

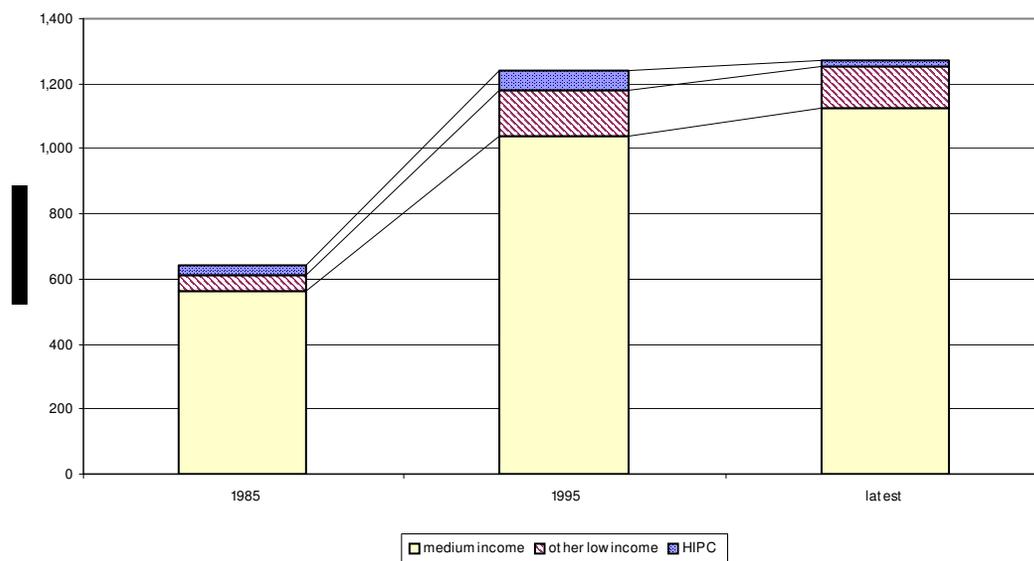
Summary: Debt Relief as if Justice Mattered

This report is the last in a series from **nef** designed to stimulate progress towards a comprehensive and fair treatment of the crisis of sovereign debt. With the end of an unprecedented period of low interest rates now in sight, such a goal is needed more than ever. This is a short summary of the paper – readers seeking further clarification are asked to see the full paper at www.jubilee-research.org¹. Comments are welcome and should be sent to david.woodward@neweconomics.org.

Debt relief isn't working

Current approaches to debt relief (HIPC and MDRI for poor countries and Paris and London Club renegotiations for middle income countries) are not solving the problems of Third World indebtedness. HIPC and MDRI are indeed reducing debt burdens but for a small range of countries, and at a high cost in terms of loss of policy space and after long delays, but non-HIPC poor countries also have major debt problems. Middle-income country indebtedness continues to grow. In 2005, for example, Lebanon (the worst case) spent 52% of its budget on debt service.

Figure 1 Third World debt 1985 to 2005



The present approach is marred by the involvement of creditors as judge, prosecution and jury in direct conflict with natural justice and by the failure to take into account either the human rights of the people of debtor nations or the moral obscenity of odious debt. Creditors use the debt relief process to further their own agenda of privatisation and trade liberalisation. It is all too little and too late.

The need for a new approach

There is a clear need for a new approach to resolving sovereign debt problems which is comprehensive, systematic, fair and transparent and above all, just. Responses from the creditors so far to criticisms such as those in the previous paragraph have been grossly inadequate.

¹ The full url is:

<http://www.jubilee-research.org/news/debt%20relief%20as%20if%20justice%20mattered.pdf>

There is as yet no consensus about the way forward. This report aims to stimulate debate and help find a just solution to the debt crisis.

