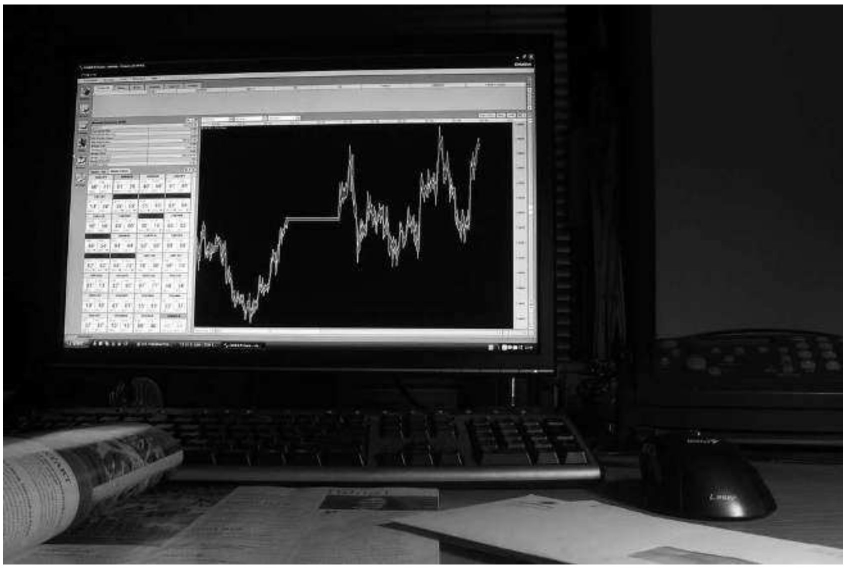
JUBILEE DEBT CAMPAIGN

March 2009 (UPDATED)

The credit crunch and the debt crisis

Another name for a debt crisis?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The "credit crunch," which caused chaos in the international financial markets, and led to the onset of recession in the rest of the world economy, has been explained as a lack of liquidity, or credit, available to banks from the financial markets. Inject these markets with enough liquidity, restore lenders' confidence enough to start lending again, and everything would come right. Hence the trillions of dollars in bail outs of individual banks like RBS and AIG, and pumped into the financial markets as a whole, both here and abroad.

But is that the full story? In fact the problems faced by the banks and the economy have not been so much about a lack of available credit, but a massive over-accumulation of debt. Debt is a sum of money, or other obligation, owed to someone. Taking out a loan – getting into debt – is a means of using future purchasing power in the present. Banks lent to mortgage borrowers, increasingly recklessly. These debts were repackaged and sold on, in ever more complicated "derivatives" which investors themselves mostly did not understand. As it became apparent that these sub-prime debts could not be repaid, international banks and investors found themselves hugely exposed to bad debts and went into free-fall. All that was left was a huge pile of debt. This is a story about a debt crisis, not a credit crunch.

Not only are we witnessing a debt crisis, but it bears a strong resemblance to the debt crisis that poor countries have faced since the early 1980s. As early as August 2008, Andrés Velasco, Chile's finance minister, stated that the credit crunch was "a more modern and a much bigger version of what we have seen in emerging markets over the last couple of decades[1]." In other words, a new form of debt crisis, but this time affecting the rich world too.

A brief history of the (developing world) debt crisis

After the Second World War and the end of most colonial regimes, many countries in Africa, Asia and

Latin America sought their own paths to economic development. Banks sought to lend money to these governments, seeing them as a safe investment.

As the Cold War deepened, governments from both East and West blocs lent increasingly recklessly as they sought to gain political influence. The situation was dramatically intensified by the oil price hikes and currency changes in the 1970s, when cheap money flooded the financial markets and banks lent it on to poor countries without regard for what it was being spent on and whether it could be repaid. The change in economic situation from the late 1970s, with rising interest rates, deflation and falling commodity prices, caught developing countries in a spiralling debt trap.

Since this time, despite many plans to reduce the debt burden, the crisis has continued to engulf countries in the Global South. Today developing countries' debt stocks stand at a staggering $2.9 trillion and every day the poorest countries pay the rich world almost $100 million in debt repayments[2]. Jubilee Debt Campaign estimates that at least $400 billion should be cancelled for around 100 countries if they are to be able to pay for essential services for their people[3], while the remainder needs to be audited so that illegitimate debts – those arising from irresponsible loans – can be written off. In particular, 38 countries, including Bangladesh, Kenya, and Zambia, are particularly vulnerable to the crisis and need a total of $270 billion in debts to be written off to help them weather the storm.

Debt crisis II

Banks have continued to lend recklessly, in recent times in the sub-prime mortgage market, which by its very nature gets people into debt who probably can't afford to repay that debt, and through ever-more intricate financial instruments in which bad debt has been re-packaged and re-sold. We are now all paying the price for the same reckless, irresponsible lending without consequence.

