Written evidence submitted by the Jubilee Debt Campaign

Summary
1. Jubilee Debt Campaign is a campaigning coalition with 12,000 supporters and 50 member organisations. We are part of a global movement demanding freedom from the slavery of unjust debts and a new financial system that puts people first.

2. Contracting, managing and resolving sovereign debt should be a major issue for government development policy. Following global campaigning against the injustice of developing country debt, $130 billion of debt has been cancelled for 35 countries through the Heavily Indebted Poor Countries (HIPC) initiative. This has saved billions of dollars every year, and led to millions more people having access to healthcare and education.

3. However, a significant number of countries were excluded from this scheme, where unjust and unsustainable debt payments continue to prevent the meeting of Millennium Development Goals. Moreover, there are signs that a boom in lending is threatening a new developing world debt crisis.

4. Debt crises in the 1980s, 1990s and 2000s caused two or more ‘lost decades of development’. In sub-Saharan Africa, the number of people living in extreme poverty (on less than $1.25 a day) increased from 205 million in 1981 to 330 million by 1993. It would be recklessly unjust for such debt crises to be recreated again.

5. This submission puts forward a range of policy recommendations which we believe should feature as key priorities for the UK’s future approach to development in order to prevent a new developing world debt crisis and avoid the devastating impacts that such a crisis would have for sustainable development and human rights and wellbeing in developing countries:

A. Cancelling unjust and unsustainable debts
1. Support the creation of a debt relief scheme for Small Island Developing States.
2. Hold a public audit into debts owed to UK Export Finance, cancel those from unjust deals such as loans for arms sales to now deposed dictators, and use the audit to adopt standards to prevent such deals being supported again in the future.

B. Controlling lending to prevent new debt crises
3. Commit that all UK bilateral aid will remain as grants.
4. Shift aid money away from sources which give loans, towards sources which give grants.
5. Require all lenders funded by the UK, including UK Export Finance, the World Bank and IMF, to sign up to responsible lending guidelines, including public scrutiny of loan terms before contracts are signed.
6. Support the creation of a fair, transparent and independent process for resolving sovereign debt crises, to show banks they won’t be bailed out for reckless loans.
7. Stop PPPs from being a condition of IMF and World Bank loans, and call for a review of the impact of PPPs, including on debt sustainability.

C. Increasing developing country tax revenues
8. Remove the gateways and exemptions from the UK’s Controlled Foreign Companies rules which prevent them from deterring tax avoidance and evasion in third countries.
9. Ensure that every tax rule and treaty adopted by the UK government has a spillover analysis to check that it won’t harm developing countries, but rather will actively help them in tackling tax avoidance and evasion.

A. Cancelling unjust and unsustainable debts
6. Policy recommendation 1: Support the creation of a debt relief scheme for Small Island Developing States to help countries out of the current debt trap, and create greater protection against future natural disasters and economic shocks.

7. To qualify for the Heavily Indebted Poor Countries (HIPC) debt relief initiative, countries both had to be classed as low income (with a GDP per person of less than £650 a year) and very heavily indebted, as well as implementing IMF and World Bank economic policies (including water privatisation, trade liberalisation, and selling off vital emergency reserves of grains and other food staples).

8. There are therefore a significant number of countries which still have large debt burdens which are preventing the meeting of the Millennium Development Goals and undermining poverty and inequality. These include Jamaica, Pakistan and El Salvador, all of which are spending more than 20 per cent of government revenue on foreign debt payments. As such, the Millennium Development Goal committed to by rich countries including the UK to “deal comprehensively with the debt problems of developing countries” has not been met.

10. One set of countries in particular need are Small Island Developing States, including Jamaica, Grenada, Antigua & Barbuda, Samoa and Tuvalu. The Jamaican government’s foreign debt payments have cost over 20 per cent of government revenue for the past 25 years, and are currently 28 per cent of revenue. The cuts in health services in response to this debt crisis has meant that maternal mortality has doubled over the same time period, whilst the proportion of children completing primary school has fallen from 97 per cent in 2010 to 73 per cent today.

11. Common economic shocks which have hit many Small Island Developing States in recent years include the loss of trade preferences to the EU, natural disasters, particularly hurricanes and typhoons, and the 2008 Western banking crisis, which has reduced tourism revenues.

12. This means many such countries are stuck in a debt-austerity trap of high debt payments, low economic growth and declining standards of public services. Whilst they notionally have a higher GDP per capita, Small Island Developing States’ dependence on imports and exports and vulnerability to negative changes in costs of imports or revenue from exports means they share many features in common with Heavily Indebted Poor Countries.

13. Policy recommendation 2: Hold a public audit into debts owed to UK Export Finance, cancel those from unjust deals such as loans for arms sales to now deposed dictators, and use the audit to adopt standards to prevent such deals being supported again in the future.

