CHAPTER VII

SUMMARY AND CONCLUSIONS
The sudden and sharp hike in petroleum prices in 1973-74 brought a wave of tremor in the economics of developed and developing countries alike. It did not take much time, for the former to adjust with the shock, however, most of the latter countries are yet to recover. The economies of the developing countries have been further hit due to recessions in the industrialized countries and imposition of tariff and non tariff walls for the goods imported from the developing countries. Consequently, the developing countries, particularly the lower income ones have been beset with growing trade deficits. Partly due to the current account deficits and also to meet their growing demand for the import of capital goods, the developing countries including those of South Asia borrowed extensively and intensively in the international markets. The borrowings of the South Asian Countries increased almost by three times during the period 1970-1984. An attempt has been made in the present study to find out -

(i) the changes in the compositions and magnitude of rise in the flow of debt;
(ii) the growth of public debt both in the nominal and real terms;
(iii) the debt paying capacity of SAC;
(iv) the contribution of different factors in the loan commitment.

We formulated the following hypothesis and have tried to test their validity :-
that the loan commitment is determined by the rate of interest;

that the maturity period influences the loan commitment;

that the grace period determines the loan commitment;

that the grant element has influenced the loan commitments.

The data for the study have been drawn from the World Debt Tables published by the World Bank, World Development Reports and the Annual Reports of the International Monetary Fund. Though there are some limitations of the data which has been explained in chapter one, however, the study is meaningful despite that. Besides calculating the compound growth rate of different sources of credit and the net flow of debt the nominal and real value of increase in debt have also been measured by deflating the general price index and also by deflating the export and import prices with the average prices of the year 1968-77. The debt paying capacity has been estimated by finding out the ratios of debt outstanding and disbursed (DOD) to the exports of goods and services (XGS) and DOD to Gross National Product and DOD to XGS to payment of interest and total debt services to XGS and GNP. Correlation matrix, multivariate analysis and analysis of variance have been applied to find out the relationship between loan commitment and maturity period, interest rate, grace period and grant element.
Official and private are the two sources of external debt. The relative importance of the former has marginally declined during the period of study (1970-89) despite that it continues to predominate as a supply of credit since almost 75 percent of the credit is still supplied by them. Among the official sources the multilateral credit agencies share is constantly rising while that of bilateral has been declining. In the year 1970, this share was in the ratio of 20:80. While in the terminating year it has been 51:49. The relative role of IBRD has marginally declined in 1985 but after that it has increased. Though private creditors contributions have been steadily growing, it is the financial markets rather than the private suppliers which are of any significance.

The individual countries, however, differ in their performance. India, Maldives, Srilanka share the experience of the region. In Bangladesh, Burma, Nepal and Pakistan however, the role of official credit continue to be growing.

The debt outstanding and disbursed of the SAC rose almost by eight times during the period of study. Since changes in the stocks of debt are suggestive but flows of capital are better indicators of the provision of resources for these countries. The loan commitment of the revion as a whole has increased by more than five times and the compound growth rate has been of the order of 13.33. The Disbursement has also been more than seven times the growth rate was 11.23. The net flow of loan and the payment of interest also reveal more or less the same growth rate.
The real and constant purchasing power value have been eroded by inflation almost all over the world, therefore, increase in debt is not significant in real terms. When the value of debt is deflated by price index or exports and imports price, we find that the growth in debt neither serious nor disproportionate. For the region as a whole the deflated price index revealed that the external debt has increased by 14.92 percent but when deflated by import or export price the rise is 13.42 and 30.85 percent respectively. Comparatively higher values of export prices are due to the fact that these countries are primary goods exporting countries and their prices did not keep pace with prices of other goods and services.

India and Pakistan's rise in the nominal value of external debt kept pace with that of South Asian Countries. Similarly their increase in the real value of external debt when deflated by general price index or export or import prices were also in tune with the SA Countries.

But the rise in real value of external debt of Maldives ran in a few thousand times. However, Nepal, Burma, Srilanka and Bangladesh too had experienced perceptible rise in the real value of their external debt.

The overall trend of debt servicing capacity of SA Countries is not dismal. The ratios of DOD to XGS declined from 279.0 to 241.7 though it increased in the case of the ratio of DOD to GNP from 15.2 to 25.9. Similarly the ratio of TDS to XGS increased from 18.3 to 21.8 and TDS to GNP increased from 1.0 to
2.3 The payment of interest to XGS also increased from 6.8 to 10.5.

The ratio of debt outstanding to exports of goods and services (XGS) have come down from 279.0 to 241.7; though a marginal rise is witnessed in the DOD to Gross National Product (GNP). Similarly the ratio of total debt services (TDS) to XGS has also increased from 18.30 to 21.8. Again a marginal rise is apparent in the ratio of TDS to GNP from 1.0 to 2.3. The ratio of payment of interest (INT) has also increased from 6.8 to 10.5.

When the debt is regressed to per capita income, we find that there is no overall tendency for DOD to rise as per capita income increases. In fact there is slight tendency for the debt level to fall with rising per capita income.

But the individual countries of SA do not share the same experience. India is the only country which witnessed the same changes in her ratios. Pakistan though quite close to India to experience the same changes in her ratios. Pakistan experienced a fall in the ratio of INT to XGS.

And lastly, we examined the factors governing loan commitment and it was found that excepting the interest rate all other factors viz., maturity period, grace period and grant element had negligible affect on loan commitment in the region as a whole. Maturity period alone affected 72.6 percent of the loan commitment.

When we study the individual country, we somehow obtained a different result. In these countries alongwith other
factors maturity period does not affect the loan commitment. However in case of Nepal, interest rate has significantly affected loan commitment.