This time poor households in the USA, rather than poor states throughout the developing world, have defaulted on debts and borne the cost of reckless lending by losing their homes.

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Meanwhile ordinary citizens of rich countries including our own are now also bearing the consequences of unregulated financial mismanagement on a grand scale – housing price collapse, spiralling personal debt, the onset of recession, and a huge public debt taken on to rescue the banks who created this problem.

But compare and contrast how developing countries are treated by rich governments to how international banks are being treated – the former told to get their house in order before they receive financial support, and meanwhile left to squander, while the latter are being bailed out by sums incomprehensible to most of us.

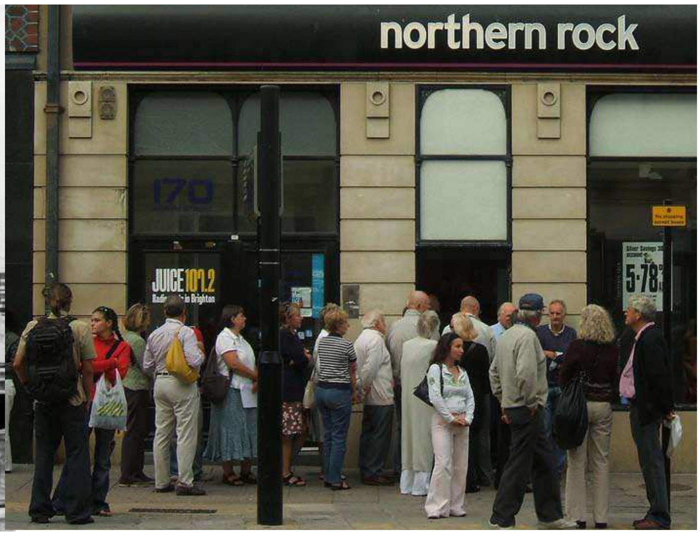
Ignoring the lessons of history

Analysts have been predicting such a crisis for some time. Ann Pettifor, former director of Jubilee 2000, and various thinkers at the New Economics Foundation, for example, have been talking about the coming "first world debt crisis" for several years[4]. If banks, and the wealthy governments that are supposed to oversee their activities, had learnt the lessons of previous debt crises, we might not be seeing such huge problems in the financial markets now. There can be no excuse for our governments presiding over the massive deregulation of finance that has occurred in recent years. Historical experience and warnings of others have been ignored, and now the current debt crisis has come.

Triple whammy for the South

Not only does the financial crisis have striking similarities to the debt crisis in the Global South – it also has a direct impact. The present financial crisis is just one of a number of factors – in addition to the challenges of climate change and food crisis – that have created a "perfect storm" for poverty and suffering in the developing world.

The financial crisis has a direct bearing on the



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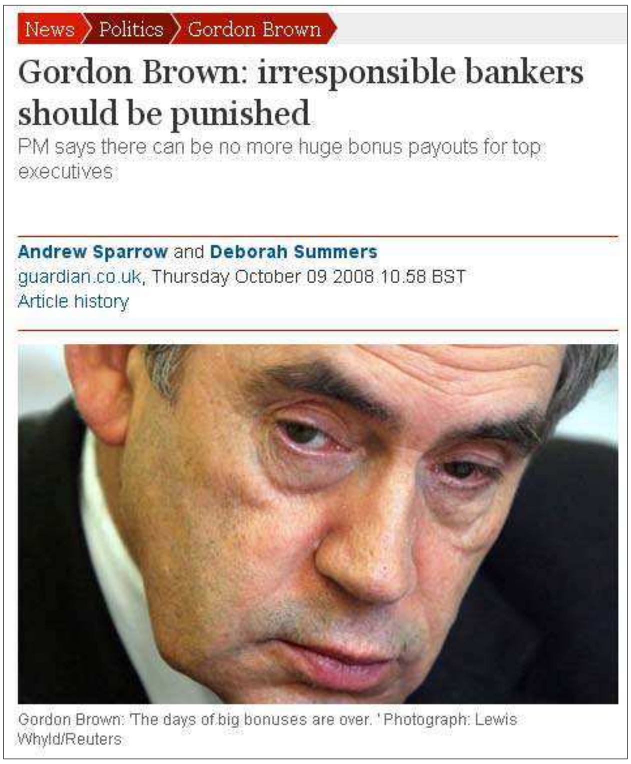
developing world in several ways. The crisis is the result of financial liberalisation that has created a volatile and unstable system, where capital flight and tax evasion are rife. This volatility and the transfer of resources away from poor countries are clearly not conducive to equitable, sustainable development. Yet developing countries have been forced to liberalise their own financial sectors, so becoming ever more vulnerable to this system. Consequences include speculation, resulting for example in soaring commodity prices, and the uneven concentration of capital flows, creating 'blind spots' where private capital will not go, or where capital 'punishes' certain policy choices, forcing many countries into an ever-tighter neo-liberal straightjacket.

