Debt Cycles in the World-Economy

Foreign Loans, Financial Crises, and Debt Settlements, 1820–1990

Christian Suter

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Preface

This book is about the structure and the long-term dynamics of periphery indebtedness. The ideas developed here emanated from a close cooperation with my teachers and my colleagues at the Sociological Institute at the University of Zurich, where the international system has been a major field of research during the past two decades.

The roots of this book go back to the research project *Indebtedness and the World-System* directed by Volker Bornschier and supported by the Swiss National Science Foundation (grant 1.060-0.84) as well as by the World Society Foundation, Zurich. Most of the research for this book was done between 1985 and 1988, and it was originally published in German in 1990 by Anton Hain Publishers (Frankfurt). The German edition is more technical. It contains a detailed data appendix of all the cases of defaults and reschedulings between 1820 and 1986 which constitutes the quantitative basis for most of the analyses in this study. Due to space limitations, however, only a summary table could be included in the English edition.

Without the exceptional support I received from many people, this book would not have been written. In particular I would like to thank Volker Bornschier, Ulrich Pfister, and Hanspeter Stamm, who collaborated on the research project at the Sociological Institute, and Christopher Chase-Dunn, who encouraged me to write this book in English. Ulrich Pfister and Christopher Chase-Dunn also provided many helpful comments and constructive critiques on earlier drafts. I would also like to thank Monica Budowski and Eva Keller, who helped me transform my ideas into readable English, and to Alice Colwell from Westview Press, who corrected and improved the translation. Finally, I am grateful for the technical support I received from Ulrich Pfister, who developed the graphics software used in this book.

Earlier versions of several chapters have been published in the following journals and readers: Parts of Chapter 2, co-authored with Volker Bornschier, appeared in the *Politische Vierteljahresschrift* (1990, special issue 21, pp. 175-197) and in *World Society Studies* (1992, vol. 2, pp. 15-50); an earlier version of Chapter 3, co-authored with Ulrich

Pfister, was published in *International Studies Quarterly* (1987, vol. 31, pp. 239-272); the second section of Chapter 4 first appeared in *Review*, the journal of the Fernand Braudel Center at SUNY-Binghamton (1989, vol. 12, pp. 1-49); and an earlier version of Chapter 6, co-authored with Hanspeter Stamm, is being published in *Comparative Studies in Society and History*. Most of the statistical material presented in Chapters 8 through 10 first appeared in a chapter of the *International Political Economy Yearbook* (1989, vol. 4, pp. 17-55; co-authored with Ulrich Pfister).

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Zurich

Introduction

Periphery Indebtedness in Historical Perspective

In late summer of 1982, when several heavily indebted sovereign borrowers could no longer meet their debt-servicing obligations, the public suddenly became aware of the debt problem of the Third World or the peripheral and semi-peripheral countries.[1] Each year between 1983 and 1989, more than 30 countries were forced to conclude multilateral rescheduling arrangements with their creditors. The management of this global debt crisis became one of the most important issues in North-South relations during the 1980s and 1990s.

Yet, in the history of the capitalist world-economy, present global debt problems do not represent a unique event. During the nineteenth and twentieth centuries, there have been many instances of debt-servicing difficulties among sovereign borrowers. The empirical material presented by this study demonstrates that from 1820 to 1945 more than 130 defaults on external public debt occurred among economically less advanced countries. Moreover, after World War II and until the outbreak of the present debt crisis in 1982, insolvent debtor countries of the Third World have had to conclude 59 multilateral reschedulings with their official and private creditors. In fact, only very few sovereign borrowers successfully paid off their foreign debts during the past 150-200 years -- including several countries of recent settlement (Australia, Canada, South Africa and the United States) or Japan. The more usual outcome of external borrowing has been national bankruptcy lasting for several years or even for decades. This is true for the debt histories of countries belonging to the European periphery (like Greece, Portugal, Spain, and the Balkans), for almost all Latin American states and also of those Asian and African countries which were independent during the nineteenth and twentieth centuries, like the Ottoman Empire, China, or Liberia.

Several peripheral countries repeatedly fell into the debt trap. Between 1820 and 1945, foreign bonds were defaulted on six times by Colombia, Costa Rica, and Venezuela, and seven times by Ecuador and

Mexico. In a statistical sense, debt-servicing incapacity and default were the normal state of financial affairs in several peripheral debtor countries during the nineteenth and twentieth centuries. A striking example of this is Honduras, which was in default for 91 years during the 118-year period from independence (in 1821) until World War II. Other debtors like Ecuador, Greece, or Mexico did not fare much better.

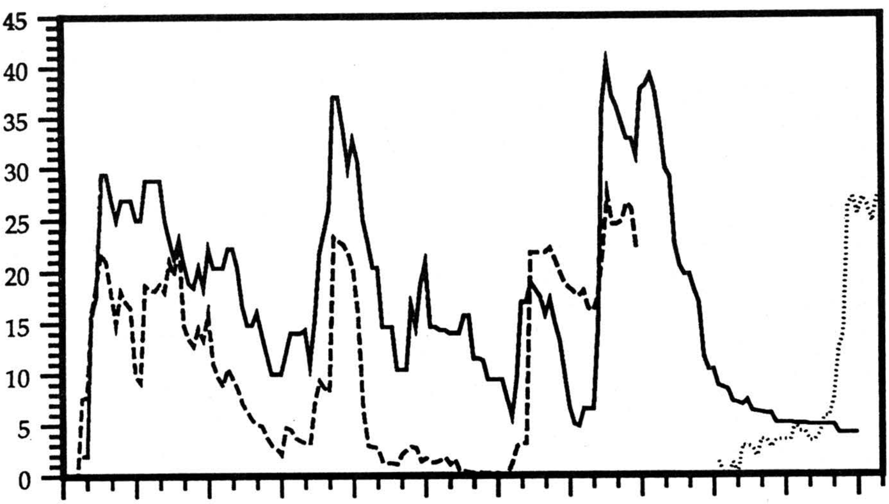
The basic argument of this study is that external debt of peripheral and semi-peripheral states during the nineteenth and twentieth centuries is characterized by cyclical fluctuations. These debt cycles are divided into three interdependent and consecutive phases: (1) the expansion of foreign credits, (2) the outbreak of payment crises and (3) the negotiation of debt-settlement agreements between debtor countries and their creditors. In the course of the nineteenth and twentieth centuries, several debt cycles occurred. Figure I.1 reveals the long-term evolution of global debt crises as indicated by the proportion of countries in default or subject to a rescheduling agreement as a percentage of all sovereign nation-states on the one hand and the share of blocked credits relative to the total accumulated net investment abroad of principal creditor nations on the other.

Together with the present debt crisis, four periods of global debt-servicing incapacity among sovereign borrowers stand out since 1800. Peaks of crises occurred from the late 1820s to the early 1840s, from the mid-1870s to the early 1880s, from the early 1930s to the late 1940s, and from the early 1980s to the present. During these periods of crisis, the number of countries in default or subject to rescheduling agreements relative to the number of all sovereign states amounted to 29 percent (late 1820s), 37 percent (mid-1870s), 40 percent (early 1930s) and 27 percent (mid-1980s). Virtually the same crisis pattern appears with respect to the estimated share of credits blocked in defaults on foreign bonds. The share of blocked credits amounted to 22 percent and 23 percent, respectively, in the late 1820s and mid-1870s, and rose to 27 percent in the early 1930s. Estimates for the present crisis suggest a similar or even higher proportion of frozen assets. In contrast, there were few blocked credits during the 1860s, from the late 1880s to World War I, and during the 1950s and 1960s. In addition to these four major crises, Figure I.1 shows two other less-pronounced debt crises peaking during the mid-1890s and in the years before and during World War I.

These principal debt crises affected various debtor countries: Spain and Greater Colombia (today's Colombia, Ecuador, Panama, and Venezuela) in the 1820s; the Ottoman Empire in the mid-1870s; Argentina and Portugal in the 1890s; Russia, the Ottoman Empire, and Mexico during World War I; Germany, Brazil, and Romania in the 1930s; and Mexico and Brazil in the 1980s. Yet, those countries experiencing debt-servicing incapacities were not necessarily those which borrowed most heavily. Thus, during the 1970s Spain and South Korea belonged to the largest sovereign borrowers but neither faced any debt-servicing difficulties during the 1980s. The same can be said for Naples or Prussia during the crisis of the 1820s or for the federal government of the United States and for Russia with respect to the crisis of the mid-1870s.

A closer inspection of Figure I.1 reveals marked differences in the appearance of debt crises between the nineteenth and the early twentieth centuries on the one hand and the postwar period on the other. Before World War I, debt crises manifested themselves in outright *defaults* on foreign bonds. As a result of such unilateral suspensions of interest or amortization payments by debtor countries, international financial flows generally collapsed, since creditors tended to stop all further lending. An agreement between individual bondholders (gener-

FIGURE I.1 Global Debt Crises: Share of Countries in Default (1820-1985) or Subject to Reschedulings (1956-1989) Relative to All Nation-States and Share of Blocked Credits (1823-1939)



—— Number of countries in default relative to all sovereign nation-states.

········ Number of countries subject to a rescheduling agreement relative to all sovereign nation-states.

- - - Share of blocked credits relative to the total accumulated net investment abroad of principal creditor nations.

Source: cf. Appendix

ally represented by committees) and debtor countries concerning a revision of future debt service usually could only be reached after several years. In contrast, since World War II, defaults have been forestalled by the arrangement of *multilateral rescheduling agreements* which bring debtor countries immediate financial relief by restructuring maturities. Since reschedulings could be arranged prior to the outbreak of state insolvency of debtor countries, international lending did not collapse. The emergence of comprehensive multilateral rescheduling mechanisms took place in the context of increasing cooperation among creditors.

This brief overview of the major historical debt crises suggests three structural features of periphery indebtedness which will be discussed in detail in this study: First and most important, there is a long-term cyclical pattern of debt-servicing difficulties, with major debt crises occurring every 50 to 60 years. I will argue in this study that these global debt cycles are linked to other cyclical processes taking place within the world-economy. Specifically, I argue that debt cycles are related to the course of both Kondratieff growth cycles lasting 45-60 years and Kuznets cycles with 18-25 years' duration. The debt cycles of the nineteenth and twentieth centuries shown in Figure I.1 provide a preliminary illustration of these relationships: The outbreak of global debt crises falls into stagnation phases of the Kondratieff growth cycle for the whole of the nineteenth and twentieth centuries (late 1820s, mid-1870s, early 1930s and early 1980s) and of the Kuznets cycle for the period from about 1860 to 1930 (mid-1870s, mid-1890s, during World War I, early 1930s).

Second, despite the periodic recurrence of global debt crises, each debt cycle shows specific characteristics. During the first half of the nineteenth century, the duration of debt crises seems to be substantially longer than during the 1870s and 1880s. Moreover, during the postwar period, the international financial system became more resistant to an open debt crisis which is visible in the emergence of multilateral reschedulings. The peculiarities of individual debt cycles will be related to the rise and fall of world hegemonic powers and trend movements operating within the international financial system.

Third, on the level of individual debtor countries, there are substantial differences concerning the specific debt pattern. As already mentioned, some countries borrowed heavily abroad but were not confronted with debt-servicing difficulties, while others remained insolvent for decades although their external debt was relatively small. This suggests that certain states and specific national administrations exhibit a different behavior towards external debt, implying that relevant processes are taking place at the level of nation-states as well. Obviously, specific economic and political structures within indebted countries are important in explaining debt patterns.

These three important aspects of the periphery indebtedness problem will be discussed in detail in the following chapters. This study aims at describing and explaining the long-term dynamics of Third World debt during the nineteenth and twentieth centuries. Continuity and change over the whole period will be discussed, with a focus on the various specific historical patterns of debt expansion, crises, and settlements. This is done with the hope that a better knowledge of past experiences may lead to a more profound understanding of the present debt crisis and its possible solutions. Let us now turn to the spatial and temporal boundaries and the thematical limitations of this study.

Some Methodological Considerations: The Spatio-Temporal Framework of the Study

With respect to the spatial dimension, the phenomenon of external debt is located on different levels of the world-system. On the one hand, external debt manifests itself on the *global* level. Debt crises are not confined to individual debtor countries; as suggested by Figure I.1, they have a strong world-systemic component insofar as their aggregate evolution follows a specific pattern. On the other hand, external debt is relevant on the *national* level of individual debtor countries characterized by rather different economic, political, social, and cultural structures. This structural diversity results in different debt careers of individual sovereign borrowers linked to specific causal relationships. If the debt problem is addressed on the global level, the primary interest will be in the general development dynamic of the world-economy as a whole, while a focus on the national level of individual debtor countries will emphasize the specific pattern and the peculiarities of each case. These two perspectives do not exclude each other; rather, they are complementary and, for an adequate description and explanation of complex social reality, both have to be considered. This study, therefore, adopts a multilevel approach to the analysis of external debt, focusing on global as well as on national processes and their mutual relationships.

The temporal framework of this study covers the nineteenth and twentieth centuries. This period is considered a meaningful unit for the analysis of periphery indebtedness for the following theoretical and practical reasons:

First, from the late eighteenth century onwards, the international state system based on the territorial nation-state expanded substantially.[2] Since this study deals with external *public* debt, the formation of the modern nation-state is of primary importance. Yet, the starting point of the analysis is not the American or French revolutions, which were important steps in the shaping of the modern territorial nation-state in the core of the world-system.[3] The formation of the modern territorial nation-state in the periphery is of relevance, and therefore the temporal framework of this study begins with the decolonization movement of the 1820s, which led to the formal political independence of most Latin American countries and Greece.

Second, parallel to the evolution of the territorial nation-state, the breakthrough of the industrial revolution provoked processes of economic growth and economic integration in the core and new forms of an international division of labor between core and periphery. As a result of unequal industrialization and growth processes in different zones of the world-economy, social differentiation and polarization between core and periphery, which was rather modest before about 1800, radically increased from the early nineteenth century onwards. This led to the formation of an international stratification system based on the level of development.[4]

The availability of data is a third and more practical reason for restricting the time period to the nineteenth and twentieth centuries. The sources on which this study is based go back to the early nineteenth century and permit the construction of yearly time series from the 1820s onwards as used in Figure I.1. Since the empirical analysis is the focus of this study, data availability is a crucial aspect.

This general spatio-temporal framework must be further limited by the following three specifications:

First, besides the global and national levels, external debt, of course, also has repercussions on the level of the individual. While the manifestation and the consequences of the present debt crisis on the individual level have been widely discussed in the literature,[5] empirical material referring to earlier debt crises is extremely scarce. Therefore, within the spatio-temporal framework of this analysis, a comprehensive treatment of the debt problem on the individual level is beyond the scope of this study.

Second, since the primary interest of this study is the analysis of the debt problem of the peripheral and semi-peripheral countries, indebtedness of core countries will be mentioned only briefly. This limitation is unproblematic insofar as core countries generally are net capital exporters. Indebtedness of core countries is usually the result of an economic decline, as can be illustrated by the cases of Great Britain (after World War I and II) and of the United States (from the second half of the 1980s onwards). Since the United States became a net debtor only after 1986, these recent developments will not be discussed in this study. A further and more important specification with respect to the countries considered refers to their political status. Only independent nations will be included in the analysis, whereas territories without modern state structures and dependent colonies (with the exception of the virtually sovereign British Dominions like Australia, Canada, New Zealand and South Africa) are excluded.

Third, there are several different forms of indebtedness. The focus of this study is on *external* (not domestic) and on *public* (not private) debt. The most important actors on the debtors' side are the national administrations of developing countries. The principal reason for this limitation is the availability of data. Furthermore, the amount of private, not officially guaranteed, external debt is rather small in Third World countries, so this restriction is actually irrelevant. Another segment of international financial flows between core and periphery not considered in this study is foreign direct investment. Since it includes complete control and property rights of capital owners over the respective investment, foreign direct investment is not a debt obligation in a strict sense. A final aspect which remains outside the scope of the subsequent analysis is forced capital transfers, as in the case of compensation payments due to war losses.

The plan of this study is based on the methodological considerations set forth by the spatio-temporal framework. Part One develops a conceptual framework for the analysis of periphery indebtedness based on world-system theory. The starting point for the discussion is an overview of the various theoretical concepts related to the phenomenon of external debt (Chapter 1). Chapter 2 deals with underlying structural features and long-term processes of the world-system, focusing specifically on cyclical processes. Chapter 3 develops a model describing and explaining the dynamic of global debt cycles within the context of world-system structures and dynamics and summarizes the basic hypotheses relevant to the discussion of the empirical material presented in Part Two and Part Three. Part Two sets forth empirical evidence with data aggregated on the global level, using cross-national research designs. The three chapters of this part refer to the three successive phases of global debt cycles: Chapter 4 examines general phases of expansion of foreign credits, Chapter 5 discusses the cyclical occurrence of global debt crises, and Chapter 6 looks at the pattern of debt settlements. Part Three analyzes the debt problem on the level of individual countries. Chapter 7 first deals with the methodological consideration for the selection of the country case studies and outlines a typology of political regimes. The subsequent chapters of this part contain the debt histories of Peru (Chapter 8), Liberia (Chapter 9), and the Ottoman Empire (Chapter 10). The implications of the country case studies for the general dynamic of global debt cycles and the prospects for a solution of the present debt crisis are discussed in the Conclusion.

Notes

1. The terms "Third World", "developing" or "less-developed" countries and "periphery and semi-periphery" are different concepts for the characterization of economically less advanced and less powerful regions within the world-economy based on differing theoretical traditions. Throughout this study I prefer the "core/semi-periphery/periphery" terminology as developed within dependency and world-system theories since it focuses on the structural dimension, i.e. the stratification of the world-economy into different powerful zones. The "core/periphery" terminology will be elaborated in more detail in Chapter 2 (cf. also Horowitz 1966 and Worsley 1984 for a discussion of the terms "Third World" and "developing countries").
2. Cf. Braudel (1979), Thomas and Meyer (1984).
3. See Bornschier (1988).
4. Cf. Heintz (1973, 1982), Bairoch (1981).
5. Cf. Altvater et al. (1987), George (1987).

PART ONE

Periphery Indebtedness in the World-Economy

The following three chapters discuss the theoretical framework adopted by this study and develop the basic arguments. Chapter 1 reviews the various theoretical concepts dealing with periphery indebtedness and the problem of debt-service incapacity. It will be argued that the different theoretical concepts that can be found in the literature are largely unrelated and mostly limited to specific contexts. An integration of these concepts into the broader spatio-temporal framework adopted by this study is attempted in Chapters 2 and 3 by using a world-system perspective as a conceptual tool with a focus on long-term cyclical fluctuations. Chapter 2, consequently, discusses the underlying structures and dynamics that characterized the world-economy during the nineteenth and twentieth centuries, whereas Chapter 3 puts the phenomenon of periphery indebtedness into the context of the general world-system structures and dynamics and develops the basic hypotheses which will be examined in the empirical parts of this study.

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External Debt of Sovereign Borrowers: Seven Approaches

There are many different but mostly unrelated theoretical concepts in the literature dealing with external indebtedness and the problem of debt-servicing difficulties of sovereign borrowers within the spatio-temporal framework adopted by this study. This heterogeneity has to be attributed to the fact that most approaches are limited to rather short time periods, specific geographical areas or singular events. Obviously, the majority of concepts are concerned with those temporal and spatial contexts where external indebtedness had become an important and problematic issue of international relations. In the past 150 years such problem areas have been the massive international capital movements prior to World War I between Great Britain and other European core countries on the one hand and countries of recent settlement on the other, the debate around the German transfer problem concerning the reparation payments after World War I, the international financial crisis of the 1930s, international development financing for the economically less advanced countries during the 1960s and 1970s, and, of course, the debt crisis of the Third World during the early 1980s and the problem of implementing adequate structural adjustment processes.

The principal shortcoming of the theoretical concepts dealing with these topics for an analysis of long-term developments of external indebtedness is their limitation to specific contexts and the lack of reference to other similar situations. Thus, studies dealing with the debt crisis of the 1980s usually choose the mid-1970s as the starting point of their discussion. Similarly, for most historical analyses concerned with international capital movements around the turn of the century, the outbreak of World War I represents a magical limit. As a consequence, there are various specific but rather fragmented approaches, whereas a comprehensive theoretical treatment of external indebtedness in the global political economy during the period of industrial capitalism of the nineteenth and twentieth centuries is still lacking. It is no accident that those studies oriented towards a broader spatio-temporal discussion are mostly descriptive and narrative and do not attempt to develop a coherent theoretical framework.[1] An exception in this respect worth mentioning is the literature dealing with the historical dimension of debt and financial crises.[2] Yet, even with respect to financial crises -- which represent only one aspect of indebtedness -- no general theory exists.[3]

In the following the various theoretical strands dealing with external debt of sovereign borrowers will be outlined. Since an in-depth analysis of these theoretical concepts is beyond the scope of this study, only the principal arguments will be described. A more detailed discussion of the theoretical reasoning of the relevant approaches is offered in the following chapters. Against the background of the above-mentioned major issue and problem areas discussed in the literature, seven broad theoretical strands can be distinguished:

1. A first group of theoretical approaches refers to the classic Marxist imperialism theories dealing with the massive flow of capital exports from the economically most advanced core countries to peripheral areas during the decades prior to World War I. This analysis has been made against the background of a general theory of the political economy of capitalism. The rise of international capital exports (and of exports of goods and services) is explained by the limits of the internal markets of advanced economies which were considered to be too narrow to absorb expanding industrial production and to guarantee the accumulation of capital. Hobson (1902) argues that capital exports are a symptom of a wrong development path of capitalism caused by the uneven distribution of domestic spending power. Hilferding (1910) and Lenin (1917, 1965), by contrast, consider capital exports to be closely linked to the development dynamic of monopoly and financial capitalism. According to Lenin, capital exports to economically less advanced countries are due to the lack of profitable investment opportunities in the most advanced economies. Low wages, low prices of land and raw materials promise high yields on investments in less-developed areas. Capital exports are thus interpreted as a means to overcome accumulation crises of core countries. The reasoning of Luxemburg (1913), Sternberg (1926) and Grossmann (1929) is similar, although Rosa Luxemburg's focus is more on exports of goods than of capital. A slightly different line of argument is followed by Bucharin (1926), who considers exports of capital to be caused by differing rates of profits among countries rather than by structural limits of capital accumulation.

2. A second school which has its roots in the classic liberal theory of international trade deals with external indebtedness from the

perspective of international capital movements. Like the Marxist imperialism theories, these approaches are concerned with the international capital movements of the late nineteenth and the early twentieth centuries. In contrast to the former's focus on the dynamics and problems of capital accumulation within core countries and the whole world-economy, these emphasize the dyadic relationship between capital-exporting and capital-importing countries. Capital flows between two countries are analyzed with reference to differences concerning interest rates and to the implications of these flows on exchange rates.[4]

3. Associated with the theoretical tradition of the classic liberal model of international capital movements, several historical studies emerged during the 1950s and 1960s focusing on the long-term cyclical dynamic of international capital movements prior to World War I. Influenced by the concept of Kuznets cycles, long swings in international capital movements were related to fluctuations in international trade, international migration movements and differences in the level of construction activities between creditor and debtor countries. In this context the theory of an Atlantic economy characterized by inversely related Kuznets cycles between Great Britain as creditor nation on the one hand and countries of recent settlement (e.g., the United States, Canada, Australia, Argentina, and New Zealand) as debtors on the other was developed.[5] Since these approaches explicitly deal with long cyclical processes, they are of special interest for this study, and their arguments will be discussed in more detail in Chapter 2.

4. A fourth group of approaches which also has roots in the classic liberal theory of international capital movements treats external indebtedness in the context of a theory of economic development. Accordingly, these concepts focus on the development problem of economically less advanced countries during the postwar period. International and national development agencies, as for instance the World Bank, played an important role in the formulation of the model which focuses on the relationships between capital imports and economic growth. According to the basic argument, higher levels of economic growth and a consequent improvement of the general standard of living can be achieved through the mobilization of external financial resources. The most important specification of this argument has been developed in the so-called gap theories aiming at determining the amount of foreign capital required for the initiation of growth processes. The two most important capital gaps specified are the gap between planned investments and expected savings (i.e. the investment-savings gap) and the gap between export and imports (i.e. the foreign exchange gap).[6] Another aspect treated in this context is the assessment of the future

debt-servicing capacity of sovereign borrowers. Conditions permitting the repayment of external debt in the long run and concepts for determining optimal borrowing have been analyzed.[7]

5. There is a large body of literature dealing with the problem of debt crises and their solution. On the one hand, the rising number of Third World countries forced to negotiate multilateral reschedulings during the 1970s and 1980s has stimulated the development of "early warning systems" assessing default and rescheduling probabilities of individual debtor countries for creditors engaged in the international loan business.[8] On the other hand, there are many studies dealing with specific historical debt crises or debt-service incapacities of individual debtor countries.[9] In contrast to the historical approaches dealing with the Atlantic economy (i.e. the third theoretical group mentioned above), their focus is on financial crises rather than on cyclical fluctuations of international capital flows and migration movements taking place within a specific spatio-temporal framework (i.e. the Atlantic economy). While most of this literature is rather descriptive and confined to specific cases, Minsky (1977, 1986) and Kindleberger (1978) developed a more general perspective that focuses on different types of financial behavior of investors. They argue that during loan boom periods investors increasingly turn to more speculative modes of financial behavior. This leads to a crisis-prone structure of the financial system (i.e. systemic fragility) eventually culminating in the outbreak of an open crisis. Important recent contributions to the historical analysis of debt crisis are the studies in the volume of Eichengreen and Lindert (1989) and Marichal's (1989) examination of Latin American debt crises, which is as yet the most comprehensive treatment of Third World indebtedness in the long run. For the explanation of the dynamics of recurrent stages of loan booms and debt crises of Latin American countries, Marichal also considers long economic cycles taking place in the more-advanced core countries. Unfortunately, the specific nature of these relationships is not explored in detail, leaving unanswered the important question of how specific economic cycles are connected with particular stages of periphery indebtedness.

6. Provoked by the debt crisis of the 1980s, a group of theoretical approaches dealing with the issue of adjustment policies required to meet debt crisis of Third World countries developed.[10] Unfavorable developments within the world-economy (e.g. high real interest rates, high oil prices, economic stagnation) on the one hand and poor economic policies or simply bad management by debtor countries on the other are considered the main reasons for the outbreak of the debt crisis of the early 1980s, whereas longer-term structural processes are not taken into account. This can partly be explained by the fact that the

development of this literature has been influenced by the need of the International Monetary Fund (IMF) to establish a theoretical framework for the formulation of adequate adjustment policies for debtor countries.

7. A last group of studies treats the problem of external debt within the framework of the international political economy.[11] Most of these studies discuss the phenomenon of periphery indebtedness in the context of a general theory of development and underdevelopment. A prominent theoretical perspective used in this respect is the "dependency approach" rooted in the classic Marxist imperialism theories. It emphasizes the dependent integration of Third World debtor countries as peripheries into the world-economy and their lack of an autonomous development dynamic. From such a perspective external indebtedness is part of the dependency relationship between economically advanced core countries and the Third World. Accordingly, the effects of capital imports and external debt on long-term growth and development of peripheral economies are predominantly judged negatively. In this respect these concepts are rather contradictory to the developmentalist-oriented approaches of the fourth group.

These seven basic approaches to periphery indebtedness, diverse as they may appear, are not irreconcilable. Rather, they represent differing perspectives due to the specific issue and problem areas they deal with and the consequent limitation of the respective spatio-temporal frameworks. This study aims at providing a general theoretical framework for an integration of these different concepts. For this purpose the next chapter offers a world-system perspective with a focus on long-term cyclical processes.

Notes

1. Examples are Wynne (1951b), Rippy (1959), North (1962), United Nations (1966).

2. See notably Kindleberger (1978).

3. The single most important recent study is that of Marichal (1989) dealing with debt crises of Latin American countries from the early nineteenth century until World War II.

4. The classic theory of international capital movements has been developed by Nurske (1935, 1961) and Iversen (1936). Early studies largely carried out within the framework of the classic theory of international trade are those of Williams (1920) on Argentina and of Viner (1924) on Canadian capital imports. For a more detailed review of theories of international capital movements, see Grubel (1982).

5. The pioneering works are the studies of Cairncross (1953) and Thomas (1954); see also Williamson (1964), Bloomfield (1968), Hall (1968), Ford (1971) and Edelstein (1982).

6. The basic formal model has been developed by Chenery and Strout (1966); see also Agarwala and Singh (1958) and Meier (1970) for a collection of the most important contributions to this concept.

7. Cf. the pioneering study of Avramovic (1964) and Bardhan (1967). More recent studies partly based on this approach also consider the possibility of default in analyzing optimal borrowing (cf. Eaton and Gersovitz 1981, Sachs 1984).

8. See Feder and Just (1977), Eaton and Gersovitz (1981), Sachs (1982) and Eichengreen and Portes (1986) for important contributions to these concepts. A detailed survey on this literature is provided by McDonald (1982) and Saini and Bates (1984).

9. See for example Landes (1958), Bazant (1968), Kindleberger (1978), Thobie (1980), Kindleberger and Laffargue (1982), Lipson (1985, 1989), Eichengreen and Portes (1986, 1989), Fishlow (1986, 1989), Pamuk (1987), Stallings (1987).

10. See for example Cline and Weintraub (1981), Williamson (1982), Cline (1984), Killick (1984).

11. See Payer (1974), Aronson (1978), Frieden (1981), Sánchez Arnau (1982), Stallings (1982), Moffitt (1983), Padoan (1986), Rothgeb (1984, 1986), Pfister and Suter (1987), George (1987), Kowalewski (1989), Stallings and Kaufman (1989), Suter (1989).

2

Structural Features and Long-Term Processes of the World-System

This chapter deals with structures and long-term dynamics that characterized the world-economy during the nineteenth and twentieth centuries. This will be done by using the theoretical framework of the world-system perspective which developed during the 1970s and has its roots in both classic Marxist imperialism theories and dependency theory. There is no unique school of thought, but rather several versions relying on different traditions which use, however, a common methodology emphasizing the systemic nature of global processes.[1]

What follows is, first, a short sketch of the most important structural features of the modern world-system. Subsequently, cyclical processes and trend movements are discussed. Since this study examines chiefly cyclical aspects of external indebtedness, the main emphasis will be on cycles.

World-System Structures

According to Immanuel Wallerstein (1974, 1980, 1988), who formulated one of the most influential versions of the world-system perspective, the modern world-system is a capitalist world-economy characterized by a single division of labor without an encompassing political order and with no common cultural system. Accordingly, the various parts of the world-economy are chiefly connected by economic networks. Another type of world-system mentioned by Wallerstein is the world-empire characterized by a central state authority and multiple cultural structures. The basic mode of integration of world-empires rests on political rather than economic mechanisms (i.e. the existence of a strong state apparatus). The best-known previous world-systems are world-empires (e.g. the Roman Empire or the Ottoman Empire), but there are also ancient world-economies (e.g. the Sumerian).[2] Social systems which are culturally integrated are called mini-systems by Wallerstein because he considers them to be confined to small and simple societies (such as hunters and gatherers). Yet, according to several authors, the post-World War II world-system has also experienced global processes of cultural integration (e.g. the institutionalization of human rights and of international law, or the emergence of global cultural values such as economic development, income and mass education) and shows first signs of a normatively integrated world-society.[3]

There is no consensus among the different approaches concerning the precise date of origin of the modern world-system.[4] Moreover, it is rather difficult to ascertain the precise boundaries of the capitalist world-economy during early modern times. There is widespread agreement in the literature, however, that at the beginning of the nineteenth century, i.e. at the starting point of this study, the European world-economy was firmly established and expanded to cover the whole globe.

According to the world-system perspective, the deep structure of the modern world-economy is capitalist. The capitalist mode of production is defined as the production of commodities for sale on competitive markets with the aim of profit maximization. Commodity production is based on commodified labor and implies a specific class relationship between capitalists (i.e. the owners of the means of production) and labor. As stressed by Chase-Dunn (1989), the world-system perspective considers the control of the means of production not confined to individual capitalists. Rather, means of production may be controlled by organizations or even whole states. Similarly, commodified labor includes not only wage labor (as contended by classical Marxist theory) but also various forms of coerced labor (as for example slave labor in plantation economies producing for the world-market).

The world-system perspective has elaborated upon the classical Marxist conception of global capitalist accumulation in two important respects: First, following dependency theory the world-economy is considered to be hierarchically structured into dominant zones, i.e. core states, and dependent and dominated areas, i.e. the periphery. In addition, there is an intermediate zone consisting of so-called semi-peripheral countries.[5] Core and periphery occupy different positions within the international division of labor. Their interaction is considered a class relationship characterized by an unequal exchange and surplus transfers from the periphery to the core. Basically, core areas produce with capital-intensive technologies and skilled and highly paid wage labor, whereas production in peripheral regions is based on labor-intensive technologies and unskilled, low-paid and often coerced labor. The semi-peripheral zone is characterized by a mix of core and periphery modes of production.[6] The core-periphery hierarchy manifests itself in the level of development of the different zones. Core countries are the economically most advanced or highly "developed" areas, while peripheries belong to the "less-developed" countries or, according to post-World War II terminology, to the "Third World." Although there is a certain social mobility of individual countries between different zones[7], the core-periphery hierarchy is the basic and most important structural constant of the world-economy.

Second, on the political level the capitalist world-economy consists of a system of autonomous but unequally powerful nation-states. From the beginnings of the capitalist world-economy onwards, the structure of the international state system has been characterized by the rise and fall of hegemonic core states. Since this structural feature is associated with cyclical fluctuations, it will be discussed in more detail in the following section dealing with world-system dynamics.

World-System Dynamics: Cycles

Within the extensive literature on cyclical processes operating within the world-economy, various and often unclear notions may be found about what is to be understood by a cycle. Modelski (1978: 214), for example, defines the concept of cycles very generally as "a recurrent pattern in the life (or functioning) of a system." Rostow (1978) refers to trend periods in the sense of alternating upswings and downswings. Kleinknecht (1981: 107) understands cyclical movements to be "the regular recurrence of a constant conditional or causal complex within a historical period." Mensch's (1975) concept of the "metamorphosis model," like Bornschier's (1988) successive societal models, emphasizes the specific novelty in each cycle, adding thus an evolutionary or trend component to the recurrent aspect.

All these notions of cycles, however, are finally based upon the concepts of structural cycles, temporal cycles, or a combination of these. The concept of the *structural cycle* asserts that certain, distinct events succeed each other regularly and recur without interruption. Timing plays no part in structural cycles. The various events can be spread in any way over time without affecting the cyclical character. Only succession without interruption or intervening episodes is the essential condition, not any regular phasing over time. A *temporal cycle* is quite a different matter: it is defined by the recurrence of an event at regular time intervals. Basically, I would argue that within social science all cyclical phenomena have to be considered as structural cycles since social, political and economic reality is much too complex and the delimitation of the respective cyclical phenomena is too unstable for any simple temporal cycle to be identified.[8] Hence, all cyclical processes discussed in this study are explicitly considered structural cycles.

The literature treats numerous varieties of cycles. Schumpeter (1939) distinguishes three sorts in his famous work on economic development and business cycles: the *Kitchin cycle* lasting three and a half years, the *Juglar cycle* lasting 8-10 years and the *Kondratieff cycle* lasting 45-60 years. Simon Kuznets (1930) pointed to cycles of 18 to 25 years' duration which later became known as *Kuznets cycles*. Apart from these mainly economically grounded cycles one must also mention the approximately century-long world political *hegemonic or leadership cycle* of the rise and fall of world powers.

Since this study focuses on long-term structural processes on the global level of the world-economy, the short-term Kitchin and Juglar cycles operating mainly within national economies will not be considered further. Rather, the following discussion is devoted to Kuznets, Kondratieff and world leadership cycles which have specifically been formulated as processes taking place within the international political economy

Kondratieff Cycles

Kondratieff cycles, or long waves, relate to the cyclical pattern of long-term economic growth. There is general agreement among cycle researchers that four cycles of the Kondratieff type have occurred since the industrial revolution in the late eighteenth century. Their high points and reversals were marked by the economic crisis of 1825, the stock exchange collapse of 1873, Black Friday of 1929 and the global economic recession starting in 1973-1975. Table 2.1 presents the periodization of the upswing and downswing phases of Kondratieff growth cycles as suggested by Van Duijn (1983).[9]

TABLE 2.1 Periodization of Kondratieff Growth Cycles

Number of Kondratieff Wave	*I*	*II*	*III*	*IV*
Upswing Phase	1782-1825	1845-1872	1892-1913 1920-1929	1948-1973
Downswing Phase	1825-1845	1872-1892	1929-1948	1973-

Source: Van Duijn (1983: 143, 155-156, 167).

Initially, Kondratieff waves were identified mainly in price series. Various authors, therefore, argue that Kondratieff cycles are purely a price phenomenon and cannot be observed in other domains. This critique of Kondratieff and Schumpeter was already formulated by Kuznets (1940) and Garvy (1943). Forty years later Eklund (1980) in a survey article repeated this old objection. And in fact, while Kondratieff waves in price series have been confirmed in numerous studies undertaken with various methods,[10] empirical evidence for the existence of Kondratieff waves in real production is contradictory. Several authors who have calculated the growth rate of industrial production in some core countries both in upswing and in downswing phases after around 1850 have been able to confirm fluctuations of the Kondratieff cycle type at the global level of the world-economy but not for all individual countries.[11] Other authors, like Van der Zwan (1980), Van Ewijk (1982) and Solomou (1986), were unable to confirm the existence of Kondratieff waves in product series. However, these studies suffer from serious methodological shortcomings.[12] In the past few years fresh work has appeared which examines the existence of Kondratieff cycles in the domain of real economic activity with new methods.[13] Goldstein (1988) analyzes ten production variables estimating the growth of industrial production and gross national product (GNP) in upswing and downswing phases with regression techniques. Kondratieff cycles showed up most clearly at the global level.[14] Gerster (1988), working with a new filtering process, detected long waves of 20 to 60 years through 130 different time series involving 16 Western countries. For product cycles in particular, however, his empirical evidence points to the existence of Kuznets cycles rather than Kondratieff waves.

The various long-wave theories relating to Kondratieff cycles can be classified into economic approaches on the one hand and socio-cultural, political and socio-economic theories on the other. The former are the dominant models and consist mainly of innovation theories relating long waves to the clustering of innovation,[15] capital accumulation theories considering changes in capital accumulation as the causal dynamic[16] and Rostow's terms-of-trade approach explaining cyclical movements through shifts in the relative prices of agricultural and mineral raw materials and industrial products.[17] The socio-cultural, political and socio-economic approaches stress factors like employment and social innovations,[18] the social and political structure of accumulation,[19] inter- and intranational inequality,[20] social movements, political and social conflict,[21] cycles of international and great-power wars[22] and changes in cultural values and cognitive codes.[23] A detailed discussion of these different and partly contradictory theoretical approaches and schools is beyond the scope of this study. Rather, the following sketch of long-wave theories will concentrate on the basic economic approaches since they are most closely related to the topic of this study.[24]

Innovation Theories. Innovation approaches are rooted in Schumpeter's (1939) work about the world economic crisis of the 1930s. They consider the intermittent appearance of technological innovations as the central explanation of long-term alternation between phases of economic boom and depression. The most prominent contemporary representative of innovation theory is Gerhard Mensch, on whose work -- though often criticized -- the following discussion is mainly based.

Mensch (1975) distinguished different types of innovations. *Basic* innovations represent commercial applications of scientific inventions which occasion fundamental changes in productive structures and functions. They thus lead to the emergence of new leading sectors and new market potentials. In each depression phase a bunch of such basic innovations appears, starting a fresh cycle. Under the pressures of competition, production processes in the leading sectors are transformed and ultimately standardized through so-called *improvement* innovations. This movement towards standardized and rationalized production for mass markets leads to a concentration of production in ever greater units of ever fewer number with tendencies towards oligopolisitic market strategies. After a certain lapse of time, demand for the goods produced by the leading sectors becomes saturated. But the oligopolistic firms miss the opportunities to introduce new basic innovations and attempt instead to maintain or increase their profit margins and market shares through so-called *sham* innovations, i.e. product renewals lacking any real technical innovation and improvement but allowing higher prices all the same. The nature of these innovations is such that the increased profits sought from them are inflationary in their effect and therefore only temporary. At the macro-economic level this leads to a stagflationary phase. Only when this strategy is no longer possible and a persistent depression sets in, which Mensch calls a technological stalemate, are entrepreneurs forced to introduce new basic innovations, which subsequently lead to a new cycle.[25]

Capital Accumulation Theories or Profit Rate Cycles. The most prominent advocate of capital accumulation theories is Ernest Mandel (1980), who considers the Marxist approach to the explanation of long waves to be essentially a theory of "long waves in the average rate of profit." An economic upswing is, in his view, occasioned by a sudden rise in the rate of profit, while on the other hand the downswing of a Kondratieff cycle is connected with a long-term decline therein. In Marxist theory, the main determinants of profit rates are the organic composition of capital,[26] the surplus rate and the velocity of capital circulation. Thus, the profit rate rises when the organic composition of capital is lowered and/or the surplus rates and the velocity of circulation of capital rise. A decline of profit rates (enhancement of the organic composition of capital, stagnant surplus rates and a slowing down in the velocity of capital circulation) implies excessive capital accumulation, which means that it becomes impossible to find investment opportunities promising adequate profit returns. While the passage from an upswing to a downswing phase is linked to the dynamics of capitalist accumulation (law of declining profit rates), Mandel sees the beginning in a rise of the profit rate as determined by exogenous factors.[27]

Terms-of-Trade Approaches. Unlike the other long-wave theories presented above, Rostow's (1975, 1978, 1985) terms-of-trade approach deals explicitly with price cycles. Upswing and downswing phases of long waves are defined as cyclical fluctuations in the relative prices of agricultural and mineral raw materials and finished goods. Rostow attempts to connect these terms-of-trade cycles with two other wavelike processes: the sequences of major technological innovations and the domestic and international flow of migration connected with cyclical fluctuations of economic growth. The upswing of a cycle is marked by rising prices of raw materials, a rapid expansion of agricultural production, high interest rates and a distribution of income which favors the agricultural sector and profits in comparison to real urban wages. The downswing, by way of contrast, witnesses falling prices of raw materials, low interest rates and a distribution of income favoring urban wage earners. Because of the low prices of raw materials during downswings, the prevailing leading sectors can expand more rapidly and with fewer constraints during this phase.[28] Rostow explains the rise in the relative prices of primary products through greater demand pressures on raw materials, occasioned on the one hand by expanded aggregate demand[29] and on the other hand through diminished supply. The downswing of a cycle is caused by tendencies towards sector-specific excess investment and production occasioned by the temporal lags inherent in the investment process[30] and by "follow-the-leader" behavior of investors. The price movements analyzed by Rostow finally reflect cycles of relative shortage (upswing) and glut (downswing) of raw materials. A specific investment pattern is closely linked to the movement of relative prices: rising prices for agricultural products and minerals channel investment capital towards the raw material sectors.

The three long-wave theories discussed above each imply specific statements and assumptions related to processes within the international financial system. Rostow in his terms-of-trade approach links changes in relative prices to international capital movements. Increasing profitability and high prices of agricultural and mineral raw materials give rise to surges of capital exports from economically advanced industrial countries to primary producers of the periphery. Foreign investment, according to this view, is mainly determined by favorable conditions in borrowing countries, i.e. by pull factors. Conversely, Mensch and Mandel relate capital outflows from core countries to deteriorating domestic investment opportunities, i.e. to push factors. According to the innovation approach of Mensch, the technological stalemate is characterized by a shift from productive investment to investments in financial assets due to the exhaustion of the innovating potential. Similarly, Mandel understands capital exports to backward areas as the principal instrument to slow down the long-term decline of the profit rate -- an argument already developed by Marx and elaborated to the key thesis of Marxist imperialism theories by Hilferding and Lenin.

Kuznets Cycles

The existence of long swings with a length of 15-25 years was first mentioned by Kuznets (1930) and Burns (1934). During the 1950s and 1960s a considerable body of statistical material on this topic was compiled by different authors.[31] Kuznets cycles relate primarily to long swings in building investments. Accordingly, periods of rapid growth in residential and nonresidential building are followed by phases of relatively depressed construction activities. The rhythm of these cycles has been mainly explained by intra- and international factor movements, i.e. by migration of labor and capital. In the context of the present study, the most important specification of such an explanation of Kuznets cycles is based on the notion of an Atlantic economy characterized by inversely related Kuznets cycles of Great Britain on the one hand and countries of recent settlement (e.g. the United States, Canada, Australia, Argentina, New Zealand) on the other hand.

