor countries, and were again rising towards the end of the decade.

Matters could be left there as far as current account balances are concerned. It is already clear that in terms of goods and services there was no outflow of resources from the developing countries as a group.

However, Table 1 also shows that in each of the years considered the inflow of external resources (net borrowing, net direct investment including repatriated

capital, transfer payments) was significantly larger than the current account deficit to be financed. Apart from statistical errors and omissions, the difference represents changes in foreign exchange reserves and capital flight. This is illustrated in Figure 2. The inflow of external funds has not only financed the current account deficit but also left scope for an increase in foreign exchange reserves and/or capital flight. This has led to a corresponding increase in debt, which would have been lower but for the borrowing in excess of the current account financing requirement. A lower level of borrowing in turn would have produced smaller (net) interest payments and hence a lower current account deficit.

Put another way, if there had been less capital flight or a smaller accumulation of foreign exchange reserves the inflow of external resources could have financed a larger current account deficit, in other words higher net imports of goods and services and hence faster growth and less misery in the developing countries.

The conclusion can therefore be drawn that if there is an outflow of resources from developing countries, it consists primarily in capital flight and not in an outflow of goods and services or in an inflow of external resources that is too small in relation to the current account deficit.

In the light of these considerations, one must ask what is the basis of the claim that a net outflow of resources from developing countries is occurring. The issue can be clarified by taking the example of the reasoning used by the World Bank.

The Reasoning of the World Bank

The World Bank breaks away from considering the current account and balance-of-payments methodology. Instead, it records and offsets particular

payment flows to and from developing countries on the basis of information supplied under the Debtor Reporting System. It considers only long-term loans, ignoring short-term credit, direct investment and transfer payments. The entire flow of funds into developing countries is therefore underestimated. Another characteristic of the World Bank's method is that (net) borrowing is offset against interest payments on old loans. Interest income, which naturally also arises, is not recorded. The balance, as shown in the World Debt Tables, is then termed the "net transfer", or "net resource transfer". An aggregate termed the "net flow", consisting of new credit less repayments, is also shown, but the World Bank's reasoning is generally based on the more dramatic figures produced by the "net transfer" concept.

The Figures make the relationship clear. External financing (A) is offset against interest payments. If A is less than the interest payments (as in Figure 1, or $A + B$ in Figure 2), the World Bank ascertains that there has been a net outflow of resources; conversely, if A exceeds the interest payments (as in Figure 3), there has been an inflow.

One could begin by raising a procedural objection that it is inadmissible on the grounds of balance-of-payments methodology to offset the capital account (or parts of it) against an item in the current account (interest payments) in determining whether there has been an inflow or an outflow of resources; the situation can be different in other instances. The capital account and the current account are mirror images of one another because of the rules of double-entry book-keeping, so that to offset or add together the capital account and parts of the current account entails double-counting and is misleading.

Table 1
Current Account Deficit and its Financing: All Developing Countries
(in US\$ bn)

	1980	1982	1984	1986	1988	1990 ^a
1. Current account balance ¹	+ 22.6	- 89.3	-40.2	-59.4	- 27.7	-34.8
2. External financing ²	115.8	126.3	71.3	74.6	49.9	81.2
3. Capital flight, change in foreign exchange reserves ³	138.5	39.3	31.6	15.1	22.2	46.2
<i>For comparison: OECD</i>						
2a. External financing ⁴	128.3	116.3	85.6	83.7	102.9	-

^a IMF estimate. ¹ Balance on goods and services account, i.e. including interest payments but excluding transfer payments. ² Payment flows that have no impact on debt (direct investment and transfer payments) and credits (development assistance loans and market loans); all net, i.e. including repatriation of foreign investment by developing countries. ³ Includes statistical adjustments. In principle, 1 + 2 should equal 3, but this is only approximately true. ⁴ OECD figures for comparison with position 2. A significant difference occurs only for 1988.

Sources: for positions 1, 2 & 3, IMF: World Economic Outlook, April 1988 and October 1989; for position 2a, OECD: Financing and External Debt of Developing Countries, Paris 1988.