Human rights and debt cancellation

We update the calculations of debt sustainability taking human rights into account for 136 countries, first carried out in our report *Debt relief as if people mattered*, using the latest figures available and taking MDRI into account. We argue for using an ethical poverty line of \$3 a day, the level at which average life expectancy starts to level out². Even after the debt relief already granted under HIPC and MDRI, 47 countries need 100% debt cancellation and a further 34 to 58 need partial cancellation, amounting to \$334 to \$501 billion in net present value terms, if they are to get to a point where debt service does not seriously affect basic human rights to food, shelter education and health services. None of the countries needing debt relief can afford to take out any extra debt and so a marked increase in grant aid is also needed if poverty is to be reduced and the Millennium Development goals achieved.

Table 1. Summary of results, human rights approach to debt cancellation

Assumptions		number of countries needing 100% debt cancellation	number of countries needing partial debt cancellation	total amount of debt cancellation (\$bn, present value)
poverty line	debt-service as % of nfr			
\$2 pd	20	43	54	425
	30	43	39	310
	40	43	32	241
\$3 pd	20	47	58	501
	30	47	39	398
	40	47	34	334

nfr = net feasible revenue pd = per day

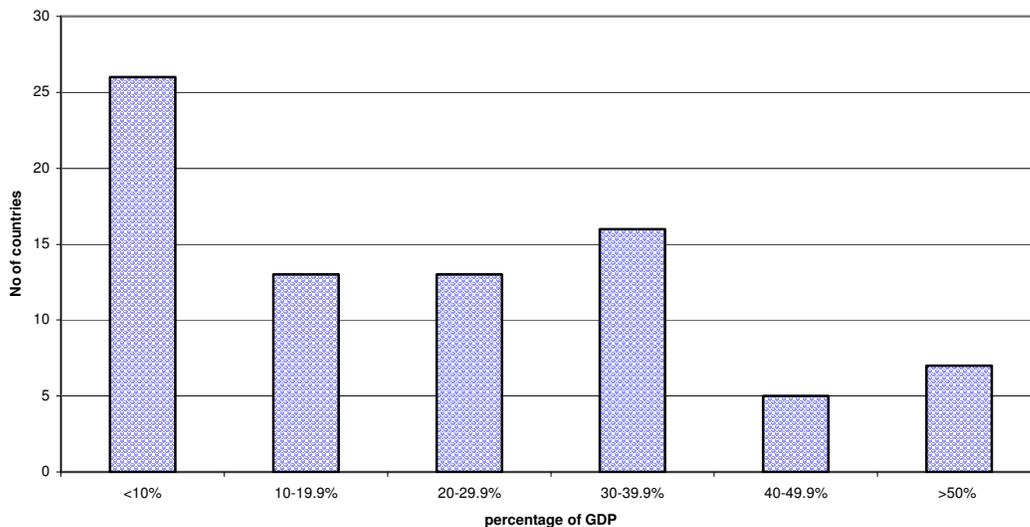
Our recommended debt cancellation amounts to between 24 and 35 per cent of all outstanding developing country debt. **This sounds a lot until it is compared with the shortfall of aid below the target of 0.7% of rich countries' GDP, which was \$120 billion in 2005 alone. If the North had met the target each year between 2001 and 2005 it could have more than wiped out all this debt.**

Domestic debt

Domestic debt was not covered by our previous reports. With increasing relaxation of capital controls on foreign exchange transactions and growing involvement of financial corporations in Third World domestic debt, the boundary between domestic and foreign debt is becoming increasingly blurred. Data is scarce but we make a first attempt to quantify the problem. From a data base of only 39 countries, Lebanon and the Seychelles top the list with domestic debt almost equivalent to their national incomes. Egypt and Jamaica come next with domestic debt amounting to about 75% of national income. This adds to the burden of debt and is a problem, especially for a number of middle income countries. A number of them are taking out domestic debt to fund the repayment of foreign debts, even though domestic interest rates are usually higher than international ones. This needs to be taken into account in any comprehensive debt analysis. More work needs to be done in this area.