TABLE 2.2 Periodization of U.S. and British Kuznets Cycles

U.S.[a]	Peak	1818 1836 1853 1871 1892 1912 1927 1941 1959 1972
	Trough	1822 1843 1861 1878 1898 1918 1933 1944 1960 1975
British[b]	Peak	1865 1876 1903 1930 1938
	Trough	1857 1869 1887 1916 1932 1944

[a]For 1818-1822: steamboat tonnage built on western rivers according to Williamson (1964: 74); for 1836-1853: Riggleman building index according to Thomas (1954: 298); for 1861-1975: adapted from Van Duijn (1983: 16).

[b]Domestic fixed capital investment derived from Feinstein (1972: T88).

According to Thomas (1968, 1972), there is a pattern of inversely related cycles between potential creditor countries (e.g. Great Britain) and debtor nations (e.g. the United States), as visible in Table 2.2. This pattern starts with a large outflow of population from the developed creditor country to the less-developed and underpopulated debtor country. Population growth in the New World leads to increasing investments in house building and infrastructure and thus provides a stimulus for other domestic investments, whereas demand for construction is reduced in countries of net emigration. The building boom in the New World attracts more labor and capital from abroad and induces an export boom in the European creditor countries. Eventually the construction boom reaches its ceiling. Due to overinvestment, profits fall and European investors turn to the more profitable and secure domestic investments. The consequences are depression in the New World and decreased immigration. The debtor country experiences a shift from home construction to increased activity in the export sector built up in the previous period by the large infrastructure investments.

This theory of the Atlantic economy has been criticized by Habakkuk (1968), who argues that British building cycles are primarily determined by domestic factors, a view that has been confirmed by empirical evidence presented by Edelstein (1982: 231). Furthermore, Kuznets cycles seem to be limited in space and time. This holds especially true for the narrow understanding of Kuznets cycles as long swings in migration, house building, and railroad construction. From this point of view, Kuznets cycles apply to immigration countries, such as the United States, Canada, Australia, and Argentina, and are most clearly visible during the time period of 1840-1914. Before 1840 and after the First World War there is, by contrast, only little evidence for the existence of Kuznets cycles. Reexamining Kuznets cycles for the U.S. economy, Abramovitz (1968) specifies the conditions for the occurrence of long swings of the Kuznets type. He argues that the basic forces are the substantial immigration movements determining population, labor force, and hence waves in house building. Further conditions relate to territorial expansion processes based on railway construction and the insignificant role of state activities. This characterization of an economic structure producing Kuznets cycles largely corresponds to the concept of extensive capital accumulation which, according to Marxist-oriented theories, prevailed in the world-economy prior to the crisis of the 1930s.[32]

Several studies dealing with international capital movements have referred to long swings of the Kuznets type. Their main focus has been on the relationship between foreign investment on the one hand and foreign trade, population movements, and construction activities on the other hand.[33] The analysis of net capital movements of thirteen countries by Bloomfield (1968) clearly shows long swings of the Kuznets type in the series for Great Britain and the United States. Kuznets cycles seem to exist also in the cases of Australia, Germany, Italy, and Sweden.

In a study on long swings in British foreign investments in Argentina, Ford (1971) explains long-term cyclical fluctuations with the notion of a development cycle that is based mainly on two forces: first, the "animal spirit" of investors (excess of enthusiasm and revulsion) and, second, time lags between the investment decision and the realization of anticipated profits in the case of large infrastructure projects. The development cycle starts with an upswing in capital imports leading to an investment boom with excessive lending and a consequent bunching of infrastructure projects. Debt-service payments rise while output initially remains low due to the gestation lag of large infrastructure projects. When investors realize their initially overoptimistic assessment, they stop lending, with the result of debt-service incapacity on the part of the borrowing country. During default the infrastructure projects are gradually completed; output as well as exports increases and interest payments can be resumed. The expansion leads to a revival of foreign investment which is, however, of a less speculative nature, since the capacity to meet debt service has improved.[34] From this reasoning (which is quite similar to Rostow's terms-of-trade approach), one has to conclude that there are long swings in capital export of economically advanced core countries and in capital imports of less-developed peripheral and semi-peripheral countries which are related to growth cycles. Yet, there is no reason to expect any cyclical pattern of debt-service incapacity.

World Leadership Cycles

The concept of world leadership or hegemonic cycles refers to the rise and fall of hegemonic powers in the world-system. According to Wallerstein (1974, 1983), hegemony, apart from politico-military dominance, must be accompanied by simultaneous economic dominance in the agro-industrial, commercial and financial arenas. A hegemonic cycle starts when a core state becomes the leading world power which can structure the economic and social order of the world-system according to its own interests. If only one state attains such a hegemonic position the power structure is monocentric. With the decline of hegemonic power, worldwide economic and political power becomes more equally distributed among several core countries, and the global power structure becomes multicentric.

While consensus concerning conditions during the early modern period is missing, there is widespread agreement as to the hegemonies prevailing during the nineteenth and twentieth centuries. Thus, after the Napoleonic Wars and for the greater part of the nineteenth century, Great Britain assumed the hegemonic position, losing its dominance towards the turn of the century. The consequent rivalry finally resulted in the two world wars. The United States emerged from the Second World War as the dominant power in the world-system. Its hegemony lasted until around the end of the 1960s, when global economic and political power became increasingly more equally distributed, as among the United States, the European Community and Japan.

There are essentially two theoretical strands to explain hegemonic cycles. Authors in the tradition of world-system analysis emphasize the economic logic and perceive a close linkage between political hegemonic cycles and economic Kondratieff waves.[35] According to this approach, hegemony is based on productivity advantages thanks to the early introduction of basic technological, institutional and social innovations. However, as such innovations are adopted by other core countries, and even by those at the semi-periphery, the advantages are narrowed before they disappear altogether. The comparative advantages of hegemonic powers are further reduced by the trend towards higher labor costs and the growing (military) outlays required to shore up the world order.

By contrast, Modelski (1978, 1987) and his followers underline the autonomy of politico-military processes. They see the rise of new hegemonies determined through the unpredictable outcome of global wars. Through victory in global conflicts, hegemonic powers triumph over their rivals and create a new world order to secure their position, which enables them to enjoy monopoly profits. The decay of hegemony results particularly from the high and rising costs of maintaining the world order.

More recent studies suggest a certain convergence of these contending approaches. As Chase-Dunn (1981, 1989) exposed first in some detail, economic power and political power have to be seen as being mutually interwoven, influencing each other.[36]

World leadership cycles also affect the relationships between core and periphery. Among others, Chase-Dunn (1989: 273) argues that the hegemony of a single core country leads to a more multilaterally structured core-periphery relationship and a relaxation of political forms of core control over the periphery. Conversely, core countries tend to tighten their bilateral relations with peripheries and to resort to political forms of control when the world-system becomes structured in a multi-centric fashion. This argument can be illustrated by the waves of colonial expansions and contraction during the nineteenth and twentieth centuries. Simultaneously with the onset of British hegemony during the early nineteenth century, Latin America reached formal political independence. A similar decolonization movement concerning Asia and Africa occurred after World War II under U.S. hegemony. Conversely, the decline of British hegemony towards the end of the nineteenth century was characterized by colonial races among core powers.[37]

World-System Dynamics: Trends

Trend movements, which are also called secular movements[38] or secular trends,[39] are long-term and monotonic (i.e. noncyclical) processes. Contrary to cyclical movements, trends are irreversible, directed and mostly cumulative processes. Within the theoretical framework of the world-system perspective, trend movements have been studied considerably less than cyclical fluctuations. According to Hopkins and Wallerstein (1977) and Chase-Dunn (1989: 51-53), the capitalist world-economy has been characterized by the following trend processes.

Economic Expansion and Deepening of Commodification

Economic expansion and growth is one of the most important characteristics of the modern world-system. The initially European-centered capitalist world-economy continuously expanded to new territories. As a consequence of this expansive logic, the whole globe was incorporated into a single hierarchically organized division of labor by the end of the nineteenth century. Economic expansion has been associated with an increasing commodification of land, labor and natural resources, i.e. with a shift from subsistence production to market production. Empirically, this trend movement can clearly be shown by the exponential growth of world production during the nineteenth and twentieth centuries.[40]

Expansion of the International State System

The institution of the modern nation-state has spread to cover the entire globe. This is documented by the rising number of sovereign nation-states and the expansion of state activity during the nineteenth and twentieth centuries.[41]

Mechanization, Automatization and Internationalization of Production

As a result of successive technological innovations, capital intensity of production and, consequently, labor productivity have increased enormously since the first industrial revolution. Mechanization and automatization of production processes have been accompanied by an increasing average size of economic enterprises and the transnationalization of capital.[42] The globalization of production has been particularly favored by the revolutionary innovations in communication technologies.

Deepening of Global Social Stratification

There has been a growing social inequality between core areas and peripheral regions. This stratification process can be illustrated by the increasing income gap between core and periphery. Thus, empirical material presented by Bairoch (1981, 1982) and Maddison (1983) suggests that during the early nineteenth century the average income per capita in core countries was twice the level of peripheral countries. The ratio of average core income to average periphery income increased to 11:1 by the outbreak of World War I and to 19:1 by 1950. Although substantial economic growth and processes of industrialization took place in peripheral and semi-peripheral areas during the postwar era, the income gap further deepened: the ratio of average core income to periphery income was estimated at 40:1 by the mid-1980s.

The cyclical movements and trend processes discussed in this chapter will be used to formulate a structural approach to the phenomenon of periphery indebtedness and to explain the evolution and specific patterns of global debt cycles.

Notes

1. Cf. Chirot and Hall (1982) and Shannon (1989) for an account of the world-system perspective.
2. Cf. Chase-Dunn and Hall (1990) for a discussion of precapitalist world-systems.
3. See the pioneering work of Peter Heintz (1972, 1973, 1982); cf. also Meyer and Hannan (1979), Thomas et al. (1987), Chase-Dunn (1989: 88-105) and Featherstone (1990).
4. Cf. Wallerstein (1974) and Braudel (1979).
5. Cf. Chase-Dunn (1989) for the following discussion.
6. There is, however, considerable disagreement about the precise classification of individual countries and areas into the semi-peripheral zone. See, for instance, Wallerstein (1979: 100) and the discussion in Arrighi and Drangel (1986).
7. Cf. Arrighi and Drangel (1986) for an empirical discussion.
8. See Goldstein (1988) and Bornschier and Suter (1992) for a discussion of this point.

9. There are, however, several differences among authors and theoretical schools concerning the precise periodization, especially with respect to the interpretation of the interwar period (cf. Goldstein 1988: 67-74). In addition, Rostow (1978) differs significantly from other authors in his dating of long waves in the second half of the twentieth century. The question of periodization, though, must always be interpreted in the light of the above remarks on the concept of structural cycles.

10. Cf. Imbert (1959), Van Ewijk (1982), Cleary and Hobbs (1983), Gerster (1988), Goldstein (1988: 195-210), Reijnders (1988).

11. Cf. Mandel (1980), Van Duijn (1983: 147-192), Screpanti (1984), Kleinknecht (1987). The manner of calculating growth rates in these studies is, however, not free of problems. Growth rates can thus depend decisively on the choice of the beginning and end years of the respective upswing and downswing phases.

12. Solomou (1986) and Van der Zwan (1980), for instance, examine a much too short period (1856-1913 and 1850/60-1913/38, respectively). Van Ewijk applied spectral analysis in his work which, like other techniques of time series analysis, only permits the examination of time series which have been adjusted for trends. But such transformational and filtering processes as are chosen for this purpose can decisively affect the findings. As a result, cycles can be artificially generated (Slutzky effect) or on the contrary be filtered out altogether when the trend is removed (cf. Metz 1984, Gerster 1988, Eisner 1990 for a methodological discussion). The problematic nature of these techniques is illustrated by the study of Reijnders (1988: 291-295), who reanalyzed Van Ewijk's (1982) data set working with a different (and more appropriate) trend adjustment and who found a confirmation for the existence of Kondratieff cycles in several variables of real economic activity, e.g. gross domestic product (GDP), GNP, employment.

13. Cf. also the review on the literature given by Goldstein (1988), De Greene (1988) and Bornschier and Suter (1992).

14. But this holds only if the product cycles are advanced by 15 years in relation to the price cycles.

15. Cf. Schumpeter (1939), Mensch (1975), Graham and Senge (1980), Van Duijn (1983), Kleinknecht (1987).

16. Cf. Kondratieff (1926), Mandel (1980), Forrester (1983), Poletayev (1989).

17. Cf. Rostow (1975, 1978: 103-304; 1985).

18. Cf. Freeman et al. (1982).

19. Cf. Gordon (1980), Mistral (1982), Perez (1983), Boyer (1984), Lipietz (1984), Bornschier (1988), De Greene (1988).

20. Cf. Tylecote (1984), Nollert (1989).

21. Cf. Barr (1980), Cronin (1980), Hobsbawm (1981), Screpanti (1984), Silver (1989), Brand (1990), Boswell and Sweat (1991).

22. Cf. Thompson and Zuk (1982), Väyrynen (1983), Goldstein (1988), Mansfield (1988).

23. Namenwirth and Weber (1987), Eisner (1991).

24. Cf. Goldstein (1988) and Bornschier and Suter (1992) for a detailed review on long-wave theories.

25. Mensch's distinction between basic and improvement innovations has been criticized by Freeman et al. (1982) and Van Duijn (1983), who distinguish between product and process innovations. Empirical evidence concerning the appearance of innovations is varied. Mensch (1975), Kleinknecht (1987) and Goldstein (1988) report their bunched occurrence, but the evidence in Clark et al. (1981) and Van Duijn (1983) about this is weak. Such differences may essentially be due to different catalogues of innovations. As for the timing of innovations within the Kondratieff cycles, the empirical evidence tends to support Mensch, according to whom they are concentrated in the downswing or -- depending on the periodization -- in the early upswing phases of these cycles (cf. Mensch 1975, Kleinknecht 1987, Goldstein 1988: 219-225).

26. The ratio of fixed to variable capital, i.e. of fixed capital investments to wages.

27. A weakness of Marxist capital accumulation theories is their weak empirical foundation. There are but few studies dealing with the existence of profit rate cycles, and the evidence is hardly convincing (cf. Poletayev 1989).

28. Cf. Rostow (1978: 109-110, 299-304).

29. E.g. through population increase or increased demand for specific raw materials on account of technological innovations.

30. E.g. lags between awareness of profit potential and actual investment practice, between the inception of investments and their maturation.

31. Cf., among others, Williamson (1964), Easterlin (1968).

32. Cf, for instance, Lipietz (1984).

33. Cf. Williamson (1964), Bloomfield (1968), Ford (1968, 1971), Hall (1968).

34. Cf. Ford (1971: 657-659).

35. Cf. Chase-Dunn (1978, 1989), Research Working Group (1979), Bousquet (1980) and the discussion of Goldstein (1988). How Kondratieff cycles fit with hegemonic cycles has yet to be entirely clarified; cf. the contradicting concepts of the Research Working Group (1979), Bousquet (1980) and Väyrynen (1983).

36. See also Väyrynen (1983), Bornschier (1988), Goldstein (1988).

37. Cf. Bergesen and Schoenberg (1980).

38. Cf. Kuznets (1930).

39. Cf. Hopkins and Wallerstein (1977) and Braudel (1979), among others.

40. Cf., for example, the figures given by Kuczynski (1986: 458).

41. Cf. Boli-Bennett (1980: 78) for empirical evidence.

42. Cf. Bergesen (1981) and Bornschier and Chase-Dunn (1985).

3

Dynamics of Global Debt Cycles: A Theoretical Model

The phenomenon of periphery indebtedness takes place in the broader context of world-system structures and dynamics. The theoretical concepts outlined in the previous chapter, however, scarcely refer to aspects of periphery indebtedness. This chapter, therefore, deals with the question of how external debt of peripheral and semi-peripheral countries is related to cyclical fluctuations and trend movements prevailing in the capitalist world-economy during the nineteenth and twentieth centuries. The basic argument is that periphery indebtedness is subject to both long cycles and secular trends. In the first section of this chapter the notion of a global debt cycle is developed. In the next three sections the course of global debt cycles is related to the movement of Kondratieff growth cycles, Kuznets cycles and world leadership cycles. Subsequently, external debt is related to trend movements. It is contended that the international financial system has undergone a trend towards greater institutionalization affecting the pattern of individual debt cycles. The final section provides a summary of the basic hypotheses, which will be empirically examined in Part Two and Part Three.

The Concept of Global Debt Cycles

The concept of the global debt cycle refers to the cyclical aspects of periphery indebtedness. A debt cycle is conceptualized as a structural cycle. It consists of three consecutive phases. The first phase is characterized by the expansion of international loans: core capital shifts from predominantly domestic to foreign investment, and peripheral countries are increasingly raising loans from abroad. The accumulation of large stocks of external debt results in rising debt-service obligations for debtor countries which, in the second phase of a debt cycle, eventually lead to the outbreak of a payment crisis. The subsequent third structural phase of a debt cycle is characterized by attempts to manage debt crisis through the negotiation of debt-settlement agreements between debtor countries and their creditors. Thereafter peripheral and semi-peripheral debtor countries may regain access to international capital markets, but due to the bad debt record credit-worthiness is rather low and, correspondingly, inflows of external financial resources are modest until the loan boom phase of a new debt cycle.

A Theoretical Model on the Relationship Between Global Debt Cycles and Kondratieff Growth Cycles

The course of global debt cycles can be linked to the movement of Kondratieff growth cycles. The following basic model on the relationship between global debt cycles and long waves of economic growth relies heavily on Mensch's (1975) innovation approach but also takes into account arguments of capital accumulation theories as stressed by Mandel (1980) and of Rostow's terms-of-trade approach. A major shortcoming of these cyclical approaches, however, is that they fail to take into account the spatial and social differentiation of the world-economy into cores and peripheries. As a basis for the integration of this aspect, I will rely on Vernon's (1966) discussion of the worldwide aspects of a product cycle. Following Mensch's (1975) classification of Kondratieff cycles into four phases (depression, recovery, prosperity, recession) the following four main stages of a cycle are distinguished:

(i) A new long cycle emerges with the occurrence of basic innovations leading to the production of new, highly desired and thus profitable goods as well as to new institutional and social structures. Production in leading sectors is highly labor-intensive and only modestly standardized during this stage. The creation of basic innovations requires the presence of an important innovating potential and close contacts to a potential high-income market. For these two reasons, a new long cycle usually takes its origin in the core of the world-economy.

During this early phase of a global growth cycle, the financial relations between core and periphery are partly interrupted since widespread debt-service incapacity originating from the earlier global debt crisis has not yet been settled. As a consequence, returns on financial assets and on foreign investment are relatively low, promoting a shift towards basic innovations which promise higher profits.

(ii) As the leading products of a long cycle mature (via improvement innovations), they cluster into a technological style specific to a long cycle that comprises the institutional and social prerequisites of production as well as a generally accepted set of consumer goods representing status symbols. As a consequence, markets of leading products turn into mass markets and their production becomes increasingly standardized and concentrated. During this stage the Kondratieff cycle extends itself over the whole core area of the world-economy, and the periphery is integrated into the upswing primarily through trade and less through production in leading sectors or the adoption of institutional structures relevant for the technological style of a new cycle. This is due, on the one hand, to the still high profit rate in the core and, on the other hand, to the low innovating potential (the shortage of human and material capital) combined with a lack of appropriate infrastructure in the periphery, both of which render identical production unprofitable. The rising demand of core industry for raw materials, however, increases the prices of the main export goods of the periphery.

The integration of the periphery into the new global growth cycle and the consequent rising export revenues promote the arrangement of debt settlements between core creditors and those periphery countries which have been confronted with debt-service incapacity. Due to the still highly profitable investment opportunities in the core, financial flows from the core to the periphery are, however, only modest.

(iii) The innovating potential fades and consumer markets become saturated in the core so that profit rates of industrial investment decline. With the standardization of production in leading industries, the previously mentioned disadvantages of the structure of peripheral economies begin to lose their weight. At the same time, peripheral markets are still unsaturated. Declining profit rates in the core and increasing profitability of industrial investment in the periphery induce capital flows into the periphery. They may take the form of direct investment or foreign loans (e.g. foreign governmental bonds, bank credits to peripheral borrowers).

While capital flows into peripheries integrate peripheral areas into the product cycle of the leading sectors of a long wave, they usually lead to the establishment of enclave segments within their economies.[1] Within those segments the technological standard of production is high, but ties with the rest of the economy are minimal. The limited integration of peripheral economies does not permit a balanced and dynamic auto-centered development, and the enclave sectors remain highly dependent on the core for trade and capital. As a consequence, the declining trend of the overall profit rate cannot be reversed by an expansion of capital flows into the periphery.

The nature of the integration of the periphery into a technological style through capital flows is specific to each cycle. This permits a certain qualification of the individual historical cycles (e.g. formation of the nation-state and railway construction during the nineteenth century, import-substituting industrialization during the twentieth century), although, as mentioned above, the different elements making up the technological style of a long cycle are transferred to the periphery only fragmentarily.

(iv) After the expansion of a technological style specific to a cycle into the periphery has been completed and the innovation potential of the core areas has been exhausted, stagnation begins to prevail in the world-economy. In the short run, high profit rates may be achieved through inflationary gains in a stagflationary setting and mergers or acquisitions of firms.[2] The latter strategy may be complemented by delineating market spheres within the framework of oligopolies or between core states (protectionism, colonialism).[3] In the long run, however, this final stage of a cycle is increasingly prone to crisis and collapse.

During this stage peripheral countries are increasingly prone to debt-service incapacity for the following main reasons: (1) Declining world demand caused by economic stagnation in the core renders previous assumptions about export and foreign exchange income of periphery borrowers overly optimistic. Shortfalls of actual against expected export earnings force peripheral countries to incur new debt burdens. Lending behavior becomes increasingly speculative, thus increasing the fragility of international financial systems. (2) Returns on external financial capital are usually relatively low. This may be due to low multiplicator effects of foreign capital (especially in enclave economies) or to the high import component and foreign exchange demand of the investment projects (as in the case of import-substituting industrialization). (3) As a result of legitimatory pressures from various social classes and groups, governments of periphery states may resort to a politically relevant but economically questionable allocation of resources (e.g. financing of subsidies, maintenance of large clientelistic networks). More specifically, the use made of external resources by peripheral states is expected to depend upon the structure of political regimes, i.e. the social base on which governments rely and which legitimize political power.[4]

The rising debt-service difficulties of periphery borrowers eventually lead to the outbreak of a global debt crisis. Only now, as profitable outlets have virtually disappeared, do core enterprises begin to invest in basic innovations that do not promise high average profit rates in the beginning. The production of new basic innovations will finally trigger a new cycle. A summary of the hypothetical relationship between debt cycles and Kondratieff growth cycles is given in Figure 3.1.

FIGURE 3.1 Hypothetical Relationship Between Kondratieff Cycle and Global Debt Cycle

	i[a]	*ii*[a]	*iii*[a]	*iv*[a]
Kondratieff Cycle	Basic innovations Labor-intensive, unstandardized production for high-income markets Periphery still unattractive for production	Process innovations Increasing standardization and concentration of production for mass markets Economic expansion	Decline of innovative potential Saturation of consumer markets and declining profit rates in the core Production in periphery becomes profitable	Exhaustion of innovative potential Economic stagnation Decline or stagnation of world trade
Global Debt Cycle	Financial relations between the core and the periphery partly interrupted due to crisis of previous cylce Low returns on financial assets promote basic innovations	Debt settlements Modest flows of capital into the periphery Integration of periphery into upswing of new cycle through trade	Increasing flow of capital into the periphery Inefficient allocation of financial resources due to political and economic constraints on Third World states	Low returns on investment in the periphery Frequent necessity to roll over existing debt and rising debt-servicing difficulties of Third World states Frequent defaults or reschedulings

[a]Refers to the cycle phase defined in the text.

Source: Pfister and Suter (1987: 246).

Global Debt Cycles and Kuznets Cycles

The hypothetical relationship between economic growth cycles and global debt cycles as it has been elaborated concerning Kondratieff waves can be extended with some qualifications to the shorter Kuznets cycles. As mentioned in the previous chapter, Kuznets cycles have no general validity but are limited in space and time. Accordingly, their relevance for cyclical aspects of periphery indebtedness is expected to be confined to the Atlantic economy and to the historical phase of extensive capital accumulation (i.e. ca. 1850 to ca. 1930). In other words, Kuznets cycles typically integrate the periphery into the world-economy through capital flows destined to construction activities (e.g. railway construction) and related to international migration movements.

Following the argument put forward by Kuznets cycle theories, flows of foreign investments from cores are expected to be inversely related to economic long swings in capital-exporting core countries and to move parallel to economic cycles in borrowing countries. Accordingly, phases of intense core capital exports and the credit-raising activity of peripheries fall into downswing periods of economic long swings in core countries and into upswing periods of economic swings in peripheral and semi-peripheral areas. Debt-service incapacity is expected to occur at the beginning of a downswing period in the economic cycle of the borrowing country. Debt crises are mainly triggered by credit rationing of lenders. Thus, in contrast to Ford (1971), I do not consider debt crises to be singular events. The agreement of debt settlements between borrowing countries and creditors is expected to cluster in the early upswing phase of the economic cycle of the borrowing country when access to new international loans is sought again.

Global Debt Cycles and World Leadership Cycles

The modern world-system has experienced two hegemonies during the industrial era, namely, those of Britain (after the Napoleonic Wars until the turn of the century) and the United States (during the postwar period until the 1970s). According to the general discussion presented in the previous chapter, I suggest that world leadership cycles affect the pattern of global debt cycles and periphery indebtedness in three important respects:

First, an important dimension of hegemony is international financial supremacy. Due to its supremacy in production and commerce, a hegemonic power is the principal center of international capital accumulation and becomes, therefore, the main source for long-term borrowing. In fact, one may show that since the sixteenth century international financial centers moved geographically with the emergence of new hegemonic powers from the northern Italian city-states (e.g. the Medicis of Florence) to the large banking houses of southern Germany (e.g. the Fuggers of Augsburg) and later to Genoa, Amsterdam, London, and New York.[5] An important element of financial supremacy refers to the role of the hegemonic power as a protector of international financial stability. Because of its dominant position within international capital accumulation, the metropolis of the hegemonic power rises to the financial center of the world and its currency becomes the principal medium of exchange. For this reason the leading power becomes a kind of lender of last resort. It is hypothesized that the presence of an international lender of last resort softens global debt crises whereas its absence results in longer, more widespread and deeper disruption of international financial relations.[6]

Second, it has been argued that world leadership cycles affect the core-periphery relationship in the sense that core rivalry leads to a strengthening of political forms of core control over peripheral areas in periods of core rivalry. This suggests that financial relations between core and periphery, i.e. between creditor and debtor countries, are more frequently regulated by political means and institutions when the world-system's core structure is multicentric than during hegemonic periods. More precisely, it is expected that debt-crisis management during periods of core rivalry is characterized by high degrees of state interference from creditor countries, whereas political regulation of debt settlements is less pronounced during a hegemonic phase.

Third, the course of world leadership cycles may affect the terms of debt settlements negotiated between debtor countries and creditors. Generally, one may argue that the bargaining power of individual peripheral debtor countries is higher when creditors are divided and poorly organized. This suggests that debtors are able to negotiate more favorable settlements during periods of core rivalry than during phases of uncontended hegemony. Yet, this argument holds only when core-periphery relations are characterized by multilateral exchange and not by a segmented, feudal structure of interaction.[7]

Global Debt Cycles and Trend Movements

The most important trend movements within the capitalist world-economy relate to growth and expansion on the one hand and to structural changes towards concentration, hierarchization and integration on the other. Over the past 200 years these trend movements also affected international financial relations between core and periphery and substantially changed the structural context of periphery indebtedness.

The most important trend within international financial relations consists of a movement towards increasing institutionalization.

By institutionalization I mean the long-term structural change of international financial relations from a noncooperative system with no capacity for self-organization or self-reflection, such as perfect market systems, towards a social system composed of cooperative subsystems capable of organizing and reorganizing their own internal structure and their relation to the environment by themselves. In more general terms, institutionalization refers to processes of *Vergesellschaftung*, of international financial relations.[8] This trend consists of two closely related developments: first, the increased domination of international financial relations by a few large actors at high system levels and, second, a process of functional integration and the emergence of cooperative institutional arrangements.

Thus, before World War II actors on the creditor side consisted of a mass of small and poorly organized individual bondholders. After World War II the actor structure radically changed as governments of core states, international organizations and large bank syndicates became the dominant international lenders. As a result, international financial relations became sufficiently surveyable so that actors could develop generalized perspectives on each other and assume roles. This structural change provided the basis for the emergence of subsystems characterized by cooperative forms of self-organization. The formation of multilateral rescheduling mechanisms can be seen as a direct outgrowth of this trend towards the establishment of dense interaction structures and strong cooperative networks among creditors.[9]

The institutionalization trend has two main repercussions on the course of global debt cycles. First, the institutionalization of strong creditor cooperation improves the capacity of the international financial system to respond quickly to crisis-prone situations and enables creditors to handle the problem of debt-service incapacity of peripheral borrowers efficiently. This modifies the previously discussed implications of world leadership cycles for international financial stability and the presence of an international lender of last resort: In the context of institutionalized creditor cooperation, a lender of last resort may also be present in periods of core rivalry. Which one of the conflicting processes of core rivalry and institutionalization eventually prevails and which one determines a specific historical phase depends upon the individual strenth of the two forces.

Second, the strengthening of creditor cooperation and the simultaneous lack of cooperative arrangements among borrowers substantially enhance the bargaining position of core creditors vis-à-vis peripheral debtor countries. As a result, creditors are able to exert far-reaching influence on debtor countries and to enforce hard terms of debt settlements against the interests of debtor countries.

Conclusion

Let us conclude the theoretical part of this book with a brief summary of the basic theoretical arguments concerning the relationship between periphery indebtedness and world-system cycles and trends.

The basic argument of this study states that during the nineteenth and twentieth centuries periphery indebtedness was characterized by a recurrence of global debt cycles. Each consists of the three consecutive structural phases of, first, intense core capital exports and corresponding booms in credit-raising activity of peripheries; second, the occurrence of debt-service incapacity among peripheral countries, and, third, the negotiation of debt-settlement agreements between debtors and creditors. Specifically, I argue that all three structural features of a global debt cycle (i.e. international loan booms, outbreak of global debt crises and arrangements of debt settlements) are linked with real economic processes on a global level, notably fluctuations of innovation activities and profit rates within the framework of Kondratieff cycles and of shorter fluctuations with regard to migration movements and construction activities within the narrower framework of the Atlantic economy between ca. 1850 and 1930.

The course of global debt cycles is affected by the trend towards increasing institutionalization of international financial relations. It is argued that institutionalization enhances the resilience of the international financial system against the outbreak of open debt crises and favors the bargaining power of creditors vis-à-vis debtor countries. As a consequence, an open crisis may be averted or at least postponed, and the burden of debt crisis has to be carried mainly by the debtors. This suggests implications for the operation of global debt cycles as well as of Kondratieff waves in general: by deferring or avoiding a crisis without contributing to its solution, the institutionalization trend may change the cyclical logic of global debt cycles and protract the initiation of a new Kondratieff growth cycle.

Notes

1. Cf. Singer (1950) and the literature within the framework of the dependency theory (e.g. Furtado 1970, Galtung 1971, Cardoso and Faletto 1979).
2. Cf. Daems (1981).
3. Cf. Chase-Dunn (1989).

4. This aspect of periphery indebtedness will be developed further in Part Three, which discusses individual country case histories (cf. Chapter 7).

5. Cf. Braudel (1979).

6. Cf. Kindleberger (1978).

7. As in the case of colonial empires; cf. Galtung (1971), Chase-Dunn (1989: 272).

8. Cf. Pfister and Suter (1987) for a more detailed analysis of the institutionalization trend.

9. Cf. also the literature on international regimes for an alternative approach to the analysis of the institutionalization trend (e.g. Krasner 1983, Keohane 1984).

PART TWO

Empirical Evidence of Global Debt Cycles

The following three chapters present empirical evidence for the existence of debt cycles on the global level of the world-system during the nineteenth and twentieth centuries. Each of the three consecutive structural phases of the debt cycle, i.e. the expansion of external debt, the outbreak of debt crises and the negotiation of debt settlements, will be examined in detail. Chapter 4 deals with the cyclical pattern of capital exports from core countries and the periodical increase of external public debt of peripheral countries. Chapter 5 examines the cyclical occurrence of global debt crises and presents cross-sectional research on the determinants of default and rescheduling probabilities. Finally, in Chapter 6, the management of debt crises and the pattern of debt settlements agreed upon between debtor countries and their creditors will be analyzed.

4

Capital Exports from the Core and Foreign Loans Raised by the Periphery

Types of International Capital Flows and Financial Instruments

International capital flows between core countries and semi-peripheral and peripheral nations during the nineteenth and twentieth centuries have assumed several distinct forms. Prior to World War II the principal financial instrument of official external borrowing consisted of foreign governmental bonds. They were issued by the borrowing government and sold to the public on the capital markets of the most important international financial centers (e.g. London during the nineteenth century and New York after World War I). Loan transactions were arranged by private businesspeople, brokers and merchant bankers who served as financial intermediaries. The conditions of foreign bonds were laid down in the loan contract and were announced to the potential investors through the loan prospectus. In most cases, foreign governmental bonds were sold to the public below par, usually at a discount of 10 to 40 percent. They had relatively long maturities (up to 30 years) and fixed interest rates varying mostly between 4 and 8 percent. Price of issue and interest rates were dependent upon the creditworthiness of the borrowing country and the risk assessment of investors.[1]

Since the value of individual shares was relatively low (e.g. £100 or £500),[2] foreign governmental bonds were generally held by a large number of individual bondholders. This is illustrated by the fact that in 1914, liabilities of tsarist Russia vis-à-vis France amounting to $11 billion were owed to 1.6 million bondholders.[3] Similarly, an investigation into the distribution of five large foreign loans sold on the U.S. capital market in the mid-1920s revealed that they were bought mainly by small bondholders: individual sales averaged $2944 to $4335, and 90 percent of all sales amounted to $5000 or less.[4]

As a result of the global debt crisis of the 1930s, foreign governmental bonds largely disappeared as a financial instrument in the core-periphery relationship. After World War II only few economically advanced semi-peripheral countries (e.g. Brazil, Mexico, Spain) had access to the international bond market. In the postwar period foreign governmental bonds were substituted by loans and credits granted by official bodies of creditor countries (e.g. development assistance agencies), international organizations (e.g. the World Bank and the International Monetary Fund) and private commercial banks. Long-term development credits (extended either bilaterally by economically advanced core countries or multilaterally by international organizations), private and official export credits, syndicated credits offered by commercial banks and short-term stabilization loans granted by the International Monetary Fund have become the principal financial instruments. The relevance of these different types of financial flows varies substantially among individual Third World countries. Thus, for countries belonging to the extreme periphery (i.e. Bangladesh and most African states), development assistance is the most important external financial source, whereas the external debt of economically more advanced countries (i.e. Latin American and Southeast Asian countries) chiefly consists of credits from private banks.

The changes in the dominant financial instruments coincided with a marked reduction in the number of actors on the creditors' side, facilitating the formation and institutionalization of a strong creditor cooperation. Thus, instead of a large mass of dispersed bondholders and financial intermediaries prevailing prior to World War II, relatively few complex institutions with a comparatively dense interaction structure, i.e. core states, international organizations and large bank syndicates, began to control international financial relations during the postwar era.

Historically, nation-states became active as direct creditors for the first time during World War I with the massive financial support provided by the U.S. government for its war allies.[5] In the wake of the Marshall Plan, which directed large official credits from the United States to Europe, official lending become an important financial source for peripheral countries.[6]

The first international organizations established after World War I, like the Bank for International Settlements (BIS) or the League of Nations, played only a minor role in the international financial system.[7] It was only after World War II that autonomous and powerful international financial organizations were founded with the creation of the two Bretton Woods "twins", the World Bank (International Bank for

Reconstruction and Development) and the IMF. The latter was designed to deal with short-term balance-of-payments and stabilization problems of its members, whereas the World Bank was originally committed to the reconstruction of war-ravaged Europe and only later (in the 1950s) turned to development financing in Third World countries. The initial structure of both institutions corresponded largely to plans prepared by the U.S. Department of State and the Treasury and mainly served the international economic interests of the United States.[8]

From the mid-1960s onwards, with the rise of Euromarket lending, large bank syndicates became an important source of capital for the Third World. Although several hundred financial institutions[9] were present in Euromarkets, Eurolending was centered on relatively few actors: according to Hardy (1979: 191), some 45 percent of all syndicated lending during the 1970s was provided by the nine most important internationally active U.S. banks -- a striking contrast to the widespread distribution of French-owned Russian securities before World War I mentioned above.

Since this study concentrates on *public* foreign borrowing, a detailed discussion of types of *private* capital imports is of marginal interest in this context and will therefore not be dealt with further. Prior to World War I private foreign borrowing chiefly consisted of corporate securities. During the postwar era foreign direct investment of transnational corporations became an important form of international capital flows.[10] Since private capital imports were often formally guaranteed or supported by informal arrangements by the respective governments, the boundaries between public and private foreign borrowing are, however, far from clear.[11]

The following sections will present empirical material dealing with quantitative developments of capital exports from core countries and of foreign loans raised by peripheral states. Subsequently, cross-national research on the determinants of the amount of foreign borrowing will be reviewed to detect the general structural factors responsible for the accumulation of foreign debt.

Capital Flows from the Core to the Periphery

There are basically three methods to estimate capital exports from core countries. First, capital exports can be computed by using statistics of new foreign capital issues (direct method); second, the value of total holdings abroad can be estimated by capitalizing the yield from foreign investment; and third, figures for net capital flows can be obtained by calculating the overall balance in the balance-of-payments accounts (indirect method).[12] None of these three procedures is perfect. As indicated by Lévy-Leboyer (1977b: 10) the first method tends to overestimate international capital movements since most foreign issues were floated simultaneously at several places. The second method stands and falls with the availability of reliable statistics on incomes from dividends and with the assumptions concerning the rate of capitalization. According to Platt (1980: 12), figures for foreign investment based on this procedure are usually overestimated. The third method is limited to net figures and does not allow the separation of capital exports from capital imports.

Which one of the different methods one will finally resort to depends on the purpose of the analysis. Since the indirect method provides annual data for long time series, it appears to be the most appropriate one for the study of long-term cyclical fluctuations. Moreover, the critical surveys of Lévy-Leboyer (1977b) for France and Platt (1980) for Great Britain indicate that the general overestimation of foreign investment is least by using the balance-of-payments statistics. Therefore, this section, which deals with capital exports from core countries, primarily uses data based on indirect estimates. A shortcoming of this method, however, is that different types of flows (e.g. short-term investment, private direct investment, and portfolio investment) are not disaggregated and no geographical distribution of foreign investment is provided. Furthermore, it is not possible to separate capital exports from capital imports. Due to these limitations, additional data from various sources and different methods will be used in the next section as well as in the country case studies presented in Part Three.

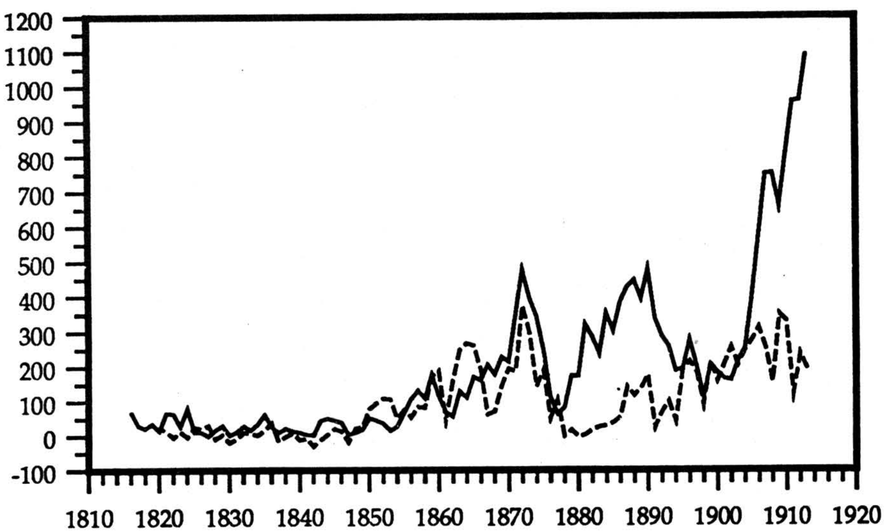
Even for capital flows derived from balance-of-payments statistics there are no series available that cover the whole period of industrial capitalism. Therefore, one has to consider separate individual series to obtain an idea of the overall long-term pattern of international capital exports.

During the nineteenth century, Great Britain and France were the major suppliers of long-term capital in the world-system. In addition, the smaller European cores like Belgium, the Netherlands, and Switzerland exported some capital. During the second half of the century, Germany and the United States rose to the status of core countries and subsequently became net capital exporters (Germany during the early 1870s and the United States from 1897 onwards). For Great Britain and France, annual data for net outflows of capital going back to 1816 and 1820, respectively, are available.[13] France is the only country for which the figures of accumulated credits abroad have been adjusted for losses. The estimates for Germany are limited to the years 1881-1913 and do not seem to be reliable.[14] Therefore, the following analysis of long-term foreign investment before World War I will be confined to Great Britain and France.

From 1920 onwards aggregate data for capital exports from the core are available, which include all major creditor countries. Figures before World War II are based on indirect estimates from the balance-of-payments accounts. For the postwar period, direct estimates of capital flows from the core to developing countries are available. Figures of capital exports of major core countries are plotted in Figures 4.1-4.3.

Figure 4.1 shows the pattern of British and French net capital exports between 1816 and 1913. The series are dominated by cyclical fluctuations of different duration. In the case of Great Britain two and a half Kuznets

FIGURE 4.1 Net Capital Exports of Great Britain (solid line) and France (broken line), 1816-1913, in Millions of U.S. Dollars



Sources: Figures for Great Britain are indirect estimates based on the balance-of-payments accounts and are derived from Imlah (1958: 72-75). They include net movements of long- and short-term capital as well as errors and omissions but exclude net export of gold and silver bullion and specie. Data for France are indirect estimates based on the balance-of-payments accounts as presented by Lévy-Leboyer (1977a: 119-121). They include net movements of long- and short-term capital, gold and silver bullion and specie as well as errors and omissions. Figures for 1871-1873 are not adjusted for indemnity payments to Germany. The data are converted into U.S. dollars on the basis of exchange rates before 1914 ($0.193 to 1 French franc, $4.867 to 1 British pound; cf. Bloomfield 1963: 95).

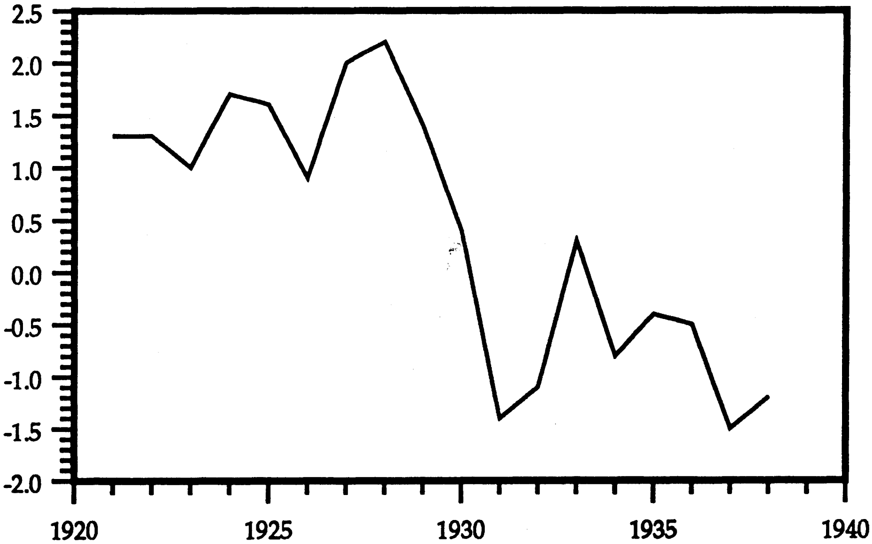
cycles are clearly visible (1862-1877, 1877-1898, 1898-1913).[15] For France the chart reveals on the one hand short-term Juglar cycles of 6-10 years' duration, and, on the other hand, from ca. 1840 onwards, fluctuations similar to Kondratieff waves, with troughs in the early 1840s and in 1876-1894 and peaks in 1872 and 1909. The absence of Kuznets cycles in French capital exports has been attributed to the fact that France was a net immigration country during the late nineteenth century and therefore not affected by the dynamics underlying the Atlantic economy.[16] During the first half of the nineteenth century, no long-term cycles seem to be present in either series, though there is a slightly marked peak in the early 1820s.[17]

The two time series move partially parallel. Both show a boom in the early 1870s, a subsequent slump in 1876-1880 and another heavy increase before the First World War. There are two major differences between the pattern of the British and the French net capital exports. First, after the trough in the late 1870s, the series for Great Britain displays a quick recovery and a new surge of capital outflows in the 1880s, with a peak in 1890 and a subsequent crisis that leads to a trough in 1898. However, the shortness of stagnation in British foreign investment during the 1870s compared with the French series might also partially be caused by the lack of adjustments for losses due to defaults in the British data. Second, the boom in foreign investment before the First World War was much more marked in the case of Great Britain.