14. Around $2 billion is still owed directly to the UK government by developing countries, mostly to UK Export Finance. These debts come from loans guaranteed by UK Export Finance for other governments to buy British exports. When the loans were defaulted on, UK Export Finance paid off the original lender, and then took the loans on themselves.

15. Of the current debts:
   - 74% of Indonesia’s debt comes from loans for the former regime of General Suharto for military equipment, including Hawk aircraft and Scorpion tanks, which were used against the Indonesian people. Despite General Suharto being toppled from power, the debts are still being paid.
   - 56% of Ecuador’s debt comes from loans to various military dictators for military equipment.
   - Loans for arms to dictators are also owed by Iraq (to Saddam Hussain for a chemical weapons factory and other arms sales), Egypt and Argentina.

16. The government of Norway has held a public audit into similar export credit-related debts owed to it, and cancelled debts owed by five countries (Ecuador, Egypt, Jamaica, Peru and Sierra Leone) for projects where it was known the exports concerned would be of no benefit to
The people of the countries receiving them. The audit has been used to help set standards for more responsible Norwegian lending in the future.

B. Controlling lending to prevent new debt crises

17. Lending to developing countries is currently booming. External loans to low income country governments doubled from 2007 to 2012, from $5.8 billion to $11.8 billion. Loans to sub-Saharan African governments more than doubled over the same period of time. Almost half (45 per cent) of loans to low income countries are from the World Bank and IMF. Together, multilateral bodies are responsible for 60 per cent of lending to low income countries, governments 30 per cent and the private sector 10 per cent.

18. This lending boom risks undermining hard won debt sustainability in some countries, and recreating new damaging debt crises. Lending to some countries means they are on track to once again be spending as much on debt payments as they were before debt cancellation. Of the 35 countries which have completed the Heavily Indebted Poor Countries Initiative, six are classed by the IMF and World Bank as at high risk of not being able to pay their debts again, and 17 at moderate risk.

19. For example, the IMF’s latest assessment of the Ghanaian government’s debt predicts that foreign debt payments will reach 20 per cent of government revenue by 2024. This assumes economic growth of 6 per cent a year, and government revenues increasing from 18 per cent of GDP to 23 per cent. One economic shock could push payments to 35 per cent of government revenue, well above the 18-22 per cent limit the IMF says governments often struggle to repay. The sources of lending to the Ghanaian government are 40% foreign governments, 30% multilateral institutions and 30% private sector.

20. Other countries who the IMF and World Bank predict will be spending as much revenue on debt payments within the next decade as they were before receiving debt relief include Tanzania, Ethiopia and Mozambique.

21. This boom in lending is being caused by two main sources, a) Increased loans from governments and multilateral institutions, especially as aid (see below) and b) Increased lending by the private sector (see page 4).

i) Increased loans from public sector, especially as aid

22. Policy recommendation 3: Commit that all UK bilateral aid will remain as grants so as not to add to the lending boom, and reduce risk for developing countries.

23. Policy recommendation 4: Shift aid money away from sources which give loans, towards sources which give grants so as to reduce the lending boom, and provide more resources for investments to allow countries to reduce their financial vulnerability in the future, whilst reducing poverty.

24. Under current rules, loans can be counted as aid if interest rates are 7% or less. Several governments give large proportions of bilateral aid as loans, including Japan, France, Germany and China. These loans have increased in recent years.

25. The UK does not currently give bilateral loans, but it does make large aid contributions to multilateral institutions, which are then given as loans, such as the World Bank and African Development Bank. Jubilee Debt Campaign estimated in 2012 that $1.26 billion of UK aid money was given to multilateral institutions to then be used as loans. This was the second highest amount of any OECD country, after Japan ($2.23 billion).
26. A representative of Agence Française de Développement told a meeting of European NGOs in June 2013 that there is currently a glut of cheap loans that the agency is hard pressed to find projects to fund as they are effectively competing with the Germans and the European Investment Bank to find viable projects.

27. However, despite this lending boom, the International Development Select Committee recommended in February 2014 that more aid should be given as loans, through giving all aid to middle income countries as loans, and some aid to low income countries as loans. These loans on top of the lending boom which is already taking place towards many countries would further exacerbate the risk of new debt crises.

28. Policy recommendation 5: Require all lenders funded by the UK, including UK Export Finance, the World Bank and IMF, to sign up to responsible lending guidelines, including public scrutiny of loan terms before contracts are signed.

29. For lending and borrowing to be more responsible requires greater accountability to people in the countries concerned. One common call of groups we work with in the global South is for all loan contracts to be made publicly available for scrutiny before they are signed, and for contracts to require the agreement of elected parliaments. Lenders can help facilitate this process by making contracts publicly available, and requiring parliamentary approval. However, UK Export Finance for example, does not release any information on loans it guarantees until up-to a year after a deal has been agreed, and then refuses to release details of the contracts.

ii) Increased lending by the private sector

30. Policy recommendation 6: Support the creation of a fair, transparent and independent process for resolving sovereign debt crises, to show banks they won’t be bailed out for reckless loans.

