PAPER 1

RETHINKING DEBT AND FINANCIAL MANAGEMENT IN THE CONTEXT OF THE DEVELOPMENT PROCESS

By Professor Christian Comeliau

Introduction

This paper touches upon three distinct yet interrelated areas, namely: (1) External borrowing and the development process; (2) Current developments in international finance and implications for Nigeria; and (3) Multilateral sources of funding and the role of the major International Financial Organisations: the example of the World Bank. Each of these areas will be treated one by one below.

1 – External borrowing and the development process

The process of indebtedness is supposed to be undertaken primarily in favour of development of the borrowing country. So what exactly is development? I shall not try to compare various theoretical definition and at the same time emphasize two major aspects of the development process.

The first aspect is that, at least in a seminar of this sort, "development" must be understood in its most general meaning: that of the *"progress of the society"* (as a modern translation of the Enlightenment idea that "the society of tomorrow may be better than the society of today"). In this context, development is a *multidimensional* phenomenon: it is not only economic and financial, but it is also social, cultural, environmental and political. It also has to be regarded as a *process of choice*, by the community concerned, regarding the components of the desired progress: development is not — and should not — be perceived as a uniform and homogeneous process of change in one unique direction. Regarding the economic aspects of this progress, especially, collective choices must be pronounced about the rhythm, the structure, the content and the time horizon of growth; about income and power distribution among social groups; about the comparative role of the State, the market and the civil society; about the modes and the degree of opening-up of the economy; and so on. These choices must be organised by each of the communities concerned, at various levels (not only national, but also local, regional and global).

The second aspect is that today, the development process is taking place in the general context of "globalisation": this context is defined, mainly, by the accelerated relations of exchange at the global level, the emergence of new actors, and the establishment of new modes of regulation. The emerging "world system" is predominantly economic : it tends to spread a more or less uniform *model of development* across the planet, which would reproduce in all countries the main features of the historical experience of the industrialised countries (these features being in particular: accelerated technology, productivity, expansionism, and predominance of market mechanisms).

The confrontation of the two basic aspects above raises a fundamental issue about the meaning of "development": is it primarily a social progress with components chosen by each community, or is it simply synonymous with the expansion of the world system and of its associated development model through all countries? And if it is both, are these meanings compatible or not? Clearly, in today's world, there is no uniform answer to these questions; and that is why development *and development choices must be conceived and organised primarily as a political rather than a technological process*. The process of indebtedness, the role of debt in development and the issues of debt and financial management are a part of these political phenomena: who decides about indebtedness? What are the objectives? Who are the beneficiaries and who is supposed to pay for the reimbursement of capital and interest?

In this framework, it is important to recall that financial capital is only one development factor among a set of others (including natural resources, equipment, infrastructure, human resources, technology, etc.), and that domestic saving usually provides a major part of these financial resources, to which external resources should be regarded only as additional resources. External borrowing is only one source of foreign capital among others that includes mainly foreign direct investment (FDI) and official development assistance (ODA). Authorities in charge of development policies are supposed to make a systematic "social cost/benefit analysis" of the use of these external financial resources, taking into consideration the specific objectives of the national (or regional) development policies.

The above considerations may seem self-evident: however, it becomes more and more obvious that they are almost completely neglected in the predominant technocratic philosophy on debt issues.

Coming to these debt issues, if one accepts their *political* nature, it also becomes evident that their solutions must be perceived in *economic* terms, in order to maximise the implementation of development objectives at the lowest social cost. The economic rule in this perspective stipulates that external borrowing (as an addition to domestic resources) may be entirely rational and desirable, provided that the development objectives and priorities be clearly defined and that the borrowed resources be primarily allocated so as to generate sufficient resources in the future for the reimbursement of capital and interest that is due. The basic question raised in the field of debt management therefore becomes: *how does one simultaneously and consistently master the development process and the debt and financial management issues?*

The history of debt in the world and in developing countries during the recent decades may appear somewhat far away from those basic principles. Let's just think about the origins of the debt crisis in the seventies: accelerated and simultaneous growth of demand and supply of financial resources as a result of oil shocks and other changes in the international economy. Let's also think about the outcome of this uncontrolled growth of indebtedness: proliferating structural adjustment programs in the eighties and the nineties, social and economic dislocations, decelerating development, increased poverty and dependence for a majority of countries. The resulting costs of the adjustment process (in economic, social, environmental and political terms) are considerable, and it becomes at the same time extremely urgent and extremely difficult for those countries to restore the necessary predominance of development over adjustment in the future. That is the main challenge of the present "development/debt question".