The pattern of international capital movements during the interwar years is presented in Figure 4.2. It displays net capital exports of six core countries (the United States, Great Britain, France, the Netherlands, Switzerland and Sweden). During this period the most important lenders of long-term capital were the United States and Great Britain. There were large capital exports from core countries during the 1920s, with peaks in 1924 (implementation of the Dawes Plan) and 1928 followed by a sharp decrease, with troughs in 1931 and 1937. The decade of the 1930s is characterized by substantial net capital imports of core countries since exports of new capital came to a virtual standstill and flows were dominated by amortization and repatriation of earlier loans. As shown in Figure 4.2, there was no recovery of international lending before the outbreak of World War II.

The development of financial flows from core countries to peripheral and semi-peripheral countries during the postwar era is shown in Figure 4.3. The series for total flows reveals one long-term cycle but virtually no short-term fluctuations as has been observed for the period before the Second World War. There were moderate increases of net outflows in the 1950s and 1960s which were caused primarily by official lending of

FIGURE 4.2 International Capital Movements of Six Major Core Countries During the Interwar Period (Net Outflow), in Billions of U.S. Dollars

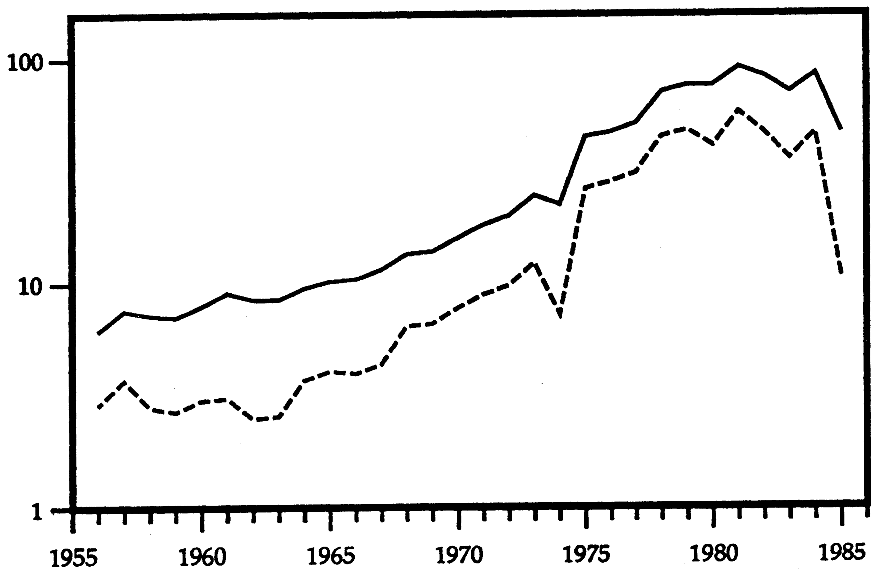


Source: The figures are indirect estimates based on the balance-of-payments accounts and have been derived from United Nations (1949: 10).

core states. From the late 1960s onwards, capital flows began to rise more rapidly. Between the mid-1970s and 1981, a boom occurred which was based primarily on private flows. After the peak of net capital exports in 1981, financial flows declined rapidly in the years 1982-1985.

The long-term cyclical pattern of capital exports from core countries since the early nineteenth century may be summarized as follows. First, no clear evidence for long-term cycles can be found during the first half of the nineteenth century. Second, there are some indications of long waves of the Kondratieff type with peaks in net capital exports from core countries in 1872, 1913/1928, and 1981. General periods of rapid growth in foreign investment are the years 1860-1872, 1904-1913/1921-1928, and ca. 1967-1981. Phases of stagnating capital exports from core countries are the 1870s and 1930s, and the years from 1981 onwards. Third, long swings of the Kuznets type are visible in the case of Great Britain between 1860 and 1913. The fluctuations in capital exports during the interwar period may also be interpreted in the context of Kuznets cycles. There is, however, only little evidence for Kuznets cycles during the postwar era.

FIGURE 4.3 Total (solid line) and Private (broken line) Net Capital Flows from DAC Countries to Developing Countries, 1956-1985, in Billions of U.S. Dollars (Semi-log Scale)



Sources: The data are direct estimates of total net flows from DAC countries (core countries organized within the Development Assistance Committee of the OECD) to developing countries and multilateral agencies. The figures for total flows include official development assistance, official and private export credits, direct investments, and bank and bond lending and are taken from OECD (*Efforts et politiques d'aide au développement*, 1966: 165-167 for 1956-1962; *Development Co-operation* 1974: 199-205 for 1963-1973; 1980: 178-182 for 1974-1978; 1984: 204-206 for 1979-1982; 1986: 232 for 1983-1985).

The Cyclical Evolution of Periphery Indebtedness: Loan Boom Phases from 1815 to the Present

Unfortunately, there are no statistical time series available providing annual aggregate data for external borrowings of the periphery during the whole period of industrial capitalism. Therefore, the examination of the cyclical pattern of foreign governmental borrowing has to be confined to general phases of loan booms. A more detailed analysis will be provided in Part Three on the level of selected individual debtor countries.

The major boom periods in peripheral borrowing during the nineteenth and twentieth centuries, together with the largest debtor countries, are summarized in Table 4.1. Seven boom phases with shifting geographical focus can be identified. They fall into the early 1820s, the late 1830s, the decade between the mid-1860s and the mid-1870s, the late 1880s, the years prior to World War I, the late 1920s and the 1970s.

During the first boom period, international capital flows were concentrated in the European periphery (Spain, Naples, Prussia) and Latin America (Greater Colombia, Mexico). Partly connected with the expansion of the American cotton economy, U.S. states and municipalities became the principal borrowers in the international capital markets during the 1830s. The principal debtors during the boom period of the 1860s and early 1870s were again the United States, together with Russia, the Ottoman Empire, Egypt and Spain. By the late 1880s, Australia and Argentina emerged as heavy borrowers besides the United States. Before World War I the center of international borrowings shifted to Russia, Canada, South Africa, Argentina and the Balkan states. During the interwar period Germany was by far the most important

TABLE 4.1 Boom Periods of External Borrowings of Peripheral and Semi-Peripheral Countries, 1822-1981

Period	*Major Borrowers (with principal lender in parentheses)*[a]
1822-1825	Spain, Naples, Denmark, Prussia, Greater Colombia, Mexico, Austria-Hungary, Russia, Brazil, Greece (all B)
1834-1839	U.S. states (B), Portugal (B), Spain (F)
1864-1875	United States (B), Russia (G, B, F), Ottoman Empire (B, F), Egypt (B, F), Spain (B, F), Austria-Hungary (F), Peru (B), Romania (F)
1886-1890	United States (B), Australia (B), Argentina (B)
1905-1913	Russia (F), Canada (B), South Africa (B), Argentina (B, F), Balkan states (G), Ottoman Empire (F, G), Austria-Hungary (G), Brazil (B, F), Mexico (U, F), Cuba (U)
1924-1928	Germany (U, N, S), France (N, B), Argentina (B), Australia (B), Canada (U, B), Cuba (U), Brazil (B, U), New Zealand (B), South Africa (B)
1970-1981	Brazil, Mexico, Spain, Venezuela, South Korea, Argentina, Algeria, Turkey, Yugoslavia, Poland, Romania, Egypt, Indonesia

[a]B=Britain, F=France, G=Germany, N=Netherlands, S=Switzerland, U=United States.

Source: Suter (1990: 66).

receiver of foreign capital. The last boom period, finally, was localized in Latin America (Brazil, Mexico, Venezuela, Argentina) and the European periphery (Spain, Turkey, Yugoslavia, Poland). Other heavy borrowers were South Korea, Algeria, Egypt and Indonesia.[18]

Already this rapid enumeration suggests that the largest debtor countries did not belong to the poorest and economically least advanced countries. Rather, most of them were middle-income countries with a substantial economic potential occupying a semi-peripheral status within the hierarchy of the world-economy. This is illustrated by the cases of Prussia, Spain, and Naples during the 1820s; the United States, Russia, Australia, Argentina, Canada and the Ottoman Empire between the mid-nineteenth century and the outbreak of World War I; Germany, France, Argentina and Australia during the interwar years; as well as Brazil, Mexico, Spain, Venezuela, and South Korea during the 1970s.

Table 4.1 also shows the most important creditor nations. The well-known dominance of international finance by Great Britain during the nineteenth century becomes evident as well as regional shifts in the allocation of foreign investment. Thus, prior to about 1875, British capital concentrated on continental Europe, the United States, the Ottoman Empire and Egypt but turned towards countries belonging to the Atlantic economy from 1880 onwards. Towards the late nineteenth century, French foreign investments show a shift from Spain and Austria-Hungary to Russia and South America, whereas German investors withdrew their money from Russia and increasingly channeled new lendings to the Balkans.[19]

Sequences of boom periods of external borrowing can be associated with both Kuznets and Kondratieff cycles. Between 1860 and 1930 they seem to be closely related to Kuznets cycles (peaks in the U.S. Kuznets cycles were in 1871, 1892, 1912, 1927; see Chapter 2 above, Table 2.2). The boom period of the 1830s also coincides with an upper turning point of the Kuznets cycle, but there was no general boom during the peak of 1853. The first wave of external borrowing between 1822 and 1825 falls into a trough of the U.S. Kuznets cycles, and after the 1930s external borrowing of the periphery seems to function independently from Kuznets cycles.

The boom periods of 1822-1825, 1864-1875, 1905-1913/1924-1928 and 1970-1981 can be related to Kondratieff cycles (peaks in the Kondratieff growth cycle were in 1825, 1872, 1929 and 1973; see Chapter 2 above, Table 2.1). Yet, the late 1830s and 1880s do not fit into the pattern of Kondratieff waves. Where peaks of Kuznets and Kondratieff cycles do not coincide (late 1830s, late 1880s), expansionary phases of international capital flows seem largely confined to the area covered by the Atlantic economy. Between 1886 and 1890, for example, all three major borrowers (the United States, Australia, Argentina) were countries of recent settlement.

Causes of Periphery Indebtedness

The empirical evidence presented above suggests a correlation between boom phases in capital exports from core countries and loan-raising activities of peripheries on the one hand and the movement of global growth cycles on the other. As suggested by the basic hypotheses developed in Part One, phases of intense capital exports and creditraising coincide largely with peaks in global growth cycles. This raises the question about the specific mechanisms for the explanation of this relationship. The basic model (cf. Figure 3.1, Chapter 3) suggests that the increase in flows of core capital into the periphery has to be attributed to the exhaustion of the innovating potential, the saturation of consumer markets in the core, and the consequent fall in the profit rate. At the same time it is argued that returns on investment financed by external debt are only low for borrowing countries. Accordingly, the following discussion on causes of periphery indebtedness first deals with this argument. Second, determinants of financial flows to the periphery as evidenced by several cross-national studies for the loan booms of the 1920s and 1970s will be discussed. Finally, empirical research on growth effects of external debt are briefly reviewed.

Declining Profit Rate

As already mentioned in the discussion of Mandel's concept of long waves, there are only few studies dealing empirically with movements in profit rate, and the evidence they provide is generally poor. Nevertheless, two comments can be made.

First, for the postwar era there is some empirical evidence for declining profits on equity investment in core countries during the 1960s and 1970s and a consequent shift from equity investment to pure financial investment. Thus, a continuous decline of profits and returns on equity investment within the major countries of the Organization for Economic Cooperation and Developement (OECD) can be documented from about 1965 through about 1980.[20] As a consequence, the gap between returns on equity investment and interest rates has narrowed. In a comparison of real returns on equity investment and real interest rates in the Federal Republic of Germany, Hankel (1984: 107) finds that by the mid-1970s assets in the financial system became even more profitable than equity investment: yields on equity investment declined from 7.5 percent to 3.9 percent between 1960 and 1975, whereas real interest rates on financial investments rose from 0.6 percent in 1970 to 6.4 percent in 1981.

Second, several historical studies dealing with long swings in international capital movements prior to World War I examined the relationships between domestic investments and capital exports of core countries. Edelstein (1982: 30) found a correlation of -.77 between the annual rates of British home and overseas investment for 1870-1913. Domestic investment and foreign lending thus show a pattern of inversely related long swings of the Kuznets type. Moreover, regression analysis on the determinants of British overseas investment (and of foreign borrowing of Argentina, Australia, Canada and the United States, respectively) revealed negative relationships between yields on British domestic investment and British capital exports.[21]

Cross-National Research on the Determinants of Periphery Indebtedness

For two of the seven boom phases of credit-raising activity identified in the previous sections, namely, the late 1920s and the 1970s, empirical evidence on the determinants of the level of foreign indebtedness and the amount of financial inflows from abroad has been presented by several cross-national studies.

The experiences of debtor countries during the 1920s and 1930s has been examined by Suter (1990: 70-82, 209-304) for the years 1926-1929 and Eichengreen and Portes (1986) for 1930-1938. Since the interwar loan boom period already collapsed by 1930, the time period covered by Eichengreen and Portes, however, is not appropriate for an analysis of international borrowing. The most important single variable to explain the stock of external debt held by borrowing countries in the late 1920s as well as the 1930s is the country size of a borrower, measured by the gross domestic product and the size of population, which may be considered rough indicators for creditworthiness. This finding confirms the conclusion made in the previous section that the principal sovereign borrowers usually were countries with a relatively large economic potential. Variables measuring the performance of debtors' economic, fiscal and monetary policies and external influences of world market developments (growth of GDP, export growth, import propensity, balance of trade, budget deficit, international reserves, export variability, terms of trade) show no impact on foreign debt. This suggests that creditors limited their decision to lend on rather vague criteria (like GDP and population), which may be attributed to the lack of development planning by debtors.[22]

Determinants of the stock of external debt and of debt inflows for the loan boom period of the 1970s have been examined by Eaton and Gersovitz (1980, 1981), Rothgeb (1986) and Pfister and Suter (forthcoming). Eaton and Gersovitz (1981), who considered accumulated debt during the early 1970s as a dependent variable, found a positive relationship between level of indebtedness and country size, import propensity and export fluctuation. The strong correlation between GDP and level of indebtedness is confirmed by Pfister and Suter (forthcoming), who examined net inflows of government loans extended by private creditors to 69 Third World countries for the periods 1970-1975 and 1975-1980. In addition, the size of investment rates and the presence of a development-oriented political regime are important explanatory variables suggesting that debt was incurred to raise resources for development financing rather than to overcome external shocks (e.g. export fluctuation as a result of world market developments) or to substitute international reserves, as argued by Eaton and Gersovitz (1980, 1981) and Edwards (1984). This result is consistent with growth cum debt models suggesting a positive relationship between external debt and long-term economic growth.[23]

Pfister and Suter (forthcoming) and Rothgeb (1986) also demonstrate that the degree of external borrowing is associated with the dependence of borrowing countries on foreign equity capital as measured by the ratio of capital stocks invested by transnational corporations to total capital stock. Specifically, peripheries which are highly dependent on foreign equity capital are also more heavily indebted than less-dependent borrowers.[24] This finding supports the argument of dependency theorists suggesting a growing demand for financial resources by Third World countries heavily dependent on foreign equity investment due to the decapitalization effects resulting from repatriation of profits by transnational corporations.[25]

Summing up, there are similarities and differences concerning the determinants of foreign government borrowing between the two loan boom periods of the late 1920s and the 1970s as evidenced by cross-national analysis. On the one hand, the country size is the most important factor determining the level of debt in both phases. On the other hand, the financing of growth and developmentalist strategies and the dependence on foreign equity capital emerge as additional variables explaining the loan boom of the 1970s. The differences can be explained by the spread of economic growth and development as a global value pursued by virtually all countries as well as the consequent expansion of the nation-state into the economic sphere and by the trend towards transnationalization of capital.

Cross-National Research on Growth Effects of Debt Dependence

The impact of external debt on economic growth of borrowing countries during the postwar period has been investigated by several empirical studies using cross-national research designs. In regard to foreign aid, its effects on economic development appear to be positive, at least for the least-developed countries (Papanek 1972, 1973, Stoneman 1975, Mosley 1980). Research carried out by the author suggests similar results for the 1970s (Pfister and Suter forthcoming), whereas Mosley (1987) found no substantial relationship. On the other hand, stocks of debt outstanding vis-à-vis private creditors (mainly bank syndicates) were negatively related to growth during the second half of the 1970s (Pfister 1984, Pfister and Suter forthcoming).[26] This relationship is particularly strong, first, for countries which do not belong to the group of newly industrializing countries with rapidly growing export markets. Second, the negative relationship between stocks of bank credits and economic growth is particularly visible in a subset of countries with political regimes preoccupied less with economic development than with supporting a large state class and/or maintaining or enlarging their legitimatory base. This supports the contention that low returns on external debts may be associated with their widespread use for unproductive or consumptive purposes.

Notes

1. See the annual reports of the British bondholders hereafter referred to as CFB. The following example may illustrate the general statements made in the text. The loan conditions for the foreign bond raised by the Ottoman empire in 1855 for financing the Crimean War were very favorable for the Empire (interest rates of 4 percent, price of issue of 102.6) since interest payments were guaranteed by the allied British and French governments. By contrast, the loan negotiated by the same borrowing country in 1874 during a period of serious financial and political stress was rather unfavorable (interest rate of 5 percent, price of issue of 43.5; cf. CFB, *Annual Report*, 1877: 60-73). A detailed analysis of the Ottoman foreign debt is presented in Chapter 10.

2. Cf. Peña (1907) for the case of foreign bonds raised by Argentina.

3. Feis (1930: xii).

4. Madden et al. (1937: 93).

5. Abbott (1979: 16).

6. Cf. Abbott (1979), Wood (1986).

7. These international agencies could not act autonomously. The credits they extended had to be guaranteed by the central banks of individual member countries (cf. Kindleberger 1973: 150-162).

8. Mason and Asher (1973: Chapter 2), Block (1977: Chapter 3), and Cohen (1983).

9. Lipson (1981).

10. Cf. Bornschier and Chase-Dunn (1985), and Bornschier and Stamm (1990) for a survey of the literature on foreign direct investment.

11. The Argentine state, for instance, supported foreign railway companies with generous profit guarantees until 1907 (cf. Ferns 1960: 343-355).

12. Direct estimates of new foreign capital issues have been developed by Jenks (1927: 419-426), Hobson (1914: 219), Cairncross (1953: 183) and Simon (1967). The second method (capitalizing yields) has been used by Paish (1909), and Feis (1930). The indirect method based on the balance-of-payments accounts has been applied by Hobson (1914), Cairncross (1953), and Imlah (1958) for Great Britain; White (1933) and Lévy-Leboyer (1977a) for France; and Williamson (1964) for the United States.

13. Cf. Lévy-Leboyer (1977a) and the classical study by Imlah (1958).

14. Cf. Bloomfield (1968).

15. The statistical material presented by Simon (1967) shows the same cyclical pattern for direct estimates of new foreign capital issues in Great Britain. The geographical breakdown suggests that this pattern of Kuznets cycles is confined to North and South America, i.e. to the principal areas integrated into the Atlantic economy. Conversely, the figures for capital exports to continental Europe show cyclical fluctuations of the Kondratieff type.

16. Cf. Lévy-Leboyer (1977a: 132).

17. The peak in the 1820s for the British series becomes more clearly visible when growth rates of total accumulated credits abroad are calculated.

18. Since 1986 the United States has belonged to the largest official net debtors of the world as well. At the end of 1987, U.S. external public debt amounted to about $370 billion.

19. Cf. Feis (1930), Cameron (1961), Simon (1967) and Lévy-Leboyer (1977a, 1977b) for a more detailed discussion.

20. OECD (1984: 56).

21. See Williamson (1964), Bloomfield (1968: 37-38) and Edelstein (1982: 91) for U.S. capital imports during the nineteenth century; Bloomfield (1968: 37) and Richardson (1972: 107) for the case of Australia; and Ford (1971) for Argentina.

22. Eichengreen and Portes (1986) also report significant positive effects for the ratio of imports to GDP and negative ones for the growth of GDP. The variance explained by their models is, however, extremely low. Moreover, a replication of this model for the late 1920s revealed no significant relationships (Suter 1990: 302). Eichengreen and Portes (1986) also present regression estimates with debt inflows as the dependent variable. Yet, their models are rather inadequate and seem to suffer from heavily skewed distributions and from problems of multicollinearity. Thus, although in a sample of 20 countries only the regional dummy variable for Australia shows a significant effect on flows of government borrowing, explained variance is reported to be extremely high (R^2=0.93).

23. The level of the investment rate (apart from the capital-output ratio) is a basic variable determining economic growth on the national level as well as of

the savings gap to be filled by external capital (see Avramovic 1964 and the arguments of gap theories outlined in Chapter 1).

24. The regression model presented by Pfister and Suter (forthcoming) with private debt inflows from 1970 to 1975 as the dependent variable shows statistically significant coefficients for the *level* of dependence on foreign equity capital. By contrast, there is no substantial relationship between debt inflows and *new inflows* of foreign direct investment.

25. Bornschier and Chase-Dunn (1985).

26. For other systematic cross-sectional investigations evidencing low or negative growth effects of external debt, see Nikbakht (1984), World Bank (1985: 45-70) and Sharma (1986).

5

Global Debt Crises

As indicated by the preliminary analysis of default and rescheduling incidence in the Introduction, global debt crises occurred repeatedly in the capitalist world-economy. The concept of "debt crisis" as utilized in this study is defined as the incapacity or unwillingness of sovereign borrowers to meet their debt-service obligations.

There is a large body of literature dealing with the historical dimension of debt crises. These studies examine the long-run experiences of individual debtor countries on the one hand,[1] as well as the response of official and private creditors to debt problems on the other.[2] In addition, specific crises have been studied in some depth.[3] Thus, one has to conclude that there is a lack of studies examining debt crises explicitly on the global level of the world-economy.

This chapter describes and explains occurrences and characteristics of global debt crises in more detail, using quantitative indicators aggregated on the global level of the world-economy covering virtually all cases of debt-service incapacity from 1820 to 1989. The examination of the cyclical pattern of global debt crises will be followed by a comparative cross-national analysis of determinants of the two global debt crises of the 1930s and 1980s.

The Cyclical Occurrence of Global Debt Crises

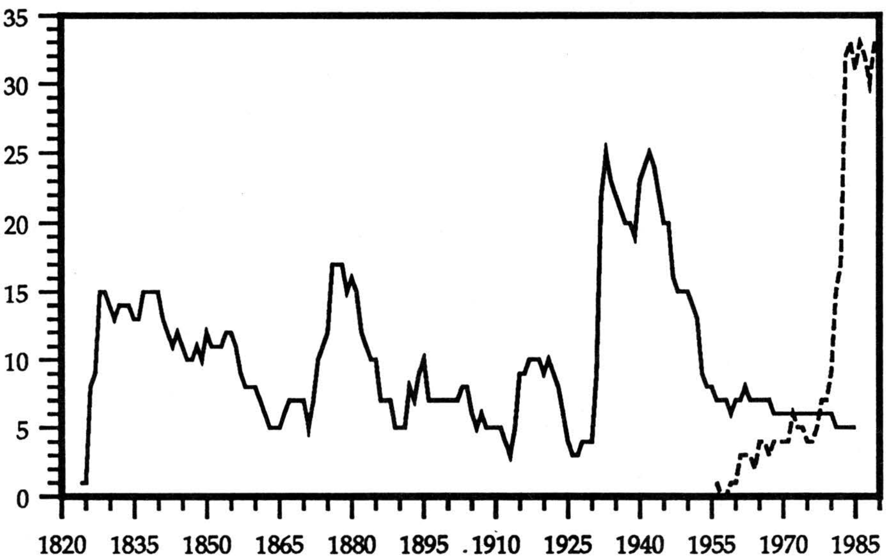
Before World War II debt-service incapacity of sovereign borrowers manifested itself chiefly in defaults on foreign government bonds. Since defaults were unilaterally declared by the borrowing country without creditors' consent, they implied a violation of the loan contract. The forms of debt-service incapacity varied substantially. Usually, a defaulting country principally accepted its debt obligations vis-à-vis creditors but did not transmit interest and/or amortization payments on the date stipulated by the loan contract. A much more serious form of debt-service incapacity was repudiation, which, however, took place only very rarely. Repudiation implies that the borrowing government does not recognize the debt obligations.[4] At the other end of the spectrum are debt consolidations. Since these arrangements were concluded before the debtor country fell into arrears on debt-service payments, they did not imply a violation of the loan contract.[5] As a result of the changes in the dominant financial instruments as described in Chapter 4, foreign bonds were substituted by credits granted by a few core actors (core governments, international organizations, large bank syndicates). The consequent institutionalization of creditors' cooperation led to the emergence of multilateral reschedulings as the dominant form of debt-service incapacity which, like the above-mentioned debt consolidations, prevented the outbreak of open default.[6]

Although defaults and reschedulings differ in many respects they may be considered to be equivalent as general measures for the occurrence of debt-service incapacity. Hence, the following examination of the pattern of global debt crises occurring during the nineteenth and twentieth centuries is based on two measures of debt-service incapacity: the number of sovereign borrowers in default between 1820 and 1985 on the one hand and the occurrence of multilateral rescheduling arrangements between 1956 and 1989 on the other. Since the international state system has substantially changed with respect to the number of nation-states during the nineteenth and twentieth centuries, these two indicators are calculated both in absolute numbers and relative to the number of all sovereign nation-states.

Yearly figures of these four indicators are plotted in Figures 5.1 and 5.2.[7] They show a clear cyclical movement of occurrence and duration of global debt crises. Peaks of global debt crises can be found in 1827-1841, 1875-1882, 1932-1945 and 1982-1989, troughs in 1820-1824, 1857-1866, 1905-1913 and 1955-1978. Thus, fluctuations in the number of sovereign borrowers experiencing debt-service incapacity appear to move largely parallel to Kondratieff waves, with high default and rescheduling propensity during downswing periods. In addition to these long cycles there are also fluctuations of shorter duration. The slight clustering of defaults in 1891-1898 and 1914-1921 together with the periods of the 1870s and 1930s mentioned above may be interpreted as cycles of the Kuznets type.

The number of countries facing debt-service incapacity continuously increased from 15 (1828-1829) to 17 (1876-1878), 25 (1933) and 33 (1984-1989) from the first global debt crisis of the late 1820s to the present crisis. This increase can be explained in part by the expansion of the international state system. Thus, as shown in Figure 5.2, the difference

FIGURE 5.1 Number of Countries in Default (solid line) or Involved in Reschedulings (broken line)

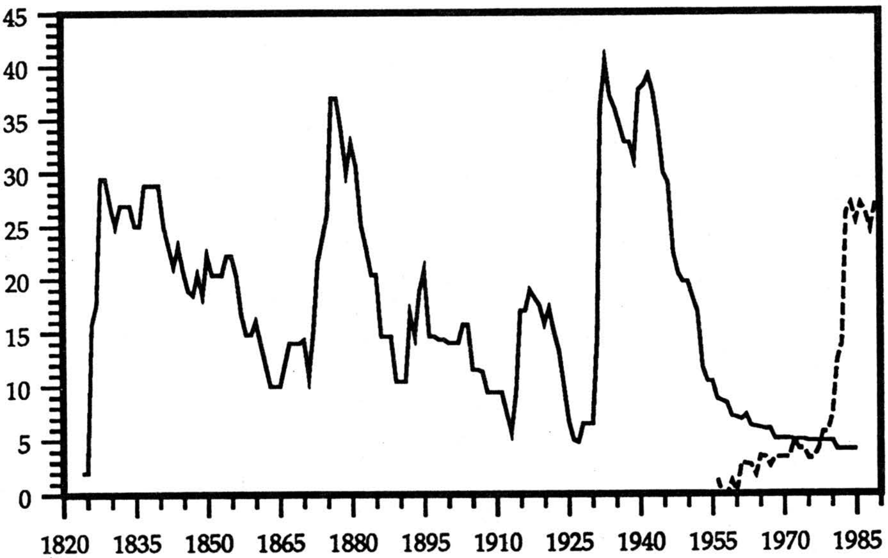


Sources: From "Global Debt Cycles and the Role of Political Regimes," by Christian Suter and Ulrich Pfister in *Markets, Politics, and Change in the Global Political Economy,* edited by William P. Avery and David P. Rapkin. Copyright 1989 by Lynne Rienner Publishers, Inc. Used with permission from the publisher. See also Appendix, and Suter (1990: 235-285), and Pfister and Suter (forthcoming: Appendix).

between the four principal global debt crises concerning the proportion of the number of countries in default or involved in reschedulings relative to all independent nation-states is less marked (29 percent in 1828-1829, 37 percent in 1876, 40 percent in 1933 and 27 percent in 1984-1989).

The indicators used in Figures 5.1 and 5.2 focus on the duration of global debt crises. Since most insolvent debtor countries remained in default for several years, the aspect of the crisis *outbreak* is measured only approximately. A more adequate indicator in this respect is presented in Figure 5.3 in which the number of countries falling in default per five-year periods from 1821/25 to 1981/85 is shown. The data are confined to defaults on foreign bonds since the consolidation period of reschedulings as shown in Figures 5.1 and 5.2 has usually been limited to one year.

FIGURE 5.2 Number of Countries in Default (solid line) or Involved in Reschedulings (broken line) as a Percentage of All Nation-States

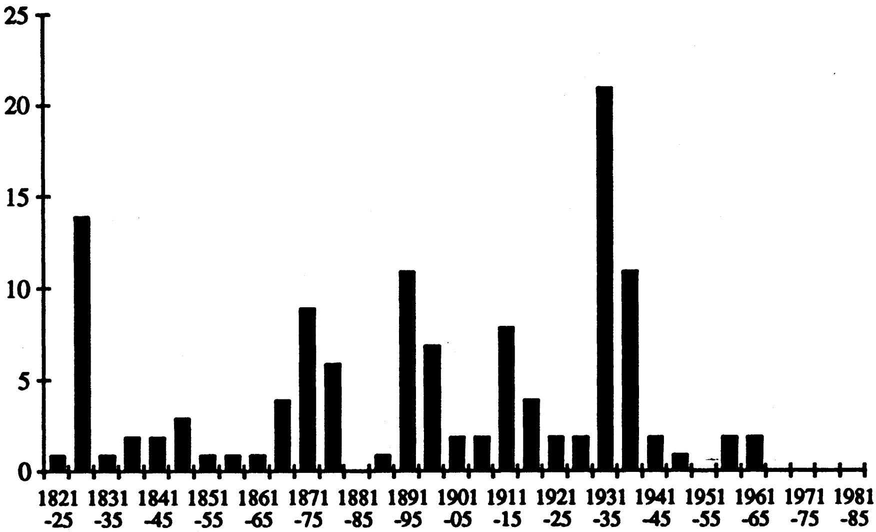


Sources: CFB (*Annual Reports,* 1873-1985), Suter (1990: 235-285), World Bank (*World Debt Tables,* 1990/91), Pfister and Suter (forthcoming: Appendix); cf. also Appendix.

Figure 5.3 reveals that at least one or two defaults occurred every five years from 1821 until the late 1940s except during the years 1881-1885. In addition to this constant level of debt-service incapacity, five crisis periods which coincided with the periods identified above are clearly visible (1826-1830, 1871-1880, 1891-1900, 1911-1915, 1931-1939), with 8-21 countries declaring default within the respective five-year period. Compared to the pattern of crisis duration as visible in Figures 5.1 and 5.2, the debt crises of the 1890s and of the years 1911-1915 are much more pronounced.

The empirical material concerning the outbreak and duration of debt-service incapacity supports the basic hypothesis that global debt crises occur during stagnation periods of global growth cycles.[8] Table 5.1 presents a summary of this relationship. It demonstrates that global debt crises break out just at the beginning of a downswing period of Kondratieff growth cycles, with the exception of the current crisis, which shows a 10-year lag. While the outbreak of debt crises is confined to the early stagnation period, the duration of debt-service incapacity covers

FIGURE 5.3 Number of Countries Declaring Default on Foreign Bonds (Year of Default Begins in Five-Year Periods 1821/25 to 1981/85)[a]



[a] Defaults on amortization payments are excluded.

Sources: CFB (*Annual Reports*, 1873-1985), Suter (1990: 235-285).

the whole downswing phase and sometimes even the first years of the subsequent upswing.

The occurrence of global debt crises between 1870 and 1920 can also be related to the movement of the shorter Kuznets cycles. This applies specifically to the clustering of outbreaks of debt crises in the early 1890s and before World War I, which cannot be explained by Kondratieff growth cycles. In fact, the crisis of the 1890s affected mainly countries belonging to the Atlantic economy, i.e. that zone of the world-economy most notably characterized by the movement of Kuznets cycles.[9] By contrast, the outbreak of the crisis of 1911-1915 has to be attributed to a political phenomenon, namely, the outbreak of World War I, rather than to the logic of economic processes operating within the Atlantic economy.[10]

The empirical discussion has so far concentrated on the calculation of the number of insolvent sovereign borrowers. An additional measure describing the extent of global debt crises more accurately refers to the share of foreign loans blocked in defaults or reschedulings relative to total foreign investment. This indicator has been computed for defaulted

TABLE 5.1 Outbreak and Duration of Global Debt Cycles and Kondratieff Growth Cycles

Number of Kondratieff Wave	*I*	*II*	*III*	*IV*
Downswing of Kondratieff	1825-1845	1872-1892	1929-1948	1973-
Outbreak of Global Debt Crises[a]	1826-1830	1871-1875	1931-1935	1981-1985
Duration of Global Debt Crises[b]	1828-1856	1873-1885	1932-1950	1983-

[a]Peaks of outbreak of defaults in 5-year periods as shown in Figure 5.3 for cycles I-III and number of reschedulings for the fourth Kondratieff wave.

[b]Duration of global debt crises as indicated by the proportion of countries in default or involved in rescheduling relative to all nation-states. Only proportions greater than 20 percent have been considered.

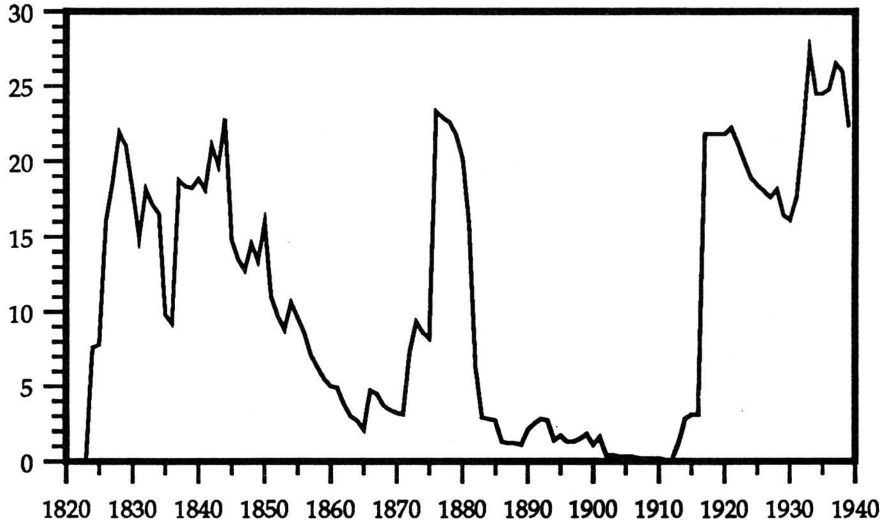
Sources: CFB (*Annual Reports*, 1873-1985), Van Duijn (1983), Suter (1990: 235-285), Pfister and Suter (forthcoming: Appendix).

foreign government bonds for the period 1823-1939 and is shown in Figure 5.4. Since annual data are unavailable for either foreign loans blocked in defaults or for stocks of total foreign investment, this indicator is a rather rough measure and should, therefore, be interpreted with caution.

Figure 5.4 reveals three principal crisis periods. The first crisis falls into the first half of the nineteenth century and reaches its peak in 1828-1829 and 1844 with a share of blocked loans of 22 percent. During the 1850s and 1860s, frozen credits continuously declined to a minimum of 2 percent in 1865. A second crisis emerged during the early 1870s with its peak in 1876-1878, when 23 percent of foreign bonds were in default. During the 1880s the share of blocked loans rapidly decreased and remained at a low level until World War I. As a result of the Soviet default on external debt contracted by tsarist Russia, the figure shot up to 22 percent by 1918 but declined again to 16 percent during the 1920s. In the wake of the world economic crisis of the 1930s, the share of frozen assets rose to a maximum of 27 percent in 1933. Concerning the extent to which periphery debt was blocked in rescheduling during the debt crisis of the 1980s, a rough estimate of Pfister and Suter (1987: 242) suggests an even higher level of frozen assets. Based on World Bank figures and the amounts of credits subject to reschedulings, they estimated that up to 40 percent of outstanding long-term international credits were blocked in reschedulings by 1983.

In the relevant literature, there are several estimates of the percentage of foreign bonds in default concerning the crisis of the 1930s. Thus,

FIGURE 5.4 Share of Foreign Bonds in Default Relative to Total Foreign Investment of Major Core Countries, 1823-1939[a]



[a]Foreign investment of major core countries refers to accumulated net capital exports of Great Britain (1823-1939), France (1833-1939), Germany (1880-1913), and the United States (1914-1939). Data for foreign bonds in default are available for the nominal value only. To adjust for the discount at which foreign bonds were sold to the public, the nominal value of all bonds raised prior to World War I has been reduced by 20 percent (except for Spain and Portugal, whose foreign bonds were discounted by 60 percent). These discount figures are based on data for price of issues of foreign government bonds offered during the nineteenth century (cf. Suter 1990: 94 for more details).

Sources: CFB (*Annual Reports,* 1873-1940) and Suter (1990: 233-282) for the value of defaulted foreign bonds and their price of issue, Imlah (1958: 70-77) and Feinstein (1972: T37-T39) for British foreign investment, Lévy-Leboyer (1977a: 119-121, 135) for French foreign investment, Hoffmann (1965: 263) and Bloomfield (1968: 42-43) for German foreign investment, United Nations (1949: 2, 41) and Williamson (1964: 255-257) for U.S. foreign investment.

according to Abbott (1979: 24-25), 35 percent of all British capital invested in foreign government bonds and 35-40 percent of dollar-denominated bonds were in default by the mid-1930s. Similar figures are reported by Madden et al. (1937: 123), Lewis (1938: 398) and Wynne (1951a: xxiii) concerning the share of frozen U.S. assets, whereas Wynne (1951a: xxii) estimated the share of blocked foreign British investment to be only less than 30 percent. The figures presented in Figure 5.4 are substantially lower (e.g. a maximum of 27 percent in 1933). This may be attributed to the fact that defaulted bonds are related to total foreign investment (and not to investments in foreign government bonds only) of the four principal creditor countries (and not of a single lender only). This suggests that the estimates made in this study are rather conservative.[11]

Basically, fluctuations of the share of blocked loans correspond to the pattern of debt crises as indicated by the measures based on the number of insolvent debtor countries outlined above. Phases of high shares of blocked credits (late 1820s to 1840s, late 1870s, 1930s) fall into stagnation phases of the world-economy, thus confirming the hypothesis on the relationship between global debt crises and global growth cycles. In addition, Figure 5.4 also provides some new insights. First, both the initial and second crisis cycle are characterized by two peaks which may be interpreted as fluctuations of the Kuznets type. In fact, the crisis peak of the 1840s is mainly due to the defaults of nine U.S. states (i.e. an area strongly integrated into the Atlantic economy) in the wake of the collapse of the cotton boom.[12] On the contrary, the crisis peak during and after World War II was caused mainly by defaults of sovereign borrowers outside the Atlantic economy (Soviet Union, Ottoman Empire, Mexico) and was a consequence of the war and of revolutions. Second, there is no debt crisis visible during the 1890s (as indicated by Figures 5.1-5.3) based on the number of insolvent debtor countries as a measure for the occurrence of debt crises. Thus, although there were prominent borrowers facing debt-service incapacity during the 1890s (e.g. Argentina), this crisis was generally confined to small amounts.

To sum up, the different measures and indicators used to describe the global debt crises suggest four principal crisis periods, namely, the late 1820s, the 1870s, the 1930s, and the 1980s. They are characterized by high levels of both the number (or proportion) of insolvent debtor countries and the share of blocked credits. In addition, three minor debt crises either confined to the number of countries facing debt-service incapacity or to the share of blocked loans can be identified during the 1840s, the 1890s as well as during and after World War I.

The geographical focus of these seven debt crises is shown in Table 5.2. The principal defaulters in the first half of the nineteenth century were Spain, the United States (state bonds), Mexico and Greater Colombia. During the debt crisis of the 1870s, the Ottoman Empire, Spain, and Egypt were by far the largest defaulting countries. In addition, substantial amounts were defaulted by Peru and Mexico. The debt crisis of the 1890s concerned Argentina, Portugal, Brazil, Greece and Uruguay. In the 1930s the center of debt-service incapacity shifted

TABLE 5.2 Debt Crises and Major Countries in Default or Involved in Reschedulings

Period	*Country (estimated amount of defaulted/rescheduled debt in millions of U.S. dollars in parentheses)*
1826-1830	Spain (100),[a] Greater Colombia (32), Mexico (26), Brazil (18), Greece (14), Peru (9), Argentina (5), Chile (5).
1840-1845	Spain (160),[b] 9 U.S. states (120), Mexico (54), Portugal (44).[b]
1875-1882	Ottoman Empire (1000), Spain (850), Egypt (ca. 440), Mexico (170),[c] 10 southern U.S. states (158), Peru (150), Colombia (32), Tunisia (30),[d] Honduras (26), Uruguay (15), Costa Rica (13), Bolivia (8).
1890-1900	Argentina (360), Portugal (300), Brazil (146), Greece (100), Uruguay (83), Serbia (68), Dominican Republic (32), Venezuela (22), Colombia (13).
1911-1915	Russia (8500),[e] Ottoman Empire (720), Mexico (500), Bulgaria (160).
1931-1940	Germany (2200), Brazil (1267), Romania (580), Mexico (500),[f] Greece (380), Chile (376), Austria (325), Yugoslavia (320), Poland (300), Hungary (250), Colombia (151), Turkey (140), Uruguay (130), Peru (120).
1982-1986[g]	Mexico (74000), Brazil (28000), Argentina (24000), Poland (22000), Venezuela (21000), Nigeria (11000), Turkey (11000), Yugoslavia (10200), South Africa (10000), Chile (9400), Ecuador (6800), Philippines (4200), Morocco (4000), Romania (4000), Sudan (3600), Peru (3000), Uruguay (2700), Zaire (2400).

[a]Suspension of 1824.
[b]Suspension of 1837.
[c]Suspension of 1866.
[d]Suspension of 1867.
[e]Suspension of 1918.
[f]Suspension of 1928.
[g]Estimates for the total amount of rescheduled debt for the years 1982-1986, in the case of Turkey for the years 1979-1986.

Source: Suter (1990: 235-284).

to Europe and Latin America, with Germany, Romania, Brazil and Mexico as main defaulters on foreign dollar bonds. Similarly, in the course of the present debt crisis, debt-service difficulties are concentrated in Latin America (e.g. Brazil, Mexico, Venezuela, and Argentina) and in the peripheral areas of Europe (e.g. Yugoslavia, Poland, and Turkey). Several African borrowers have been affected as well (e.g. Nigeria, South Africa, Morocco, Sudan, Zaire).