A developing country would probably go along with this formal reasoning, but would reply that as far as the individual country was concerned the inflow of resources did consist of the balance between (net) new credit and the outflow of interest payments. This viewpoint and the net resource transfer defined in this way dominate the international debate. As we shall see below, only offsetting in this way produces a negative transfer of resources.

Offsetting new credit against interest payments may be perfectly understandable from the point of view of the debtor, but is it objectively justified? If an inflow of resources is understood to mean a current account deficit and an outflow of resources a surplus, the balance between borrowing and interest payments is certainly not an inflow or outflow of resources but something else that may perhaps reflect a change in a country's liquidity situation or its ability to pay for imports. If offsetting is to be meaningful, interest payments must be an item of the current account that is distinct from all other items of the account. There are only two possible ways of achieving such a distinction:

- ☐ one could say that interest payments, and nothing else, are objectively linked with (past) borrowing and hence may be offset against such borrowing;
- ☐ secondly, it could be argued that interest payments are unavoidable and enjoy the highest priority and hence that they, but not other items in the current account, reduce the inflow of resources by a corresponding amount.

Linking all interest payments with new borrowing is certainly a weak argument, since interest represents remuneration for capital that has already been loaned and not yet repaid, not for the raising of new credit. Moreover, the old loans not only entail an obligation to pay interest but also increase the ability to do so – or at least that was the intention.

If one argues that interest payments are a priority, one must also examine other current account expenditure items that may be equally important. The payment of the agreed remuneration for the loan of capital is undoubtedly a priority, but the same could be said of payments for raw materials, technology, food or even weapons. The economic problems would be similar whether a country attempted to save on interest payments by reducing its debt or to reduce payments to the rest of the world by cutting essential imports.

We therefore arrive at the following results:

- ☐ the balance-of-payments methodology must be followed in order to have an unambiguous definition of "resource transfer";
- ☐ with regard to the question of inflows or outflows of resources, there is no obvious reason why interest payments should be treated differently from other items of the current account;
- ☐ in order to record the "resource transfer" correctly, flows of funds that give rise to no obligations must also be included.

Other Ways of Recording the Flow of Resources

These principles are followed by the OECD, which like the World Bank does not base its calculations on the current account balance itself, but looks at the way in which it is financed, in other words the balance of capital transactions and transfer payments. However, the OECD does cover more payment flows in its analysis,¹ extending the coverage to include long and short-term credit, direct investment and transfer payments. The statistics are broken down into:

- ☐ official development assistance: loans and transfer payments from the governments of industrialised DAC countries, granted directly or indirectly via international organisations;
- ☐ export credits;
- ☐ private flows of resources: primarily bank loans, but also direct investment and transfer payments from non-governmental organisations.

Here too, neither interest income nor information on capital flight are recorded. Let us first consider the level and behaviour of the net inflow of resources into developing countries calculated in this way.

Table 2 shows that the net inflow of resources to the developing countries as a whole and to the relevant sub-groups has always been positive. This does not rule out the possibility that individual countries had a net outflow of resources, as in the case of Korea and Taiwan, which are not included in the table.

The table also shows that the inflows of resources to some country groups declined sharply in the mid-eighties and subsequently recovered only slowly, so that by 1988 the figures for developing countries as a whole and for some country groups had not yet returned to the 1980 level. However, the flow of resources to the poorer countries was higher in 1988 than in 1980.

The behaviour of the sub-aggregate "official

¹ OECD: Financing and External Debt of Developing Countries, Paris 1988.

Table 2
Total Net Inflow of Resources
(Official Development Assistance, Export Credits,
Private Funds) into Developing Countries
(in US\$ bn)

Country groups	1980	1982	1984	1986	1988
All developing countries	128.3	116.3	85.6	83.7	102.9
Poorest developing countries ¹	11.3	10.6	10.4	12.6	16.0
Poor developing countries ²	32.2	38.0	34.6	45.6	54.4
Middle-income countries ³	75.8	61.0	36.6	22.3	31.6
Sub-Saharan countries	16.1	17.7	12.2	19.5	25.2
Poor developing countries, Asia	14.5	15.5	17.8	20.5	30.0
Middle-income countries, Asia	10.2	12.0	7.7	3.0	2.5
Latin America	57.2	49.3	29.8	18.3	22.7

¹ Per capita GNP up to US\$ 250. ² Per capita GNP up to US\$ 500.