There is no immediate cause to worry for the SA Countries as a whole as far as external debt even as we find for the Latin American Countries of Brazil, Mexico or R Argentina which have fallen in debt trap. However, caution is needed right now, even for the SA Countries. The major problem before the South Asian Countries are that the net flow of debt is not increasing in time with their requirements. Secondly the relative decline in the importance of official sources of creditors has forced them to borrow from the private sources where the rate of interest is higher, maturity period is shorter and grant element is nil. Thirdly, for a majority of the countries of SA the ratio of DOD to XGS, DOD to GNP, TDS to XGS have been rising. When compared to LOD the situation become still worse. Therefore it appears that the solution lies not only in making constant efforts on the part of debtor countries but also those of creditor countries.

The problem of external debt is very closely associated with the economic development of these countries. Therefore, the countries should be advised to pursue the policies conducive to their rapid economic development.

Economic growth is needed both to increase consumption and to servicing existing debt. The pace of growth should be accelerated to products, whose costs would be low rather than following a policy of import substitution regardless
of costs. No doubt for some strategic and basic needs self sufficiency is vital. But self sufficiency across the board is neither attainable nor desirable. Import substitution must be selective in these countries.

At the same time, countries of South Asia must emphasis on the modernization and the rehabilitation of their old industries which have become uneconomic due to obsolescence of their plant and machinery. Therefore, priority be given to the rejuvenation of old industrial plants rather than establishing the new once.

To help in this task and to motivate the owners of older industrial units to go in for modernization, they should be exposed to competition. But it should be done gradually so as not to make them collapse. Initially these industries be exposed to freer domestic competition. Restrictions on output be lifted at the same time, they should be given necessary financial and fiscal help to face competition at home and abroad.

For some of the SAC the volume of investment is found to be exceed to the domestic savings. A high rate of growth in these countries can be sustained by the inflow of external capital whether from official sources like the World Bank or by way of private equity capitals or in the shape of commercial loans. At the same time they must avoid the mistakes which many developing countries have made and which has led to their fall into debt trap.

One of the factors to be taken into account in regard to loans is that the schedule of repayments must not be
such as to become too heavy in particular years in relation to the export earnings. Otherwise, the economy may be in good health for a long term viewpoint it may fall a short term crisis.

And lastly, stable macroeconomic environment is a prerequisite for a successful transition to medium term economic growth. Maintaining macroeconomic stability typically requires holding the fiscal deficits to a low fraction of gross domestic product; keeping tight discipline on monetary expansion and maintaining a realistic exchange rate policy.

The creditor countries should reduce the tariff and non-tariff walls imposed against the imports of developing countries including that of SA. When the exports of these countries rises then ability to discharge their debt improves and their deficits are avoided.

The official sources need to provide more credit to them at concessional rates and for higher maturity period. In fact, the trade needs of these countries can not be adequately met by adherence to GATT rules of non-discriminating multilateral trading systems with its emphasis on Most Favoured Nation Treatment on reciprocity in trade negotiations. A policy of a differential and more favourable treatment in a non-reciprocal basis for the developing countries, so as to enhance their access to markets of developed countries and thereby increase their share of world trade is needed. It is essential that a positive international action is needed to increase export earnings of these countries. It is necessary that an active intervention in
the commodity markets viz., the international commodity agreement to secure stable, just and remunerative prices of primary commodities exported by developing countries.

If the developed countries could adopt positive measures such as provision of adjustment assistance to facilitate phasing out of those industries and processes in which the developed world no longer enjoys comparatively advantages. Finally as an extension of the classical infant industry protection argument the developed countries could give preferential treatment to exports of these countries by adopting a system of generalized non-discrimination tariff preferences in the favour of South Asian Countries.

Specific Recommendations

Given the level of external debt carried by these countries in recent years, and given the "harsh" international economic circumstances which seem likely to prevail during the rest of the 1980s, it appears fairly appropriate that the SACs should exercise better management of their external debt. An this must come about as part of a general improvement in economic, monetary and fiscal policies. The improvement required in these policy areas should be designed to secure high growth during the coming years. In this endeavor, certain policy criteria should be seriously considered. Thus, these Islamic debtor countries would be well advised to do the following:

(a) Apply more effective methods of mobilizing domestic financial resources and enlarge participation of
their national banking system in developing financing;

(b) Ensure maximum efficiency in the allocation and utilization of all domestic resources;

(c) Economize on capital, whenever possible, through applying capital saving technologies, especially those which save foreign exchange resources;

(d) Refrain from short-term borrowing to finance long-term development;

(e) Minimize borrowing from foreign commercial banks as long as their terms of lending remain excessively hard;

(f) Borrow only what is "really" needed (that is only what can be used efficiently);

(g) Avoid excessive deficit financing, improve on economic performance and rationalize development planning and allocation of development resources in favour of dissatisfying basic home needs;

(h) Revise trade policy in favour of development and growth;

(i) Promote interregional co-operation and economic integration among the Islamic economies and readjust or co-ordinate development strategies accordingly; and

(j) provide sufficiently effective incentives for interregional flows of capital, including private direct investment.
The rationale of the proposals is based on the fact that the interest of creditors and debtor countries are intertwined, and the general purpose is to help to make the international economic environment more favourable to growth in the developing countries (and thus create a sounder base from improved debt management). However, since the national policies are the crucial factor in economic development, it follows that the developing countries, in their turn, should improve on their domestic policies in order to secure:

- Better mobilization of domestic resources;
- More efficient use of these resources;
- Better management of external debt.