TABLE 5.3 Default on Foreign Government Bonds, 1820-1985, by Country

Country	*Years of Debt-Service Incapacity*[a]
Argentina	1828-57, 1890-93
Austria	1868-70,[b] 1914-15, 1932-33, 1938, 1940-52
Bolivia	1875-79, 1931-48
Brazil	1826-29, 1898-1901, 1902-10,[b] 1914-19,1931-33, 1937-43
Bulgaria	1916-20, 1932-
Chile	1826-42, 1880-83,[b] 1931-47
China	1921-36, 1939-
Colombia	1826-45, 1850-61, 1873,[b] 1880-96, 1900-04, 1932-34,[b] 1935-44
Costa Rica	1828-40, 1874-85, 1895-97, 1901-11, 1932-52, 1962
Cuba	1933-34, 1960[bc]
Czechoslovakia	1938-46, 1960-
Dominican Rep.	1872-88, 1892-93, 1897, 1899-1907, 1931-34[b]
Ecuador	1826-55, 1868-90, 1894-98, 1906-08, 1909-11, 1914-24, 1929-54
Egypt	1876-80
El Salvador	1828-60, 1898, 1921-22, 1932-35, 1938-46
Germany (FRG)	1932-38, 1939-53
Germany (GDR)	1949-
Greece	1826-78, 1894-97, 1932-64
Guatemala	1828-56, 1876-88, 1894, 1899-1913, 1933-36
Honduras	1828-67, 1873-1925
Hungary	1932-37, 1941-67
Italy	1940-46
Japan	1942-52
Liberia	1875-98, 1912,[b] 1914-15,[b] 1917-18,[b] 1919-23, 1932-35
Mexico	1828-30, 1833-41, 1844-50, 1854-64, 1866-85, 1914-22, 1928-42
Morocco	1903-04
Nicaragua	1828-74, 1894-95, 1911-12, 1915-17, 1932-37[b]
Otto. Emp./Turkey	1876-81, 1915-28, 1931-32, 1940-43
Panama	1932-46
Paraguay	1874-85, 1892-95, 1920-24, 1932-44
Peru	1826-48, 1876-89, 1931-51
Poland	1936-37, 1940-52
Portugal	1837-41, 1850-56, 1892-1901
Romania	1933-58
Soviet Union	1918-
Spain	1824-34, 1837-67, 1827-82
Tunisia	1867-70
Uruguay	1876-78, 1891, 1915-21,[b] 1933-38
USA (states)	1842-44, 1873-81
Venezuela	1826-40, 1848-59, 1860-62, 1865-81, 1892, 1898-1905
Yugoslavia	1895,[b] 1933-50
Zimbabwe	1965-80

[a]Years with debt-service incapacity of 6 months or longer.
[b]Consolidation loan, partial default or suspension of amortization only.
[c]Data for resumption of debt-service payments not available.

Source: Data appendix of Suter (1990: 235-284) and Marichal (1989).

TABLE 5.4 Official and Private Multilateral Reschedulings, 1956-1989, by Country

Country	*Consolidation Period*[a]	*Country*	*Consolidation Period*[a]
Angola	1989	Mauritania	1985-89
Argentina	1956, 1961-65, 1983-88	Mexico	1983-89
Bangladesh	1974	Morocco	1983-89
Bolivia	1981-87, 1989	Mozambique	1984-88
Brazil	1961-65, 1983-89	Nicaragua	1980-84
Cambodia	1972-73	Niger	1984-89
Cameroon	1989	Nigeria	1983, 1986-87, 1989
Cent. Af. Rep.	1981, 1983, 1985-86, 1989	Pakistan	1971-78, 1981-82
Chile	1965-66, 1972-75, 1983-89	Panama	1983-86
Congo	1986-88	Peru	1968-72, 1978-80, 1983-85
Costa Rica	1982-86, 1989	Philippines	1984-89
Cuba	1983-86	Poland	1981-89
Domin. Rep.	1983-89	Romania	1982-83, 1986-88
Ecuador	1983-89	Senegal	1981-89
Egypt	1987-88	Sierra Leone	1976-81, 1984, 1986-87
Gabon	1978, 1987-89	Somalia	1984-85, 1987-88
Gambia	1987	South Africa	1986
Ghana	1966-74	Sudan	1980-85
Guinea	1986, 1989	Tanzania	1986-87, 1989
Honduras	1983-84, 1986-89	Togo	1979-85, 1988-89
India	1968-77	Trinid./Tob.	1989
Indonesia	1966-70	Turkey	1959-63, 1965-67, 1977-83
Ivory Coast	1984-89	Uganda	1981-83, 1987-89
Jamaica	1978-89	Uruguay	1983-89
Jordan	1989	Venezuela	1983-88
Liberia	1980-85	Yugoslavia	1983-89
Madagascar	1981-89	Zaire	1975-82, 1984-89
Malawi	1982-84, 1988-89	Zambia	1983-86
Mali	1988-89		

[a]Years with consolidation period of 6 months or longer.

Sources: Data appendix of Pfister and Suter (forthcoming) for 1956-1986, World Bank (*World Debt Tables*, 1990/91) for 1987-1989.

A comparison of the principal countries facing debt-service difficulties and the largest debtor countries (cf. Chapter 4, Table 4.1) shows that countries that borrow heavily are not necessarily those that go into default during crises following a boom period. Apart from the southern U.S. states in the two crises of the nineteenth century and Germany in the 1930s, the countries figuring among the more highly developed ones (mostly the former European periphery but also the U.S. government during the 1870s, Australia, Canada, Japan, Argentina during the 1930s and South Korea during the 1980s) are much less represented among defaulting countries than among the main recipients of international capital. Hence, it appears that global debt crises usually break out at the periphery of the world-system.

Several peripheral debtor countries repeatedly encountered debt-service difficulties during the nineteenth and twentieth centuries. This is documented by Tables 5.3 and 5.4, which list the debtor countries and the years of their debt-service incapacity. Concerning defaults on foreign government bonds, Ecuador and Mexico take the lead with seven defaults, followed by Costa Rica, Colombia and Venezuela with six and Brazil, the Dominican Republic, El Salvador, Guatemala, Liberia, Nicaragua and Austria-Hungary with five each. The most notorious defaulters were obviously Latin American countries. With respect to the number of multilateral reschedulings concluded during the postwar period, Zaire (which negotiated seventeen agreements) is the borrowing country which had to restructure external debt most often. Peru and Poland (twelve arrangements each) come next followed by Sudan (ten reschedulings), and Turkey (nine).[13] Thus, contrary to the defaults of earlier debt crises which were concentrated in Latin America, the debtor countries most frequently involved in reschedulings during the postwar period are spread throughout all major geographic regions and zones of the world-economy. Obviously, the expansion of the international state system in the wake of decolonization was accompanied by a corresponding spread of debt-service incapacity.

Debt-service incapacity of borrowing countries often continued for several years or even decades. This is illustrated by Table 5.5 containing the duration of defaults and consolidation periods of reschedulings by debtor country. The figures show that Ecuador, experiencing debt-service incapacity during 97 years (94 years of default, 3 years of reschedulings) of the period 1820-1985, is the debtor country with the poorest debt-service performance. Honduras with 93 years (91 years of default, 2 years of reschedulings) of state insolvency and Greece with 88 years did not fare much better. Except China, the debtor countries with the poorest debt record belong either to Latin America (Ecuador, Honduras, Mexico, Peru, Colombia, Nicaragua, Costa Rica, Guatemala) or to the European periphery (Greece, Soviet Union, Bulgaria).[14] This confirms our finding concerning the geographical focus of major debt crises as discussed above, which showed that debt-service incapacity was concentrated in Latin America and peripheral areas of Europe.

TABLE 5.5 Duration of Debt-Service Incapacity of Debtor Countries, 1820-1985

Debtor Country[a]	*Def.*[b] *(years)*	*Res.*[c] *(years)*	*Total*[d] *(years)*	*Debtor Country*[a]	*Def.*[b] *(years)*	*Res.*[c] *(years)*	*Total*[d] *(years)*
Ecuador	94	3	97	Dominican Rep.	29	3	32
Honduras	91	2	93	Hungary	31	-	31
Greece	88	-	88	Paraguay	30	-	30
Mexico	67	3	70	Bolivia	23	5	28
Soviet Union	67	-	67	Austria	21	-	21
Peru	55	11	66	Serbia-Yugoslavia	18	3	21
Colombia	63	-	63	Germany (FRG)	19	-	19
China	61	-	61	Portugal	19	-	19
Nicaragua	56	5	61	Panama	15	3	18
Costa Rica	55	4	59	Poland	13	5	18
Guatemala	58	-	58	Uruguay	14	3	17
Bulgaria	56	-	56	Zimbabwe	15	-	15
Venezuela	51	3	54	India	-	10	10
Spain	50	-	50	Japan	10	-	10
El Salvador	45	-	45	Pakistan	-	10	10
Romania	43	2	45	USA (states)	10	-	10
Chile	35	9	44	Zaire	-	10	10
Argentina	32	9	41	Ghana	-	9	9
Liberia	34	6	40	Jamaica	-	8	8
Otto. Emp./Tur.	22	15	37	Sierra Leone	-	7	7
Brazil	29	8	37	Togo	-	7	7
Germany (GDR)	36	-	36	Italy	6	-	6
Czechoslovakia	33	-	33	Sudan	-	6	6

- = no defaults or no reschedulings.

[a]Only debtor countries experiencing debt-service incapacity for more than 5 years are included.

[b]Duration of defaults.

[c]Consolidation period of reschedulings.

[d]Sum of duration of defaults and consolidation period of reschedulings.

Sources: CFB (*Annual Reports*, 1873-1985), Suter (1990: 98, 235-285), Pfister and Suter (forthcoming: Appendix).

Determinants of Debt-Service Incapacity: A Comparison of Cross-National Evidence for the 1930s and the 1980s

As demonstrated by the empirical material in the previous section, global debt crises have repeatedly emerged in pronounced sequences at the beginning of longer stagnation phases of the world-economy. The basic explanatory model on the relationship of global debt and growth cycles attributes these developments to the following three complementary factors (cf. Chapter 3).

First, due to economic stagnation in the core and the consequent stagnation or even decline of world trade, export earnings of peripheral debtor countries tend to shrink. This increases the burden of debt-service payments and reduces import capacity. Insofar as the debtor country is forced to cut back imports necessary for the maintenance of production, economic growth and development are adversely affected. The financial losses of shortfalls on export receipts may be financed temporarily by new external borrowing which, however, further increases debt service. In the long run, declining export earnings coupled with rising debt-service payments result in serious debt-service incapacity.

Second, debt-service incapacity is caused by inefficient and consumptive use made of external financial resources. On the one hand, this may be due to the financing of import-substituting industrialization strategies by external capital. The development model of importsubstitution is associated with growing import requirements of the industrial sector and a consequent need of foreign exchange and often leads to misallocation of resources. On the other hand, governments of peripheral states may resort to politically relevant but economically questionable allocation of foreign capital to maintain or enhance their legitimacy. Such is the case for many infrastructural projects providing amenities for particular groups important to the regime in power but with rather low growth effects, even in the long run. The same holds true for a great number of transfer payments, particularly of subsidies for food and petrol prices. These politically motivated expenditures become problematic when they cannot be met by an adequate tax base and when the government has to resort to external borrowing instead. In this case, payment obligations are incurred without assuring higher income flows.

Third, the outbreak of debt crises can be triggered by creditors' behavior. Thus, declining confidence of foreign investors in the creditworthiness of the borrowing countries may result in a stop of further lending. As outlined in Chapter 2, this argument has been elaborated by theorists dealing with long swings of international capital movement within the Atlantic economy. Changing creditors' behavior has been attributed to initially overoptimistic assessment of yields by investors who did not fully take into account the gestation lag usually associated with large investment projects. Yet, the revision of creditors' risk assessment can also be caused by other factors, such as decreasing liquidity of international financial markets, poor debt-service performance by neighboring borrowing countries, etc.

During the 1970s and 1980s several empirical cross-sectional analyses investigated factors determining debt-service incapacity of sovereign borrowers. Most of them examine rescheduling probabilities during the 1960s and 1970s;[15] only Eichengreen and Portes (1986) deal with the incidence of default during the 1930s. While earlier studies used various statistical techniques,[16] recent work has mainly employed logit analysis, which proved most appropriate.[17] A rarely discussed methodological problem associated with logit analysis is the instability of estimates not only between different samples and studies but also between equations using a different set of explanatory variables,[18] which has to be attributed either to multicollinearity among independent variables or to the extremely skewed distribution of the dependent variable.[19]

Most empirical studies dealing with the incidence of rescheduling or default are based on the debt-servicing capacity models as developed by Avramovic (1964) and Dhonte (1975). As basic explanatory variables for debt-servicing capacity, several indicators of the extent of external indebtedness have been used, such as the debt-service ratio (i.e. the ratio of debt-service payments to export earnings), the ratio of external debt to GDP, the maturity of debt, new inflows of foreign capital and liquidity measures (e.g. the ratio of international reserves to imports). Recent studies have added structural economic variables (e.g. economic growth, growth of exports, rate of investment, income per capita, external shocks, rate of inflation). Their theoretical relevance remained, however, rather vague.[20]

The choice of the time period considered by these studies is rather arbitrary and not based on theoretical reasoning. Thus, most studies examining rescheduling probabilities focus on the 1960s and 1970s during which, however, only few cases of debt-service incapacity occurred. Eichengreen and Portes (1986) unfortunately limit their pioneering analysis of the 1930s to the period 1934-1938, i.e. to the years after the actual peak of the debt crisis. Obviously, the time period most relevant for an analysis of incidence of debt-service incapacity has to focus on the critical years of the initial outbreak of a global debt crisis manifested in the rapidly increasing number of insolvent debtor countries.

Consequently, the following cross-sectional analysis of the determinants of default and rescheduling incidence during the global debt crises of the 1930s and the 1980s covers the periods 1931-1933 and 1978-1985, both of which are characterized by an increasing number of debtor countries in default or involved in reschedulings from 9 to the maximum of 25 (1931-1933) and from 7 to 33 (1978-1985), respectively. As the statistical technique, logit analysis will be employed.[21] This allows regression analysis of a binary dependent variable taking the value of one for the countries in default or involved in reschedulings and of zero for the solvent countries. The sample is based on pooled data. For the 1930s it consists of 66 cases involving 23 countries[22] with 21 defaults, whereas the analysis for the 1980s relies on 627 cases, including some 80 peripheral and semi-peripheral countries and 127 observations for rescheduling.

The independent variables are derived from the theoretical arguments which have been developed above. In addition, several indicators discussed in the empirical literature will be included for comparative purposes and as control variables. The independent variables can be divided into the following six groups.

First, since the cross-sectional analysis uses pooled data, the year of the dependent variable is selected as an important control variable measuring the time trend. This indicator is expected to be positively related to the incidence of debt-service incapacity because the time period considered is defined by increasing numbers of default and reschedulings. It is expected, however, that this correlation can be explained by the effects of the other independent variables included in the model.

A second independent variable is a measure for the debt-service performance in the past. This indicator is computed as a dummy variable for the incidence of debt-service incapacity for the preceding 15 years in the case of the model for the 1930s and the preceding 5 years in the case of the analysis for the 1980s. On the one hand previous debt-service incapacity is a measure for the autocorrelation; on the other hand it can be considered as an indicator for the stigmatization of unsafe borrowing countries by the international financial community.

Third, several indicators reflecting the problem of stagnating or declining export receipts coupled with rising debt-service payments have been selected. A first variable is the ratio of debt service (interest and/or amortization payments) to exports. Another variable measures the growth of export receipts.

Fourth, two independent variables were selected to operationalize the aspect of the inefficient and consumptive use of external resources. A first indicator is economic growth, which is expected to be inversely related to the incidence of debt-service incapacity. Following Eichengreen and Portes (1986), deficit spending, i.e. the growth of the budget deficit of the central government, is used as another independent variable (only for the model of the 1930s).

A fifth category of independent variables refers to the impact of creditors' behavior. As argued above, it is expected that the stop or reduction of new lending is associated with high default and rescheduling probabilities. The indicators calculated include the ratio of new lending to GDP (for the 1930s) and the ratio of net transfers, i.e. disbursements minus interest and amortization payments (for the 1980s).

The last group includes a number of variables which proved useful in other empirical studies. The ratio of external debt to GNP has been used as a measure of the magnitude of debt burden as well as of the debt dependence from international financial markets of the borrowing country. Similarly, the ratio of exports to GDP is considered an indicator for the openness and the vulnerability of the debtor's economy from world market developments. The ratio of international reserves to imports is a liquidity measure. It takes into account that large foreign exchange reserves coupled with low imports may serve as a buffer against the outbreak of debt-service incapacity. Finally, following Eichengreen and Portes (1986), regional dummy variables for Latin America and the British Empire will be included for estimates referring to the crisis of the 1930s.

The results of the pooled cross-sectional logit analysis are presented in Table 5.6 for the crisis of the early 1930s and in Table 5.7 for the crisis of the late 1970s and early 1980s. As mentioned above in discussing methodological problems, logit analysis may suffer from instability. Therefore, several equations with a different combination of independent variables have been estimated.

Equation 1 in both tables shows the estimates for the time trend and for the previous debt-service incapacity. The equation shows an effect of the time trend for the model of the 1980s but not of the 1930s. As predicted, the effect of previous debt-service incapacity is positive and statistically significant for both crisis periods. This strong association is replicated in all other equations, indicating the relevance of processes of stigmatization of unsafe borrowers by creditors. The further equations show the results concerning the other independent variables. Although not all effects are statistically significant, they are quite consistent with the hypotheses on the relationship between global debt and growth cycles.

The basic argument that the combination of stagnating export receipts and rising interest and amortization payments provokes the outbreak of global debt crises is strongly supported by the positive effects of the debt-service ratio (for the model of the 1930s) and the ratio of interest payments to export earnings (for the model of the 1980s). The latter variable also partly explains the time trend of rising rescheduling incidence (cf. the low t-value for the time trend in equation 7 of Table 5.7). Growth of exports, which has only been included in the model for the 1930s, shows the expected negative effect on the incidence of default.

TABLE 5.6 Determinants of Default Incidence, 1931-1933 (pooled logit analysis, number of observations=66, regression coefficients, t-values in parentheses)[a]

	(1)	(2)	(3)	(4)	(5)	(6)
Year	0.0 (0.0)					
Previous Default	1.37 (3.69)	1.66 (3.52)	1.43 (3.66)	1.44 (3.67)	1.08 (1.77)	1.43 (2.52)
Debt-Service Ratio		7.93 (2.38)			8.83 (1.74)	8.46 (2.10)
Export Growth		-10.89 (-2.74)			-11.74 (-1.99)	-14.84 (-2.67)
Economic Growth			-0.11 (-2.07)	-0.11 (-2.07)	-0.08 (-0.96)	
Budget Deficit			0.02 (0.19)			
New Borrowing				-0.13 (-0.04)		
Reserves/Imports					-0.50 (-1.53)	-0.46 (-1.46)
Export/GDP Ratio					-5.06 (-0.41)	
Latin America					0.73 (1.37)	1.02 (2.02)
British Empire					-4.25 (-0.21)	
Constant	-0.07	-2.81	-1.05	-1.06	-4.93	-1.44

[a]*Variable definitions: Year:* year of dependent variable (1931, 1932, 1933); *Previous default:* dummy variable for incidence of default during the period T-15 years to T-3 years (T denotes year of dependent variable); *Debt-service ratio:* debt service/exports ratio (for T-1), i.e. (external debt*debt service/external debt)/exports; *Growth of exports:* average yearly growth rate of export revenues (over years T-3 to T-1); *Economic growth:* average yearly growth rate of nominal GDP (over years T-3 to T-1), for several countries data refer to gross or net national product (cf. sources for more detail); *Budget deficit:* growth of budget deficit of central government (over years T-2, T-1); *New borrowing:* difference of stock of external debt between T-3 and T-1/GDP; *Reserves/imports:* international reserves requirements for imports of a month, i.e. international reserves (foreign exchange, gold and silver)*12/imports (for T-1); *Export/GDP ratio:* exports/GDP (for T-1); *Latin America:* dummy variable for Latin American countries; *British Empire:* dummy variable for countries belonging to the British Empire.

Sources: CFB (*Annual Reports*, 1910-1940) and Suter (1990: 235-283) for year of default, actual and previous default and for external debt and debt service for Mexico; Société des Nations (*Annuaire Statistique International*, 1928-1935/36) for debt, debt service, exports, imports and reserves; Mitchell (1975, 1982, 1983) for GDP, growth of GDP, budget deficit and prices; Wilkie (1974: 227) for prices.

TABLE 5.7 Determinants of Rescheduling Incidence, 1978-1985 (pooled logit analysis, number of observations=627, regression coefficients with t-values in parentheses)[a]

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Year	0.188 (2.96)		-0.065 (-0.78)	0.120 (1.81)	0.184 (2.82)	0.056 (0.74)	0.092 (1.34)
Previous Rescheduling	1.848 (13.24)		1.847 (10.91)	1.790 (12.29)	1.895 (12.83)	1.823 (12.63)	1.851 (12.29)
Debt/GNP Ratio		2.954 (5.31)	1.482 (2.00)	2.521 (4.71)			
Reserves/ Imports		-0.150 (-2.68)	-0.223 (-3.08)		-0.218 (-3.58)		
Economic Growth		-1.664 (-3.47)	-1.434 (-2.32)			-1.944 (-3.25)	
Interest/ Exports		12.017 (4.56)	16.518 (4.77)				17.183 (5.50)
Net Transfer		-9.857 (-3.14)	0.286 (0.07)				
Constant	-16.19	-0.745	4.978	-11.707	-15.197	-3.163	-9.521

[a]*Variable definitions: Year:* year of dependent variable (1978-1985); *Previous rescheduling:* dummy variable for incidence of rescheduling during the period T-5 years to T-1 years (T denotes year of dependent variable); *Debt/GNP ratio:* public and publicly guaranteed long-term external debt/GNP (for T-1); *Reserves/imports:* central bank reserves/imports (for T-1); *Economic growth:* average yearly growth of nominal GNP (over years T-3 to T-1); *Interest/exports:* interest payments/exports (for T-1); *Net transfer:* new debt inflows minus debt-service payments/GNP (for T-1).

Sources: World Bank (*World Debt Tables,* 1978-1989/90), Pfister and Suter (forthcoming).

As hypothesized, low economic growth contributes to a high probability of debt-service problems. The impact of economic growth is rather strong for the 1980s but only weak for the 1930s, especially when further independent variables are included. The relevance of economic growth for the course of the debt crisis of the 1980s is further documented by the fact that the time trend, i.e. the drastic increase in the number of countries involved in reschedulings, can be explained -- together with the above-mentioned ratio of interest to exports -- by declining economic growth (cf. equation 6 of Table 5.7). Contrary to what has been expected, there is no substantial association between deficit spending and debt-service incapacity. This finding is inconsistent with the conclusion drawn by Eichengreen and Portes (1986) from their analysis for the second half of the 1930s that governments pursuing austere budgetary policies were best able to avoid default.[23]

The theoretical argument least supported by the empirical evidence refers to the contention that creditors contribute to the outbreak of global debt crises through their policy of credit rationing. Thus, estimates for the 1930s show no impact of new lending on default incidence. With respect to the model for the 1980s, equation 2 of Table 5.7 shows the predicted inverse relationship between net transfers and rescheduling probabilities. Yet, this effect disappears when previous debt-service incapacity and the time trend are included (cf. equation 3 of Table 5.7). This suggests that countries repeatedly involved in reschedulings tend to be excluded from access to capital markets.

The results of the remaining explanatory variables which have been used as control variables are consistent with empirical evidence as reported by other studies. Thus, high levels of debt dependence of borrowing countries (ratio of external debt to GNP) increase the probability for the incidence of debt-service incapacity,[24] whereas the openness of debtors' economies to the world market (ratio of exports to GDP) seems to have no impact.[25] High liquidity as measured by the ratio of international reserves to imports tends to protect a borrowing country from falling into default or rescheduling.[26] The regional dummy variables for the British Empire and Latin America that have been included in the model for the 1930s confirm the conclusion that Latin American countries in particular are prone to debt-service incapacity, drawn from the descriptive analysis of the geographical location of major debt crises presented in the previous section.[27]

In sum, cross-sectional evidence for determinants of debt-service incapacity for the two global debt crises of the early 1930s and the early 1980s suggests the relevance of similar working mechanisms during both crisis periods. Two causal factors are of primary importance for the explanation of incidence of debt-service incapacity: first, the occurrence of previous debt-service problems and, second, declining export revenues combined with rising interest and amortization payments. Deteriorating growth prospects and declining liquidity are additional factors triggering the outbreak of the global debt crises of the 1930s and the 1980s, whereas credit rationing by creditors seems to play only a minor role. This causal logic of global debt crises is consistent with the basic theoretical argument concerning the relationship between global economic processes and debt cycles as hypothesized in Chapter 3.

Notes

1. See, for example, Wynne (1951b), Landes (1958), Bazant (1968), Thobie (1980), Scheetz (1986), Pamuk (1987), Aggarwal (1989), Cardoso and Dornbusch (1989).

2. For example, Kindleberger (1978), Fishlow (1986), Stallings (1987), Lipson (1985, 1989).

3. Cf. Kindleberger (1984), Eichengreen and Portes (1986, 1989), White (1986), Fishlow (1989), Dawson (1990).

4. Usually, repudiations occurred in the context of revolutionary regime changes. A typical example is the repudiation of the external debt contracted by the Mexican emperor Maximilian by the republican government of Benito Juárez in 1866 after the overthrow of Maximilian. Similarly, several communist regimes repudiated external debt raised by their predecessor governments (e.g. Bulgaria, China, the German Democratic Republic, the Soviet Union).

5. An example is the consolidation of Serbia in 1895.

6. Differences between default and rescheduling strategies will be examined in greater detail in Chapter 6.

7. Data source of the figures of this chapter is the appendix of Suter (1990: 235-284), which contains detailed information on all defaults and reschedulings occurring between 1820 and 1986. Data for defaults on foreign bonds are mainly based on the annual reports of the British Council of the Corporation of Foreign Bondholders from 1873 to 1985 and the weekly issues of *The Economist* (1843-1939), whereas data for multilateral reschedulings have been gathered from publications of the IMF, the World Bank and the OECD. A summary table of these data with yearly figures from 1821 to 1986 is provided in the Appendix of this book.

8. Although Kowalewski (1989) draws the same conclusion from his analysis, the pattern of debt problem waves based on global media sources (which, however, seem to me less reliable than the primary sources used here) differs from the empirical results described above. Thus, according to Kowalewski's (1989: 83) figures, the percentage of countries with debt problems peaked in the mid-1850s, in the 1880s, around 1903 and in the 1940s.

9. Thus, the crisis was triggered by the state insolvency of Argentina, the Latin American debtor country most strongly incorporated into the Atlantic economy. The debt crisis subsequently spread to other Latin American debtor countries (e.g. Brazil, Chile, Uruguay) and to the European periphery (e.g. Portugal; cf. Kindleberger 1984 and Marichal 1989: 149-170 for a more detailed account of the international financial crisis of the 1890s).

10. Uruguay was the only defaulting country belonging to the Atlantic economy, whereas four debtor countries (Austria-Hungary, Bulgaria, Liberia, Ottoman Empire) suspended payments solely due to war reasons.

11. This does not apply, however, to the first half of the nineteenth century, since foreign investments of the Netherlands have not been taken into account due to lack of data. Since the Netherlands was still an important creditor country during the early decades of the nineteenth century, the peaks in the share of

blocked loans in the late 1820s and mid-1840s are presumably overestimated by 4-6 percent (cf. Woodruff 1966: 159, Riley 1980).

12. The nine states were Arkansas, Florida, Illinois, Indiana, Louisiana, Maryland, Michigan, Mississippi, and Pennsylvania. The sum of defaulted debt amounted to roughly $120 million (or some 60 percent of the total indebtedness of the states), of which approximately two-thirds was held abroad (Lewis 1938, Ratchford 1941: 105). All states resumed payments rather quickly except Florida and Mississippi. The latter was still in default at the end of the 1980s with respect to two bonds issued in the 1830s amounting to $7 million (CFB, *Annual Report*, 1985).

13. Cf. Pfister and Suter (forthcoming: Appendix) and World Bank (*World Debt Tables*, 1990/91).

14. Kowalewski (1989: 84), whose data is confined to initiations of debt problems and does not include duration of debt-service incapacity, presents a somewhat different list of debtor countries affected the most by debt crises: Mexico ranks first followed by Peru, Brazil, Chile, Colombia, Argentina and Egypt.

15. Cf. Frank and Cline (1971), Dhonte (1975), Feder and Just (1977), Mayo and Barrett (1978), Feder et al. (1981), Cline (1984), Schmidt (1984), and the review on this literature given by McDonald (1982) and Saini and Bates (1984).

16. E.g. discriminant analysis (cf. Frank and Cline 1971, Sargen 1977) and factor analysis (cf. Dhonte 1975).

17. Cf. Saini and Bates (1984), Schmidt (1984).

18. Cf. for example, Cline (1984: 227).

19. Usually, the dependent variable is measured as a dummy variable which distinguishes between solvent and insolvent debtor countries. Since the number of countries facing debt-service incapacity is rather low (e.g. 10-20 rescheduling cases as compared to several hundred non-rescheduling cases in studies examining the 1960s and 1970s), estimates become unreliable due to the limited number of degrees of freedom.

20. Cf. Saini and Bates (1984), Callier (1985).

21. Cf. Cox (1970) and Hanushek and Jackson (1977) for a discussion of logit analyis.

22. The following countries have been included: Argentina, Australia, Austria, Brazil, Bulgaria, Canada, Chile, Colombia, Czechoslovakia, Denmark, Finland, Germany, Greece, Guatemala, Hungary (for 1932 and 1933 only), India, Italy, Japan, Mexico, New Zealand (for 1933 only), Norway, South Africa, Spain.

23. Yet, the effects of budget deficits as reported by Eichengreen and Portes (1986) are relatively weak and attain statistical significance only in one of four equations.

24. Cf. Schmidt (1984) and Callier (1985) for similar findings. Due to problems of multicollinearity this indicator has to be excluded from the model for the 1930s.

25. This variable was only included for the 1930s. The lacking effect is consistent with the findings of Eichengreen and Portes (1986) for the late 1930s.

26. Similar findings are reported by Feder and Just (1977) and Schmidt (1984) for the 1960s and 1970s.

27. Surprisingly, the high default probabilities for Latin America cannot be explained by the other variables included in the model.

6

The Pattern of Debt Settlements

As we have seen in the previous chapter, the capitalist world-economy has experienced four principal periods or waves of global debt-service incapacity since the early nineteenth century, with peaks of crisis in the late 1820s, the late 1870s, the early 1930s and the early 1980s. While global debt crises prior to World War II were characterized chiefly by outright default, the open outbreak of debt-service incapacity during the postwar period has been forestalled by the arrangement of multilateral debt-rescheduling agreements. Yet, as the present debt crisis is still far from settled, it would be risky already to conclude that the rescheduling strategy is superior to the previously used "default strategy." On the background of the historical evidence discussed in Chapter 5, one may rather ask how exactly earlier debt crises were finally settled and what can be learned from those experiences for a better understanding of and an improved coping with the present difficulties.

Hence, this chapter describes and explains the pattern of debt settlement by comparing the present debt crisis with the three previous ones. This comparison is done on the basis of four principal dimensions. The *first* and basic dimension relates to the actor structure underlying the financial relations between creditors and debtor countries and the resulting institutional framework associated with the debt-settlement processes. An important element with respect to the actor structure refers to the strength of cooperative arrangements among creditors. The other three dimensions deal with the pattern of debt settlements. The *second* dimension refers to the efficacy of the crisis management, the *third* dimension to the degree of economic and political influence exerted on debtor countries by creditors, and the *fourth* dimension to the terms of the debt settlement, i.e. to the degree of debt relief granted by creditors.

As hypothesized in Chapter 3, the basic argument suggests that the three dimensions referring to the pattern of debt settlement, i.e. the efficacy of the crisis management, the degree of creditors' influence and the extent of debt relief, are determined by the actor structure or, more specifically, by the actor structure on the creditors' side. Thus, I argue that a quick and efficient crisis management, the ability of creditors to exert far-reaching influence on debtor countries and to enforce hard terms of debt settlements against the interests of debtor countries, is dependent upon the establishment of strong cooperative networks among creditors. The institutionalization of such creditor clubs on their part presupposes the predominance of relatively few actors with a dense interaction structure.[1]

Cooperative arrangements already took place before the current debt-servicing problems occurred. These arrangements could subsequently be used as a starting point for fast action. For example, official lending was confined to the few most-developed core countries organized within the Development Assistance Committee of the OECD. With the foundation of the DAC in 1960, official donors set up a joint forum and established cooperative decisionmaking processes in the field of development assistance. Moreover, official donors and international organizations promoted further cooperation in development aid by the formation of aid consortia, consultative groups and roundtables. Commercial banks, for their part, provided the large loans needed by sovereign borrowers jointly in the form of so-called syndicated credits and were largely dependent upon each other owing to the system of interbank credits.

The basic hypothesis concerning the relations between actor structure on the one hand and efficacy of crisis management, degree of creditor's influence and extent of debt relief on the other may be developed further by using the concept of world leadership cycles. As outlined in more detail in Chapter 3, one may argue, first, that debt crises are more quickly negotiated during hegemonic phases when the world-system is economically and politically dominated by a single world power which is interested in the maintenance of financial stability and may act as a kind of international lender of last resort. Second, following Chase-Dunn's (1989: 273) argument that political forms of core dominance on peripheries increase during periods of core rivalry, economic and political influence exerted on debtor countries by creditors is expected to be more pronounced when the power structure becomes multicentric due to the rising competition among core countries. Third, the terms of debt settlements are suggested to be most favorable for debtors during periods of core rivalry.

In addition, one may expect differences in the settlement pattern between different hegemonic powers, i.e. between the British and the U.S. hegemony. Thus, Lipson's (1985, 1989) comparison of security policies concerning foreign capital between Victorian Britain and postwar America suggests more interventionist policies during the U.S. hegemony.

What follows is, first, a discussion of the settlement of defaults on foreign government bonds, the dominant mode of debt settlements prior to World War II. The next section analyzes the settlement of debt-servicing incapacities during the postwar period, i.e. the pattern of multilateral reschedulings of official and private credits. The final section summarizes the differences between the two modes of debt settlement and relates them to the basic hypotheses outlined above.

The Settlement of Defaults on Foreign Government Bonds: Debt-Crisis Management Prior to World War II

Before World War II the settlement of defaults on governmental bonds was rather weakly institutionalized, especially during the first three quarters of the nineteenth century. With their unilateral suspension of interest or amortization payments, defaulting countries violated the provisions of the loan agreements. A debt settlement thus implied a formal renegotiation of this contract between the debtor country and its bondholders. Such arrangements, however, were rather difficult to realize since the negotiation process was complicated by the dispersion of creditors over a large mass of small bondholders.

During the nineteenth century bondholders were badly organized. When default occurred, they tried to establish committees in order to protect their interests and to enter into negotiations with representatives of the defaulting country. The mere formation of such ad hoc committees was, however, rather time-consuming. Moreover, these committees usually had only limited competence. For instance, they were not entitled to conclude binding agreements with the debtor country. Rather, the arrangements concluded by the committees had to be approved by a general meeting of the bondholders concerned. But even if the majority of bondholders accepted the arrangement, it was not binding for individual bondholders. In addition, the committees lacked the necessary financial resources, infrastructure and access to information on the economic and political situation of debtor countries. The bargaining power of bondholders' representatives was often further weakened by the rivalry between several competing committees.[2]

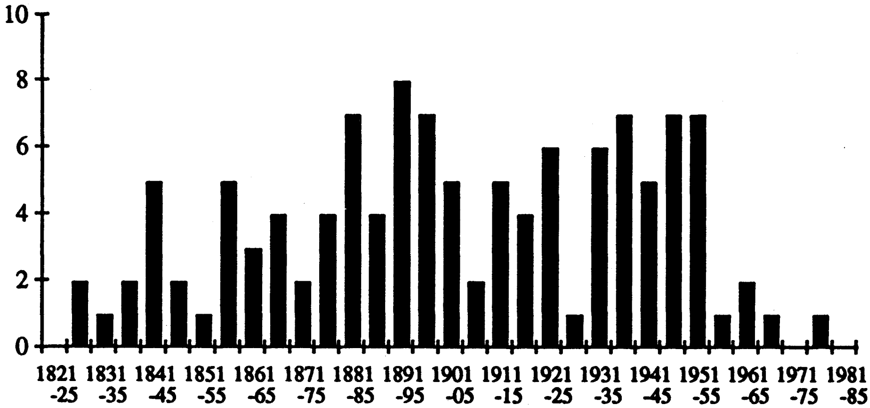
As a reaction to these problems of creditor coordination and cooperation, permanent central national bodies were established in most important creditor countries from the late nineteenth century onwards. The first and most important of these national committees emerged in Great Britain with the formation of the Council of the Corporation of Foreign Bondholders in 1868. Similar bodies were established in other creditor countries like France and Belgium (1898), Switzerland (1912), Germany (1927) and the United States (1933).[3] The task of these central councils was to set up committees to protect bondholders' interests when a default occurred. They nominated the members of the committee but usually organized a general meeting of bondholders to ratify their appointments. For countries with a bad debt record the committees were established on a permanent basis. The national bodies supported the committees with infrastructure (e.g. localities, secretarial services), financial resources (e.g. travel expenses) and know-how. The committees entered into negotiations with the defaulting country and worked out an agreement with the respective debtor country for a settlement of defaulted debts. The national council then recommended the bondholders to accept this agreement, which was, as noted above, not binding for individual bondholders, however.

In addition to the negotiation of formal agreements between bondholders' committees and defaulting countries, two further forms of debt adjustment can be discerned. First, in the case of temporary suspensions or of defaults on amortization payments, only bondholders' claims were in general simply met by a repayment of arrears. Second, existing obligations were sometimes converted into new debts by a concerted action of creditors before the debtor country was forced into open default. Yet, such consolidations, which are rather similar to the multilateral rescheduling technique of the postwar period, could be realized in only four cases.[4]

We now turn to a closer inspection of the pattern of debt settlements concerning defaulted foreign governmental bonds. From 1820 to 1985 they number about 120[5] and relate mainly to defaults on interest payments or on both interest and amortization payments; amortization payments alone were adjusted in only five cases. The principal sources for the following analysis are the annual reports of the British Council of the Corporation of Foreign Bondholders from 1873 to 1985, which contain a detailed record of the negotiation processes and the terms of the settlements agreed upon between bondholders and debtor countries. In addition, annual reports of French and Belgian bondholders' associations and the weekly issues of *The Economist* (from 1843 until 1939) were used.[6]

A first research question which may be derived from the basic hypotheses elaborated in Chapter 3 refers to the occurrence of debt settlements. It has been hypothesized that the conclusion of debt settlements is not distributed evenly over time but is concentrated in the early upswing phases of global growth cycles. Figure 6.1 plots the number of debt settlements concerning defaulted government bonds concluded between debtor countries and their creditors per five-year periods from 1821-1825 to 1981-1985.

FIGURE 6.1 Number of Debt Settlements Concerning Defaulted Foreign Bonds per Five-Year Periods, 1821-1825 to 1981-1985



Sources: CFB (*Annual Reports*, 1873-1985), Suter (1990: 235-282).

Figure 6.1 shows that debt settlements occur discontinuously, although the cyclical pattern is not as pronounced as in the case of default incidence (cf. Figure 5.3). Peaks in the number of debt settlements fall into the periods 1841-1845 and 1856-1860 (five arrangements each), 1891-1895 (eight) and 1946-1955 (seven arrangements per each of the two five-year periods), whereas troughs occur in 1821-1835, 1851-1855, 1871-1875, 1906-1910, 1926-1930 and after 1956. A comparison with the periodization of Kondratieff and Kuznets growth cycles reveals that settlements tend to be concluded most frequently during the early upswing phases of global growth cycles and lowest in the transition phase from up- to downswing. Although this correlation is not perfect, it supports the contention that the debt settlements occur discontinuously and are associated with cyclical processes of economic growth operating on the global level of the world-economy.

As outlined in the preceding section, the pattern of debt settlements will be examined concerning (i) the efficacy of the crisis management, (ii) the degree of economic and political control exercised by creditors over debtor countries, and (iii) the degree of debt relief granted by creditors. These three dimensions, which are supposed to be closely associated with the actor structure and the strength of cooperative arrangements among creditors, will be analyzed separately for the settlement of each of the three major debt crises before the 1980s. For the following empirical analysis, three default-settlement periods have been defined delimited by the trough years of the three principal debt crises.

As documented by the material presented in Chapter 5, the number of sovereign borrowers in default was lowest in 1871 (5 countries) and in 1926/27 (3 countries), while the number of reschedulings started to rise from 1975/76 onwards (cf. Figure 6.1 and 6.2). Hence, the first default-settlement period covers the years 1821-1870, the second the years 1871-1925 and the third the years 1926-1975.

In principle, each of the three periods defined above begins with a wave of defaults characterizing the outbreak of a global debt crisis (i.e. late 1820s, mid-1870s, early 1930s) and comes to an end when all defaults have been settled by arrangements between defaulting countries and bondholders' representatives. This conception presupposes that the default-settlement sequences of the three principal debt crises are not overlapping, i.e. that each default is settled before the next principal debt crisis breaks out. Yet, as mentioned above, five sovereign borrowers which had suspended payments in the wake of the first global debt crisis were still in default when the crisis of the mid-1870s broke out. Similarly, three defaulting countries of the second period reached a settlement only after the outbreak of the crisis of the 1930s. Since we are interested in a comparison of the settlement strategies of the three principal debt crises, these eight cases which cannot be classified clearly into one of the three default-settlement periods and could thus distort the underlying configuration of the crisis-specific settlement patterns have been excluded in the following empirical examination.

(i) Efficacy of crisis management: The efficacy of a debt-crisis management strategy is measured by the duration of defaults, i.e. the time span between the outbreak of debt-service incapacities and the final conclusion of the debt-settlement arrangement. The figures presented in Table 6.1 for 114 debt settlements for which data are available show an average duration of defaults on foreign bonds of nine years, i.e. on the average nine years passed after default before debtor countries reached a final settlement with their creditors.[7] This empirical evidence suggests that bond defaults were not at all rapidly followed by settlements as claimed by Jorgensen and Sachs (1989: 49) but that the efficacy of crisis management was rather poor. This has to be attributed to the low level of institutionalization of bondholders as it has been discussed above.

This interpretation is supported by the fact that differences between the individual default-settlement periods are relatively minor and that no clear trend is visible. The duration of defaults was highest during the period 1821-1870 (14 years)[8] and lowest in 1871-1925 (6 years). A one-way analysis of variance suggests statistically significant but relatively weak differences in group means of settlement periods.[9] Scheffé's test for contrasts between individual group means shows significant differ-

TABLE 6.1 Average Yearly Duration of Defaults on Foreign Bonds[a]

Default-Settlement Period	*Duration of Defaults (in years)*
(1): 1821-1870	14.0 (25)
(2): 1871-1925	6.3 (52)
(3): 1926-1975	10.1 (37)
Total: 1821-1975	9.2 (114)
F-Value	6.4*
Eta^2	0.10

[a]*F*-Value and Eta^2 for one-way analysis of variance with default-settlement periods as the independent variable.
*denotes a significance level of .01.

Sources: CFB (*Annual Reports*, 1873-1985), Suter (1990: 235-282).

ences only between the periods 1821-1870 and 1871-1925.[10] On the background of the hypotheses formulated earlier, the evolution of the mean duration between default and settlement can be interpreted as follows:

The extremely long duration of defaults during the first default-settlement period (1821-1870) may be attributed to the lack of permanent bondholder committees. Furthermore, most debtor countries which went into default during the debt crisis of the late 1820s suffered from heavy political instability and a weak state apparatus with a narrow financial resource base, as was the case for Greece and several Latin American debtor countries which had just become independent.

The comparatively quick settlement of defaulted bonds during the period 1871-1925 is more difficult to explain. One may argue that in contrast to the deep and protracted crisis of the 1930s, the depression of the world economy during the 1870s was quickly overcome. In addition to the rapid expansion of the world-economy from the 1880s onwards, the gradual institutionalization of creditor cooperation through the establishment of national bondholder committees may have accelerated the settlement processes. An alternative line of reasoning refers to the concept of world leadership cycles. The defaults occurring in the wake of the debt crisis of the mid-1870s came during the uncontended financial supremacy of Britain, whereas the defaults of the 1930s took place in a period of rivalry between different powers in the core of the world-system.[11]

The argument of core rivalry for the explanation of the relatively long duration of defaults in the wake of the crisis of the 1930s can be further elaborated. It may be expected that the rivalry between the two military superpowers, the United States and the USSR, and their political allies that emerged after World War II and culminated in the Cold War delayed the debt-settlement process in cases of debtor and creditor countries not belonging to the same political alliance. In fact, most communist governments repudiated the foreign bonds raised by their predecessors from Western core countries. During the 1950s and 1960s four communist countries (Poland, Romania, Hungary and Yugoslavia) eventually concluded a debt settlement with their creditors. The average duration of these defaults amounted to 21 years; this is more than twice the average of the default-settlement period 1926-1975. Moreover, five communist countries (Bulgaria, China, German Democratic Republic, Czechoslovakia, USSR) were still in default in 1975.