2 - Current developments in international finance and implications for Nigeria

A serious study of this broad set of issues would require an examination of a large list of data, and a comparison of this data with detailed information about the present development problems of the Nigerian economy. Such a study was obviously not possible in the short time available for the Seminar in question. I shall limit myself to referring very briefly to some major changes in the field of international finance, and more specifically to raising some basic *questions* (rather than implications) to the Nigerian development policy makers about those changes.

(1) There has been a major announcement regarding the so-called "international development policy" when the United Nations proposed the list of the *"Millennium Development Goals"*: This list includes quantitative objectives in the fields of poverty alleviation, primary education, gender equality, infant mortality, maternal health, AIDS and other major epidemics, sustainable environment, as well as proposals for global partnerships in finance, trade, technology, health, debt management and reduction, etc. The major question addressed to Nigerian policy makers in the new context resulting from this declaration is therefore: what is your own assessment of these Millennium Development Goals, and *what is your translation of these international goals in terms of national development objectives in Nigeria for the following decade?*

(2) *Poverty alleviation* has become a major slogan of international policies, in terms of development goals, as well as for new instruments in international finance. Examples are: recent discussions among donor countries about ODA; the proposed International Financial Facility; the IMF Facility for the Reduction of Poverty and for Growth; and more generally, the recent discussions and proposals for the replacement of Structural Adjustment Programs through various strategies and procedures of poverty reduction. There is even a preliminary discussion in international forums in view of promoting various forms of international taxation, with poverty alleviation among the key priorities. One of the major criticisms about these poverty reduction strategies, however, is that such strategies are targeted towards the effects or the results of poverty, rather than towards the *causes* – and especially the "systemic" causes – of poverty. The question for Nigerian development policy makers regarding these perspectives is: *what is your own view on these proposals and, more specifically, on the very notions of poverty and poverty alleviation in an African and Nigerian context?*

(3) Regarding the recent changes in the *structure of international financial flows*, it appears that FDI (foreign direct investment) flows remain heavily concentrated among industrialised countries, and that the flows towards the developing world are extremely selective in favour of less than a dozen countries. The impacts of those flows must be carefully debated in terms of development : there may be a positive impact, at least in terms of economic growth and export revenues (usually less in terms of employment), but the impact is less clear on the balance of payments and may be negative in terms of overall dependence of the country. On the other hand, ODA global flows (Official

Development assistance) have been constantly decreasing up until recently, and the changes in their structure have certainly not been favourable for Sub-Saharan Africa. Three basic questions to Nigerian development policy makers are therefore: (1*) Is it possible for Nigeria to reverse these negative trends of selectivity of the external financial flows, and if so, by what means?* (2) *What is Nigeria's own preference in the use of external financial resources* (taking into account the country's cost/benefit analysis of the three categories of these flows) as compared to the specific objectives of the country's development policy for the future? and (3) Do you consider that in the present context, the policy priority, for Nigeria and for developing countries, has become to act collectively in order *to change the commercial and financial rules of the global economy,* rather than to ask permanently for an increase in the flows of financial resources towards developing countries?

(4) Finally, there have been many international discussions in the recent years on *possible strategies for debt reduction or even debt cancellation*. Still, the present modalities of debt negotiations (around the Paris Club or the London Club, in particular) confront clubs of creditor countries to each of the debtor countries taken separately: there have not been any examples of associations or even alliances of debtor countries in debt negotiations. The result must be considered, of course, in terms of comparative strength and weaknesses of the various parties in the negotiations. The question is: why is this so? And the particular question to the Nigerian authorities in debt and financial management is: given the importance of the Nigerian economy in the African context, *is it feasible and desirable to develop a Nigerian initiative to organise an alliance among African countries for debt negotiations?*

3 – <u>Multilateral Sources of Funding and the Role of the Major International Financial Institutions: the Example of the World Bank</u>

This topic is very broad, and requires the discussion of very extensive literature. My objective is more modest: it is only to illustrate how the international financial institutions function — especially the Bretton Woods institutions (i.e. the International Monetary Fund and the World Bank Group, with their voting power distributed among countries, in proportion to their level of income) — with the World Trade Organisation being among the dominant public actors and rulers of the world system described above. I shall try to suggest how the example of the World Bank emphasizes some of the basic challenges for national and international development prospects that are raised by the emerging world system.

Before discussing the case of the World Bank, I would like to summarize the present "development philosophy" of the world system through a short assessment of what has been called the "Washington consensus". I am conscious of the fact that many commentators consider that the time of this consensus is now behind us and that we should try to identify the main features of a "post-Washington consensus". However, I do not personally believe in this change, and I think that the lines of this international development philosophy, as described under this wording ten years ago remain basically valid. What are these lines?