² See Debt relief as if people mattered (Mandel, 2006) for full details. (http://www.jubileeresearch.org/news/debt_relief_final.pdf)

Figure 2 Domestic debt (ratio to GNI or GDP)



Odious debt

It seems inherently unfair if a blatantly corrupt and dictatorial regime can take out loans in the name of its country, but without the consent of the people, steal the proceeds and then leave the unfortunate inhabitants and their children to pay back the creditors, without those creditors taking any responsibility for knowingly lending to these odious regimes. Our second report, *Debt relief as if morals mattered*³, calculated the cost of odious lending to 13 case study countries and showed that 10 of them had odious debt greater than their current outstanding debt and that 5 of them have odious debt greater than their national income. Lenders must be held to account for irresponsible lending, including lending that sustains regimes that violate human rights. This last report updates these calculations, with the results summarised in Table 2.

Table 2: Odious debt and income per person

Country	Odious debt per cap (US\$)	per cap income (Atlas method) 2005 US\$	ratio of odious debt to income
Congo, Dem. Rep.	283	120	236.2%
Nicaragua	2,067	950	217.6%
Nigeria	734	560	131.1%
Malawi	206	160	128.6%
Argentina	4,537	4,470	101.5%
Indonesia	1,001	1,280	78.2%
Sudan	477	640	74.5%
Philippines	848	1,320	64.2%
Ghana	236	450	52.4%
Peru	1,373	2,650	51.8%
Pakistan	300	690	43.4%
Haiti	102	450	22.7%
South Africa ⁴	378	4,770	7.9%

³ <http://www.jubileeresearch.org/news/Odiouslendingfinal.pdf>.

⁴ It should be noted that the total of odious debt for South Africa should be considerably higher but no figures are available in the World Bank database for debt service during the apartheid regime.

Mechanisms needed

This report then goes further than the two previous ones in setting out proposals for dealing with odious and unsustainable debt in a systematic and comprehensive manner.

We propose four basic principles for dealing with odious debt:

1. Unrepresentative and undemocratic governments do not have the right to impose external debts on subsequent representative and democratic governments.
2. Creditors act irresponsibly in lending to such governments, thereby promoting the latter's continuation in office, and therefore forfeit the right either to profit from such loans or to recover the capital so provided, except from the persons directly profiting from the loan.
3. Legitimate governments (and their populations) should be no worse off, in terms of external indebtedness, as a result of odious debts having been incurred by previous governments than they would have been had these loans been refused.
4. Arbitration over the extent and treatment of odious debts should be in the hands of an independent international body, which is neither a creditor in its own right, nor controlled by creditors or debtors, and which conducts its activities in a transparent fashion.

We conclude that put these into practice there needs to be a quasi-judicial process whereby regimes can be declared odious and mechanisms put in place for an orderly work-out of both odious and unsustainable debt. As soon as there is such a working mechanism there is going to be a need for the inclusion of an assessment procedure for existing regimes. Otherwise there will be the unintended consequence that finance becomes a lot more expensive or even impossible for any regime which creditors think might be considered odious in future. While this is a powerful potential sanction for the international community, it needs to be used in a highly selective, conscious and targeted way.

We therefore recommend the creation of a panel of adjudicators chosen on a regional basis by all legislatures. This procedure is recommended as a means to reduce the chances of "capture" of the institution by partisan governments. These adjudicators would sit in panels of three to assess the legitimacy of all regimes at the point of regime change. Present regimes could also ask for the panel to review the legitimacy of past governments. If a regime were to be declared odious, loan agreements would cease to be enforceable in court.

Whether on grounds of the odious nature of their debts or their unsustainability, governments should be able to call for a "Fair and Transparent Arbitration Procedure" (FTAP) in which equal nominees of creditor and debtor would sit with a mutually agreed chair to determine an orderly debt work-out. Unlike the panels described in the previous paragraph, which would be permanent and have a brief covering the whole world, the arbitration committee would be ad hoc and a separate one would be needed for each country. All creditors would be bound by such a work-out, thus outlawing the behaviour of vulture funds.

Loans declared odious should be cancelled and compensation payable by the creditor for any debt service paid. Odious loans "laundered" by being repaid (often by taking out new loans) should be compensated for by a rolling fund, which would itself seek recompense from the original odious lender and the direct beneficiaries of the loan (ie the corrupt rulers and their cronies).

Only in this way can there be debt relief *as if justice mattered*.