(ii) Creditor pressure on debtor countries: Insolvent debtor countries sometimes came under political and economic control of their creditors. The most frequent form of political and economic control was the establishment of debt administration councils and the control of public finance of debtor countries by creditors' representatives. Debtor countries usually had to cede some financial revenues to these councils, such as state monopolies, taxes and customs duties, which were used for the financing of interest and amortization payments. In most cases, the revenues assigned were collected by the councils themselves. The degree of creditors' influence on these debt administration councils varied according to the composition of the council. In the case of Serbia (1895), for instance, the council was dominated by representatives of the debtor government and the influence of the bondholders was rather weak.[12] By contrast, the debt administration of Liberia (1912) was largely controlled by the creditors and was vested with far-reaching financial competence. Creditors directly supervised tax and duty collection and reorganized Liberian public finance. As a consequence, the Liberian government completely lost its financial autonomy (cf. Chapter 9). Between 1821 and 1975 there were, however, only nine cases of political and economic intervention through the formation of debt administration councils. This is equivalent to 8 percent of all debt settlements. Most of these cases, i.e. seven out of nine, fall into the default-settlement period 1871-1925.[13]

In addition to the establishment of debt administration councils by bondholders and creditor countries, there were also two instances of open military intervention by creditor countries against defaulting debtors which refused to honor their debt-service obligations. One of them was the invasion of Mexico by France, which was initially also supported by Spain and Britain and was directed against the republican regime of Benito Juárez. In 1863 France installed the Austrian archduke Maximilian, a brother of the Austrian emperor Franz Joseph, as emperor of Mexico. In the second case, Germany, Britain and Italy jointly blockaded Venezuelan ports in 1902/03 since the Venezuelan government under Cipriano Castro did not resume debt-service payments after the termination of the civil war. Venezuela also refused to pay any indemnities for war damages to foreign property. While the French intervention against Mexico proved rather unsuccessful,[14] claims of European powers were largely met in the settlement with Venezuela.[15]

Apart from such political pressures, debt settlements sometimes included elements of exclusive *economic* control. Thus, in nine debt arrangements debtor countries ceded property rights to the creditors. In most cases either land or railways were assigned to the bondholders in return for a partial liquidation of existing debts. A telling example is the Peruvian debt settlement of 1889, which became known as the Grace contract (cf. Chapter 8). In this arrangement outstanding debts of some $30 million and arrears of interest of $23 million were cancelled in return for the assignment of the state railways for 66 years, 2 million tons of guano and the concession for the operation of steamboats on Lake Titicaca. Other debtor countries that ceded some property rights to bondholders were Colombia (1861 and 1873, land), Costa Rica (1885, railways), the Dominican Republic (1893, railways), Ecuador (1885, land; 1897/98, railways), El Salvador (1899, railways) and Paraguay (1855, land).[16] This record shows that seven out of nine cases occurred during the default-settlement period 1871-1925.

These results demonstrate that instances of purely economic control by creditors are as important as the better-known political ones. Surprisingly, most studies on creditors' intervention in the wake of defaults on bonds only rarely discuss economic control.[17]

Overall it must be said that creditors' political and economic control over debtor countries was rare. It can be demonstrated for only 20 out of 113 debt settlements. Yet, most of these cases, i.e. 15, occurred during the default-settlement period 1871-1925. Four fall into the period 1821-1870 and only one into the period 1926-1975.[18] This pattern suggests that political and economic pressures by bondholders and creditor countries can be interpreted against the background of the rising rivalry among core countries towards the end of the nineteenth century and the resulting imperialist policies pursued by the European powers and the United States. Political and economic control in the context of debt settlements was part of this strategy. This is demonstrated by the cases of Tunisia, Egypt and the Dominican Republic, which were integrated into the colonial and quasi-colonial empires of their principal creditor countries in the wake of payment difficulties.

(iii) Degree of debt relief granted by creditors: Three dimensions of debt relief have been selected for examination: (1) the reduction in arrears of interest, i.e. the capitalization or conversion rate of arrears of interest

into new debts, (2) the reduction in interest rates and (3) the reduction in the face value of outstanding foreign bonds.[19]

(1) Since defaults lasted more than ten years on the average, the most important dimension with respect to the degree of debt relief is the settlement of arrears of interest. Thus, when a settlement was finally reached, these arrears often exceeded the face value of defaulted bonds. Usually, arrears of interest were converted into new bonds at a certain discount, and interest rates of these new debts were considerably lower than of the original bonds. Only in the case of the forced Mexican debt settlement of 1864 were arrears converted at a substantial premium for bondholders.[20]

The average conversion rates of arrears of interest for 54 debt settlements for which data are available are shown in Table 6.2. From 1821 to 1975 arrears were converted at a rate of 67 percent into new bonds. Hence, on the average 33 percent of arrears had to be written off by the bondholders. Since compound interest has not been taken into consideration, real debt relief was even higher. Over the three default-settlement

TABLE 6.2 Average Degree of Debt Release Granted by Creditors: Capitalization Rate of Arrears, Percentage Reduction of Interest Rates and of Outstanding Debts (number of agreements in parentheses)[a]

Default-Settlement Period	*Capitalization Rate of Arrears*[b] *(in %)*	*Reduction in Interest Rates*[c] *(in %)*	*Reduction in Outstanding Debts*[d] *(in %)*
(1): 1821-1870	80.7 (18)	15.4 (17)	2.6 (20)
(2): 1871-1925	71.6 (24)	16.3 (36)	22.8 (38)
(3): 1926-1975	35.2 (12)	34.5 (26)	23.2 (23)
Total: 1821-1975	66.5 (54)	22.1 (79)	17.9 (81)
F-Value	5.0*	8.0**	3.4*
Eta^2	.16	.17	.08

[a]*F*-Value and Eta^2 for one-way analysis of variance with default-settlement periods as the independent variable.

[b]Average conversion rate of accumulated arrears of interest into new bonds.

[c]Average reduction in new interest rates as a percentage of original interest rates.

[d]Average percentage reduction in the face value of outstanding bonds.

*denotes a significance level of .05.

**denotes a significance level of .01.

Sources: CFB (*Annual Reports*, 1873-1985), Suter (1990: 235-282).

periods the conversion rate fell from 81 percent to 35 percent. Thus, in the wake of the debt crisis of the 1930s, roughly two-thirds of arrears were cancelled. This trend is significant statistically: Scheffé's test shows differences at the .05 significance level between the periods 1821-1870 and 1926-1975 as well as between the periods 1871-1925 and 1926-1975.

(2) The settlement of defaulted debt also included a renegotiation of interest rates. For 79 debt settlements the average reduction of interest rates as a percentage of the original rates has been computed. As shown in Table 6.2, interest rates were lowered by 22 percent on the average. If one takes into account that interest rates on converted arrears were also lowered considerably, interest reductions were even more substantial. The reduction of interest rates was relatively modest during the default-settlement periods of 1821-1870 and 1871-1925 but became substantial during the period 1926-1975. Thus, Scheffé's test shows contrasts at the .01 significance level between the periods 1821-1870 and 1926-1975 as well as between the periods 1871-1925 and 1926-1975.

(3) In most settlements debtor countries and bondholders' representatives converted defaulted bonds into new debts. As a result of such conversions the amount of outstanding debt was newly fixed. Table 6.2 presents the average percentage reduction in the face value of foreign bonds for the 81 settlements for which data are available. On the average, outstanding debts were lowered by 18 percent. Yet, the face value of foreign bonds remained virtually unchanged during the default-settlement period 1821-1870, while it was substantially lowered in 1871-1925 and 1926-1975. These differences between default-settlement periods are statistically significant. A posteriori contrasts between the three periods show significant differences at the .05 level between the periods 1821-1870 and 1871-1925.

The comparatively high degree of debt release during the default-settlement period 1871-1925 has to be attributed partly to debt liquidations that were granted by the creditors in return for political and economic control. As discussed above, several debtor countries ceded land and railways to bondholders in exchange for debt release. If settlements containing any form of political and economic control are excluded from the calculation, reduction of outstanding debts decreases to 12 percent for the period 1871-1925, while the figures remain virtually unchanged for the periods 1821-1870 (2 percent) and 1926-1975 (24 percent). Despite these elements of political and economic control, debt relief granted by creditors in the wake of the debt crisis of the 1870s was considerably more substantial than during the first half of the century.

Considering all three dimensions of debt relief together, one discerns a trend towards more favorable terms for debtor countries. The degree of debt relief was lowest during the default-settlement period 1821-1870 and highest during the period 1926-1975. As discussed above, the higher degree of debt relief during the period 1871-1925 compared to the period 1821-1870 may be attributed partly to debt liquidations as a result of rising political and economic control of debtor countries by the creditors. This stands in line with the fact that the evolution was slight with regard to the other dimensions of debt relief during the first two periods. The comparatively high degree of debt relief during the default-settlement period 1926-1975 may be explained by the dynamic of world leadership cycles, as hypothesized in Chapter 3. Thus, the settlement of defaults after the crisis of the 1930s coincided with the transition from British to U.S. hegemony. This situation was rather favorable for debtor countries since they were mainly indebted to the old and decaying hegemonic power (i.e. Britain). The United States as the new world leader did not support British interests but rather tried to integrate debtor countries at the periphery into its own hegemonic power system by granting substantial concessions at the expense of Britain.

To sum up, the pattern of debt settlement with respect to defaulted foreign governmental bonds and its change in the course of the three default-settlement periods may be characterized as follows: During the first default-settlement period (1821-1870) foreign bonds remained in default for a relatively long period. The terms of debt settlements were comparatively unfavorable for debtor countries, but there were only few attempts of creditors to control debtor countries politically and economically. During the second default-settlement period (1871-1925) debt settlements were concluded comparatively quickly. The arrangements also contained some elements of debt release, especially so with respect to reductions in the nominal value of outstanding bonds. However, debtor countries often had to pay for the liquidation of foreign bonds with a loss of their political and economic autonomy. As compared to the period 1871-1925, the efficacy of the crisis management declined somewhat during the third default-settlement period (1926-1975). Yet, the terms of the settlements were extremely favorable for debtor countries. Furthermore, the substantial debt relief was not tied to political and economic control of debtor countries by their creditors.

Multilateral Debt Rescheduling During the Postwar Era

After World War II multilateral debt rescheduling became the single most important strategy to cope with debt crises. "Rescheduling" quite simply refers to a process of renegotiating the terms – particularly interest rates, maturities and grace periods – of a part of credits falling due during a specific time period (the consolidation period) or of credits already in arrears. In contrast to the strategies discussed above, multilateral reschedulings are usually applied before debtors have formally defaulted on their debts. By negotiating debt-rescheduling agreements, creditors as well as debtors are able to maintain the impression of orderly financial relations. Thus, rescheduling has the significant advantage of preventing debt problems from widening into an uncontrollable crisis.

There are, however, some serious limitations to the rescheduling approach, some of which will be discussed later in this section. Before this, a brief outline of the institutional features of debt rescheduling will be presented. Subsequently, the development of rescheduling activity since World War II will be described. Thereafter, empirical evidence concerning the three dimensions of (i) efficacy of crisis management, (ii) political and economic influence on debtors and (iii) the extent of debt relief provided by rescheduling operations will be presented. As in the previous section, the empirical analysis aims at covering all cases of rescheduling. The data used have been gathered from official sources (IMF, World Bank, OECD) as well as international financial press releases (*Financial Times, Neue Zürcher Zeitung, Euromoney, Institutional Investor*). They are fully discussed and evaluated in the appendices to Pfister and Suter (forthcoming) and Stamm (1987). Unless otherwise mentioned, all quantitative data presented in this section are taken from those two sources.

With reference to the institutional framework of rescheduling, a qualification concerning its multilateral nature must be made. Due to the segmentation of financing activities during the postwar era -- which is visible in the division of commercial, concessional (development) and trade finance among different actors of the financial system -- it has not been possible to create a truly multilateral framework that includes all creditors and borrowers simultaneously. Instead, individual debtors are confronted with specialized creditor clubs of banks and official lenders, i.e. the development- and trade-financing agencies of highly industrialized core countries. Small private suppliers, on the other hand, have generally not been able to create similar frameworks and thus have remained largely dependent on the goodwill of debtors.[21] Yet, it should be noted that the establishment of the rescheduling mechanism has greatly profited from the structure of present-day international financial relations. As the specialized creditor groups are quite homogeneous, comparatively small and have a dense interaction structure, creditor cooperation has been easier to implement than during earlier crises.

In addition, multilateral development and financial institutions such as the World Bank, the regional development banks and the IMF have not yet directly participated in debt reschedulings but have secured themselves preferential treatment by stressing the special nature of their credits. They have, however, played a crucial role in promoting cooperation between creditors and debtors and in maintaining discipline among debtors as well as creditors. This has mostly been achieved by binding debt-rescheduling agreements to the previous conclusion of a standby agreement with the IMF, which generally included the implementation of restrictive economic policy measures and a close supervision of the performance of the debtor's economy. Conversely, the IMF repeatedly made standby agreements dependent upon the readiness of creditors to advance new credits. In addition, cofinancing arrangements with the World Bank and the occasional provision of bridging finance by central banks and the Bank for International Settlements have further enhanced cooperation and with this the stability of the system. Thus, the rescheduling strategy is part of a complex field of interaction among international financial institutions as the supervisors and strongly organized creditor clubs that confront debtors individually.

As will be illustrated below, creditor clubs usually only provide debtors with very limited debt relief on a case-by-case basis. The idea behind this strategy is that it is important to keep borrowers on a "short leash"[22] in order to restore payment capacity quickly -- an assessment of the situation that has been widely promoted by the Bretton Woods institutions. Consequently, many debtors with chronic debt problems had to undergo several reschedulings during the past years. Only from the late 1980s onwards were more far-reaching reschedulings which include longer consolidation periods and partial write-offs (particularly for the heavily indebted low-income countries) implemented.[23]

The different creditor groups were often afraid of being played off against each other by debtors. As official and private creditor clubs have never succeeded in establishing direct cooperation, there was a climate of mutual distrust that often resulted in protracted negotiations. The difficulties of cooperation within creditor clubs have, on a lower structural level, also contributed to this outcome. To make this last point clear, it would be necessary to differentiate between clubs of official and private creditors and to elaborate their contrasting organizational problems. As those differences have been discussed elsewhere in some detail, only a short overview will be provided here.[24]

Most problems of cooperation within official creditor clubs stem from political and ideological differences of the participating governments. Still, in most instances it was possible to implement a strategic consensus among creditors who usually have to cooperate not only in creditor clubs but also in other international institutions (DAC, OECD). Most notable in this respect is the so-called Paris Club, whose operations account for the bulk of rescheduling agreements with official creditors of the past decade. Although the Paris Club maintains its image as an informal club which only meets on special occasions, it could not prevent its operations from becoming institutionalized. Consequently, the individual reschedulings show similar procedural features and outcomes.[25] Despite some conflicts concerning the best possible strategy of debt relief and around some individual debtors, the Paris Club has generally been able to rally its members in a relatively short time along the lines of interpreting reschedulings as extraordinary short-term measures that should not be confused with development efforts.[26]

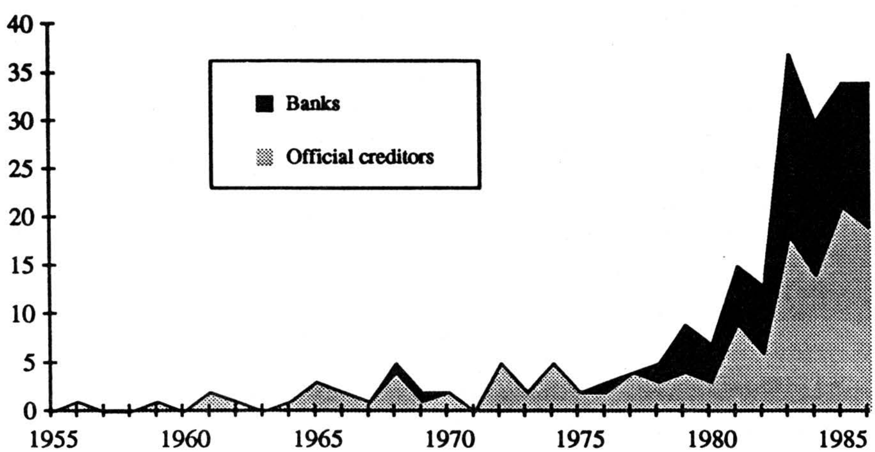
This observation does not apply to all other clubs of official creditors that have been in operation during the postwar era. Political disputes on the treatment of Poland and Cuba, for example, as well as the lack of their IMF-membership have delayed agreements for several months or even years in these cases.[27] Still other official creditor clubs that have mainly been working during the 1970s have provided more far-reaching rescheduling operations for either very poor or very important debtors by also considering developmental needs.[28]

Cooperation problems have been more accentuated among commercial banks. In general, they have found themselves to be more vulnerable to debt-servicing problems due to their private nature and an often considerable exposure to risks in Third World lending. As there have often been a large number of banks involved (up to 1000), so-called steering or advisory committees of about 10 to 20 of the most important banks (usually the leaders of the syndicate) were formed. The preliminary agreements negotiated by these committees often included -- at the insistence of official creditors and the Bretton Woods institutions -- the renewal of credits or even the provision of new money, and thus many banks found themselves in conflict with their principle of not throwing good money after bad money. In addition, smaller and less exposed banks were often speculating on being able to get out of their credit contracts at the cost of bigger institutes. Consequently, their resistance against signing debt-relief agreements was considerable and could not always be broken by the more cooperative banks.[29] Thus, we find similar organizational problems such as those which were faced by individual bondholders during earlier crises.

As can be seen in Figure 6.2, commercial banks also have concluded a large number of rescheduling agreements during the past decade. Overall, 226 rescheduling agreements have been concluded involving 52 countries and covering credits worth roughly $275 billion between 1956 -- when the first multilateral rescheduling agreement with Argentina was signed -- and 1986. Ninety agreements ($204 billion) were negotiated by private creditors,[30] 99 ($39 billion) by the Paris Club and 37 ($32 billion) by other groups of official creditors. Not surprisingly, the agreements have not been distributed evenly over time but are concentrated during the 1980s. Figure 6.2 illustrates the explosion of rescheduling activity from the early 1980s onwards. More specifically, only 56 agreements were concluded before 1980 and these were largely accounted for by official creditors (46) involving mainly some chronic problem borrowers (India, Argentina, Chile, and Indonesia). In addition, seven of the ten bank reschedulings before 1980 were concluded in 1978 and 1979. At the same time, average amounts of reschedulings grew significantly, particularly in connection with commercial banks' rescheduling operations. This can be explained by the debt problems of large borrowers (Mexico, Brazil, Argentina, the Philippines and Poland) but also by a tendency to reschedule a greater share of total credits falling due (see also Table 6.3 below).

Yet, it has to be noted that despite the importance of multilateral debt rescheduling, it is not the only form of crisis management. As noted in the previous section, the process of settling defaulted prewar external debt has yet to be fully concluded, and some additional countries have repudiated their debts during the postwar era.[31] Other countries with debt problems have undergone bilateral debt reschedulings and some others received only short-term temporary deferments of debt repayments.[32]

FIGURE 6.2 Number of Multilateral Debt-Rescheduling Agreements by Type of Creditor, 1956-1986



Sources: Pfister and Suter (forthcoming: Appendix), Stamm (1987: Appendix).

Let us now turn to a short discussion of the three dimensions of crisis management that have already been analyzed in the last section concerning the pattern of debt settlement prior to World War II.

(i) Efficacy of crisis management: With reference to the time span between the onset of debt problems and their settlement, reschedulings have undoubtedly been very efficient -- at least at first sight. As noted above, reschedulings have usually been negotiated before formal debt suspensions by debtors occurred. Based on the discussion of the features of creditor clubs above, one would expect official creditors to be more efficient than private creditors in concluding rescheduling agreements. In fact, one of the unwritten principles of the Paris Club expects creditors and borrowers to conclude an agreement in principle within only two days of negotiations in Paris. This seems to have worked quite well in the past, but it should be noted that usually an extensive phase of consultations involving creditor and debtor governments as well as the IMF preceded these meetings.

Still, the hypothesis of official creditors' being more efficient is also supported by data on the duration of renegotiations from the onset of debt problems (coded as the application of a debtor for a debt relief operation) and the conclusion of agreements. Although there are data for only 45 agreements, the average duration can be tentatively estimated to be about one year -- with higher average values for private banks and lower ones for official lenders. However, not only due to the small data base, this finding is bound to be misleading, as data on the conclusion of the bilateral agreements of Paris Club creditors are lacking and, consequently, an additional time span of several months between the negotiation of agreements in principle and their actual implementation must be added in some instances.

Yet, even more important is the fact that reschedulings are not usually debt settlements in the true sense of the word but rather provisional solutions involving short-term delays of repayments. Many debtor countries had to conclude a series of reschedulings and even renew their older agreements repeatedly because they were unable to restore their solvency in the short time frame provided by the creditors. More precisely, between 1976 and 1986 a total of 48 countries had to reschedule their external debt, and 38 of them met more than once with their creditors. The median value for this period is three agreements per country, with the lead taken by Sudan with ten agreements, followed by Poland and Zaire (nine each) and Cuba and Madagascar (eight each). From this perspective, most of the debt settlements of the present crisis have been pending for several years. Thus, the speed of intervention must not be confounded with the modest durability of the settlements reached.

(ii) Creditor pressure on debtor countries: Apart from some largely unsuccessful attempts, there has not been any direct political or economic influence exerted by creditors.[33] Instead, this task has been delegated to international financial institutions -- particularly the IMF, whose adjustment programs indirectly reflect the preferences of the principal (official) creditors, who are also the most influential members of the IMF. Consequently, the IMF has been identified as one of the central places where creditors formulate their interests. The IMF supports creditors by coordinating creditor club actions and providing statistical materials on debtors. Thus, creditors have relied heavily on the IMF's operations and, not surprisingly, 77 percent of all reschedulings concluded by the end of 1986 were accompanied by IMF adjustment programs. The remaining agreements were concluded either with non-IMF members of the or with countries that took an explicitly conflictive stance towards this organization. In both situations, the negotiations have been on the average more protracted and the terms negotiated have tended to be harder. Despite the absence of *direct* and *open* influence by creditors, we thus find a great deal of *indirect* pressure exerted through international institutions that play an important role as "policemen" in the financial system.[34]

(iii) Degree of debt relief granted by creditors: As the debt-settlement strategy of reschedulings differs from that of defaults, slightly other indicators than those employed in the previous section have to be used. This makes a direct comparison of reschedulings and default settlements difficult. For example, interest arrears have scarcely been rescheduled and therefore it is impossible to construct a comparable indicator covering the capitalization of those arrears (see Table 6.2). More or less the same applies to the reduction of outstanding debt, as it has been renewed rather than reduced during the postwar era. Yet, as in the previous section, the behavior of the interest rates and the extent of debt relief provided by the reschedulings will be investigated. The consolidation periods and the new maturities and grace periods are especially illustrative in this respect, and the actual amounts rescheduled as well as the percentage of those amounts in relation to the total amount falling due during the consolidation period give further useful indications as to the amount of debt relief.

All these data are presented in Table 6.3, grouped according to the type of creditor and the time of conclusion of the rescheduling agreement. The first column covers the pre-critical period before 1983, which is characterized by sporadic debt renegotiations with comparatively few chronic problem borrowers. The next two columns exhibit the data from

TABLE 6.3 Average Terms of Reschedulings with the Paris Club and Commercial Banks, 1956-1986 (number of cases used in the calculation in parentheses)

		1956-82[a]	*1983-84*	*1985-86*	*1956-86*[a]
Amount	Paris Club	266 (37)	412 (27)	532 (33)	397 (97)
($ Mil.)	Banks	663 (22)	1642 (34)	4782 (27)	2404 (83)
Share[b]	Paris Club	83.6 (28)	91.6 (16)	91.4 (21)	88.1 (65)
(%)	Banks	93.2 (22)	97.0 (32)	97.1 (14)	95.8 (68)
Cons.[c]	Paris Club	23.1 (37)	13.5 (26)	20.1 (34)	19.5 (97)
(Months)	Banks	17.6 (16)	20.9 (29)	38.5 (26)	26.6 (71)
Maturity[d]	Paris Club	9.9 (36)	9.9 (23)	9.8 (24)	9.9 (83)
(Years)	Banks	6.5 (22)	7.1 (34)	9.6 (22)	7.6 (78)
Grace[e]	Paris Club	3.8 (29)	4.7 (16)	4.8 (24)	4.3 (69)
(Months)	Banks	3.1 (20)	3.0 (32)	3.6 (21)	3.2 (73)
Spread[f] (% over LIBOR)	Banks	1.65 (21)	1.94 (33)	1.47 (22)	1.73 (76)

[a]The time period for the banks begins in 1978; the three agreements concluded before that year were omitted in the calculation.

[b]Rescheduled credits as a percentage of the total amount of credits falling due.

[c]Consolidation period.

[d]Time after which the whole principal must be paid back, including grace period.

[e]Grace period, the time in which only interest payments are due.

[f]Spread, indicated as a percentage over the London Interbank Offered Rate (LIBOR); there are no data on interest rates agreed by official creditors.

Sources: Pfister and Suter (forthcoming: Appendix), Stamm (1987: Appendix).

the actual crisis. Here it was convenient to distinguish between two two-year periods, as it was assumed that with the persistence of the crisis, debt-rescheduling terms were adjusted to the long-term nature of the crisis. For reasons of simplicity, data for official creditor clubs other than the Paris Club have been omitted.

A clear general picture emerges from Table 6.3. Average amounts renegotiated have continually grown and the terms agreed to by debtors have generally been very hard. Consolidation and grace periods as well as maturities were relatively short and on an average 3 percent to over 15 percent of the rescheduled debt had to be paid as scheduled or as a down payment. Unfortunately, there are no data on the interest rates agreed upon by official creditors, but they seem to have been on a commercial basis,[35] as was the case with the banks' interest rates. During the two years immediately following the onset of the debt crisis, banks negotiated for higher than the original interest rates (2 percent over LIBOR on average) and on several occasions exacted so-called rescheduling fees of around 1 percent of the total amount renegotiated. In sum, reschedulings have largely been concluded on commercial terms with only little long-term debt relief.

There are several qualifications in order, however. Most indicators improved significantly during the 1985-1986 period, and this trend continued during the following years.[36] The Paris Club, for its part, has recently deviated from its standard practice of providing debtors with consolidation periods of only one year, maturities of ten, and grace periods of five years. While this rule still applies to the larger debtors, poor debtors have often been provided with 25-year maturities and 10-year grace periods, and in some instances consolidation periods of several years were included in one and the same agreement. In addition, some creditors have unilaterally converted some of their loans into grants on special occasions.[37]

This trend towards better terms for debtors has even been more pronounced for commercial banks. As can be seen in Table 6.3, during the 1985-1986 period interest rates dropped by almost .5 percent (from an average of 1.94 percent to 1.47 percent over LIBOR), and consolidation periods have almost doubled to an average of more than three years (38.5 months). At the same time, maturities have on average lengthened by 2.5 years to 9.6 years and grace periods, too, improved, although only by about half a year (from 3.0 to 3.6 years). From 1987 onwards this trend was consolidated. Presently, interest rates have dropped to an average of under 1 percent over LIBOR, rescheduling fees have been left totally aside and the other terms have also improved. In addition, a large proportion of agreements also included the provision of new money and the maintenance of short-term credit. The fact that during the past years the terms of banks' reschedulings have become more favorable for debtors than those granted by the Paris Club may be associated with the lesser capacity of private creditors to coordinate their interests.

To sum up, the rescheduling strategy can be characterized as follows: (1) The settlement of debt problems is rather quick but also rather provisional. (2) Creditors do not exert any direct influence on debtors, but indirect -- largely economic -- pressure is applied by international organizations, notably the IMF. (3) There has not yet been debt forgiveness on a large scale.

Explaining the Pattern of Debt Settlement

The empirical analysis of this chapter has revealed marked differences between the debt-settlement regimes before and after World War II with respect to the efficacy of the crisis management, the degree of debt relief and the degree of political and economic pressure exerted on debtor countries by the creditors.

The *first* and most obvious difference refers to the efficacy of the debt settlement. In the case of multilateral reschedulings the crisis management is able to respond much more quickly. While agreements between bondholders and debtor countries concerning the settlement of defaulted bonds could be reached only after 6-14 years on the average, multilateral reschedulings were generally concluded within a time span of just one year. Conversely, the durability of debt settlements is considerably higher in the case of default settlements. The fact that debt reschedulings only provide provisional settlements hints at the existence of a trade-off between speed of intervention and durability of solutions.

Second, for debtor countries the terms of debt settlements were much more favorable with respect to defaulted foreign bonds than concerning multilateral reschedulings. Several empirical studies dealing with the interwar period already showed that the settlement of the crisis of the 1930s brought debtor countries a substantial amount of debt relief.[38] The findings of this study demonstrate that this argument can be generalized to all settlements of bond defaults during the nineteenth and twentieth centuries. Moreover, due to the quantitative nature of the indicators, a more precise assessment of real debt relief can be made. Thus, the empirical analysis suggests that on average the settlement of defaulted foreign bonds comprised a reduction of outstanding debts (including arrears of interest) of about 30 percent. With respect to the debt settlements of the crisis of the 1930s, it may be conservatively estimated that up to 50 percent of outstanding debts (including arrears of interest) was liquidated. In addition, interest rates on these reduced debts were lowered by more than one-third. This substantial debt release stands in marked contrast to the harsh terms of rescheduling agreements, especially so during the first years of the debt crisis of the 1980s.

Third, concerning pressures exerted on debtor countries by creditors, it can be concluded that with respect to settlements of defaulted foreign bonds there were only few cases of (open) political and economic control of debtors by creditors. By contrast, there has been substantial but indirect economic pressure by creditors in multilateral reschedulings due to IMF adjustment programs imposed on debtor countries. The empirical analysis has shown that the majority of reschedulings have been tied to such adjustment programs.[39] Basically, this finding is in accordance with Lipson's (1989) hypothesis of more interventionist policies during U.S. hegemony than during British supremacy. Yet, Lipson deals only with political pressures, leaving aside the more important economic control exerted by creditors.

These three regularities are closely associated. Thus, the quick and efficient intervention of creditors together with their capacity to exert pressure on debtor countries to carry out adjustment programs permitted the prevention of any substantial debt relief in the present debt crisis. In accordance with the basic hypothesis, these three regularities can be explained by the increasing institutionalization of creditors' cooperation during the postwar era which has been made possible by the marked concentration of international lending among relatively few actors.

An analysis of the actor structure and the institutional framework of the debt-settlement processes prior to World War II clearly shows a low degree of creditor cooperation. The large number of dispersed individual bondholders made it virtually impossible to organize the creditors which were, consequently, unable to respond quickly to adverse developments and to protect their interests against the borrowers. This explains the low efficacy of debt management, the favorable terms of settlements for debtor countries and the failure of creditors to enforce political and economic control upon debtors.

After World War II the actor structure on the creditors' side substantially changed: instead of individual bondholders, nation-states, international organizations and large bank syndicates began to prevail. This process implied a substantial reduction in the number of actors, which allowed a dense interaction structure. This made it comparatively easy to organize creditor interests in the instances of debt problems, and as those problems grew in number, creditor clubs with clearly defined structures and aims were institutionalized. Yet, owing to the particular features of official and private lending, differences in the organization and efficacy of different creditor clubs exist. The comparative strength of official creditor clubs was partly due to the fact that the principal official lenders also were the most important decisionmaking units in the international organizations, mainly the IMF. These organizations could readily be used as promoters and supervisors of debt and adjustment strategies. Thus, the institutionalization of creditor clubs involved an effective linkage of debt management and economic influence on adjustment. The political and social implications of these austerity policies are the occurrence of massive and unprecedented protests by social movements in debtor countries.[40]

In addition to this basic change in the debt-settlement regime from defaults to rescheduling, two further though less important differences in the crisis management between the three earlier default-settlement periods (1821-1870, 1871-1925 and 1926-1975) have been demonstrated which are consistent with the hypotheses drawn from the concept of world leadership cycles: First, the efficacy of debt settlements was highest during the period 1871-1925. This may be attributed to the stabilizing role of the British financial hegemony during the debt crises of the 1870s and 1890s. Second, there is a trend towards a higher degree of debt relief, with the most favorable terms granted to debtors during the default-settlement period 1926-1975. The high degree of debt relief granted in the settlements concluded after the debt crisis of the 1930s has been explained by the transition of hegemonic power from Britain to the United States.

The relevance of world leadership cycles can also be demonstrated with respect to two aspects of the postwar debt-crisis management: First, the change within the actor structure on the creditors' side which can be considered as the basic prerequisite for the institutionalization of creditor clubs occurred in the context of the shaping of the new economic and political world order by the United States during and after World War II. Thus, the World Bank, the IMF as well as the OECD, which were all established under the leadership of the United States and which initially served as important organizational pillars of U.S. hegemony, have become the institutional core of the rising creditor cooperation during the postwar era. Second, the provisional nature of the current rescheduling approach together with the unfavorable terms for debtors may well be related to the accelerating decline of U.S. hegemony since the 1970s.

Notes

1. Cf. Voss (1985: 203), Pfister and Suter (1987).

2. In the wake of the Portuguese default of 1892, for example, three different bondholders' committees were established in France alone (Union des Porteurs Français de Rentes Portugaises 1893: 21).

3. Cf. Winkler (1933: 153-178), Borchard (1951: 214), Eichengreen and Portes (1989: 15-25).

4. These instances are Colombia (1873), Serbia (1895), Morocco (1903/04) and Liberia (1912); in the case of the Argentine debt crisis of 1890 a consolidation was reached a few months after the suspension (Suter 1990: Appendix A).

5. This figure relates to final agreements only. Temporary arrangements and agreements which did not become effective have been excluded.

6. Cf. Association Française, Association Belge, CFB, *The Economist*. For a more detailed description of the data set and the sources cf. Suter (1990).

7. The average default duration rises to ten years when those eight cases which were not classified into one of the three default-settlement periods are included in the calculation.

8. This figure is lower than Marichal's (1989: 60) estimation of 15-30 years for the duration of defaults by Latin American countries during this period. This difference may be attributed to the more prompt settlement negotiated by the non-Latin American defaulting countries (e.g. Spain or the U.S. states, which were also the most important debtors of those days), indicating the greater relevance of the European periphery and the United States for the international financial system of the early nineteenth century.

9. The model explains only 10 percent of total variance (cf. the value for Eta^2 in Table 6.1).

10. Scheffé's test is the most conservative test for a posteriori contrasts.

11. Similarly, Kindleberger (1973, 1978) explains the severeness of the crisis of the 1930s with the lack of a hegemonic power that felt responsible for the stability of the international financial system. He argues that Britain was not able to act as a lender of last resort and the United States was not willing to do so.

12. Born (1986).

13. The following debtor countries were subject to the establishment of debt administration councils: Tunisia (1869/70, joint debt administration), Egypt (1876, British-French debt administration), the Ottoman Empire (1881, debt administration by Britain, the Netherlands, France, Italy, and Austria-Hungary), Serbia (1895, joint debt administration), Greece (1898, international debt administration by Britain, France, Germany, Italy, Austria-Hungary and Russia), Morocco (1903/04, customs administration by France), the Dominican Republic (1904/08 and 1931, customs administration by the United States), Liberia (1912, debt administration under the direction of the United States with Britain, France and Germany; cf. CFB, *Annual Reports*, 1873-1960).

14. Maximilian was dethroned and executed in 1867, and the Mexican government never paid back the so-called Maximilian debts of some £ 20 million (see also Aggarwal 1989: 143-145).

15. Cf. Lipson (1989: 202-204), Suter (1990: 281-282).

16. Cf. CFB (*Annual Reports*), Suter (1990: 235-282).

17. E.g. Lipson (1985, 1989), Marichal (1989).

18. See also Lindert (1989: 237) and Eichengreen and Portes (1989: 18-20) for an account of government pressures by creditor countries following the crisis of the 1930s.

19. A fourth dimension of debt relief which cannot be analyzed due to the lack of data refers to the reduction in amortization rates. Yet, since amortization rates of foreign bonds usually are rather low, they are only of secondary importance with regard to the degree of debt relief. A further dimension on which systematic data lack is direct buy-backs on capital markets by debtors. Jorgensen and Sachs (1989) estimated the amount of such buy-backs by Latin American defaulters during the crisis of the 1930s at 5-30 percent of total debts.

20. This debt settlement was concluded after the installation of the Austrian archduke Maximilian as emperor of Mexico by France. The arrangement included the conversion of arrears of interest of £2.9 million into new debts of £4.9 million. In addition, France supported the regime with a new 6% bond of £12.4 million of which Maximilian had to pay £4 million to the French government as indemnification for the French military expedition (CFB, *Annual Reports*, 1877: 59, 1930: 260; Wynne 1951b: 27-30; Bazant 1968: 91-96).

21. IMF (1985: 34-39).

22. Lipson (1981: 622).

23. See the discussion in the Conclusion for a more detailed review of recent developments.

24. See Suter et al. (1990).

25. Cf. IMF (1985: 20-25).

26. Cizauskas (1979: 202), IMF (1981: 22).

27. Somewhat the same applies to the reschedulings of Ghana (1966-1974) and Yugoslavia (from 1983 onwards).

28. This was the case in the recurrent debt reschedulings with India, Bangladesh, and Pakistan that took place within an aid consortium chaired by the World Bank. Strategic considerations were involved in the reschedulings of Turkish debts by a group of OECD creditors (1978-1980).

29. IMF (1986: 12), Padoan (1986: 101-102, 131-132).

30. One of them (Nigeria's in 1984) was negotiated with private suppliers.

31. E.g. China 1949, Czechoslovakia 1959, Cuba 1963, Rhodesia 1965 (Suter 1990: 235-282, Cline 1984: 90).

32. Bilateral agreements have been concluded with Uruguay (1965), Egypt (1966), Yugoslavia (1965, 1971), Philippines (1970), Vietnam (1985) and Chile (on several occasions since 1985) (Bittermann 1973: 108-203; Dhonte 1975: 183; *Financial Times*, December 3, 1985; Stamm 1987), whereas temporary deferments were accorded to Zaire, Bolivia, Guyana during the late 1970s and early 1980s (Stamm 1987: 173). Note also that temporary deferments are usually agreed upon as a first emergency measure when a debtor runs into debt-servicing problems. Those deferments are to be substituted by a formal rescheduling agreement. Thus, the renewal of deferments indicates negotiation problems causing the delay or the failure of rescheduling efforts.

33. These attempts include the failure of private banks to implement an economic adjustment program in Peru (1970s, cf. Cline 1981), the fruitless installation of an external financial supervisor in Zaire (1978, cf. Körner et al. 1984: 134-144) as well as the economic sanctions of creditors against Poland in the early 1980s (Stamm 1987: Appendix).

34. Cf. Aronson (1985: 141), Kahler (1986: 265), Eichengreen and Portes (1989), and Lipson (1989).

35. Hardy (1982: 25-26), Lindert (1989: 239-244).

36. Recent developments are discussed in the Conclusion.

37. IMF (1988: 12).

38. Eichengreen and Portes (1989), Jorgensen and Sachs (1989).

39. See also Eichengreen and Lindert (1989).

40. Cf. Walton and Ragin (1990).

PART THREE

Case Studies: The Debt Histories of Peru, Liberia and Turkey

This part deals with the debt histories of individual peripheral countries, thus moving the focus of our analysis from a general perspective of global processes to a more specific examination of the debt problem on the level of the nation-state. This provides a basis to develop a deeper understanding of the interplay between world-system processes and national characteristics. The empirical material presented in Part Two confirmed several basic hypotheses of this study, whereas other important research questions have been left unanswered. Thus, at the global level of the world-economy there is strong evidence for the existence of debt cycles which can be shown to be correlated to long swings in real economic phenomena.

Yet, with the exception of the well-known relevance of declining export receipts coupled with rising debt-service payments for the emergence of debt crises, the basic research questions dealing with the underlying causes of increasing indebtedness and of the outbreak of debt crises have not as yet been explored. A more detailed analysis of these research questions requires a careful examination of the relationships between external debt and the basic economic, political and social structures and dynamics of peripheral borrowers on the level of individual country case studies.

Thus, a basic argument of the theoretical reasoning of this study says that debt-service incapacity has to be partly attributed to inefficient and consumptive use of external financial resources by the periphery due to political and economic constraint to which Third World states are subject (cf. the discussion in Chapter 3). Essentially, this argument rests on a multi-level conception of the world-system: global phenomena – the periodical recurrence of rising indebtedness and of general state insolvency – is explained in part by processes operating on the lower level of individual Third World countries, namely, the interaction between political regimes and external debt.

The theoretical concepts of this interaction together with the methodological considerations for the selection of the country case studies will be outlined in Chapter 7. Chapters 8-10 discuss empirical evidence of the three case histories of Peru, Liberia as well as the Ottoman Empire and Turkey, which present a fair sample of the different debt patterns and the structural diversity of peripheral borrowers.

7

Selection of the Country Case Studies: Methodological Considerations

This chapter deals with theoretical and methodological considerations concerning the choice of the country case studies. Individual Third World countries have experienced quite different debt histories during the nineteenth and twentieth centuries. This diversity may be attributed to the nature of the structural linkages with the world-economy and the related national characteristics of the various debtor countries. In order to disentangle the complex relationships between economic, political and social development on the one hand and the evolution of external debt on the other, this chapter presents a typology of political regimes. Basically, it is postulated that a specific debt pattern on the level of individual countries depends in part on the structure of a given political regime. Thus, the decision to raise foreign loans, the specific use made of external credits, the decision to enter into default on external obligations and to withdraw temporarily from the world-economy are expected to depend on a particular political configuration.

This reasoning presupposes a differentiation of the global mode of production according to systemic levels. While the capitalist mode of production is global in character, its local or regional unfolding requires the presence of coercive state apparatuses which set the rules for surplus appropriation, sometimes even performing this appropriation themselves. In turn, the precise shape of a specific state reflects the interests and alliances of classes present. Thus, it can be argued that the way peripheries are related to the world-system produces specific classes and alliances between them that effect a specific shape and dynamic of the state in the Third World. In addition, the operation of the Third World state has repercussions on processes operating on the level of the world-system at large.

Political Regimes and Their Interaction with External Debt: Concepts and Hypotheses

A political regime is defined as the dominant alliance between the social classes and factions that underlies a given administration.[1] Among those which may be party to an alliance the following can usually be identified: the state class (mainly the military and civilian bureaucracies, including employees of state enterprises), the bourgeoisie divided into different factions according to economic interests (export production, industry, banking and trade), and the urban petty bourgeoisie and labor classes; smaller and medium farmers and rural labor are rarely politically relevant. Depending on the political economy of a society (which in turn is determined in part by its relation to and position within the capitalist world-economy), different constellations of these groups may emerge. Four ideal-typical political regimes will be differentiated: (1) regimes based on a state class, (2) capitalist regimes, (3) populist regimes, and (4) disarticulated regimes.[2]

(1) *Regimes based on a state class:* This type of regime is largely based on a tributary mode of production, that is, surplus is not appropriated through ownership of capital and the commodification of labor but rather through taxes, levies and tributes of all kinds collected from producers by a state class -- be it a feudal group, a group of warriors or a modern state bureaucracy.[3] Three subforms of this regime may be distinguished: (a) former *world-empires* with high autonomy from the capitalist world-economy and based on a powerful cohesive ruling group that controls the sources of tributes; (b) countries where the ruling class is highly fragmented and the state is largely absent, such as the *caudillaje* system in early postcolonial Latin America;[4] (c) *postcolonial states* where a bureaucratic class derives its income mainly from the taxation of a tiny export sector frequently controlled by foreign enterprises. Due to the low articulation of the domestic economy, few socially relevant groups are present besides the state class in all subtypes mentioned above. Lines of conflict emerge primarily between rival factions claiming to pursue strategies which benefit both their own members and the rest of the ruling class. State classes tend to use financial resources largely for consumption, either for themselves or to establish and expand clientelistic networks to enhance regime legitimacy.[5]

(2) Under *capitalist regimes* political power rests in the hands of the class controlling the means of production and deriving its incomes from them. In peripheral economies the groups based on export production (cash crops, meat, minerals) and associated service activities (trade, banking) are usually the dominant elements of the bourgeoisie since the

industrial elite is too weak to dominate the regime. Economically, such regimes are mainly interested in the expansion of the export economy.

(3) The main distinctive feature of *populist regimes* is that they are legitimized by strong support from the urban middle and lower classes or certain rural groups, mobilized by a charismatic political leader.[6] The existence of these classes presupposes a certain development of a domestic capitalist sector with a considerable demand for labor. Hence, the economic base of a populist regime is often provided by light industry oriented towards the processing of raw materials and import-substituting industry. Due to the weakness or hostility of local entrepreneurs, the state is an important agent of development through the creation of infrastructure, social services and perhaps even nationalized industries. Development policies are often aimed at raising the living standards of the urban middle and lower classes and may, through the state expenditures mentioned above, assume a clientelistic character.