Secondly the "credit crunch" has dried up, or made much more expensive, sources of private capital for developing countries. The very banks that lent so recklessly, as they have come under the protection of Western states, have become safe havens for capital, which follows a 'flight to safety' pattern in times of financial crisis. Meanwhile developing countries that have played no part in creating the problem are left to bear the consequences. Yet they are not in any position to inject their own economies with stimulus packages, or to protect their citizens from job losses and poverty. And the huge sums of public money spent on our economies are likely to eat further into existing overseas development budgets, just when the need is greatest.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Gordon Brown: irresponsible bankers should be punished

PM says there can be no more huge bonus payouts for top executives

Andrew Sparrow and Deborah Summers
guardian.co.uk, Thursday October 09 2008 10.58 BST
Article history

Gordon Brown: 'The days of big bonuses are over.' Photograph: Lewis Whyld/Reuters

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The global downturn we are now witnessing is having serious and multiple effects on poor countries. Falling growth, declining markets for exports, instability, and less money available for aid are just some of these. These economic effects will make it harder for some countries to repay their debts. They will simply have less money in the bank to pay out. Important factors in this will include the amount of short-term debts countries owe – for example Sub-Saharan Africa will have around $40 billion up for repayment in the next 12 months. Also how local currencies are faring is critical: where exchange rates fall, repaying dollar-denominated debts will be much harder. As poor countries get into difficulties, they will become more beholden to institutions like the IMF, and their conditions, which have already proven time and again to be disastrous for poor people.

Where do we go from here?

One key difference between this debt crisis and the long-standing developing world one is that there is significant political will to bring about change. Prime Minister Gordon Brown says he is "angry at irresponsible behaviour" of bankers and financiers and that where there has been excessive and irresponsible risk-taking those involved must be "punished". Brown is seeking to lead the world in creating a new financial architecture, largely through his Chairmanship of the G20 summit in London in April. But many countries seem divided as to what the solutions should be.

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Campaigners want to see a new economy that works for people and planet: transformative change that creates decent jobs, tackles global poverty and confronts the threat of climate change.

The scale of the problem and the responses needed should mark a watershed in global economic policy, and it is vital that any such change in direction is targeted towards tackling global poverty. This would include measures to tackle unjust and unpayable debts, to make banks and companies accountable and transparent, close down tax havens, and reform the global financial architecture so that responsible financing is enforced.

The G20 summit is by no means the end of the story. Not only does it take far more than one meeting to resolve this systemic crisis, but there are other, more legitimate processes ongoing. The UN has appointed Nobel Prize winning economist Joseph Stiglitz to head its commission of experts, and their recommendations will form part of the discussions at a UN conference on the financial crisis in June. The G20 itself will have its regular meeting of finance ministers in St Andrews, Scotland, in November.

In addressing the problems faced by developing countries, measures are needed to reverse the current flow of resources from South to North. To give a few examples, developing countries repay on average $456 billion a year in debt service while an estimated $619 billion disappears in illicit capital flight. $130 billion is lost to the developing world every year through multinationals remitting profits back to their home countries. $250 billion vanishes through tax dodging because $11.5 trillion of global assets are currently held in tax havens, like the UK, one of the centres of financial globalisation. The most recent figure of $106 billion in aid to developing countries (in 2006) is dwarfed by these huge sums[5].

Take action

PUT PEOPLE FIRST!

▶ **PUT PEOPLE FIRST:** The UK is chairing the G20 in 2009, and we're working with an unprecendented alliance of organisations – from trade unions to development organisations, environmental networks to faith groups – to demand global action to Put People First. Read our manifesto, and check out our latest campaign activities at: **www.jubileedebtcampaign.org.uk/ppf**

The current crisis provides an opportunity for these issues to come centre stage. Our challenge is to make sure they are tackled and that the murky world of global finance is brought under control.

NOTES

1. Quoted in *Credit crunch 'echoes Latin debt crisis'*, Financial Times, 11 August 2008.
2. All figures from *Global Development Finance*, World Bank, 2008.
3. Calculations based on research by New Economics Foundation, 2007.
4. Ann Pettifor, *The coming first world debt crisis*, openDemocracy Ltd, September 2003, at www.opendemocracy.net/globalization-americanpower/article_1463.jsp.
5. Most figures from Eurodad, except tax figures from Tax Justice Network, and 2006 aid figures from OECD.

JUBILEE DEBT CAMPAIGN

Charity no. 1055675 | Company no. 3201959

Jubilee Debt Campaign works for 100% cancellation of unjust and unpayable poor country debts. We are a UK coalition of around 90 national organisations and nearly 100 local and regional groups, as well as thousands of individuals nationwide.

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