³ Per capita GNP up to US\$ 3,000.

Sources: OECD: Financing and External Debt of Developing Countries, Paris 1988; own calculations.

Table 3
Official Development Assistance (Net)
(in US\$ bn)

Country groups	1980	1982	1984	1986	1988
All developing countries	45.6	44.3	47.7	56.1	67.0
Poorest developing countries ¹	9.0	9.0	18.9	11.6	14.6
Poor developing countries ²	22.9	23.3	25.2	31.3	38.6
Middle-income countries ³	11.4	10.5	11.9	13.3	16.1
Sub-Saharan countries	10.6	10.9	12.5	15.4	20.4
Poor developing countries, Asia	9.8	10.0	10.5	13.5	17.8
Middle-income countries, Asia	1.9	2.6	2.4	1.7	1.5
Latin America	6.5	7.8	9.8	11.4	14.4

¹ Per capita GNP up to US\$ 250. ² Per capita GNP up to US\$ 500.

³ Per capita GNP up to US\$ 3,000.

Sources: OECD: Financing and External Debt of Developing Countries, Paris 1988; own calculations.

Table 4
"Offset" Net Inflow of Resources
(Net Inflow of Resources less Interest Payments)
(in US\$ bn)

Country groups	1980	1982	1984	1986	1988
All developing countries	67.3	28.6	4.2	6.1	12.6
Poorest developing countries ¹	10.8	9.9	9.0	10.8	13.9
Poor developing countries ²	21.5	24.0	19.4	28.8	31.4
Middle-income countries ³	30.9	-5.3	-21.3	-28.9	-24.1
Sub-Saharan countries	11.3	12.9	7.9	14.6	19.3
Poor developing countries, Asia	4.3	3.6	3.0	2.6	n.A.
Middle-income countries, Asia	4.0	2.9	-3.7	-7.4	n.A.
Latin America	34.3	10.6	-2.9	-13.6	-9.7

¹ Per capita GNP up to US\$ 250. ² Per capita GNP up to US\$ 500.

³ Per capita GNP up to US\$ 3,000.

Sources: OECD: Financing and External Debt of Developing Countries, Paris 1988; own calculations.

development assistance" (Table 3) shows that the trends in total resource flows would have been far less favourable in the absence of this item. In contrast to total flows and private flows of finance, official development assistance hardly faltered, only stagnating in the early eighties before rising again strongly, so that in 1988 the figures for developing countries as a whole and for all sub-groups except the more wealthy Asian countries were significantly above the 1980 level. Official financing has therefore increased considerably as a proportion of the total net resource flow.

We can therefore state the following:

□ there has not been a negative resource transfer, in other words an outflow of resources, from the developing countries as a group;

□ the poor developing countries experienced only a temporary and slight reduction in their inflow of resources; at the end of the eighties the inflow was considerably higher than in 1980;

□ the industrial countries have committed a substantial volume of additional official funds, partly offsetting the fall in private inflows of resources and outweighing it in the case of the poor developing countries.

We consider the definition of the net resource flow based on balance-of-payments methodology, in other words the OECD approach, to be a meaningful measure. At the same time, however, one cannot ignore the fact that the international debate is being conducted on the basis of figures obtained by using a different definition, that is to say the offsetting of new loans against interest payments that we have rejected above. For purposes of comparison, we shall now examine the figures produced by this definition.

In Table 4 the figures from Table 2 have been corrected by (gross) interest payments and (net) drawings on the IMF. Since no interest income is included, the remaining "offset net resource inflow" is underestimated. Direct investment and transfer payments are included as before. This way of recording the net resource transfer also accords with the practice recently adopted by the IMF.² However, the IMF includes more payment flows than the World Bank, namely direct investment, trade credit and transfer payments.