(4) *Disarticulated regimes* try to keep social conflict under control through a forced disarticulation or demobilization of political interests. At the same time, political issues are objectified and handed over to a cabinet of specialists or simply to the state administration for resolution or palliation. Such a regime is inclined to take measures to stabilize the state budget and the economic situation in general, including debt-service obligations. The social base of a disarticulated regime is not linked to productive relations; it consists mainly of the control over the repressive apparatus exerted by a faction of the state class (usually the armed forces) or an alliance of several small elite groups. The incapacity of potential opponents to conclude counteralliances sufficiently broad to make a bid for power ensures the regime's survival.[7]

What is the attitude of the four regime types towards external debt? In accordance with the structural features of a debt cycle and with the basic hypotheses and research questions, the following three aspects of external debt will be considered: first, the degree of dependence on external resources and economic efficiency of the investments financed by external resources; second, the proneness to debt-servicing difficulties; and, third, the handling of debt problems.

Regimes based on a state class are commonly heavily dependent on external resources. Declining world-empires are often faced by decreasing tributary revenues. Similarly, the economic base of post-colonial state class regimes is often too narrow to maintain large bureaucracies and clientelistic networks on which their power is based. This suggests that regimes based on a state class tend to borrow abroad whenever their creditworthiness permits it, and that they use external resources largely for consumption. Thus, frequent debt-servicing difficulties may be expected from regimes of this type. Since regimes based on a state class remain dependent on the expansion of the bureaucracy, they often prove incapable of taking effective stabilization measures which bring the state budget under control. Their capacity to manage debt problems is accordingly weak.

Capitalist regimes based on export interests rely little on external finance, and if they resort to it resources are mostly spent productively to expand the infrastructure of the export economy (e.g. railways, roads and harbor works). This implies that capitalist regimes are much less prone to debt-servicing problems. Financial difficulties may possibly emerge as a consequence of stagnating world trade. If debt-servicing difficulties occur they may be promptly managed (at least as long as the export economy remains intact) since the application of temporary stabilization measures does not really threaten the social base of these regimes.

As noted, *populist regimes* rely heavily upon the expansion of state expenditures. Since they find it difficult to broaden their tax base accordingly (usually because the propertied classes form the most important threat to the regime), they depend on a heavy influx of external resources. Because these are mostly spent in an unproductive fashion, debt-service incapacity may loom over the long run. As in the case of regimes based on a state class, populist regimes are usually not very successful in handling debt problems since stabilization policies directly undermine their social base (i.e. the support from urban middle and lower classes).

Disarticulated regimes rarely depend on foreign debt. However, if they resort to external resources they may be inclined to spend them in an unproductive fashion to expand the military apparatus. If debt-servicing difficulties occur during disarticulated regimes, they may often be traced back to previous regimes (e.g. to regimes based on a state class or populist regimes). Due to the demobilization of political interests and their reliance on technocratic expertise, disarticulated regimes are expected to be most capable of firm stabilization measures to manage existing debt problems and restore financial health.

Methodological Considerations

The reader of the previous section may have noted that the classification of different political regimes is based on ideal-typical constructs. Ideal types have been used by Max Weber as important methodological instruments and conceptual tools. An ideal type is not a description of a real situation but an analytical construct focusing on certain properties (or on a configuration of several characteristics) of a phenomenon. For Max Weber (1949, 1978), ideal types are constructed by a one-sided accentuation of one or more viewpoints. With its conceptual purity, the ideal type serves as point of reference for comparisons with concrete empirical phenomena. The construction of ideal types is a useful method for comparative research.[8] Therefore, in this study ideal types serve less to illuminate a specific empirical situation (as was Weber's approach) than to provide a conceptual tool for a systematic cross-national analysis of case histories. More specifically, the typology of political regimes developed in the previous section is used to understand and to explain varying national debt histories against the background of the general debt pattern on the global level of the world-economy as examined in Part Two.

Apart from availability of data, the decision concerning the inclusion or exclusion of a country is based on the following reasoning: First, attempts were made to include countries with varying debt patterns and debt careers regarding the involvement in subsequent debt cycles. Second, to get a fair sample of the structural diversity present among peripheral countries, debtors of varying economic, political, social and cultural characteristics were considered. Hence, I selected three countries[9] which appear to be representative of the major forms of relationships peripheries have had with the world-system over the last 200 years -- the main variable behind the formation and dynamic of political regimes.

Peru forms the classical case of an average peripheral country. It was integrated early into the world-economy through a primary commodity-producing export sector whose dynamic moves quite parallel to global Kondratieff cycles. Periodically, it experienced limited national industrial development providing the prerequisites for the emergence of capitalist and populist regimes. Finally, Peru was involved in all major debt cycles. A number of other less-developed Latin American countries shared this experience to a varying degree (e.g. Bolivia, Chile, Mexico, Uruguay).

Liberia is taken as an example of the extreme periphery, integrated into the world-economy much later than Peru through an important primary sector geared to export production. The difference with regard to the case of Peru lies basically in the relative weakness of its national social, economic and political structures. It consists of an economy whose modern sector is exclusively based on a foreign-dominated enclave economy producing for export and possessing only weak linkages to the domestic economy. Its political evolution is characterized by a continued dominance of the state class. Like Peru, Liberia was involved in all major debt cycles since its political independence. However, the weakness of its economic structure implies that Liberia was subject to further debt crises in between brought about by developments largely outside of its immediate control. Similar examples from the post-World War II period are the mining economies of Sierra Leone, Zaire or Zambia.

Turkey (and formerly the *Ottoman Empire*) presents the case of a world-empire which was gradually dissolved and peripheralized within the capitalist world-economy during the nineteenth century. The Turkish republic is one of the nation-states emerging after its final dissolution in the early twentieth century. The initial presence of a strong state not geared to capitalist development and the gradual loss of control by the state class led to a specific dynamic with regard to external debt; together with other remnants of former empires (northern Africa, China, and with certain qualifications Spain), the Ottoman Empire was a chronic heavyweight debtor before World War I.

The case studies of the following chapters are largely based on the existing economic, sociological and political literature dealing with the respective countries. Primary research was confined to a reconstruction of individual debt histories.[10] Due to space restrictions the presentations necessarily remain very schematic. The discussion of the case studies focuses on four basic research questions and hypotheses. A first aspect refers to the empirical evidence concerning the existence of debt cycles (i.e. the occurrence of consecutive phases of debt expansion, debt-service incapacities and debt settlement on the level of the nation-state), with special emphasis on similarities and differences between the national and the global pattern. A second research question concerns the economic, political and sociological factors causing debt expansion, with a focus on the uses made of foreign loans by the respective debtor countries -- an aspect not considered in the empirical analysis of Part Two. A third question refers to the causes and determinants of debt-service incapacity, especially with respect to the period prior to 1930 for which no data was available on the global level. Finally, the negotiation process between creditors and insolvent individual debtor countries and the specific outcome of the debt settlements will be dealt with.

Notes

1. This definition is inspired by Cardoso's (1979: 38-40) conception of the state and by the studies of Hischier and Heintz (1982) and Hischier (1987).

2. Cf. Pfister and Suter (1989) for a detailed discussion of this typology.

3. Cf. Wolf (1982: 79-88).

4. Wolf and Hansen (1967).

5. Cf. Djilas (1957), Alavi (1972), Petras (1977), Elsenhans (1981) and Evans (1989) for a discussion of the concepts of "state bourgeoisie," "state-capitalist

bureaucracy," "bureaucratic-military oligarchy," "bureaucratic class" and "state class."

6. Cf. Di Tella (1965) and Germani (1978); see also the terms "inclusionary bureaucratic-authoritarianism" or "inclusionary corporatism" as discussed by Cardoso (1979), Collier (1979) and Stepan (1978).

7. This definition of disarticulated regimes corresponds to the concepts of "bureaucratic authoritarianism" introduced by O'Donnell (1973) and of "exclusionary corporatism" suggested by Stepan (1978); cf. also Collier (1979).

8. Cf. Kohn (1987) for a methodological discussion of comparative and cross-national research strategies.

9. A fourth case study (on Argentina) is discussed in Suter (1990) and summarized in Suter and Pfister (1989).

10. The material used in the following three chapters is based on the data gathered by Suter (1990), which consists of a detailed compilation of credit-raising activity, defaults and debt settlements of the respective sovereign borrowers between 1820 and 1986 (cf. also the Appendix of this book).

8

Peru: The Classical Case

When people lend to Peru . . . they are simply speculating in guano. We need not . . . point out that such a speculation is not for private investors.
—*The Economist*, March 23, 1872, four years prior to Peruvian default in 1876

The debt history of Peru can be divided into four cycles all passing through the same sequences of debt expansion, outbreak of financial crisis and debt settlement. Chronologically these cycles may be determined as follows: the first cycle from about 1820 to about 1840; the second cycle from about 1840 to about 1880/90; the third cycle from about 1890 to about 1940/50; and the fourth and current debt cycle starting in the 1950s. In the following sections each of these four historical debt cycles is described and explained in detail.

The First Debt Cycle: The Formation of the Nation-State

The Peruvian nation-state emerged during the war of independence against the Spanish colonial rule in South America. Compared to the rest of Latin America, the movement of independence in Peru was successful only at a late stage. Among other things this had to do with the fact that the colonial administration in Spain's most important and richest viceroyalty was quite large and powerful, and therefore it stayed intact even during the early years of the nineteenth century. At the same time the liberal movement in Lima was weak and did not principally object to the imperial structure but rather advocated reforms within the colonial framework. Eventually, Peru was conquered by the army of San Martín, who in 1821 announced independence. Nevertheless, the final victory over the Spanish troops could only be achieved in 1824 with the help of Bolívar.[1]

Between 1822 and 1825 the Peruvian state raised its first two foreign loans from British bankers. The interest rate of the foreign bonds nominally totalling £1.816 million was 6 percent. Since the issues were sold to the public at a price varying between 78 and 88 percent, the amount actually realized only came to £1.5 million. Real receipts were even lower, since the Peruvian government was additionally charged for commissions to brokers and financial intermediaries. Interest payments for the first two years were also deducted from the amount paid out. The proceeds from the loans were mainly used for financing the national war of independence. Thus, with the money from the 1822 bond, Peru bought ammunition from Britain; the bond raised in 1825 was used to pay arrears of wages to the troops.[2]

By the time of the final victory over the Spanish army in early 1826, only three years after the first bond had been raised, the Peruvian government fell into default on its external obligations and remained so until 1848. The main reason for these first debt-servicing difficulties lies in the failure of the young Peruvian nation-state to collect a sufficient amount of taxes for debt service. The fragility and weakness of the Peruvian state after independence have to be considered in the context of the political and economic disintegration that took place after the end of the Spanish colonial rule. On the political level a *caudillaje* system characterized by unstable governments and frequent takeovers by local military *caudillos* prevailed. Against the background of the typology of political regimes developed in the previous chapter, the *caudillaje* period of 1827-1845 represents a fragmented state class. This period saw a rapid succession of sixteen governments led by military entrepreneurs that were supported by factions of the provincial-based landed aristocracy.[3] The Peruvian elite consisted of the large landowners of the highland (sierra), called *gamonales,* who mainly produced foods for the local market (and in the south leather and wool for export); coastal *hacendados* engaged in commercial agriculture (mostly sugar and cotton plantations, originally based on slave labor); as well as the urban commercial and financial bourgeoisie.[4] Yet, these ruling groups did not succeed in building up a common political base. Rather, a political stalemate between the different factions within the elite prevailed.

This political instability went hand in hand with an economic decline. The wars of independence caused a decay of the administrative and economic infrastructure of the old colonial order. In the sierra production relapsed to subsistence level. Mining suffered from technological backwardness, the exhaustion of the silver mines and a chronic shortage of labor. The coastal plantation-economy lost its cheap slave labor force as the slaves were recruited to the national liberation army and were liberated later. As a result of economic stagnation, state income diminished, making it impossible to build up a strong national government. After Peru had blocked itself from getting any foreign credits by defaulting on its external debts, the Indian tribute (head tax) collected by local *caudillos* remained the main (and highly unstable) source of state income. Particularly through the Indian tribute, the provincial elite gained a strong economic base enabling them and allied military *caudillos* to challenge the central government. Only the abolition of the tribute (in 1854), made possible by the development of new sources of state income from guano sales, permitted weakening the provincial elite decisively.[5]

The Second Debt Cycle: Rise and Decline of the Guano Era

Peru's economic situation improved only with the discovery of large deposits of guano in the 1830s and 1840s and the subsequent demand for this fertilizer from European core countries.[6] In 1842 the Peruvian government declared the deposits of guano a state monopoly and thus secured a new source of state income. The government did not carry out the exploitation itself though. Initially, extraction and exportation of guano was predominantly in the hands of foreign enterprises but became completely controlled by the Peruvian commercial bourgeoisie by the early 1860s.[7]

The Peruvian guano economy represents a typical enclave economy showing only few ties with the rest of the national economy and initiating, therefore, no growth processes in other sectors and areas of the national economy. The exploitation of guano on the islands off the Peruvian mainland was separated even geographically from the rest of the economy. Because guano could be extracted without any capital investment worth mentioning by using very simple technologies (shovel and pick) and could be transported by traditional means, it had hardly any economic forward linkages. Similarly, there were no backward linkages since no further processing was needed. Moreover, the necessary labor force was not provided by Peruvians but by Chinese coolies.[8]

Politically, the breakthrough of the guano economy marked the end of the unstable *caudillaje* governments. Receipts from the guano monopoly increased public income of the central government considerably and enabled it to put the national budget back on its feet within a short time. As a result, a marked shift in the financial base of the state occurred: By the early 1860s guano revenues made up some 80 percent of state income. Conversely, the Indian tribute, the principal source of state income during the first half of the nineteenth century, was abolished in 1854, leading to a weakening of the economic base of the provincial elite, which now became more dependent upon the central bureaucracy in Lima. The new financial means were mainly used for the expansion of the civilian and military state bureaucracy, thus allowing the strengthening of the central government in Lima against provincial revolts. Another part of the resources were spent on payments for coastal *hacendados* in compensation for the abolition of slavery. This led to a reorganization and to considerable new investments within commercial agriculture and caused the revival of the coastal area's cotton and sugar production. In addition, a national bank system emerged channelling parts of private profits from the guano business into the agricultural export sector, which as a result of the rising demand caused by the American Civil War, experienced a boom.[9]

During the guano era the dominant political system showed characteristics of both an export oligarchy and a regime based on a state class. The social base of the regime consisted of a coalition of the urban commercial and financial bourgeoisie engaged in the guano business, coastal *hacendados* engaged in agricultural export production as well as the expanding state bureaucracy. A remarkable role in the consolidation of this regime was played by President Ramón Castilla (1845-1851, 1855-1862). Politics was exclusively controlled by the narrow oligarchic elite. Interest articulation took place within elite clubs and elite producer associations. By the turn of the century only 2 percent of the total population was entitled to vote. Moreover, landed interests of the highland controlled parliament due to the electoral law which favored the provincial aristocracy. It has to be mentioned though that during the guano era the oligarchic rule was never firmly institutionalized. Thus, an elite association which could have integrated the different elite factions was missing; only in 1896 was the Sociedad Nacional Agraria (SNA), the association of large landowners, established.[10] During the late phase of the guano era a clear shift towards a regime based on a state class took place when President José Balta (1868-1872), supported by the provincial elite and the newly emerged state bureaucracy, transferred the monopoly of guano sales from local merchants to the French Dreyfus company, which offered more favorable conditions to the government.

As a consequence of its improved financial situation at the end of the 1840s, Peru was striving for a regulation of the foreign bonds defaulted in 1826 (see Table 8.1). Already in 1846 first suggestions were being discussed by Peru and its creditors. A formal debt-settlement agreement was finally signed at the end of January 1849. The outstanding debts of £1.8 million were converted at par into new loans, and the interest rate was fixed at initially 4 percent, rising annually by 0.5 percent up to a maximum of 6 percent. The accumulated arrears of interest were converted at a rate of 75 percent into new bonds amounting to £2 million, with an interest rate starting with 1 percent (from 1852

TABLE 8.1 Debt-Servicing Difficulties and Debt Settlements of Peru, 1826-1953

1826-1849	All loans in default. 1849 debt settlement agreed with creditors: conversion of outstanding principal into new bonds and capitalization of arrears of interest at 75 percent into deferred bonds; payments secured by guano sales to Great Britain.
1876-1889	Default on all external obligations. A settlement with bondholders was reached in the Grace contract of 1889; the loans of 1869-1872 cancelled altogether in return for (1) the assignment of the state railways for 66 years, (2) 2 million tons of guano, (3) annual payments of £28,000 for 30 years from custom revenues, and (4) the concession for the operation of steamboats on Lake Titicaca.
1931-1953	Default on all external obligations (roughly some $100 million). A settlement with U.S. bondholders reached in 1951 and with British bondholders in 1953; payments resumed during the same year; 90 percent of arrears of interest cancelled and interest rates reduced to 3 percent.

Sources: CFB (*Annual Report*, 1877: 52-75, 1960: 316), Wynne (1951b: 107-195), Mathew (1970), Suter (1990: 270-272).

onwards) and rising to a maximum of 3 percent (from 1856 onwards). Interest payments were guaranteed by the proceeds from half the guano sales to Britain. As a result of the capitalization of arrears of interest, total foreign debt of the Peruvian state more than doubled to about £4 million through this debt settlement.

The debt settlement agreed on with creditors as well as the expansion of guano exports made Peru creditworthy on the international capital markets again. Only four years after Peru had resumed interest payments it succeeded in raising a 4.5 percent bond at a face value of £2.6 million. The proceeds of the bond were used for the repayment of the loans consolidated in 1849 (£1.5 million), the repayment of old revolutionary debts to Chile (£600,000), and the consolidation of internal debts.[11] Similarly, subsequent foreign bonds contracted in 1862 and 1865 (£5.5 million and £10 million nominal, respectively), were exclusively spent on the consolidation of existing external and internal debts. In connection with the war against Spain, in 1866 Peru and its ally Chile tried to raise a medium-term loan in the United States. Yet, out of the initially envisaged amount of $10 million, only $2 million was issued, of which just $1.5 million was eventually subscribed, which was used to buy military equipment.[12] To sum up, during the first two decades after the debt settlement of 1849, foreign loans were not used to finance any productive investments but rather to restructure existing external and internal debts.

Since the early 1860s the stagnation of guano sales, caused by the progressive exhaustion of guano deposits and the introduction of artificial fertilizer, brought Peru's export-led development into difficulties. The war against Spain (1864-1866) severely disturbed public finances. As a result, all existing contracts with local guano merchants were terminated and the monopoly on the guano sale to Europe was transferred to the French company Dreyfus, resulting in more favorable terms for the government. Apart from taxes on guano sales, Dreyfus also took over all internal debts of the Peruvian government vis-à-vis the former guano traders, as well as debt-service payments to foreign creditors, and committed itself to mobilizing new foreign credits for Peru.

Between 1869 and 1872 Peru raised large foreign loans to finance an ambitious railway construction program. A first but small 5 percent bond of £290,000 contracted in 1869 was used to finish the short railroad leading from Pisco to Yca in the coastal area south of Lima. Two large bonds amounting to £12 million and £37 million were raised in 1870 and 1872, respectively. Besides the consolidation of former debts, they were used to realize two railway lines across the Andes, namely, from Callao/Lima to La Oroya in the north and from the port of Mollendo to Arequipa and to Puno/Lake Titicaca in the south. In the mid-1870s Peru had the longest railway network among all Latin American countries and, at the same time, the largest amount of foreign debts, totalling up to £40 million.[13]

The shorter railroads in the coastal area were profitable investments, whereas the long and spectacular railroads in the Andes turned out to be a financial fiasco. The northern of the two Andean lines could not be completed due to a shortage of funds. Moreover, the railways crossed largely uninhabited areas without any trade worth mentioning. Thus, only one wagon a month was needed to transport silver production from the Andean mining region. Hence, it is not surprising that in the mid-1880s the mere maintenance costs highly exceeded the income from the existing lines.[14] The Peruvian president Pardo (1872-1876), who came to power in the midst of the debt crisis, quite bluntly complained about the unproductive railway investments:

> My predecessor, Balta, formed the idea to convert our guano into railways. In two years he contracted for nine railways, to cost 125 million dollars -- say, 24 millions sterling, which money being raised by foreign loans. . . . Such enormous loans soon crippled us, as the railways were unproductive.[15]

However, economic motives may have played a secondary role in Balta's plans, as railway construction was also considered a means to further the national integration of the Peruvian society and to acquire new sources of state income.[16]

The 1870s were characterized by an increasing disintegration of Peru's guano economy. As a result of declining guano exports the government was confronted with increasing payment difficulties. The proceeds from guano shipments were nearly fully absorbed by the accruing debt service: In 1869 guano exports still brought in more than £4 million and debt-service payments came to £1 million, whereas in 1875 revenues from guano exports dropped to £2.6 million while, at the same time, debt-service obligations rose to £2.57 million.[17] In 1873 the French company Dreyfus which had been entrusted with the marketing of Peruvian guano deposits refused to continue meeting Peru's debt service from the profits of its guano sales as originally agreed. Peru and Dreyfus came to the compromise that Dreyfus continue payments until mid-1875. Yet, for interest falling due on January 1, 1876, the necessary financial resources were lacking and, since Peru was unable to mobilize any new credits, debt-service payments were suspended (see Table 8.1).

After the collapse of the guano economy, export-oriented agricultural production of the coastal area underwent a crisis in the second half of the 1870s.[18] After a decade of boom, world market prices of sugar collapsed. Indebted planters suffered from a general cutback of credits and a decreasing supply of cheap Chinese labor. The government of Pardo (1872-1876), which relied on the newly founded *civilista* party, a coalition between the exporting planter-elite of the coastal area and the urban commercial bourgeoisie, tried to overcome the crisis by reducing military expenses and by nationalizing the nitrate deposits.[19] Both policies turned out to be gross failures, though: The cutback of the military budget provoked several military uprisings and caused the temporary loss of political control by the central government. The efforts of the Peruvian government to establish a monopoly on nitrate extraction and export that was controlled by Chilean and British capital led to the Pacific War (1879-1881) between Chile, Peru and Bolivia. The superior Chilean military forces devastated the rich coastal agricultural areas, occupied most important ports in the guano and nitrate provinces and thus deprived the Peruvian state of its principal sources of income. The agricultural production of the coastal region declined to subsistence level, and at the end of the war, the guano economy had totally broken down.

The Third Debt Cycle: From Grace Contract to Populist Deficit Spending

The 1880s were characterized by continuous economic stagnation and political instability. The authoritarian government of General Cáceres (1884-1890) tried to overcome depression by economic adjustment policies and attempted to rebuild an economic structure based on exports. As a prerequisite some degree of financial health had to be restored, and negotiations were taken up with foreign bondholders to reach a settlement on external liabilities and, at the same time, to attract new foreign capital.[20] This led to a debt-settlement agreement with foreign creditors in 1889 known as the Grace contract which cancelled the claims of foreign bondholders of the loans of 1869, 1870 and 1872, including the accumulated arrears in interest, amounting altogether to about £55 million. In return for this debt release, Peru handed 2 million tons of guano over to foreign bondholders and ceded the whole national state railways with a network of seven lines and a length of 769 miles for a period of 66 years to them, while bondholders committed themselves to the construction of certain extensions. In addition, the Peruvian state had to pay bondholders an annuity of £28,000[21] over a period of 30 years and to assign the concession for the operation of steamboats on Lake Titicaca to them. In additional agreements, 5 million acres of land were given to bondholders for colonisation purposes (cf. Table 8.1). Thus, the Grace contract released the Peruvian state of virtually all of its foreign debt burdens, but only at the price of a massive denationalization of its economy.

However, the harmony between Peru and its foreign creditors did not last long. The London Baring crisis and a steep decline of the world silver price around 1892 made foreign investment unattractive and resulted in a serious recession in Peru, with its silver-based currency. As a consequence, the government coalition which supported Cáceres and which pursued an outward-looking path of development was weakened and finally dissolved. The close relationship between debt management and political events is documented by the great importance the critique of the conditions of the Grace contract had in the political life of those years.[22]

Despite the debt settlement of 1889, Peru did not succeed in mobilizing new foreign credits until 1906, when £600,000 destined for the purchase of war ships could be raised from German banks. The foreign bond of 1906 was payed off three years later by means of a new bond granted by French bankers. In addition, the bond of 1909 was used to consolidate internal public debts and to purchase ammunition from

France.[23] These two quite small bonds remained the only foreign debts of the Peruvian state until the 1920s.

The second half of the 1890s and the first years of the twentieth century were characterized by a considerable degree of autonomy with regard to development.[24] On the one hand, new export sectors developed (sugar, wool, rubber and copper in particular) which were mostly in domestic hands. On the other hand, conditions were favorable for an import-substituting industrialization: The depreciation in the wake of falling silver prices increased the relative prices of imports, and the government, deprived of half its revenues by the Grace contract of 1889, began to levy import tariffs. Hence, capitalists engaged in the thriving export sector reinvested part of their immense profits of the late 1890s in the industrial sector producing for a domestic market. Demand was provided by the workers engaged in labor-intensive export industries (sugar, copper, silver) and the growing urban population. What we find, therefore, is the emergence of a diversified structure of commodity exports combined with an industry geared to substitute for the import of simple consumer goods (notably textiles, but also matches, soap, etc.).

On the political level, these developments are reflected in the emergence of a stable regime that was based on export interests. A coalition ascended to power that consisted of coastal export-oriented *hacendados*, the traditional elite of the sierra, and the local merchant and financial bourgeoisie. This alliance of a typical export oligarchy organized mostly within the *civilista* party dominated the Peruvian state until 1919. The *civilista* hegemony reached its climax during the first term of José Pardo y Barreda (1904-1908), son of the first *civilista* president.

During the first two decades of the twentieth century, a considerable denationalization of the Peruvian economy set in, which, combined with a declining level of industrialization, accentuated peripherization again.[25] In most cases, existing and profitable Peruvian enterprises were taken over by large foreign (mostly U.S.) firms. The main reason for this can be seen in the larger technological and financial capacity together with a greater availability of information which led the international firms to attach higher value to the Peruvian enterprises than did the Peruvians themselves.[26] Likewise, increasing international competition with regard to industrial products, declining shipping rates and faltering levels of protection decreased the profitability of investment in the local industry. As long as exports were profitable (particularly during the First World War), capital in part shifted to the export sector. Paradoxically, this was aided by a powerful local financial system which had emerged during the 1890s. As a consequence, the importance of industry declined in comparison with the primary sector during this period.[27]

The penetration of foreign private capital into the Peruvian economy caused losses in state income and foreign earnings (through repatriation of profits) and affected adversely the domestic potential for national capital accumulation.[28] The consequent weakening of the domestic industrial bourgeoisie and the emergence of large new urban groups led to increasing pressures on the ruling export oligarchy by populist forces. In 1912-1914 there was a proto-populist interlude with President Guillermo Billinghurst, and in 1919 a populist alliance came to power with the *oncenio* of Augusto Leguía (the 11-year period of Leguía's rule, 1919-1930).[29]

Supported by the middle classes (including the industrial bourgeoisie) and at least in the beginning by labor and student movements, Leguía was strongly opposed to the export-oriented oligarchy and the landed aristocracy of the sierra.[30] The government secured the interests of national industries by protectionist trade policies. In order to raise the living standards and employment opportunities of the urban groups, Leguía expanded the state apparatus and increased government spending for infrastructure and public utilities. The financial resources were provided by domestic and external borrowing and increased taxation, mainly of the agricultural export oligarchy. As a result, a new wave of massive external borrowing by the Peruvian government took place. Thus, during Leguía's *oncenio*, foreign debts of the Peruvian state increased from about $6 million to $120 million.[31]

Apart from Leguía's policy of externally financed populist deficitspending, the debt wave of the 1920s has to be attributed to the race after profitable investment opportunities by U.S. bankers. Owing to high commissions and charges, which could amount up to 10 percent of the face value of a bond, the bankers made exorbitant profits.[32] In 1922 the Peruvian government raised its first two foreign bonds after the loan of 1909 amounting to $2 million and £1.3 million, bearing interest rates of 8 percent and 7.5 percent, respectively. The two bonds were used to finance large budget deficits caused by a drastic decline in state revenues due to the collapse of world market prices for raw materials after World War I. Between 1924 and 1927, five foreign bonds with a total amount of $47.5 million were issued in the United States destined for the realization of large public infrastructure projects.[33] A substantial part of these financial resources, however, was wasted within the growing state bureaucracy and the entourage of Leguía. Thus, Juan Leguía, son of the president, received a commission of $416,000 for arranging foreign bonds.[34] In 1927/28 outstanding capital of all foreign loans, with the exception of two bonds, was consolidated into new debts. Originally, $100 million was issued. Due to the declining creditworthiness of Peru, only $85 million was eventually subscribed. Debt-service payments on the loan were secured by the whole state revenues except proceeds from the customs and from several state monopolies (i.e. guano, telegraphs).[35]

The Peruvian economy suffered from low productivity of public-sector investments and from waste and misallocation in the use of financial resources borrowed abroad.[36] This caused a deterioration of the financial situation towards the end of the 1920s. In the second half of 1929 the government was forced to raise short-term credits amounting to $5 million from New York bankers since the country was not able to get long-term loans due to its rapidly declining creditworthiness.[37] At the same time, the government of Leguía lost its political support within the urban lower and middle classes and increasingly took refuge in repressive policies. The final blow came from the collapse of world trade after 1929, which hit export receipts badly. Thus, Peruvian export revenues fell by 71 percent from 1929 to 1933.[38] The resulting decline in government income together with the inability to raise further loans due to the collapse of international and local capital markets destroyed the economic base of the regime. When the government finally tried to cut back military expenses, the army revolted and deposed Leguía. Shortly afterwards, in May 1931, the new Peruvian government suspended debt-service payments on all its foreign bonds.

The outbreak of the debt crisis in 1931 has to be attributed to a combination of internal and external factors. The most important internal reason is the unproductive use made of the external resources. The external and more immediate factors include the drastic collapse of export earnings from 1929 onwards and the complete failure to mobilize new loans.

The Fourth Debt Cycle: Buildup and Crisis of Import-Substituting Industrialization

The fall of Leguía provoked a political crisis in Peru. The traditional export oligarchy which had been seriously weakened by both Leguía's policy and the collapse of the world market was largely disorganized and not able to seize and control political power exclusively. Rather, it was forced to ally with the right-wing populist and fascist movement of Luis Sánchez Cerro, who was president from 1931 to 1933.[39] The government of Sánchez Cerro was challenged though by the working class organized within the Alianza Popular Revolucionaria Americana (APRA). Under the charismatic leadership of Haya de la Torre, APRA organized several uprisings and armed revolts.[40] The conflict between the export oligarchy and the populist forces organized within the APRA continued under the governments of General Oscar Benavides (1933-1939) and Manuel Prado y Ugarteche (1939-1945). The general policy pursued by these governments protected the interests of the export oligarchy. Since the social base of the regime was rather narrow, it had to rely on repression rather than on social consensus. The political regime during the period 1933-1945 can thus be characterized as disarticulated.[41]

Regarding economic development, the years between the end of the Leguía government and 1948 were marked by a certain degree of autonomy which was, however, less pronounced than in other Latin American countries. This was probably due to the fact that Peru was less hit by the Great Depression than its neighbors: Exports recovered quickly after 1933, particularly those of cotton,[42] but on the whole it took a long time to get back to the earlier dynamic. The rapid expansion of cotton production meant that a greater share of export revenues remained in the country and could be reinvested. Furthermore, the income derived from cotton production was distributed comparatively equally, resulting in an expansion of local demand for mass products. As a consequence, Peru experienced a certain amount of autonomous development through import substitution.[43] This tendency, however, was less pronounced than in other Latin American countries or compared to the 1890s. Hence, economic policy during the 1930s largely followed a liberal path in trying to restore financial health, mostly in response to Leguía's discredited policy of externally financed deficits.

In spite of the default of 1931, Peru occasionally made some payments to foreign creditors during the 1930s and 1940s. Thus, in 1938 a settlement reducing interest rates from 7.5 percent to 4 percent was agreed upon with the British investors of the bond raised in 1922.[44] Debt-service payments for the rest of foreign liabilities remained suspended though. Suggestions made by the Peruvian government in 1947 and 1949 to reduce interest rates to 2.5 percent and to release all arrears of interest were rejected by bondholders. Eventually, a settlement was reached in 1951 with the American investors and two years later with the British bondholders. It included a reduction of interest rates to 3 percent (from originally 6-7 percent) and a cancellation of 90 percent of accumulated arrears of interest (cf. Table 8.1).

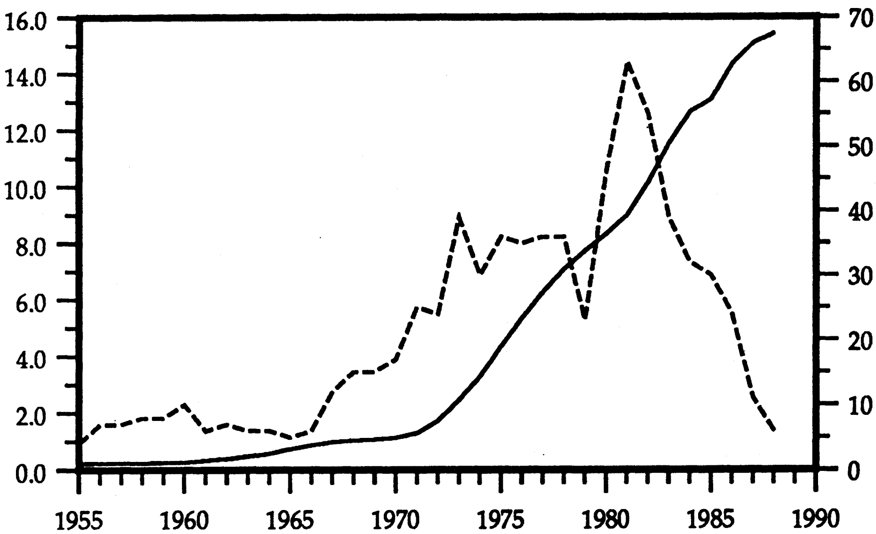
The debt settlement of 1951/53 was extremely favorable for Peru -- especially if compared with the agreements of 1849 and 1889. It took place within the framework of the outward-oriented development strategy pursued by the regime of General Odría (1948-1956), who had overthrown a short-lived populist alliance under Bustamante. The government of Odría relied mainly on the army and the traditional agrarian elite of the sierra. In the beginning Odría was also supported by the export-oriented factions of the Peruvian oligarchy, which was strongly opposed to the populist regime of Bustamante. After his deposition the export oligarchy demanded a civil government which

Odría refused. As a result of losing support within the export oligarchy, Odría tried to co-opt the labor class and the urban poor through the introduction of employment policies as well as programs of urban development.[45] Economically, Odría's government profited from favorable price developments for raw materials on the world market due to the Korean boom. The export sector was promoted by liberalizing foreign trade regulations and by a new mining law favoring foreign capital. This led to a quick expansion of exports, with copper and fish meal replacing cotton and sugar as the most important export goods. It was mainly foreign capital (from the United States) that gained, at the expense of the domestic enterprises, from this development.[46] The main reason for the declining importance of local capital seems to have been the great amount of capital necessary to render new projects profitable, which only transnational enterprises could mobilize. The declining profitability of small and medium-sized production units in the export sector was also in part responsible for the decline in the export dynamic from the mid-1960s onwards.[47]

Odría's outward-oriented development model was continued during the second term of Manuel Prado (1956-1962). Prado mainly relied on the urban financial and commercial bourgeoisie and the agricultural export interests. Compared to the government of Odría this represents a shift from the traditional (and not export-oriented) agricultural elite to the urban and export-oriented factions of the oligarchy. Yet, to get elected Prado also needed some mass support. The fact that he depended on the support of the APRA for this indicates the organizational weakness of the export oligarchy, which had no party structures but was still confined to narrow elite clubs and associations. The political compromise of Prado and APRA, which became known as the *convivencia* brought APRA back into political legality. The willingness of APRA to compromise with the oligarchic government of Prado enabled new reformist and anti-oligarchic parties to gain a foothold among the lower and middle classes. In the left-wing side of the political spectrum, several Marxist parties and movements and in the center the Acción Popular (AP) and the Christian Democrats emerged.

With Fernando Belaúnde Terry and his AP, a reformist liberal populist regime came to power in 1963 which basically relied on the urban middle class and the industrial bourgeoisie. Belaúnde was also able to gain support from peasants and the labor-class movement. Belaúnde envisaged several important structural reforms, such as an agrarian reform and a tax reform. He promoted the formation of an import-substituting industry of durable consumer goods. Yet, since the government had no majority in the parliament, most of these reform projects were aborted.[48]

FIGURE 8.1 Peruvian External Public Debt and Debt-Service Ratio, 1955-1989



—— Outstanding external public and publicly guaranteed long-term debt, including undisbursed debt, in $ billion, 3-year moving averages (left scale).
--- Percent share of debt-service payments to export earnings (right scale).

Sources: Avramovic (1958: 163, 1964: 104), Scheetz (1986: 184), Uriarte (1986: 48), World Bank (*World Debt Tables*, 1986/87-1990/91).

Stimulated by both favorable developments of the terms of trade and massive public spending, Peru experienced a substantial economic growth amounting to 5-7 percent annually during the first three years of Belaúnde's government.[49] Most of the gains of economic growth during this period went to capital; wages barely increased in real terms.[50] Therefore, political pressure towards a redistributive populist policy grew. Under Belaúnde the rising demands of the popular sector were met by an expansion of government spending, mostly on unproductive current expenditure (increase in the salary of teachers -- a politically highly important group -- and generous retirement provisions).[51]

Due to the political stalemate in the parliament, the expansion of public expenditure was not accompanied by an increase of tax revenue.[52] Belaúnde tried to finance the resulting deficits by resorting to inflationary policies and by raising foreign loans. Domestic credit expansion together with an overvalued exchange rate contributed to massive import increases in 1965/66, a time in which exports began to lose their dynamic partly due to declining investments in response to the unfavorable political situation. For a short time balance-of-payment deficits could be bridged by further external borrowing, particularly from private sources. As a result, outstanding indebtedness, which mainly consisted of short- and medium-term credits, began to increase enormously. As demonstrated in Figure 8.1, foreign debts doubled between 1963 and 1966 and reached $1,000 million at the end of the decade. Increasing deficits and waning export receipts together with a lower inflow of new loans led to the outbreak of a public budget and balance-of-payments crisis in 1966/67.

At the same time an intensification of political and social turmoil occurred. Political conflict reached its peak in 1965/66 when the government of Belaúnde was confronted with a guerrilla movement which could only be overcome by military action. In parliament a stale-

TABLE 8.2 Debt-Servicing Difficulties and Multilateral Rescheduling Agreements of Peru, 1968-1985

1968	Restructuring of maturities between July 1968 and December 1969 by bilateral arrangements: 1) $128 million covered by U.S. and Canadian banks; 2) $58 million taken over by European governments and Japanese official and private creditors.
1969-1970	Restructuring of maturities 1970-1972 granted by bilateral arrangements: 1) $40-90 million covered by U.S. and Canadian banks; 2) some $300 million granted by European and Japanese official and private creditors.
1978	IMF stabilization program and multilateral reschedulings with official and private creditors for credits falling due between June 1978 and December 1980: 1) Paris Club rescheduling amounting to about $500 million with 14 official creditors; 2) private bank rescheduling of $500-800 million; 3) bilateral arrangement of $140 million with the USSR.
1983	Two multilateral reschedulings with official and private creditors: 1) Paris Club rescheduling with 20 official creditors for maturities from May 1983 to April 1984 amounting to $400-500 million; 2) private bank rescheduling for maturities from March 1983 to March 1984 amounting to $400 million.
1984-1985	Two multilateral reschedulings with official and private creditors: 1) Paris Club rescheduling with 18 official creditors for maturities from May 1984 to July 1985 amounting to about $1,000 million; 2) private bank rescheduling for maturities from March 1984 to June 1985 amounting to about $1,500 million.

Sources: Bittermann (1973: 179), Hardy (1982: 7, 36, 64), World Bank (1985), IMF (1985: 57), Pfister and Suter (forthcoming: Appendix).

mate between the relevant social forces prevailed and none of them succeeded in building up a dominant position. These combined political and economic crises eventually provoked a military coup and the deposition of Belaúnde in 1968. During the last few months of Belaúnde's government, Peru negotiated rescheduling agreements with private and official creditors to overcome its balance-of-payments crisis (see Table 8.2). Debt relief granted by the restructuring of maturities was not sufficient, though, and the new military government had to conclude new rescheduling agreements only one year afterwards. By 1970, four reschedulings were agreed upon altogether, which resulted in an extension of a substantial part of debt service.

The reformist project of the Peruvian military which seized political power in 1968 has been extensively discussed in the economic, political and sociological literature.[53] This and the fact that during military rule Peru experienced its fourth boom of massive external borrowing culminating in one of the deepest financial and economic crises of the country since independence require a more detailed discussion of this specific phase.

The most important social force of the government under Velasco Alvarado (1968-1975) was the reformist segment of the military bureaucracy, which Stepan (1978) has named a strategic elite. A key element for the organizational strength of this elite was the ideological consensus achieved by joint socialization of the military cadre.[54] The political stalemate prevailing in Peruvian politics at the end of the 1960s strengthened the power of the state class under the leadership of the reformist military faction vis-à-vis the other social forces. With its reform policies, the government of Velasco was sharply antagonistic to the traditional export oligarchy composed of the landed interests and the urban financial and commercial bourgeoisie. This became manifest with the dissolution of the SNA, the elite's association of agrarian interests, and with the nationalization schemes within the financial sector. As a result of realizing important structural reforms, Velasco achieved at least limited support from peasants, the urban poor as well as parts of the union movement, the Catholic church, and the industrial bourgeoisie. The government thus succeeded at least in its first years in gaining large parts of the populist spectrum at the cost of previous parties (APRA, AP).

The mode of political domination envisaged by Velasco was the installation of a state corporatist structure in order to link the autonomous social forces to the regime. This installation attempt can be illustrated by the shifting relations between the regime and the labor movement. In the beginning the regime obtained support from the communist labor movement. The preferential treatment of the communist faction among the labor class was part of Velasco's strategy to weaken the influence of the APRA, which had dominated the union movement hitherto. In 1972 the regime established its own union movement. This and the increasing competition among the different national union movements (APRA-based union, communist union, official state union) stimulated the mobilization and unionization of the labor class and led to a marked increase in strike activities. The failure of the regime to monopolize interest articulation of the union movements led to attempts at incorporation by using redistributive policies on the level of enterprises. This included the establishment of the so-called Industrial Communities and Social Property Enterprises and the creation of workers' participation (in management, in capital and in the distribution of profits). The individual enterprises were linked to the regime by national associations structured along corporatist lines. Yet, the attempt of Velasco to mobilize and incorporate the labor class outside of its autonomous interest associations failed and the union movement succeeded in penetrating the corporatist institutions.[55]

The regime's policies of incorporation which aimed at peasants and urban poor were somewhat more successful. The distributive policies in favor of these groups included land reform for peasants and urban development and distribution of land property titles for squatters. Institutional links to the regime for the incorporation of peasants were established by the creation of the national peasant confederation as the sole representative body of agrarian interests.[56] Urban squatters were tied to the regime by clientelistic relations and a hierarchically structured system of representation controlled by SINAMOS (Sistema Nacional del Apoyo a la Movilización Social), the principal mobilization system of the regime.[57]

Due to the regime's policy of worker participation which mainly affected small and medium enterprises, the relations to the industrial bourgeoisie became strained and finally broke down after the government dissolved the national industrial association as the sole representative institution of entrepreneurs. The relations between foreign capital and the regime were rather complex. Thus, while traditional foreign enterprises engaged in extraction were nationalized (like International Petroleum Company, Cerro de Pasco) growth-oriented transnational corporations producing with advanced technologies (like Volvo, Bayer, Southern Peru Copper Corporation) benefited from preferential treatment.[58]

The expansion of the national industrial sector was at the core of Velasco's economic program. Industrialization should create a material base for the social integration of the labor force. The attempt to build up an import-substituting industry was strongly supported by the government by granting credits, tax exemptions, and the formation of state-owned industrial enterprises. To finance the nationalization schemes and the envisaged large public investment plans to accelerate industrialization, Peru was totally dependent on the international capital market since there was no corresponding increase of state revenues and the expected profits from nationalized foreign enterprises failed to materialize.[59] After a temporary stabilization of the level of external indebtedness between 1968 and 1970, the country resorted to massive external borrowings once again.

