Fifty Years Forgetting London

By Eduardo Gudynas | April 10, 2003

The foreign debt in southern countries continues to grow and is once again becoming a major problem. By the end of 2002, the Latin American debt had grown to over $725 billion; the most indebted nations were Brazil ($230 billion), Argentina ($150 billion), and Mexico ($140 billion).

The origin and composition of this debt differs from that accumulated in the eighties, when the last widespread financial crisis hit the region. In contrast to the past, the current debt was contracted by democratic governments and many of those governments applied the development strategies emphatically promoted by the industrialized countries, the World Bank, and the International Monetary Fund. Also, the composition of the debt has diversified. There has been a notable increase in the issuance of bonds and other papers—both by governments and private companies—that are now held by brokers, and investment and pension funds.

Although this heavy debt burden has negative consequences throughout the continent, these have been largely ignored due to the crisis in the Middle East. The most dramatic case is Argentina, where the government took on new debt to pay other debts, unleashing a process that ended in the collapse of the country. Argentina had one of the highest per capita incomes in Latin America, excellent educational levels, and manageable poverty levels. The debt and changes in production were major factors leading to the present situation, in which over half the population lives in poverty, 50% of workers earn approximately $100 a month, and the wealthiest 10% of the population receives nearly 40% of the total income of the country, coming close to Brazil and Chile for the most regressive income distribution on the continent.

The debt burden in Argentina and other Latin American countries is huge; in 2002 the region registered a net transference of resources abroad, largely attributable to the foreign debt. This debt is becoming a serious brake on development.

All attempts at changing the mechanisms for managing foreign debt have failed. Today, wealthy countries, international organizations (the World Bank and the IMF), and private institutions all reject any modification. Words like “moratorium,” “reduction,” or “arbitration” provoke nervousness that is immediately reflected in the markets, regardless of the social situation in the country. The response of these institutions is cause for serious concern when we consider that they have accepted the financial and social collapse of a country as if it were an inevitable consequence of indebtedness. The last-minute bail-outs that happened in Mexico and Turkey did not happen when Ecuador and Argentina declared moratoria on IMF payments.

Creditor nations, international banks, and the IMF have been forgetting that there is another path. It seems nobody remembers the foreign debt agreements of 1953 in London. This lack of memory is unpardonable since those resolutions are exactly what several southern countries are calling for today.

The novel approach in London was designed to solve the debts of the recently created Federal Republic of Germany, including those pending since the First World War and others generated in the Second World War (especially as a result of the Marshall Plan). Estimates from those days indicated a total of nearly 40 billion Marks owed on principal and accumulated interests to the allied powers.

The United States actively promoted the negotiations, and sought to create a solid basis for the German economy in order to avoid political crisis and assure internal stability, permit economic development, and offer fair treatment for both debtors and creditors. Washington still retained some of Germany’s public debts to assure German dependence. France, the United Kingdom, Canada, and a long list of 26 other countries also participated in the negotiations.

The talks lasted a year, and finally on February 27, 1953 the parties signed the “Agreement on the German Foreign Debt” in London. The agreement stipulated a reduction of 50% of the debt.

The attitude of Washington and its allies back then is nearly the complete opposite of today. Today they reject any debt reduction, they are not interested in a country's internal stability, and they did little in the face of the political chaos that took place in Argentina and Ecuador.

In contrast, the London agreement featured many novel approaches. Payments were suspended for five years and reinstated in 1958 at very low interest rates (2.5% for part of the debt, and 4.5 to 5% for the rest), and the agreement established annual payment limits. Today, these kinds of conditions are unheard of.

But London achieved something even more surprising: the agreement recognized that Germany should be able to develop economically and export its products, and indicated that the surplus in foreign trade should be applied to payment of the foreign debt without demanding that the country dip into monetary reserves to pay its debt. Germany was granted facilities to export, and the agreement established a ceiling of 5% of export income for debt payment. If payment did not proceed on schedule, the parties accepted a mechanism of arbitration between Germany and its creditors.

These conditions do not apply today. On the contrary, "free trade" is preached but trade barriers imposed by the United States and the European Union create serious obstacles to export in southern countries. Likewise, both the IMF and the banks have demanded that financial reserves be used to service the debt. Finally, debt payments are completely delinked from export income. I am not exaggerating—both Argentina and Uruguay were forced to use national resources to pay the debt and the cost of debt servicing has at times exceeded 100% of export income.

Our countries have become caught up in a vicious cycle where they cannot export, so their financial resources are scarce, so they are forced to contract new debt. So the foreign debt becomes an eternal fact of existence.

Today many citizens' organizations have demanded mechanisms similar to the London Agreement. They have developed proposals that link the payment of foreign debt to improvements in the international prices of products exported by Latin American countries and to fair access to northern markets. Others postulate the creation of an international tribunal for the arbitration of sovereign debt. Still others demand that payment be conditioned on the state of the national economy.

These demands are very similar to the London Agreement of 1953—a fact many governments have forgotten throughout the past fifty years. It is time to remember.

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