31. Low interest rates and quantitative easing in the Western world are fuelling a private lending bubble to developing countries. Open capital markets mean money can be borrowed at low interest rates in the West, and lent on to developing countries.

32. Furthermore, the current system of responding to debt crises incentivises the private sector to lend recklessly. The IMF and other institutions (such as the EU or World Bank) lend more money to countries in crisis, bailing out the original reckless lenders, whilst leaving the country in debt. When debt relief is finally agreed, for example through the Heavily Indebted Poor Countries initiative, it is the public sector which bears the cost.

33. Instead, a fair and transparent debt workout process, independent of lenders and borrowers, would indicate to lenders that they would have to be involved in debt restructurings. This would incentivise private lenders to be more responsible, thereby reducing the frequency of debt crises, whilst also protecting the public sector from the costs of more bailouts. Creating such a process has been supported in recent years by the G24 group of developing countries at the World Bank, lenders such as Germany, Norway and Switzerland, and borrowers such as Argentina and Grenada.

34. The G77 group of developing countries (which actually consists of 133 developing countries) has unanimously submitted a resolution to the UN General Assembly calling for the creation of a legal regulatory framework for the sovereign debt restructuring process. Due to be voted on 9 September 2014, the UK government may vote against this welcome move because they prefer discussions on debt restructuring to take place in the IMF. However, the IMF has a clear conflict of interest in assessing and arbitrating over sustainable debt levels, as it is a major creditor itself.
35. Policy recommendation 7: Stop PPPs from being a condition of IMF and World Bank loans, and call for an independent review of the impact of PPPs, including on debt sustainability.

36. All the discussion above does not include ‘hidden debts’ often referred to as contingent liabilities. These are financial responsibilities a government does or could have, but which are not included in the official debt figures for that government.

37. One key area is Public Private Partnerships (often known as the Private Finance Initiative in the UK). Rather than the government borrowing money to invest in infrastructure such as a road or hospital, PPPs enable the private sector to borrow the money instead, whilst the government commits to a set level of payments to the private sector. These payments are effectively the same as debt payments, but are not included in debt figures. Moreover, they are likely to be higher than if the government borrowed directly, because the interest rate paid by the private sector is higher, the private borrower demands a (high) rate of profit, and the private sector has consistently negotiated better deals for itself than the government.

38. A recent review of PPPs for the World Bank found that “PPPs are more common where governments suffer from heavy debt burdens … Yet PPPs do not provide additional fiscal space” and that of 442 PPPs supported by the World Bank, assessments of their impact on poverty was conducted for just 9 of them (2%), and of their fiscal impact for just 12 (3%).

39. In Lesotho, Oxfam and the Consumer Protection Association have shown how one health PPP, supported by the World Bank, has led to an increase of 64 per cent in how much the Lesotho government has to spend on the health service. The annual return on investment for the private provider is expected to be 25 per cent every year over the lifetime of the project, whilst rural health services are facing a real terms cut in funding because of the diversion of money to pay for the PPP.

40. There are major concerns about the financial impact of PFI contracts on the UK government through the exorbitant rates of payments the government is now committed to. However, similar contracts are now being exported to developing countries, particularly through IMF and World Bank economic policy conditions.

41. Policy recommendation 8: Remove the gateways and exemptions from the UK’s Controlled Foreign Companies rules which prevent them from deterring tax avoidance and evasion in third countries.

42. Policy recommendation 9: Ensure every tax rule and treaty adopted by the UK government has a spillover analysis to check that it won’t harm developing countries, but rather will actively help them in tackling tax avoidance and evasion.

43. One reason developing country governments are dependent on foreign loans is because of the large quantities of money they lose to tax avoidance and evasion. The OECD has estimated that developing countries lose three times more money to tax havens than they get in overseas aid.

44. As a major financial centre, the UK government has a responsibility to ensure its policies help developing countries receive more of the money due. However, in recent years policies implemented by the UK government have actually made the situation even worse for developing countries. The Controlled Foreign Companies rules have been changed so that they no longer deter tax avoidance by UK companies in third countries. Instead, the rules now offer an incentive to UK companies to maximise their use of offshore financing transactions within their own company, because of a 75% tax break on the profits from these transactions.

45. The negative impacts of the changes to the Controlled Foreign Companies rules indicates that one useful policy would be for there to be a requirement on the UK government to
conducted a spillover analysis that every tax rule and treaty adopted by the government does not harm the ability of developing countries to collect adequate tax revenues, but actively helps them to tackle tax avoidance and evasion.

References

1 The percentage increase was from 51.5 per cent of the population to 59.4 per cent. World Bank. Global Development Finance database.
3 World Bank. World Development Indicators database.
4 World Bank. World Development Indicators database.
5 World Bank. World Development Indicators database.
6 World Bank. World Development Indicators database.
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