As demonstrated in Figure 8.1, the amount of external public debt increased from $1 billion to $4 billion between 1970 and 1975; it reached $8 billion at the end of 1980 and surpassed $13 billion in 1985. Unlike the predominantly trade-related debts of the 1960s, most foreign loans in the 1970s and 1980s were syndicated credits lent by international banks. This massive increase of external borrowing has to be attributed partly to the high liquidity on the international capital market during the 1970s and the resulting competition among private banks for profitable investment opportunities. A substantial part of the financial resources raised abroad was used unproductively by the Peruvian government. Thus, according to Devlin (1986: 6, 17), 49 percent of capital borrowed from foreign private banks between 1971 and 1976 was used for refinancing purposes, but only 17 percent to finance investment projects and to import capital goods. Another 6 percent was employed to finance nationalization schemes.

Until 1974 Velasco's development strategy proved quite successful. The country profited from favorable developments of terms of trade which rose from a level of 130 in 1968 to 178 in 1974.[60] After 1975 prospects for the Peruvian economy deteriorated drastically due partly to adverse external developments which included declining terms of trade as a result of the first oil crisis and the breakdown of the fish meal industry. Yet, the development model of import-substituting industrialization also experienced a structural crisis due to imbalances in the productive capacities of an export sector based on primary goods and the growing import requirement of the industrial sector and the resulting foreign exchange demand.[61]

In 1975 Velasco was replaced by Morales Bermúdez, who pursued a more liberal economic policy. To overcome its financial and economic crisis Peru succeeded in mobilizing a balance-of-payments loan of $400 million from U.S. banks but refused to enter a standby agreement with the International Monetary Fund in 1976.[62] The stabilization plan agreed upon with private banks failed, since Peru's financial crisis worsened and the banks were unable to enforce compliance with the targets set in the agreement. Hence, in 1977 the balance-of-payments situation deteriorated again. This time the banks refused to grant any new credits and forced Peru to negotiate a stabilization agreement with the International Monetary Fund.

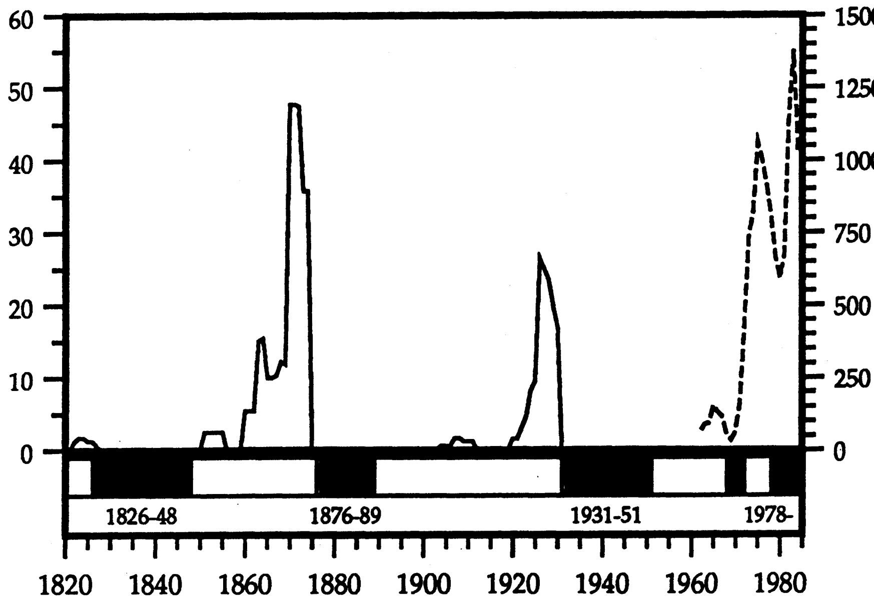
Peru's economic adjustment process was extremely conflictive. Several attempts to realize stabilization plans failed, and a final agreement with the International Monetary Fund was reached only at the end of 1977 after several rounds of negotiation. Due to its tough conditions the IMF program foundered after a few months, and in September 1978 new credits had to be granted on easier terms. On a political level the government's stabilization policy was opposed by the labor movement, which organized massive strikes and protests in the whole country and thus provoked the resignation of the military government.[63]

Despite short recovery phases, Peru's deepest economic recession since the 1930s still continued under the new civilian government of Belaúnde (1980-1985), which tried to overcome the crisis by a privatization and liberalization policy. Partly due to adverse world market developments, Belaúnde's neoliberal export-led growth strategy, which was chiefly based on traditional mineral raw materials, however, completely failed.[64] Among other things, the chronic nature of Peru's debt crisis becomes apparent by the fact that after 1978 debt-service payments could only be maintained thanks to extensive multilateral debt reschedulings granted by official and private creditors. Between 1978 and 1985 seven reschedulings were concluded and maturities of up to $5 billion were restructured (see Table 8.2 above). With a unilateral limitation of debt-service payments to 10 percent of export revenues, the new populist regime of the APRA government under President Alan García (1985-1990) virtually declared partial default.[65]

Summary and Conclusion

The case study of Peru confirms the cyclical course of consecutive phases of loan boom, debt crisis and debt settlement found on a global level in Part Two. Peru experienced four big boom phases of external borrowing and each of them was concluded by a rather long-lasting period of financial crisis. Pronounced boom phases took place in 1822-1825, 1862-1872, 1924-1928 and from about 1972 until the early 1980s. Protracted phases of unsettled debt crisis occurred in 1826-1848, 1876-1889, 1931-1951 and from 1978 onwards. The only exception to this cyclical movement parallel to global debt cycles is the short credit boom of 1963-1967 and the subsequent minor debt crisis of 1968-1972. A summary of these cyclical fluctuations is given in Figure 8.2.

FIGURE 8.2 External Public Debt of Peru and Suspension Periods



—— Nominal value of foreign bonds in U.S. $ million, 5-year moving averages (left scale).
--- Net flow of foreign loans in U.S. $ million, 3-year moving averages (right scale).
■ Phases of default on foreign bonds and consolidation periods of multilateral reschedulings.

Sources: Partly from "Global Debt Cycles and the Role of Political Regimes," by Christian Suter and Ulrich Pfister in *Markets, Politics, and Change in the Global Political Economy*, edited by William P. Avery and David P. Rapkin. Copyright 1989 by Lynne Rienner Publishers, Inc. Used with permission from the publisher. See also Suter (1990: 161, 235-284).

Concerning the purpose of the loans raised abroad, each boom phase shows a different pattern. During the first boom period (1822-1825) the resources were used consumptively for weapons. Yet, since the war of independence and the subsequent formation of the Peruvian nation-state represent an institutional prerequisite for domestic capital accumulation, the loans may also be considered as productive investments in the long run. During the first part of the nineteenth century, the project of state formation, however, was only realized to a small extent. During the second boom phase (1862-1872) foreign loans were used unproductively at first (mainly for debt consolidations). After

1869, however, they were employed for extensive infrastructure investments (railway construction) which served political rather than economic purposes. During the third loan boom of 1924-1928 external resources were used to maintain an expanding state apparatus on the one hand and to realize public utility projects on the other. Both can be interpreted as an attempt to realize a new social model based on the economic integration of urban middle and lower classes. The financial means raised during the fourth credit boom during the 1970s were mainly employed to realize import-substituting industrialization which, at least indirectly, also served the economic integration of marginal segments of the population.

A comparison of the different debt crises concerning the causes leading to the outbreak of payment difficulties shows remarkable similarities. A crucial mechanism is the decrease of state income as a result of declining export revenues, which is caused by two different factors: first, the exhaustion of existing and the failure to develop new raw material deposits partly connected with technological backwardness in the first, second and fourth debt crises (1826: silver mining, 1876: guano, 1978: fishing and oil) and, second, the deteriorating world market prices in the second but mainly in the third and fourth debt crises (1876: sugar, 1931: sugar and cotton, 1978: sugar and copper). Besides declining export revenues, the collapse of international capital markets that stopped any further lending from abroad was another immediate factor triggering Peruvian debt crises. This was especially true for the crisis of the 1930s, although during the other three crises new lending also virtually came to a standstill due to the drastic deterioration of Peruvian creditworthiness. In addition to these external factors the unproductive use of externally mobilized financial resources has to be mentioned as an important internal factor relevant in all four debt crises.

Despite the relevance of these rather direct economic causes, structural factors have to be taken into account, too. Thus, the debt crisis of the 1820s can only be understood against the background of the prevailing political and social *caudillaje* system resulting in weak state structures. Similarly, the social stalemate between the different relevant social forces hampered a successful debt management during the 1930s and 1970s. The fragility of the Peruvian society is shown by the fact that an economic integration and participation of middle and lower classes had to get financed by raising foreign loans, that is, without burdening the traditional economic elite.

Substantial differences exist between the settlement pattern of the respective debt crises. Conditions of the agreements concerning defaulted foreign bonds were extremely unfavorable for Peru in 1849 and

1889, particularly if compared with those of 1951/53. Thus, the settlement of 1849 demanded a full capitalization of arrears of interest, whereas they were totally released in the agreement of 1951/53. Due to the denationalization of parts of the domestic economy, the arrangement of 1889 turned out especially painful for Peru. The rescheduling agreements of the 1970s and 1980s are similar to the agreement of 1849 with regard to their conditions: No debts were released (unlike in 1951/53) and no cedation of property rights to foreigners occurred (unlike in 1889). Rather, debt-service payments due were transferred to the future by restructurings. The Peruvian experience thus follows closely the general pattern of debt settlement discussed on the global level of the world-system in Chapter 6.

An examination of the debt behavior of political regimes in Peru suggests that regimes dominated by state classes (e.g. *caudillaje* during the 1820s, Balta during the early 1870s) and populist regimes (Leguía during the 1920s, Belaúnde during the 1960s, Velasco during the 1970s) resorted most heavily to external borrowings. As a consequence of the above-mentioned consumptive use of financial resources, these regimes were also most often affected by debt crises. Debt settlements, by contrast, were predominantly concluded by capitalist regimes (e.g. Castilla in 1849, Odría in 1951/53) and disarticulated regimes (Cáceres in 1889, Bermúdez and Belaúnde 1978-1985).

Notes

1. Pike (1967: 42-53), Friedman (1984: 100-107).

2. Peruvian external borrowing during the 1820s is well documented; see CFB (*Annual Report*, 1877: 52), Wynne (1951b: 109-111), Mathew (1970: 82-83), Scheetz (1986: 59). For a comparison of the Peruvian experience with other Latin American debtor countries, see the recent study of Marichal (1989: 12-42).

3. Pike (1967: 56-90), Mathew (1981: 247).

4. For a more detailed account of the Peruvian social structure, see Bourricaud (1967), Mariátegui (1971), Quijano (1979), Burga and Flores Galindo (1981) and Basurco Valverde (1985).

5. Pike (1967: 56-90), Berg and Weaver (1978: 70), Gorman (1979: 397-398), Mathew (1981: 247), Friedman (1984: 122).

6. Guano is bird excrement which has been deposited during centuries on the islands and rocks off the Peruvian coast. Because of its great content of nitrogen, ammonite, phosphates and alkali-salts, it provided an excellent fertilizer.

7. Gorman (1979: 400), Mathew (1981), Friedman (1984: 171).

8. Berg and Weaver (1978: 72-73), Mathew (1981: 22).

9. Klarén (1973: 7), Gorman (1979: 402), Friedman (1984: 126, 171-173), Scheetz (1986: 62).

10. Matos Mar (1972), Burga and Flores Galindo (1981), Basurco Valverde (1985).

11. Wynne (1951b: 112).

12. Wynne (1951b: 114).

13. According to McQueen (1926: 14), outstanding external debt of the Peruvian state amounted to £33 million in 1876. The figure given by Wynne (1951b: 120) is £35 million whereas the London financial journal *The Economist* (November 2, 1878, p. 1287) talks about £41 million.

14. Miller (1976: 82).

15. Pardo, quoted in *The Economist*, April 24, 1875, p. 484.

16. Randall (1977: 103), Friedman (1984: 175).

17. Figures given by Pike (1967: 134). According to the sources used by Marichal, guano exports amounted to only £1.6 million in 1875. However, until 1875 export losses in guano sales were counterbalanced by rising sugar and nitrate exports (Marichal 1989: 108).

18. Klarén (1973: 56).

19. Pike (1967: 128), Friedman (1984: 176-178).

20. Thorp and Bertram (1978: 23-24).

21. Initially, the annuity was fixed at £80,000.

22. Only after three years did the Grace contract successfully pass the Peruvian congress. Moreover, the government could only overcome congressional opposition by ordering elections to replace oppositional deputies. For a detailed discussion of the Grace contract and its implications on the Peruvian economy, see McQueen (1926) and Miller (1976).

23. McQueen (1926: 22), Wynne (1951b: 182).

24. Thorp and Bertram (1978: Chapter 3).

25. See Quijano (1979).

26. For the case of copper and the textile industry, see Thorp and Bertram (1978: 80-86 and 121-123, respectively).

27. Thorp and Bertram (1978: Chapter 6.2).

28. Thorp and Bertram (1978: 80-95, 121-123, Chapter 6.2).

29. See Klarén (1973: 44) and Berg and Weaver (1978: 78). The success of the early populist movement led by Billinghurst and supported by urban lower classes and the union movement was made possible by a deep crisis within the *civilista* party. See Blanchard (1977) for a detailed account.

30. Klarén (1973: 44), Berg and Weaver (1978: 78).

31. Scheetz (1986: 66), Marichal (1989: 213).

32. Carey (1964: 68).

33. Wynne (1951b: 185-186).

34. Carey (1964: 74) and Thorp and Londono (1984).

35. Wynne (1951b: 187).

36. Thorp and Londono (1984), Scheetz (1986: 66).

37. Wynne (1951b: 186).

38. Thorp and Bertram (1978: 151); see also Kindleberger (1973).

39. Stein (1980: 188).

40. Klarén (1979), Stein (1980).

41. Goldberg (1983: 127), Basurco Valverde (1985: 82).

42. This was due to the introduction of quota restrictions in the United States to support prices at a minimum level acceptable to U.S. farmers. Other producers expanded their share by selling at a price slightly below the U.S. level (Thorp and Bertram 1978: 176). The expansion of Peru's cotton production thus reflects the operation of comparative advantage.

43. Thorp and Bertram (1978: Part IV).

44. CFB (*Annual Reports*, 1930-1960).

45. Cf. Collier (1975).

46. Thorp and Bertram (1978: Chapters 11 and 12).

47. Thorp and Bertram (1978: 255).

48. Kuczynski (1977: 81), Thorp and Bertram (1978: Chapter 13.2), Basurco Valverde (1985: 93-103).

49. FitzGerald (1979: Appendix, Table A.4).

50. Weeks (1985: Chapter 7).

51. For this, see Kuczynski (1977).

52. Kuczynski (1977), Webb (1977: Chapter 6).

53. Lowenthal (1975), FitzGerald (1976), Stepan (1978), Cline (1981), Becker (1983), Booth and Sorj (1983), McClintock and Lowenthal (1983), Jaquette and Lowenthal (1987), Pfister and Suter (1991).

54. This ideological consensus has been designated the "new military professionalism" (Stepan 1978), which includes ideas of socio-economic reform and national development in order to secure political stability of society along with the traditional military goals of protecting the country against foreign threat.

55. Cf. Knight (1975), Stephens (1980), Scurrah and Esteves (1982), Haworth (1983), Palacios (1983).

56. For an account of the land reform and of the relations between the military government and peasants, see Bourque and Palmer (1975), Cleaves and Scurrah (1980) and McClintock (1981).

57. Cf. Collier (1975), Dietz (1977), Stepan (1978: Chapter 5).

58. Cf. Hunt (1975), Becker (1983), Stallings (1983).

59. Thorp and Bertram (1978: 301-318), FitzGerald (1979), Weeks (1985).

60. 1963=100; cf. FitzGerald (1979: Appendix, Table A.4).

61. This explanation is stressed by Schydlowsky and Wicht (1983). Other scholars argue that the economic failure of the reformist Peruvian experiment has to be attributed to excess demand (Cline 1981; but see also Uriarte 1986).

62. With their balance-of-payments loan, U.S. banks also tried to support the moderate faction around Morales Bermúdez against the reformist groups within the Peruvian military; see Stallings (1979) and Hardy (1982: 30).

63. Goldberg (1983: 440), Scheetz (1986: 142-145).

64. Cf. Abugattas (1987) and Wise (1989).

65. See Ugarteche (1988) and Wise (1989) for an account of the Peruvian debt strategy under García.

9

Liberia: An Enclave Economy at the Extreme Periphery

Liberia is a child of the United States. . . . I believe that we can build up Liberia through our own operations to a point where, in addition to being our great rubber source, it will also be a large market for American goods.

—Harvey S. Firestone (1926: 264, 269)

We can only save and develop our hinterland by the help of the European trader.

—Arthur Barclay, president of Liberia, inaugural address, 1904[1]

Liberia's debt history can be divided into three phases. The first phase covering the nineteenth century is characterized by attempts at state and nation building. Threatened by foreign commercial capital and opposed by the native population of the hinterland, the state of the young republic, however, remained weak during this period. During the second phase, the first half of the twentieth century, Liberia was incorporated into the world-economy as an enclave economy based on rubber exports. During the third period, after World War II, this outward-oriented development model was further deepened by adding an important mineral sector to the rubber economy.

The Formation of the Republic and the Raising of the First Foreign Bond

The foundation of Liberia took place during the early 1820s when Christian colonization societies from the United States began to settle former American slaves in West Africa. However, Liberia did not become a formal colony of the United States but proclaimed an independent republic in 1847. Nevertheless, the young republic remained heavily dependent on the United States in an economic, political and cultural sense.

Liberia's settlement history is reflected in its social structure. The dominant social group consisted of descendants of repatriated American slaves called Americo-Liberians who were divided into two factions. A first and relatively small group consisted of fairer-skinned mulattoes who dominated until the end of the nineteenth century. They controlled local trade and were often rich plantation owners. The second group of Americo-Liberians, which outnumbered the first, consisted of darker-skinned and poorer immigrants who were mostly small farmers or retail dealers. Besides the Americo-Liberians, there was another group of immigrants called Congoes, who were descendants of Africans who had been freed from slave vessels. Like the poorer Americo-Liberians, they were mainly small farmers or agricultural workers. At the bottom of the social hierarchy there was a large native tribal population. Pushed back into the hinterland, it was integrated in the Liberian society only in the course of the twentieth century.[2]

The economic base of the young republic rested mainly on different trading activities until about 1870 (local trade with the hinterland, coastal and foreign trade). Only towards the end of the nineteenth century did a plantation system for palm-oil and coffee production emerge. Local trade was dominated by the Americo-Liberian elite even though foreign merchants as well as native African traders opposed the trade monopoly of the Americo-Liberians. Profits from the flourishing trade business were partially used by the Americo-Liberian commercial bourgeoisie to build up plantations. The wealthy Americo-Liberian merchants were also engaged in the coastal trade which was, however, dominated by foreign merchants. Foreign trade was completely controlled by U.S. and European (mainly British and German) capital. During the nineteenth century the most important export product was palm oil, used as raw material in the European soap industry. Further export goods such as coffee, rubber and piassava (plant fibers from different kinds of palm trees) gained importance at the beginning of the twentieth century.[3]

During the republic's first twenty years (1847-1869) Liberia was ruled exclusively by the Republican Party, which represented the interests of the mulatto faction of the Americo-Liberian elite. This period is called the phase of the "merchant princes" since all presidents were wealthy merchants of the capital, Monrovia. The main interest of this ruling elite was to establish a monopoly for local and coastal trade. In order to control foreign capital, international trade was restricted to six ports in 1864 by the Ports of Entry Law. This policy, however, was opposed by foreign commercial capital as well as the native African population of the hinterland, who circumvented these restrictions. Thus, the native population of the hinterland evaded taxation and challenged the national government with several armed revolts. Similarly, state income from customs revenues was substantially diminished since foreign merchants did not comply with the Ports of Entry Law.[4] Since the Liberian state did not succeed in controlling illicit trade, it remained weak and without an economic base.[5]

In 1869 the True Whig Party supported by the descendants of immigrant blacks (i.e. poorer groups of Americo-Liberians and Congoes) took over political power from the mulatto faction.[6] The government of President Roy (1869-1871), the first pure-blooded black president of the country, propagated a renunciation of the hitherto pursued "closed door policy" in favor of an opening towards international capital. It is, therefore, no surprise that the government of Roy raised the first foreign loans in the history of the country. The small credit of $38,684 granted in 1869 by the U.S. government was used to purchase ammunition. This obligation was cleared off in 1880, although the loan was supposed to be paid back within three years.[7] In 1871 the Liberian government raised a foreign bond with a nominal value of £100,000 in London to be used for carrying out public works.[8]

The conditions of the bond of 1871 were rather unfavorable for the Liberian government. Although the bond had been sold at a rate of 85 percent to the public by the contracting London bankers, the Liberian state received only 70 percent of the nominal amount. The interest rate amounting to 7 percent was comparatively high. Interest payments for the first three years (£20,000) as well as provisions and premiums for bankers, agents and several intermediaries were deducted from the proceeds of the bond. The Liberian government eventually received only some £20,000, which was used to purchase an overpriced small steamboat armed with a cannon as well as secondhand uniforms for the Liberian army. A substantial amount of money also disappeared in the corrupt state bureaucracy and in the hands of the ruling elite. Actually only £8,000 appears to have reached the Liberian treasury. President Roy signed the loan contract without the parliament's consent. Partly due to the scandalous circumstances associated with the foreign bond, a rebellion occurred leading to the deposition of President Roy. Only a year later, in 1872, Roy's successor declared the conditions of the loan contract unacceptable to Liberia. In 1874, after the three years during which debt service had already been paid in advance, Liberia defaulted the bond of 1871.

While the extremely unfavorable loan conditions played a certain role in the decision to default, it must be borne in mind that the bond probably would have been suspended anyway due to economic reasons.

State revenues to service the debt were lacking, and the use made of the loan did not contribute to a broadening of the tax base. According to the loan contract, the annual interest payments of $35,000 were secured by one-fifth of customs revenues. Yet, as Liberia's entire annual customs revenues totalled only $75,000-100,000 in the beginning of the 1870s, guaranteed payments amounted to $20,000 at most, which was far from being sufficient to meet the whole debt service. For repayment of the principal a special head tax of $1 annually for all males was introduced. Due to the resistance of the tribal population, state income from this tax was substantially lower than expected.

After President Roy's deposition the republicans, led by the mulatto elite, took over the political power again. They did not succeed in restoring their previous hegemony, however. Rather, there was an intensive party competition between the Republican Party and the True Whig Party. From the mid-1880s onwards, the True Whig Party eventually became dominant and succeeded in forming the new state party. Its regime stayed in power uninterruptedly until the military coup of Sergeant Samuel K. Doe in 1980.[9]

Despite the dominance of the True Whig Party, Liberia kept pursuing a "closed door policy" towards foreign capital. Until the turn of the century the country remained in default on its foreign bond suspended in 1874. As a result of this long-lasting payment incapacity, external political pressure exerted on the Liberian republic by European colonial powers intensified considerably. Thus, during the late 1870s and the 1880s, France, but also Spain and the German Reich, tried to establish a protectorate over Liberia. In return, they offered to take over the Liberian foreign debt. The Liberian republic preserved its political independence only thanks to diplomatic interventions on the part of the United States. Nevertheless, until the early twentieth century, Liberia had to cede about one-third of its territory to the neighboring French and British colonial empires.[10]

The Opening of Liberia: Establishment of the Rubber Enclave Economy and the Loss of Financial Autonomy

After prolonged negotiations a debt settlement was concluded between Liberia and its foreign bondholders in 1898/99. Liberia agreed to resume debt-service payments at an interest rate reduced from 7 percent to 3-5 percent. The accumulated arrears of interest were converted into interest-free debts redeemable after the repayment of the loan (cf. Table 9.1). The debt settlement created the prerequisites for a second and more successful attempt to open Liberia to the world-economy. The administration of Arthur Barclay (1904-1912) intended to mobilize international trade and foreign capital to advance economic development and to improve the control of the hinterland.[11] At the same time, the provision of credits was an integral part of the strategy of international interests to penetrate the Liberian economy. In exchange for a 6 percent loan of £100,000 raised in 1907, the British-owned Liberian Development Company was granted extensive privileges in mining, rubber exports, and the erection of infrastructure. The loan was spent on the consolidation of £30,000 of internal debts. The remaining £70,000, put at the disposal of the Liberian Development Company, was designed for road construction. The Liberian Development Company used the money to purchase a small steamboat as well as two motorcars and constructed an unpaved road of 15 miles leading to its rubber plantations. For the Liberian economy, however, these investments turned out to be of little value: after a few years, the badly built road fell in decay and became impassable and the cars had broken down.[12]

The failure to ensure the productive use of the 1907 loan made it necessary to raise a further loan in 1912 amounting to $1.7 million from U.S. banks. Debt-service payments for these debts ate up 40 percent of total income of the Liberian state. The new loan was entirely used to consolidate existing internal and external debts (i.e. the foreign bonds of 1871 and 1906 as well as the capitalized arrears of interest of the debt settlement of 1898/99), which had risen to more than $1.6 million. In connection with that loan, foreign creditors set up a committee to directly supervise tax and duty collection in order to secure the loan and to reorganize Liberian finances. The committee was chaired by the U.S. government and consisted of representatives of the United States, Great Britain, France and Germany. With the loan of 1912 the Liberian state virtually lost its financial autonomy, which it was to regain only after World War II.[13]

Despite the reorganization and supervision of Liberian finances by foreign creditors, the country was confronted with payment difficulties during World War I and its aftermath due to heavy losses in export revenues.[14] In 1914-1915 the Liberian government suspended amortization payments of principal and between 1917 and 1923 interest payments as well. Debt service was only resumed after world market prices for rubber had recovered.[15]

In 1927 all external debts of the Liberian government were converted into a new $2.25 million loan granted by the Finance Corporation of America, a financial agency owned by Firestone.[16] This transaction was part of a contract with Firestone that granted the latter concessions for the operation of rubber plantations and the construction of related infrastructure. Firestone's objectives behind the debt conversion were seen as an attempt to eliminate its rivals from Liberia (who were paid off with the new credit) and the acquisition of a certain control over Liberian economic policy. There was, however, no immediate need for the Firestone loan since in the meantime the financial situation of Liberia had improved due to a rise in rubber prices. Moreover, the terms of converted debts (interest rate of 5 percent) were substantially more favorable for Liberia than the 7 percent loan offered by Firestone. Firestone, however, made the acceptance of a rubber plantation concession (1 million acres for a period of 99 years) dependent on the loan. Obviously, Firestone wanted to safeguard its investments by exercising some political control over the Liberian government.[17]

TABLE 9.1 Phases of Debt-Servicing Difficulties and Terms of Subsequent Debt Settlements of Liberia, 1874-1935

1874-1898	Foreign bond of 1871 in default. 1898/99 debt settlement agreed with creditors: 1) resumption of debt-service payments by the Liberian government; 2) reduction of interest rate from 7 percent to 3 percent rising 0.5 percent every three years until the maximum of 5 percent; 3) 1 percent amortization payments for principal from 1904 onwards; conversion of arrears of interest of about £170,000 into interest-free debts redeemable after extinction of the principal; payments secured by export duty on rubber.
1912	Debt consolidation. Creditors established an international debt administration to supervise tax and duty collection.
1914-1915	Suspension of amortization payments. Repayment of arrears in 1916.
1917-1923	Suspension of amortization and interest payments due on the consolidation loan of 1912. Debt-settlement agreement in May 1923: resumption of debt service and repayment of arrears by the Liberian government.
1932-1935	Default on the Firestone loan of 1926-1927. Debt settlement in 1935 by supplementary agreements to the Firestone loan and concession arrangement: 1) reduction of interest rate from 7 to 5 percent until 1945; 2) cancellation of interest payments if state revenues were lower than $450,000; 3) reduction of payments for salaries for foreign financial advisers from about $50,000 to $9,000.

Sources: CFB (*Annual Reports*, 1889-1937), Radke and Sauer (1980: 38), Van der Kraaij (1980: 211-212), Suter (1990: 260-261).

The Firestone loan of 1927 put Liberia virtually under the financial control of the United States: Liberia had to accept an American financial adviser appointed by the U.S. government who had to approve the national budget. In addition, the Liberian government could contract new credits only with the approval of the financial subsidiary of Firestone which had granted the 1927 loan. Together with the loan agreement Firestone received a concession for rubber plantations as well as privileges for the construction of roads, railroads, and telegraph and telephone networks. In addition, taxes and duties Firestone had to pay were extremely low (i.e. an annual tax of 6 cents per acre, and an export tax of 1 percent).[18]

The expenditures under the loan agreement (salaries of U.S. advisers, interest charges, amortization payments) amounted to $260,000 a year or about 40 percent of total expenditures of the Liberian government in the mid-1920s and caused a considerable strain on the national budget. Due to the gestation lag of rubber production, the Firestone concession did not increase export revenues immediately. In the early 1930s when the first rubber planted under the Firestone concession was exported, prices had fallen to 5 cents per pound (from a level of 48 cents in 1926).[19] As a consequence of shortfalls in export earnings, customs duties and government revenues decreased and in 1932 Liberia had to suspend payments on the 1927 loan (see Table 9.1). In order to protect its investments Firestone demanded military interventions in Liberia by the U.S. government, which, however, confined itself to diplomatic pressure.[20]

The rubber economy set up by Firestone in Liberia is an outstanding example of the establishment of an enclave segment with only few ties to the rest of the economy: the input provided by the Liberian economy is confined to unskilled labor and natural resources. All equipment has to be imported (mainly duty-free, as agreed upon in the concession arrangement). Similarly, no rubber processing has developed in the domestic economy; virtually all rubber produced in the country is exported as crude rubber. Thus, Liberia has been integrated as a supplier of raw materials into the international division of labor with a marked dependence on one single transnational firm: in 1951-1955 rubber accounted for 80 percent of all Liberian exports.[21] During the same period taxes paid by Firestone amounted to 31 percent of total government revenues[22] and roughly two-thirds of the wage-earning labor force was employed by Firestone in 1950.[23] Up to about 1960 Firestone was the only foreign rubber producer. From the 1930s onwards, Liberian farmers (mostly Americo-Liberians) began to produce rubber, too. Firestone provided equipment and technical assistance and purchased the rubber products. Most of the larger Liberian rubber planters were government officials and absentee farmers.[24] Thus, the interests of Firestone and the Liberian state class became closely linked.

Expansion of the Enclave Economy During the Postwar Period: Growth Without Development

In the second half of the 1930s, the economic and political situation for the Liberian government under Edwin Barclay (1930-1944) started to improve again. After a rise of rubber prices supplementary agreements to the 1927 loan and concession arrangement were reached in 1935 which lowered the financial burden of the Firestone loan (see Table 9.1). On a political level, the government of Barclay succeeded in consolidating the authority of the state by finally pacifying the tribal population of the hinterland. The economic policy pursued by Barclay was to link Liberia more closely to the world-economy. He repealed the Ports of Entry Law of 1864 and accepted the U.S. dollar as the sole legal tender,[25] thus creating the institutional base for the "open door policy" propagated by his successor, Tubman, after World War II.

The government of William Tubman (1944-1971) brought a gradual expansion of the social base of the dominating state class. Unlike his predecessors, Tubman himself did not originate from the narrow circle of the old Americo-Liberian elite. A political integration of the hinterland population was attempted by extending suffrage and by linking clan leaders to the state bureaucracy through clientelistic networks. On the economic side, this policy was complemented by infrastructure projects and social-sector programs (education, health service).[26] All this served to build up a social power base outside the old Americo-Liberian elite which was partly opposed to Tubman and his "open door policy."[27] Through the True Whig Party which had opened towards the lower classes and the tribal population of the hinterland, the government controlled the means of patronage for the establishment and maintenance of clientelistic networks (e.g. job opportunities in the government, subventions, the granting of commercial licenses and government contracts, approval of land purchases).

During the 1950s Liberia added an important mineral sector to its economy hitherto concentrated on rubber exports. The exploitation of the iron-ore resources of the country was undertaken by four companies, all controlled by foreign capital (mostly from Europe). Production increased rapidly and reached a dominant position in Liberian economy: in the early 1970s the mining industry accounted for 30 percent of the gross domestic product and about 70 percent of total exports.[28] Through direct tax and dividend payments the mining sector increased state revenues dramatically from $4 million in 1950 to $32 million in 1960 and to $67 million in 1970.[29]

As discussed in the case of rubber, the iron-ore sector, however, remained confined to an enclave economy and did not stimulate economic development in other sectors through the establishment of linkages with the domestic economy: the strong forward linkages generally associated with mining (processing of iron ore) are transferred to the core countries, while the backward linkages of iron-ore exploitation were limited to a handful of products.[30]

In 1952 the Liberian government completely paid back Firestone's forced loan of 1927. The growth in government revenues as a consequence of the prospering rubber and iron-ore enclave economy increased Liberia's creditworthiness: external borrowing in 1955-1963 was large compared to the country's size and amounted to some $20 million annually in the early 1960s.[31] In addition, Liberia received substantial amounts in foreign aid from core countries, with the United States the largest single donor: between 1944 and 1962 the United States extended roughly $174 million in grants and development loans, rendering Liberia one of the largest recipients of American aid in terms of per capita receipts. The high degree of aid dependence of Liberia is demonstrated by the fact that during the early 1960s U.S. aid amounted to about one-third of total revenues of the Liberian government.[32] As shown in Table 9.2, the consequence of this increasing reliance on external resources by the Liberian government was a drastic rise of foreign debt from virtually zero in the early 1950s to $170 million in the mid-1960s.

Loans of private creditors and the U.S. Export-Import Bank were predominantly used to construct roads and public buildings and

TABLE 9.2 External Public Debt of Liberia, 1904-1989 (in U.S. $ millions)[a]

Year	Amount	Year	Amount	Year	Amount
1904	0.8	1955	8.7	1975	276.7
1912	1.6	1960	42.6	1980	778.9
1927	2.3	1965	171.8	1985	1073.0
1949	0.6	1970	175.7	1989	1141.0

[a]Public and publicly guaranteed long-term debt, including undisbursed debt; figures for 1949-1960 also include short-term debts.

Sources: Kappel (1982: 170) for 1904-1912, CFB (*Annual Report*, 1937: 339-340) for 1927, Bittermann (1973: 179) for 1949-1960, World Bank (*World Debt Tables*, 1974-1990/91) for 1965-1989; cf. also Suter (1990: 174).

cover budget deficits, while official aid and grants served mainly to finance expenditures on education and agriculture. Substantial amounts of external credits, however, were spent consumptively for prestige projects and wasted in the overstaffed Liberian government administration. Up to 1962 there was no development or industrialization planning. General administrative expenditure amounted to 42 percent of all current expenditures in 1960, a figure markedly higher than in any other country.[33]

The rapid growth in rubber and iron-ore production for export had little developmental effect: it did not stimulate growth of the domestic market; rather, the demand for imported consumption goods increased. The enlarged government revenues were not spent productively in order to initiate an autonomous development process but served the consumptive interests of the expanding state class. Accordingly, the whole phase has been characterized as "growth without development."[34]

The accumulation of huge amounts of mostly short- and medium-term external debts brought Liberia into a serious financial crisis in 1963. Advisers of the International Monetary Fund formulated a debt-rearrangement plan which stretched out repayments. After prolonged negotiations with the individual creditors, the Liberian government reached a substantial reduction of debt-service payments for 1964-1971 (see Table 9.3).

TABLE 9.3 Debt-Servicing Difficulties and Multilateral Rescheduling Agreements of Liberia, 1963-1985

1964-1968	Restructuring of maturities 1964-1968 granted by 23 private and official creditors in different bilateral arrangements agreed to in 1963.
1969-1971	Restructuring of maturities 1969-1971 granted by U.S. and German private and official creditors in different bilateral arrangements agreed to in 1968.
1980-1985	Several multilateral reschedulings with official and private creditors: 1) Four successive Paris Club reschedulings with official creditors for credits falling due between July 1980 and June 1985 amounting to some $100 million. 2) Two private bank reschedulings for credits falling due between July 1981 and June 1985 amounting to about $100 million.

Sources: Bittermann (1973: 174-179), Hardy (1982: 6), IMF (1985), World Bank (1985), World Bank (*World Debt Tables*, 1986/87-1989/90), Pfister and Suter (forthcoming: Appendix).

Liberia's heavily export-based economy was hit hard by worldwide stagflation from 1974 onwards, which posed a serious threat to an elite finding its economic base in an export sector consisting of few primary commodities.[35] A way to safeguard the interests of the sizeable state class which had emerged in association with the expansion of state revenues during the 1950s and 1960s was to embark on a strategy of domestic economic development. A National Socio-Economic Development Plan (1976-1980) was set in place and financed primarily (to some 60 percent) with foreign loans. The plan, however, was badly conceived and most of the funds were again channelled into largely unproductive projects. As a result of foreign borrowing Liberia's external public debt, which had stagnated since the mid-1960s, rose rapidly after 1974 from some $200 million to $800 million at the end of the decade (see Table 9.2 above), burdening the economy of the country with a heavy debt-service obligation.

The failure of the developmentalist strategy and the resulting growing economic difficulties led to rising opposition against President Tolbert (1971-1980) by an alliance of articulated urban groups (students and workers) organized in the Progressive People's Party and other progressive movements. An important factor contributing to the increasing articulation of mass protest was the government's financial losses through the collapse of state income derived from the enclave economy and the subsequent necessity to create new financial sources by raising personal taxes. Eventually, the government of Tolbert and the ruling True Whig Party was deposed by a military coup led by the 28-year-old Sergeant Samuel K. Doe.[36] The government of Doe (1980-1990) relied, at least during the first years, on the hitherto marginal groups of the state class (i.e. the African Liberians) and on the urban middle and lower classes.[37] After 1981, however, Doe replaced the representatives of the organized progressive forces and mass movements in his government and banned all forms of political activities. As a consequence, Doe rapidly lost the mass support and increasingly had to rely on repression. This suggests a clear shift towards a disarticulated regime that culminated, by the end of the decade, in a bloody civil war between different factions of the state class, triggering the deepest crisis of the Liberian republic since its very formation.[38]

The economic failure of Tolbert's externally financed developmentalist effort and the resulting social and political conflicts led to Liberia's second and significantly deeper debt crisis of the postwar era. Between 1980 and 1985 the country had to conclude six rescheduling agreements with official and private creditors and was forced to negotiate five successive adjustment and stabilization programs with the International Monetary Fund.[39] As shown above in Table 9.3, after July 1980 virtually all repayments due were restructured in annually agreed-upon arrangements. In the middle of 1985 these rescheduling agreements amounted to some $200 million.

Summary and Conclusion

The case history of Liberia was presented as an example of an enclave economy at the extreme periphery established by core capital. Through the enclave sector Liberia gradually got integrated into the world-economy as a supplier of raw material for core industry. At the same time, the enclave economy provided the economic and financial base for the maintenance of the ruling state class.

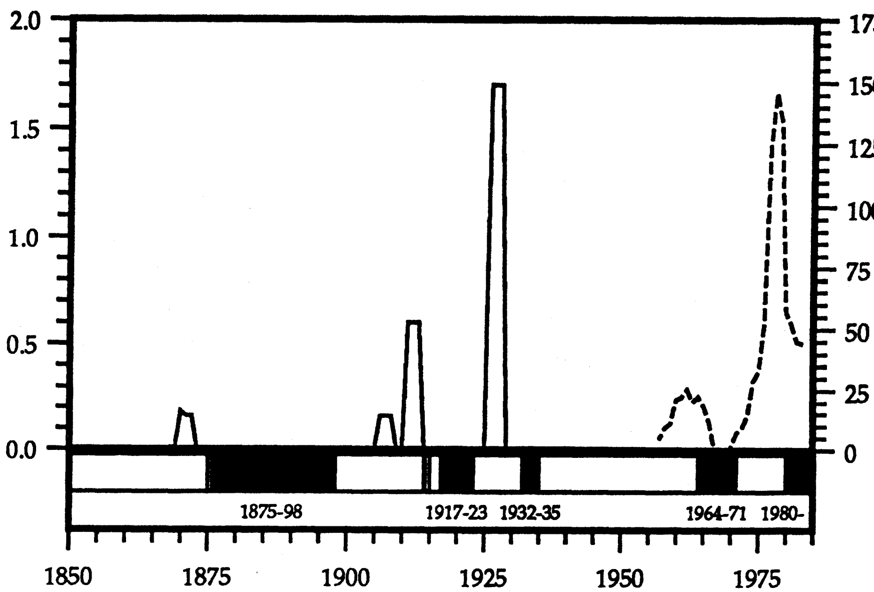
With respect to external borrowing, four pronounced boom phases may be discerned which are summarized in Figure 9.1: first, the early 1870s; second, the years before and after World War I; third, the late 1950s; and, fourth, the 1970s. With the exception of the boom phase of the late 1950s; all these periods coincide with the global loan boom phases discussed in Chapter 4.

Until the middle of the twentieth century an important structural reason for external borrowing was the chronic shortage of financial resources of the weak Liberian nation-state, whose sovereignty was threatened by both core countries and the tribal population of the hinterland (e.g. circumventing of trade regulations and taxes, loss of territories to European colonial powers, temporary loss of financial authority to core capital). During the postwar era, though, the main cause of increasing external indebtedness was the expansion of the social base necessary for the maintenance of the political regime, e.g. the integration of hitherto marginal groups into an expanding state class. The Liberian credit boom of the 1950s is in accordance with the hypothesis that regimes based on a state class borrow whenever their creditworthiness permits it.

Since the first foreign loan during the second half of the nineteenth century, Liberia was involved in all major global debt crises (default and debt-service incapacity in 1874-1899, 1932-1935, 1980-1985; see Figure 9.1). In addition, the country was confronted with payment difficulties in 1912, 1914-1923 and 1964-1971. The first of these additional periods of crisis coincides with the minor increase of debt problems on the global level during and after World War I (cf. Chapter 5). The occurrence of additional debt-service difficulties outside global crises indicates the proneness of regimes based on state classes to debt crises.

Debt-service incapacities of the Liberian government were often caused by stagnating or declining export earnings and the resulting drop in state income (especially during the crises of 1914-1923, 1932-1935, but also in 1980-1985). Unfavorable loan conditions for Liberia due to its peripheral position in the world-economy are another important factor contributing to the occurrence of payment difficulties, at least until World War II (mainly for the crises of 1874 and 1932-1935). A third causal factor which probably is relevant for all debt crises but stands out particularly for the crises of 1874, 1912, and 1964 refers to the unproductive use made of external resources. This can be explained by the considerable amount of financial resources required for the maintenance of a state class.

FIGURE 9.1 External Public Debt of Liberia and Suspension Periods



— Nominal value of foreign bonds in U.S. $ million, 3-year moving averages (left scale).

--- Net flow of foreign loans in U.S. $ million, 3-year moving averages (right scale).

■ Phases of default on foreign bonds and consolidation periods of multilateral reschedulings.

Sources: Partly from "Global Debt Cycles and the Role of Political Regimes," by Christian Suter and Ulrich Pfister in *Markets, Politics, and Change in the Global Political Economy,* edited by William P. Avery and David P. Rapkin. Copyright 1989 by Lynne Rienner Publishers, Inc. Used with permission from the publisher. See also Suter (1990: 179, 235-284).

With the exception of the arrangement of 1923, the debt settlement agreements concluded between the Liberian government and its foreign creditors resulted in a substantial relief of debt burden (e.g. interest rate reduction in 1898/99 and 1935). Yet, this has to be interpreted against the background of the originally hard and unfavorable loan conditions. As a result of the consolidation loan of 1912, Liberia largely lost its financial sovereignty, which was even more limited through the Firestone concession and loan agreement of 1927. Between the 1870s and the 1930s, creditor countries made several attempts to establish some formal control over Liberia. In this respect, Liberia shared the same fate as other Third World countries which were exposed to external pressures of core countries during this period (cf. Chapter 6).

Notes

1. Quoted in Guannu (1980: 203).
2. Fraenkel (1964), Liebenow (1969), Jackson (1970), Akpan (1973), Lowenkopf (1976), Kappel (1982).
3. Radke and Sauer (1980: 26-29), Kappel (1982: 141, 151).
4. Kappel (1982: 173).
5. Van der Kraaij (1983: 13).
6. Lowenkopf (1976: 22-23).
7. Kappel (1982: 171).
8. The subsequent discussion of the bond of 1871 is based on Büttikofer (1890), CFB (*Annual Reports*, 1875-1937), Radke and Sauer (1980), Kappel (1982: 164-187) and Van der Kraaij (1983: 13-25).
9. Liebenow (1969: 63), Lowenkopf (1976: 23, 123).
10. Kappel (1982: 180), Van der Kraaij (1983: 27-29).
11. Van der Kraaij (1983: 33).
12. Radke and Sauer (1980: 34), Van der Kraaij (1983: 35).
13. CFB (*Annual Report*, 1937: 339), Radke and Sauer (1980: 38).
14. Export revenues declined from $1.3 million in 1913 to $600,000 in 1917; cf. Van der Kraaij (1983: 39).
15. Van der Kraaij (1983: 39).
16. The $2.25 million loan was the first tranche of an authorized issue of $5 million with a maturity of 40 years. The second tranche which had been made dependent upon the amount of the Liberian state revenues (exceeding $800,000 for two consecutive years) was never disbursed (CFB, *Annual Report*, 1937: 339-340). See Chalk (1967) for a detailed account of the Firestone loan.
17. Chalk (1967), Van der Kraaij (1980: 203-205).
18. Van der Kraaij (1980: 205-207); see also Chalk (1967: 30), who gives somewhat different figures.
19. Van der Kraaij (1980: 211); see also Kindleberger (1973: 91).
20. Chalk (1967: 31).
21. Clower et al. (1966: 145-146).