The perhaps surprising outcome of Table 4 is that here too the net resource transfer is positive for developing countries as a whole and for the groups of poor countries. Negative values emerge only for the more

² See International Monetary Fund: World Economic Outlook, October 1989.

wealthy developing countries and those in Latin America. The table also shows that the 1988 figures, insofar as they are already available, are better than the 1986 figures for all the country groups listed; in the case of the poorest country groups the latest figures are better than at any time in the eighties.

There is obviously a clear case for comparing these figures with the World Bank statistics that dominate the debate, but this is difficult owing to a lack of comparability (different countries, different definition of country groups, inclusion or omission of certain payment flows by comparison with the OECD). The figures on the net transfer for selected country groups summarised in Table 5 are the most comparable with the OECD figures shown in Table 4.

Comparison of Table 5 with Table 4 shows first that the World Bank figures are generally more pessimistic than the OECD figures, which, it should be remembered, have also been reduced by the amount of interest payments. Whereas the World Bank shows a negative net transfer for "all developing countries" from 1984 onwards and a steady worsening thereafter, the OECD figures for "all developing countries" are consistently positive, falling to a minimum in 1984 and then rising strongly.

In both tables the figures for black African countries are always positive, but in the OECD version they are far higher and increase more sharply in absolute terms. Only for low-income Asian countries does the World Bank show better figures than the OECD. In the case of Latin American countries, the World Bank figures are again significantly worse than those produced by the OECD.

Hence, even if one accepts the concept of net transfers as such, one does not have to use the World Bank's figures. Even within the framework of this concept, to have a meaningful definition of "net transfers" one should include short-term credit, direct investment and transfer payments; one would then obtain more favourable figures than those of the World Bank in Table 5.

Conclusions

We return to the question posed at the outset, namely the extent to which the net resource flow can serve as an indicator that the world economic environment is hindering structural adjustment. In the light of the considerations set out above, the answer emerges in the following terms:

□ On the evidence of their current account deficit, there can be no question of the developing countries as a

Table 5
"Net Transfer" according to the
World Bank's Definition
(in US\$ bn)

Country groups	1980	1982	1984	1986	1987
All developing countries ¹	30.0	18.2	-10.2	-28.7	-38.1
Sub-Saharan countries	6.1	6.5	0.5	1.7	2.5
Poor developing countries					
Asia	5.5	3.7	4.1	5.5	5.7
Eastern Asia ²	6.1	6.2	4.3	-4.1	-13.1
Latin America	5.5	2.1	-16.4	-21.9	-18.6

¹ All developing countries, including those in Eastern Europe, such as Poland. ² Including South Korea, Singapore and Thailand.

Source: World Bank: World Development Report 1989.

group having a net outflow of resources in terms of goods and services.

□ The financing side of the balance of payments shows that the inflow of funds was so large that it covered not only the current account deficit but also capital flight and additions to foreign exchange reserves.

□ If the "net resource flow" is measured without double counting or major omissions, as the OECD does, not one relevant group of developing countries has a net outflow of resources. By 1988 the poor developing countries had greatly increased their net resource inflow by comparison with 1980.

□ The achievement of these figures is due largely to the greatly increased commitment of official development aid by industrialised countries.

□ Even if interest payments and IMF drawings are set against the net inflow of resources, the developing countries as a whole and all groups of poor developing countries have positive values, which in 1988 were actually significantly higher than in 1980.

□ This "offset net resource inflow" is negative, however, for the more wealthy developing countries, mainly those in Asia, and for the heavily indebted countries of Latin America.

From the point of view of the net flow of resources, it can therefore not be said that the international economic environment has had an overall prejudicial effect on the efforts of developing countries to carry out structural adjustment, although obviously it cannot be denied that the economic environment and resource flows could both have been better. Third World countries are at a disadvantage and encounter serious obstacles, particularly as concerns raw materials prices and access to the industrial countries' markets in industrial goods and especially agricultural products.