The "Washington Consensus" does not result in a formal international agreement: the formula was used at the beginning of the nineties by an American economist, John Williamson[1], to describe and summarize the rules of macro-economic and macro-financial management established by the Bretton Woods institutions (in accordance with the American Treasury, hence the reference to Washington D.C). Those rules are imposed on the majority of developing countries, but they are also "internalised", it could be argued, by the majority of countries, including industrialised nations. The ten principles of management proposed as a summary by John Williamson are related to the balance of payments management (financial liberalisation, single exchange rate, encouragement of FDI, and trade liberalisation), to the fiscal system (fiscal discipline, priorities in state expenditures, and tax reform), and more broadly to the necessary predominance of market mechanisms (privatisation, deregulation, and property rights). I will not present these ten rules in detail as in Williamson's presentation; instead I prefer to insist more on the development perspective involved in this so-called consensus, and I will personally summarize this perspective through the following five principles[2]:

- long term development is basically assimilated to limitless GDP growth;
- "social" development will automatically follow from GDP growth through the so-called "trickle-down effect";
- countries should maximise their engagement in international trade and relations;
- market principles should be systematically preferred to State regulation mechanisms, and the State should be considered as "subordinate" to market rules; and
- there is only one development model that is rational and desirable, in the line of the experience of developed countries.

Given these principles, one can understand why international institutions are so important in the present practices of the world system. In actuality, the role of the "financial" multilateral institutions like the World Bank in the development process is not primarily financial. While providing information, technical aid and finance, these institutions consider themselves primarily as the authorised sources of a sort of official "development doctrine" that should be generalised to all countries.

The World Bank is a fascinating example of such a concept. The speeches of the successive presidents of the World Bank, about their strategies, are full of slogans regarding priorities such as "basic need satisfaction" (Mr. McNamara in the seventies) and "poverty alleviation" (Mr. Wolfensohn).

In fact, the World Bank's official definition of the word "development" is precisely defined in Article 1 of the I.B.R.D.[3] statutes, which mention the World Bank's basic objectives as the following:

---

[1] See : John WILLIAMSON (ed.) : *The Political Economy of Policy Reform*, Institute for International Economics, Washington D.C., 1994.

[2] See a special issue of the *International Sciences Journal (*UNESCO), December 2000, n° 166, on « The development Debate : beyond the Washington Consensus », and especially my own paper in this issue on « The limitless growth assumption », pages 457-465.

[3] International Bank for Reconstruction and Development, which is today the main component of the « World Bank Group ». These statutes have been written and voted in Bretton Woods in 1944, and the article 1 has not been modified since then.

- "to assist in the reconstruction and development" (with the word "development" meaning essentially "the development of productive facilities";
- "to promote private foreign investment"; and
- "to promote the long-range balanced growth of international trade".[4]

However, one will notice that poverty is not mentioned anywhere in these founding texts. Of course I am not accusing the World Bank of omitting this information. I am only trying to identify the official *priorities* of the World Bank, as defined and imposed by the founders to the members states — and consequently to the staff of the World Bank. I also believe that the texts are very clear. This does not imply, of course, that the role of the World Bank should be considered as basically negative. It only means that, if the development process is to be regarded as a process of *choices, the autonomy of national authorities is seriously limited* by these institutions and the rules of the present world economic system.

[4] I propose a broader analysis in : Christian COMELIAU, *The Impasse of Modernity. Debating the Future of the Global Market Economy,* Zed Books, London and New-York, 2002.

A NEW APPROACH TO DEBT MANAGEMENT

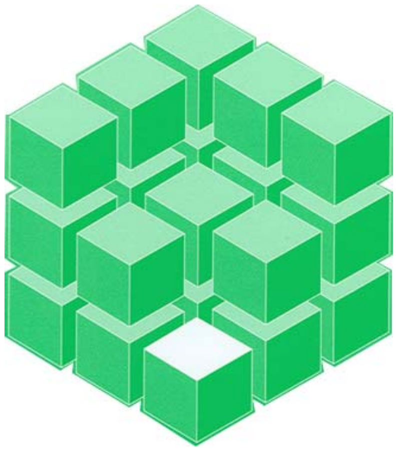
Papers written following a UNITAR Seminar on
"The Legal Aspects of Debt and Financial Management"
for Officials from the Nigerian Debt Management Office
(Geneva—Switzerland, 6 to 10 December 2004)

GENEVA, January 2005

UNITAR

UNITAR TRAINING PROGRAMMES IN THE LEGAL ASPECTS
OF DEBT AND FINANCIAL MANAGEMENT

A NEW APPROACH TO DEBT MANAGEMENT



Document No. 21