22. Van der Kraaij (1980: 224).
23. Clower et al. (1966: 259).
24. Van der Kraaij (1980: 241).
25. Van der Kraaij (1980: 43).
26. Liebenow (1969: 70-72), Jackson (1970).
27. Jackson (1970), Kappel (1982: 32-33), Lowenkopf (1976: 41-46, 123-130).
28. McLaughlin (1966: 74), Carlsson (1980).
29. Hinzen (1980), Van der Kraaij (1980: 224).
30. Mainly fuel and explosives; cf. Carlsson (1980).
31. Dalton and Walters (1969: 290).
32. Clower et al. (1966: 361).
33. Clower et al. (1966: 26, 95-110, 362), Hinzen (1980: 305), Lowenkopf (1976: 131-134).
34. Clower et al. (1966).
35. Hinzen (1980); for the iron-ore industries, cf. Carlsson (1980).
36. Kappel (1980: 99, 121-136) and Korte (1986).
37. In the first cabinet of Doe five of eight members were leaders of the Progressive People's Party and other opposition movements (cf. Chaudhuri 1986).
38. Kappel (1982), Boley (1984), Chaudhuri (1986).
39. Cf. Dziobek (1986).

10

Ottoman Empire/Turkey: From World-Empire to Periphery

We have repeatedly said, for many years, that countries with an unstable and incapable administration were unsafe borrowers, and that the system of borrowing money to pay interest on old debts, by which their credit was artificially maintained, was always in danger of collapse. The longer the delay the greater would be the crash in the end.

—*The Economist*, October 9, 1875, after default of the Ottoman Empire

The political economy of Turkey during the nineteenth and twentieth centuries is characterized by the transition from a decaying world-empire to a nation-state fully incorporated as a periphery into the capitalist world-economy. In the middle of the nineteenth century, when the Ottoman state raised its first foreign loan, the empire included, besides the central region of Anatolia, Syria (inclusive Palestine), Iraq, Cyprus, Crete, the northern part of today's Greece (Macedonia), today's Romania (Wallachia and Moldavia), Albania as well as today's Yugoslavia (Bosnia, Herzegovina, Montenegro, Serbia). The Ottoman Empire lost substantial parts of both its territory and its population in the course of three phases: first, Romania, the northern part of Bulgaria, Bosnia, Herzegovina, Montenegro and Serbia as well as parts of Armenia after the Russo-Turkish War of 1877-1878; second, Cyprus, Crete, Albania, Macedonia and East Rumelia (southern part of today's Bulgaria) after the Balkan Wars of 1908-1913; third, Syria and Iraq after World War I. The Turkish republic was thus established at the beginning of the 1920s in the remaining territory (i.e. Anatolia).

The first section of this chapter deals with the relationship between the decay of the Ottoman Empire and its debt history. The developments after the dissolution of the empire are discussed in the second section, with Turkey as the most important successor state of the Ottoman Empire.

The Decay of the Ottoman Empire and Its Incorporation into the World-Economy

In the heyday of the Ottoman Empire during the fifteenth and sixteenth centuries, political power was concentrated in the hands of the Sultan and his extensive civilian and military palace bureaucracy. The establishment of a centralized state apparatus took place in particular under Sultan Mehmet II (1451-1481), who succeeded in limiting the power of the provincial aristocracy.[1] The loyalty of the bureaucracy towards the Sultan was secured through a carefully organized recruitment system. Slaves captured during wars were employed as palace servants and warriors while boys were recruited among the Christian subjects and trained in special palace schools to enter a career as civil servant or military officer. Mehmet II also expanded the famous Janissary corps which was directly responsible to the Sultan. The Janissaries not only served as the palace guard but were also stationed in the provincial centers.

The economy of the Ottoman Empire was based on free agricultural production and the complete control of the economic life by the state, a pattern which has been characterized as the Asian mode of production in Marxist theory. According to this view, there were two basic social classes: free peasants as surplus producers on the one hand and the bureaucracy consisting of the administrative, the military and the religious segment as the surplus-appropriating class on the other.[2] In the terminology of types of political regimes developed in Chapter 7, this constellation corresponds to a regime based on a (traditional) state class.

Land, which was principally owned by the Sultan, was rented to peasants in return for taxes. Taxation of agriculture took place on the basis of the feudal *timar* institution. The administrator of the state land was the *sipahi*, usually a member of the cavalry who had distinguished himself on the battlefield. He rented the land to the peasants and collected the taxes. In return, he had to provide soldiers in times of war. The *sipahis* also formed the rural state bureaucracy. But neither their administrative position nor the tax rent were hereditary, and the Sultan could remove the *sipahi* anytime.[3] Through its administrative machinery the Ottoman state absorbed and controlled the economic surplus. Production and trade were strongly regulated and supervised by state action (price fixing, distribution of raw materials, maintenance of trade routes, allocation of trade licenses, control of market places). The accumulation of capital outside the state was thus largely prevented.[4]

It is generally agreed that the disintegration of the Ottoman Empire from the seventeenth century onwards was caused by the weakening of state institutions and a consequent loss in state control over the economic sphere.[5] This process may be partly attributed to the influence of the capitalist world-economy rising in Western Europe: as a result of cheap American silver the Ottoman currency depreciated and prices rose. Due to the circulation of foreign coins, the state lost its coinage monopoly and thus the control over its currency. Increasing international demand especially for cereals, cotton and tobacco and subsequent price increases led to rising differences between regulated internal and free world market prices. This process resulted in massive smuggling and eventually in the gradual liberation of merchant capital. Together with retained revenues of local tax collectors and provincial potentates, parts of these funds were invested in commercial agricultural export production. Parallel to the weakening of internal regulations the empire lost its control of the international trade routes (rise of the Atlantic economy). Thus, the state increasingly lost its control over production and allocation of the economic surplus.

Partly related to these developments caused by the interference between a rising capitalist world-economy and a declining empire, contradictions originating in the internal structure of the Ottoman Empire and in the Islamic societies in general became manifest. The gradual loss of state control over agricultural production and the concomitant strengthening of the centrifugal forces of local potentates through an institutionalization of tax collection can be considered the most important processes in this respect. As a consequence of the introduction of modern firearms leading to a replacement of the light cavalry (provided by *sipahis*) by foot soldiers, the existing land and tax administration of the *timar* system started to dissolve. Maintenance and armament of the expanding central imperial army composed of foot soldiers led to increasing military expenditures requiring the development of new financial sources. Since the Ottoman state was no longer interested in military services and men supplied by *sipahis*, the feudal land administration was changed into a system of tax farm auctioning and subcontracting, providing cash.[6]

Local notables, but also former officers of the army, government officials, merchants and wealthy peasants became the new tax collectors and the intermediaries between the central government and the local population. The *ayans*, as the emerging local elite have been called, succeeded in consolidating their economic position and therewith gained de facto control over their territories. They invested part of their profits in commercialized agricultural production for export (especially in the Balkans), thereby, using means of coercion to tie the peasants to their landholdings.[7] Together with the merchants the *ayans* opposed the authority of the Sultan and supported numerous provincial revolts against the central government. These centrifugal forces were reinforced by the emergence of nationalist movements in the Balkans during the nineteenth century articulated by privileged peripheral groups which had been excluded from participation in the political power of the empire (such as Greeks, Serbs, Armenians). As the authority of the central government decayed, the special recruitment system for the state bureaucracy disappeared as well. Instead of Christian slaves, free Moslems were employed, thus creating a new bureaucratic class from which several reform movements of the nineteenth century originated (e.g. Young Ottomans and Young Turks).[8] All these developments resulted in a steady decline in the state revenues of the Ottoman Empire. Faced with growing expenditures due to rising military outlays the Ottoman state experienced chronic budget deficits.

The reforms initiated at the beginning of the nineteenth century during the era of Mahmut II (1808-1839) and the Tanzimat period (reorganization, 1839-1876) were designed to reverse this trend and to restore the authority of the central government.[9] As a prerequisite the provincial elite, the *ayans*, were deprived of power. Their property was confiscated and distributed among peasants.[10] The economic reform program resulted in an opening of the internal market to foreign trade and capital. European financiers were allowed to perform banking operations and a liberal trade regime was established. This caused the displacement of local merchants and the decline of handicraft production, especially in the domain of textiles. The Ottoman export became confined to agricultural raw materials (tobacco, wheat, fruit). The reforms of the Tanzimat period thus accelerated the incorporation of the Ottoman Empire as a periphery into the international labor division.[11]

Faced with massive financial needs, the Ottoman Empire increasingly relied on foreign capital from the first half of the nineteenth century onwards, which ended in bankruptcy and foreign financial control within only three decades. The debt history of the Ottoman Empire from the beginning of the Tanzimat period until the final disintegration of the empire after World War I can be divided into four phases (1839-1853, 1854-1875, 1876-1881 and 1882-1923).[12]

The *first phase* (1839-1853) started with the permission of banking operations for foreigners. Even though the Ottoman state did not contract long-term loans during this period, it financed its deficits partially by raising short-term credits from Levant and European financiers in addition to issuing paper money. The short-term credits were charged with extremely high interest rates and commissions and negotiated usually between corrupt and bribed government officials and unscrupulous foreign financiers.[13]

The *second phase* (1854-1875) began with the first foreign governmental bonds contracted in 1854-1855 after Britain and France allied themselves with the Ottoman Empire against Russia in the Crimean War. The loans amounting to a nominal £8 million were primarily used to purchase war materials. These loans marked the beginning of massive external borrowing. Between 1858 and 1874 thirteen foreign loans were raised rendering the Ottoman Empire one of the principal debtors of those days (cf. Chapter 4).

The nominal value of foreign loans contracted between 1854 and 1874 amounted to £223 million, yet, net receipts of the Ottoman state (after making allowance for the price of issue and commissions to bankers) totalled only £120 million. As shown in Table 10.1, most of these loans fall into the period 1865-1874. Since government borrowing by the Ottoman Empire is well documented, there is ample evidence for the consumptive use of external funds: only one loan was spent for productive investment (railway construction in the European part of the empire), whereas all other fourteen loans were used consumptively

TABLE 10.1 Foreign Governmental Bonds of the Ottoman Empire, 1850-1914

Period[a]	*Nominal Value (£ millions)*	*Net Value*[b] *(£ millions)*	*Interest Rate*[c] *(%)*	*Number of Bonds*
1850-1854	3.0	2.3	6.0	1
1855-1859	10.0	8.8	5.0	2
1860-1864	18.0	12.4	6.0	3
1865-1869	64.4	34.1	5.7	3
1870-1874	127.8	62.5	5.7	6
1875-1879	5.0	2.6	5.0	1
1880-1884	-	-	-	-
1885-1889	7.5	7.0	5.0	2
1890-1894	29.5	24.5	3.9	6
1895-1899	3.0	2.5	5.0	1
1900-1904	49.5	42.0	4.0	6
1905-1909	31.0	26.5	4.0	5
1910-1914	31.0	27.2	4.6	6

[a]Refers to the signing date of the loan contracts.
[b]After deduction of commissions and calculated on the basis of the issue price.
[c]Nominal interest, calculated as unweighted average.

Source: Suvla (1966: 100-106).

either for financing military operations for covering budget deficits, or for refunding and refinancing purposes.[14]

Debt-service obligations imposed a heavy burden on the Ottoman economy. From the early 1860s to the middle of the 1870s the ratios of debt-service payments to export earnings and of debt-service payments to government revenue both increased from 10 percent to 50 percent.[15] At the end of the loan boom, debt service due could only be financed by new foreign money. In the early 1870s the Ottoman Empire was forced to raise short-term credits bearing interest rates of up to 24 percent.[16] The enormous debt accumulation of some £200 million[17] ended in October 1875 when the government reduced interest payments unilaterally. Finally, in April 1876, the Ottoman Empire had to declare total default.[18]

A first cause for the outbreak of the debt crisis resides in the consumptive use of external credits, which has to be attributed to the insatiable financial needs of a declining world-empire. *The Economist*, branding the default as barbarity, considered the mismanagement within the state bureaucracy of the Ottoman Empire as the main cause of payment incapacity.[19] A second important factor leading to the crisis is the unfavorable development of foreign trade. After a period of substantial export increases between the late 1850s and the early 1870s, foreign trade declined by 50 percent during the second half of the 1870s and stagnated at this level until the middle of the 1890s. Terms of trade of the empire vis-à-vis the economically more advanced countries deteriorated from a level of 114 in 1871 to 85 in 1889.[20] The extremely unfavorable loan conditions were a third factor contributing to the outbreak of the crisis. A comparison of the nominal value of bonds with the amount actually realized (cf. second and third columns in Table 10.1) reveals a clear deterioration of loan conditions. Whereas net receipts still amounted to 85 percent of the nominal value during the decade of the 1850s, they fell to 68 percent between 1860 and 1864 and to 50 percent during the loan boom of 1865-1874. The average real interest rate (interest rate based on the issue price) of foreign bonds raised between 1865 and 1874 came to 12 percent (i.e. twice as high as the nominal interest rate given in Table 10.1), demonstrating thus the low creditworthiness of the Ottoman Empire on the international capital markets. Additional factors leading to the debt crisis of 1875 were the fall in tax revenues as a result of bad harvests from 1872 onwards and growing military expenditures to protect the empire against external attacks (Russo-Turkish War) and internal uprisings (Balkan provinces).

The *third phase* of Ottoman debt history (1876-1881) includes the years of crisis after the outbreak of payment incapacity until the final debt settlement concluded with the creditors. The collapse of public finance and the economic depression provoked a political crisis. The reform movement of the so-called Young Ottomans, founded already in 1865 and supported by the nationalist Muslim faction emerging within the state bureaucracy, succeeded in forcing the resignation of the ruling Sultan, Abd ül-Aziz (1861-1876). The new Sultan, Abd ül-Hamid II (1876-1909), had to appoint a grand vizier favoring modernization and was forced to accept a constitution and to establish a parliament. Yet, the nationalist reform attempt did not last long. After only two years, the parliament was dissolved and the reformist grand vizier was dis-

TABLE 10.2 Phases of Debt-Servicing Difficulties and Terms of Subsequent Debt Settlements of the Ottoman Empire, 1876-1940

1876-1881	Suspension of debt-service payments. A debt settlement between representatives of foreign bondholders and the Ottoman government was agreed on in November 1881 with the promulgation of the Decree of Muharrem: 1) reduction of foreign debt (including arrears of interest) by 50 percent to £114 million; 2) reduction of interest rates to 1-4 percent depending upon state revenue; 3) cedation of state revenues from several monopolies, taxes and tributes for debt-service payments; 4) establishment of the international Public Debt Administration composed of representatives from Britain, the Netherlands, France, Germany, Italy, Austria-Hungary, the Ottoman Empire and the British-French controlled Imperial Ottoman Bank for the collection of ceded revenues.
1915-1928	Suspension of payments to Allied countries during World War I. Regular debt-service payments were resumed only in 1928 when a settlement with bondholders concerning the Turkish portion of the old Ottoman debt was agreed on: 1) repayment of the old Ottoman debt in annual installments of £1.8-3 million; 2) reduction of interest payments until 1950; 3) capitalization of arrears of interest at 75-100 percent redeemable within 30 years in annual installments; 4) debt service secured by customs revenues.
1931-1932	Suspension of payments agreed upon in the settlement of 1928. A new settlement concluded in April 1933 contained: 1) a reduction of the outstanding principal of the old Ottoman debt by 65 percent and the conversion into new bonds with an interest rate of 7.5 percent; 2) the reduction of annual payments to £640,000.
1940-1943	Suspension of debt-service payments due to World War II. Liquidation of the old Ottoman public debt in devaluated French francs by 1944.

Sources: CFB (*Annual Reports*, 1930: 374-388, 1954: 388), Blaisdell (1929: 85-134, 189), Wynne (1951b: 413-516), Thobie (1972: 12, 102), Suter (1990: 267-269).

missed.[21] The political crisis eventually culminated in the defeat of the Ottoman Empire in the Russo-Turkish War (1877-1878), resulting in substantial territorial and financial losses.[22]

An agreement on the settlement of defaulted foreign debt between the Ottoman Empire and its creditors was concluded in 1881 and resulted in the establishment of foreign financial control (cf. Table 10.2). The formation of an international committee supervising Ottoman finance had already been recommended by the European great powers at the Congress of Berlin in 1878. Negotiations between the Ottoman government and foreign bondholders to settle default had started in December 1875. Due to the Russo-Turkish War and internal political turmoil prevailing during the second half of the 1870s, discussions were postponed until 1880 when the Ottoman Empire invited bondholders to send representatives to Istanbul to negotiate a debt-settlement agreement. To appoint their representatives, the different national bondholders' associations, however, needed almost a year. The final negotiation, therefore, was taken up in September 1881.[23] The terms of the debt settlement reached in November 1881 were promulgated in the Decree of Muharrem. In return for a substantial debt reduction of about 50 percent and a reduction of interest rates to 1-4 percent, creditors established foreign financial control under the so-called Public Debt Administration.

The *fourth phase* of Ottoman debt history (1882-1923) was characterized by the control of Ottoman finance by the international debt administration. It was composed of seven representatives of the respective national bondholders' committees and was designed to administrate the debt-service payments and to secure the interests of foreign bondholders in general. According to Owen (1981: 192) the debt administration played a semi-official role since its members were appointed with the support of the respective national governments. It represented the political and economic interests of the principal European powers, the representatives of foreign bondholders, and the major foreign banks and foreign railway companies with the aim of opening up the economy of the Ottoman Empire. The debt administration acted as a general guarantor of Ottoman credit and as an intermediary between foreign banks and concessionaires on the one hand and the Ottoman government on the other. It further administered and collected revenues to pay for railway guarantees and to service external debts.[24]

Under international financial control the Ottoman Empire experienced a second wave of external borrowing between 1886 and 1914, with a climax during the first decade of the twentieth century. As shown in Table 10.1, a total of 26 loans with a nominal value of about £150 million were raised between 1885 and 1914. As during the 1860s and the early

1870s, only a minor part of these funds were spent for productive purposes. According to the material presented by Suvla (1966: 104-106), 17 loans from a total of 26 were used for refunding and for covering general budget deficits, 3 for financing of wars and 6 for infrastructure purposes (mainly railroad construction). In addition to foreign government loans, large flows of foreign direct investment entered the Ottoman Empire from the 1890s onwards, totalling £63 million in 1914, of which two-thirds was invested in railways. The leading investors were Germany, holding 45 percent of all assets (mainly railways), and France, contributing 26 percent (with an emphasis on mining).[25]

The opening of the Ottoman Empire to foreign direct investment contributed to a remarkable economic expansion. Between 1881 and 1913 national income grew on the average by 1.5 percent per annum and the volume of foreign trade doubled.[26] Numerous private enterprises were set up in manufacturing, most of them with foreign capital. There is a marked contrast between this economic expansion and the continuing political decay of the indebted Ottoman state which had lost its former control over the economy.

The dominant influence of foreign capital on the Ottoman economy and society favored the emergence of nationalist factions within the state bureaucracy. With their successful revolt in 1909, this reformist faction, the so-called Young Turks, forced Sultan Abd ül-Hamid II to resign and reestablished the constitution of 1876. Despite the appointment of a new Sultan, political power was mainly in the hands of the Young Turks and their secret association, the Committee of Union and Progress.[27] Opposed to the interests of foreign capital and the allied commercial bourgeoisie mainly composed of non-Muslims (mostly Greeks and Armenians), the Young Turks supported the formation of a "national," that is, a Muslim bourgeoisie.[28] In contrast to the movement of the Young Ottomans of the 1870s, which was supported by leading government officials, the Young Turks originated from the lower ranks of the civilian and military bureaucracy as well as from urban middle-class groups outside the administrative apparatus (e.g. professionals). Due to the lack of financial sovereignty, the government of the Young Turks was not able to realize the envisaged etatist economic policies. After the defeat of the empire in World War I the Committee of Union and Progress was dissolved and the movement collapsed. Yet, the nationalist ideas survived and provided an important ideological resource for the Kemalist movement of the early 1920s.[29]

The external control of the Ottoman debt was formally maintained until the Lausanne Treaty of 1923 but ended in fact with the outbreak of World War I since the political contradictions among the European powers paralyzed the Public Debt Administration. The Ottoman Empire entered the war on the side of the Central powers and borrowed huge amounts of short-term credits from Germany to finance the war. These obligations, however, were cancelled by the Allied powers after the war.[30] In 1915 the Ottoman Empire suspended debt-service payments to the Allied powers. After the end of the war some temporary payments were made, but a final settlement of the old Ottoman debt which had been distributed among the different successor states of the empire in the Lausanne Treaty was achieved only in 1928.

The Turkish Republic (1923-1985)

After the final demise of the Ottoman Empire and the war of independence against Greece, France, and Britain, the Turkish republic was established in 1923 by the nationalist movement headed by Mustafa Kemal (Atatürk). The Kemalist liberation movement succeeded in establishing a social pact of rather different social forces. It relied on factions of the state bureaucracy, the military, the urban middle class and the intelligentsia but also on the rural elite and thus gained mass support of the population. After the formation of the republic the liberation movement was transformed into the Peoples Republican Party, which ruled the country from 1923 until 1950. The civilian and military bureaucracy retained its dominant position within the state. This is documented by the large number of officials (43 to 54 percent) in the national assembly between 1920 and 1943.[31]

With the Lausanne Treaty the Turkish republic regained its financial sovereignty but was bound to maintain its low prewar tariff level. Only in 1929 was national tariff autonomy fully reestablished. Thus, despite the fact that the political regime was based on the nationalist forces, the period 1923-1929 was characterized by an exceptional openness of the Turkish economy (no restrictions on capital movements, absence of a central bank in addition to the liberal trade regime) and marked the final peripheral incorporation of Turkey into the world-system. This integration process, however, was not based on external indebtedness but was largely confined to international trade: During the expansionary 1920s Turkey abstained from external borrowing mainly due to the lack of settlement of the old Ottoman debt and the political instability associated with the process of state and nation building.[32]

After prolonged negotiations with the representatives of foreign bondholders, a debt settlement concerning the old Ottoman debt assigned to the Turkish republic could be reached in 1928 (see Table 10.2).[33] Turkey agreed to repay its obligations in annual installments amounting to 2 million Turkish pounds (equivalent to £1.8 million) for 1929-1936 and rising to 3.4 million Turkish pounds by 1952. Yet, only two years later, in February 1930, the Turkish government demanded a reduction of payments. Bondholders agreed to postpone two-thirds of payments due until October. Finally, in November of the same year, Turkey unilaterally reduced debt payments. The outbreak of debt-service incapacity was triggered by the collapse of export earnings, which had declined between 1928 and 1933 from 170 million Turkish pounds to about 90 million. Although a special crisis tax had been raised, state revenue decreased by 24 percent between 1929/30 and 1932/33.[34] In April 1933, a new debt settlement was agreed on, in which bondholders granted a reduction of two-thirds of outstanding debt and a corresponding reduction of the annual payments to £640,000. This arrangement was slightly modified in two additional agreements.[35] After the outbreak of World War II, Turkey suspended debt-service payments once again. In 1944 the whole old Ottoman debt was finally repaid with devaluated French francs, resulting in substantial debt relief.[36]

The economic depression of the 1930s caused a marked shift in the development strategy pursued by Atatürk's ruling Peoples Republican Party. In 1931 it adopted etatism as the official economic strategy. National development was considered to be subject to planning with the state as the pioneer and director of industrial activity. The instruments of etatism were state entrepreneurship, a social contract between capital and labor, price control and protectionism. Thus, the period between 1930 and 1950 was characterized by nationalizations (especially in the railway and mining sectors), the implementation of development plans and the foundation of state enterprises. The main emphasis during this first period of import substitution was on the establishment of state enterprises in light industries (especially textiles). In a general sense etatism may be regarded as an at least initially successful attempt to overcome the peripheral characteristics of the Turkish economy.[37]

After World War II the etatist regime declined rapidly due to both external and internal developments. Under the new political hegemony of the United States the world-economy experienced rapid growth. Due to its strategic location Turkey was quickly integrated into the Western alliance and the country became a candidate for U.S. assistance. The dissolution of etatism was accelerated by contradictions within the Turkish society. Associated with the industrialization process generated by the etatist development strategy, a rapidly growing commercial and industrial middle class had emerged which demanded a limitation on state interventionism.[38] These internal tensions eventually resulted in the separation of the liberal faction from the ruling Peoples Republican Party. The growing articulation of social groups outside the state class and the increasing integration into the world-system led to a gradual decline of etatism in the post-World War II years.

With Mederes' Democratic Party (1950-1960), an alliance of landlords and the commercial bourgeoisie came to power.[39] A gradual opening towards the world-economy followed, supported by a rapid growth in export receipts. The opening of the Turkish economy is documented by the adoption of a liberal foreign investment law and the reliance on foreign assistance mainly through the Marshall Plan and U.S. economic and military aid. Between 1946 and 1970 the United States provided some $5.8 billion, of which $4.3 billion was in the form of grants (mostly for military purposes).[40] The influx of foreign investment reached substantial levels but remained low compared with other countries.

Despite this marked opening, the state maintained its significant role in the Turkish economy. During the 1960s and early 1970s the share of the public sector in total investment accounted for 40-50 percent. Nevertheless, during this period a private sector concentrated mainly in light industries (food, textiles, light engineering) emerged. At the same time, state investment turned from previously favored light industries to heavy capital-intensive industries such as steel, petroleum and petrochemicals, fertilizers, pulp and paper.[41]

After the end of the Korean War boom, export revenues faltered and the growth dynamic of Menderes' outward-oriented development model waned. The government tried to overcome increasing balance-of-payments pressures by raising short-term and medium-term credits. As a consequence, external public debt, which had stagnated at low levels between the 1930s and the mid-1950s, considerably increased during the late 1950s (see Table 10.3). Due to these unfavorable developments, debt-service payments rose to more than half of the export revenues. By 1958 payments in arrears amounted to more than $400 million and forced the Turkish government to request debt relief from its creditors.[42] Within the framework of the Turkish aid consortium of the OECD, official creditors eventually granted two reschedulings in 1959 and 1965 for payments falling due 1958-1963 and 1965-1967 amounting to $600 million (see Table 10.4).

The economic and financial crisis of the late 1950s contributed to the loss of the government's support. In 1960 Menderes was overthrown by a military coup and the Democratic Party was dissolved. After several coalition governments had failed, the Justice Party under the leadership of Suleyman Demirel succeeded in forming a new stable political alliance. His administration (1965-1971) can be described as a capitalist regime since it relied on an alliance of different factions of the bourgeoisie (commercial capital, small manufacturers, and big industrialists). Yet, it was also supported by the agricultural elite.[43]

As a consequence of the strong representation of industrial interests, the regime again favored an import-substitution development strategy that produced fairly high growth rates in the short run. Nevertheless, Turkey's development model broke down in the wake of the economic recession during the late 1970s. The failure of import substitution may be attributed to several factors: The capital-intensive and technology-intensive import substitution had little effect on employment. High import propensity combined with a small export potential resulted in imbalances in foreign trade which could only be financed by growing remittances from emigrated workers. The creation of domestic ancillary industries largely failed, leading to a pervasive dualism between the state and the private sector.[44] The returns on investments in the state enterprises seem to have been rather low, and most industries remained dependent on continued protection. As shown in an empirical study by Krueger and Tuncer (1982), strongly protected Turkish industries, however, did not experience higher growth than less-protected ones. In addition to these economic factors developments on the social and political level are important as well. As a consequence of industrialization, the labor force emerged as a new social group organized in the Peoples Republican Party, trade unions and communist labor parties.[45] The completion of the easier stages of import substitution (around 1970) and the growing political articulation of the working class led to an erosion of Demirel's political base. In 1971 Demirel was overthrown by a military coup. The following years until 1980 were marked by pervasive political instability. An unsuccessful attempt to establish an authoritarian military regime (1971-1973) was followed by a rapid sequence of thirteen weak coalition governments (1973-1979).[46] Attempts by several

TABLE 10.3 External Public Debt of Turkey, 1924-1989 (in U.S. $ millions)[a]

Year	Amount	Year	Amount	Year	Amount
1924	482	1960	865	1980	19016
1939	176	1965	1199	1985	25168
1947	259	1970	2693	1989	43013
1956	249	1975	4770		

[a]Public and publicly guaranteed long-term debt, including undisbursed debt; figures for 1939-1947 also include short-term debts.

Sources: Conseil de la Dette Publique (*Rapport* 1968/69: 6) for 1924, Ducruet (1964: 131) for 1939-1947, Bittermann (1973: 189) for 1956-1965, World Bank (*World Debt Tables*, 1976-1990/91) for 1970-1989; see also Suter (1990: 194).

governments to gain legitimatory support through populist policies largely failed.[47]

As shown in Table 10.3, Turkish external public debt increased continuously from the mid-1960s onwards. External borrowing accelerated markedly during the 1970s as a result of a rapidly deteriorating balance-of-payments situation due to the massive oil price increases and the impact of the international recession on the Turkish economy.[48] As a consequence, external public debt quadrupled between 1975 and 1980 from $5 billion to about $20 billion.

In 1977 the Turkish government became unable to meet debt-service payments. This marked the beginning of a severe debt crisis: between 1977 and 1983 Turkey remained virtually insolvent, a fact documented by the recurrent debt restructurings negotiated with official and private creditors. As shown in Table 10.4, seven multilateral reschedulings, restructuring maturities amounting to some $11 billion, had to be provided.

This most severe financial crisis in the history of the Turkish republic was caused by several factors:[49] The most immediate reasons were the massive oil price increases after 1973 and the drop in remittances of migrant workers due to the outbreak of recession in the European core countries. In addition, long-term structural factors were important, too. They include particularly the failure of capital-intensive import substitution and the social and political stalemate prevailing between 1973 and 1980. In fact, none of the populist-oriented administrations of the late 1970s was able to introduce effective stabilization measures as demanded by the International Monetary Fund and foreign creditors.

TABLE 10.4 Debt-Servicing Difficulties and Multilateral Rescheduling Agreements of Turkey, 1958-1983

1958-1963	Multilateral rescheduling of payments falling due between August 1958 and December 1963 amounting to about $400 million agreed on with 14 official creditors within the OECD aid consortium in 1959.
1965-1967	Multilateral rescheduling of payments falling due between 1965 and 1967 amounting to $220 million agreed on with official creditors within the OECD aid consortium in 1965.
1977-1983	Seven reschedulings, three with official creditors within the OECD aid consortium (totalling some $5 billion), four with private banks (totalling some $6 billion) for payments falling due between 1977 and 1983.

Sources: Hardy (1982), IMF (1983), Pfister and Suter (forthcoming: Appendix).

When radical measures were finally taken under the last Demirel government, with Özal as minister of economic affairs, social conflict became so intense that the military intervened. Initially with strong support by the repressive power of the army, Özal's disarticulated regime carried out liberal reforms that largely dismantled the inherited structure based on the etatist development model and import substitution. While this policy resulted in a successful stabilization of Turkey's external debt situation, political and social costs were considerable.[50]

Summary and Conclusion

The case of the Ottoman Empire and Turkey may be regarded as typical for the peripheral incorporation of former world-empires into the capitalist world-economy. This incorporation process determined the debt history, at least until 1923. The Turkish case stands as an example for other world-empires and regimes based on a traditional state class, such as China, Egypt, Morocco and Tunisia.

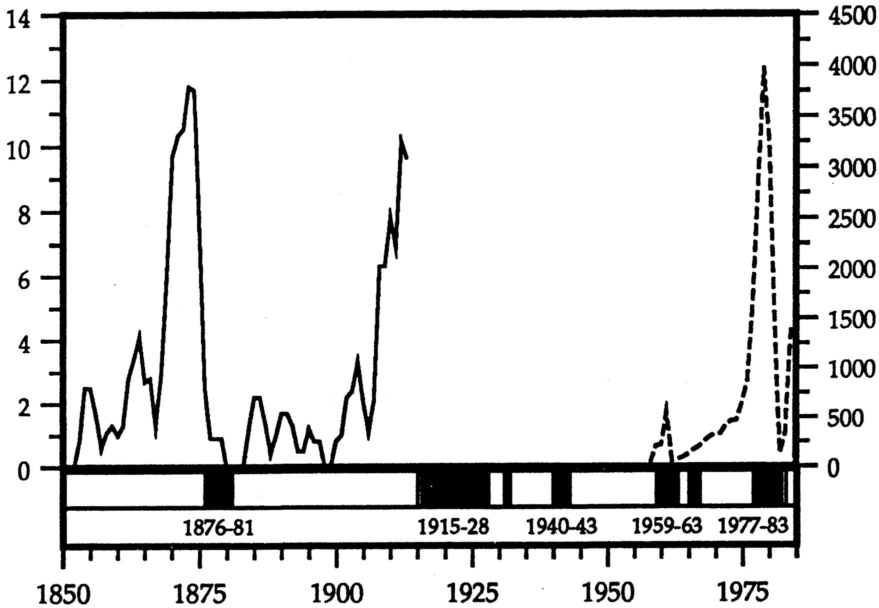
As summarized in Figure 10.1, the Turkish case fits fairly well into the pattern of the concept of cyclical loan booms and debt crises occurring parallel to Kondratieff waves. Since the middle of the nineteenth century when the Ottoman Empire/Turkey entered international capital markets, the country experienced three major booms (1865-1874, 1900-1914, 1973-1980) which all ended in subsequent debt-service incapacities (1876-1881, 1915-1943, 1977-1983). Only the two rescheduling arrangements of 1959 and 1965 do not fit this pattern.

Despite this regularity, the pattern of each crisis was quite different. The first debt crisis represents an outstanding example of consumptive use of foreign capital. Additional factors contributing to the outbreak of the crisis are the exploitation of the Ottoman state by European finance and a decline of export earnings. The prolonged second crisis can be attributed to the combination of political disruptions (the two world wars, the final dissolution of the Ottoman Empire and the Turkish war of independence) and the collapse of international trade in the wake of the global economic depression. Finally, the crisis of the late 1970s and the 1980s (with its precursors in the late 1950s and early 1960s) was caused by the failure of capital-intensive import substitution and was triggered by the decline in export revenues (including workers' remittances).

The settlement of the first and second debt crises resulted in a massive reduction of foreign debt (50 percent in the arrangement of 1881, some 70 percent in the settlements of 1928, 1933 and 1944). In contrast, the rescheduling technique applied in the crisis of 1977-1983 and its precursors in the 1960s only postponed debt-service payments to the future.

Yet, in the settlement of 1881 debt relief granted by foreign creditors had to be paid for with the loss of financial and economic sovereignty.

FIGURE 10.1 External Public Debt of the Ottoman Empire (1850-1913) and Turkey (1958-1984) and Suspension Periods



—— Inflow of foreign capital from foreign governmental bonds in £ million, 3-year moving averages (left scale).
--- Net flow of foreign loans in U.S. $ million, 3-year moving averages (right scale).
■ Phases of default on foreign bonds and consolidation periods of multilateral reschedulings.

Sources: Partly from "Global Debt Cycles and the Role of Political Regimes," by Christian Suter and Ulrich Pfister in *Markets, Politics, and Change in the Global Political Economy*, edited by William P. Avery and David P. Rapkin. Copyright 1989 by Lynne Rienner Publishers, Inc. Used with permission from the publisher. See also Suter (1990: 200, 235-284).

Notes

1. Inalcik (1970c, 1985), Shaw and Shaw (1976).

2. Cf. Islamoglu and Keyder (1977), Bailey and Llobera (1981), Keyder (1987).

3. Karpat (1973: 32-33), Decdeli et al. (1984: 399).

4. Islamoglu and Keyder (1977), Decdeli et al. (1984: 400).

5. For this and the following, see Lewis (1961), Davison (1968), Inalcik (1970a), Shaw and Shaw (1976), Islamoglu and Keyder (1977), Decdeli et al. (1984), Kasaba (1987), Keyder (1987).

6. Inalcik (1970a: 345-347), Karpat (1973: 33-34), Kasaba (1987: 807-809).

7. Islamoglu and Keyder (1977), Decdeli et al. (1984: 402-403), Kasaba (1987: 822-830).

8. Inalcik (1970b: 362-363); on nationalism in the Balkans, see Chirot and Barkey (1983).

9. Davison (1963), Inalcik (1970b), Shaw and Shaw (1977: 1-171), Findley (1980).

10. Pamuk (1987: 87).

11. Ubicini (1966), Issawi (1980: 75, 275), Pamuk (1987: 120), Quartaert (1988). For a comparative treatment of the Ottoman incorporation into the world-economy, cf. Pamuk (1988). The political integration of the Ottoman Empire into the Europen state system is discussed by Naff (1984).

12. Cf. Manzenreiter (1982).

13. Suvla (1966: 98), Davison (1980).

14. Wynne (1951b: 394-413), Suvla (1966: 100-101), Pamuk (1987: 59).

15. Hershlag (1980: 305-307), Pamuk (1987: 59).

16. *The Economist*, October 9, 1875.

17. Blaisdell (1929), CFB (*Annual Report*, 1930: 373).

18. Yet, the Ottoman Empire continued paying debt-service obligations of its first two foreign bonds (raised in 1854-1855) since they were secured by special guarantees (interest payments on the war loan of 1855 were guaranteed jointly by the British and French governments). A small bond contracted in 1871 was defaulted only in 1877 (cf. CFB, *Annual Report*, 1930: 371-373; Wynne 1951b: 394-396).

19. *The Economist*, October 9, 1875.

20. Pamuk (1987: 24, 50).

21. Inalcik (1970b: 370), Karpat (1973: 45-46), Shaw and Shaw (1977: 174-187).

22. As a result of the agreements reached at the Congress of Berlin, the Ottoman Empire lost two-fifths of its territory and one-fifth of its population and had to pay a war indemnity to Russia of 802 million francs (cf. Shaw and Shaw 1977: 190-191).

23. Blaisdell (1929: 90), Wynne (1951b: 425-435).

24. Blaisdell (1929), Thobie (1980), Owen (1981).

25. Issawi (1966: 94), Pamuk (1987: 64, 75).

26. Keyder (1980: 324).

27. Ahmad (1969, 1980, 1988), Zürcher (1984).

28. Keyder (1979: 6). Yet, there are rather different interpretations of the class character of the Young Turks. According to some authors, the Young Turks

represented the interest of the rising bourgeoisie, while others identify them as a bureaucratic class; see Keyder (1987, 1988) for a more detailed discussion.

29. Ahmad (1969: 16-18, 157), Neyzi (1973).

30. Blaisdell (1929: 184-196).

31. Özbudun (1981: 85); cf. also Karpat (1973), Neyzi (1973), Shaw and Shaw (1977: 340-404) and the contributions in Kazancigil and Özbudun (1981).

32. Keyder (1981), Berberoglu (1982: 9).

33. In the Treaty of Lausanne total debt of the old Ottoman Empire was fixed at £148 million. From this amount, 67 percent (£99 million) was allotted to Turkey and 33 percent to the other twelve successor states, i.e. Albania, Bulgaria, Greece, Iraq, Italy, Lebanon, Palestine, Saudi Arabia, Syria, Trans-Jordan, Yemen, Yugoslavia; cf. Conseil de la Dette Publique (*Rapport*, 1968/69: 6), Thobie (1972: 188).

34. Thobie (1972: 149).

35. According to the agreement of May 1936, the Turkish government could make half of payments due in Turkish pounds. After the devaluation of the French franc an agreement with French bondholders was concluded in 1938 that all payments would be made in Turkish pounds (cf. CFB, *Annual Reports*, 1937-1954; Wynne 1951b: 510-515).

36. From the amount of £99 million of total Ottoman debt allotted originally to Turkey, only £29 million was finally paid back (cf. Conseil de la Dette Publique, *Rapport* 1968/69, Thobie 1972).

37. Walstedt (1980), Hershlag (1984), Landau (1984), Birtek (1985).

38. Lewis (1961), Neyzi (1973).

39. Berberoglu (1982: 54), Birtek (1985).

40. Bittermann (1973: 137), Walstedt (1980: 81).

41. Walstedt (1980: 31-32, 235).

42. Hardy (1982: 66).

43. Keyder (1979: 25, 31), Hale (1981: 123-126).

44. Walstedt (1980), Martner (1982), Keyder (1987: 150-198).

45. Ecevit (1973).

46. Berberoglu (1982: 108).

47. Ahmad (1977), Keyder (1979), Acikalin (1983: 211).

48. Martner (1982: 312).

49. For the following, see Martner (1982) and Acikalin (1983).

50. For a detailed discussion of the military rule during the 1980s, see Acikalin (1983), Harris (1985), Heper and Evin (1988), Hershlag (1988).

Conclusion

The aim of the present study has been to describe and to explain the structure and the long-term dynamics of periphery indebtedness during the nineteenth and twentieth centuries. The study's fundamental thesis states that the phenomenon of periphery indebtedness is subject to long cyclical processes. Specifically, I argue that expanding foreign indebtedness at the periphery (or rising capital exports from the core), the occurrence of debt-service incapacity and negotiations of debt-settlement arrangements are related structural periods of a single global debt cycle. The pattern and the dynamics of these debt cycles have been associated with fluctuations of global economic growth (i.e. Kondratieff and Kuznets cycles), with long cycles in the rise and fall of hegemonic powers and with secular trend movements leading to an increasing institutionalization of international financial relations. The basic theoretical arguments have been examined empirically on both the global level of the world-economy and the national level of individual debtor countries to investigate the interplay between world-system processes and national characteristics.

The conclusion first summarizes the empirical evidence and examines the implications of the country case studies for the operation of global debt cycles. The second section suggests an evolutionary model of periphery indebtedness based on a combination of different world-system forces. Section three discusses recent developments of the present debt-settlement strategy and the prospects for a long-term solution to the present debt crisis in the light of the historical experiences. The final section speculates about the future working of debt cycles.

Summary of the Empirical Evidence and Implications of Country Case Studies for the Operation of Global Debt Cycles

According to the basic hypotheses developed in Chapter 3, the empirical examination has focused on four aspects: first, empirical evidence for the existence of debt cycles; second, causes for the expansion of periphery indebtedness; third, reasons for the outbreak of debt crises and; fourth, the pattern of debt settlement. In addition, the debt behavior of individual peripheral countries concerning these aspects has been associated with the structure of the respective political regimes.

Existence of Debt Cycles

At the global level of the world-economy, strong empirical evidence has been found for the existence of debt cycles: capital exports from the core, international loan-raising activity of the periphery, the outbreak of debt-service incapacity and the conclusion of debt-settlement agreements were all subject to cyclical fluctuations. Boom phases in credit-raising activity occurred during the early 1820s, during the late 1860s and early 1870s, during the 1920s as well as during the 1970s; debt-service incapacity was concentrated in the years between the late 1820s and the late 1840s, between the early 1870s and the mid-1880s, between the early 1930s and the late 1940s and from the early 1970s onwards; the conclusion of debt settlements clustered during the 1840s and 1850s, during the 1890s, as well as during the late 1940s and the early 1950s. The discontinuous nature of periphery indebtedness is most clearly visible in the case of global debt crises.

The analysis of the country case studies has shown the existence of quite different debt careers within the framework of the general cyclical processes taking place at the global level of the world-economy. Out of the three cases considered, Peru corresponds exactly to the global cyclical model. This similarity between global debt cycles and the Peruvian debt pattern can be explained by the comparatively strong and early incorporation of Peru as a raw-material-producing periphery into the world-economy (first guano, then cotton, sugar, copper, fish meal). As a consequence, the national Peruvian economy was strongly exposed to the influences of world-system processes.

A cyclical pattern of periphery indebtedness, although less obvious than in the Peruvian case, is also present in the cases of Liberia and the Ottoman Empire/Turkey. Due to their initially weak linkages to the world-economy, neither Liberia nor the Ottoman Empire raised foreign loans during the first half of the nineteenth century. After their incorporation into the expanding world-economy, external debt of both Liberia and the Ottoman Empire reveals a cyclical pattern from the middle of the nineteenth century onwards. Yet, particularly in the case of the outbreak of debt-service incapacity, the cyclical fluctuations differ from the global pattern. Liberia as well as the Ottoman Empire shows frequent payment difficulties even in between the general global debt crises (Liberia: 1875-1898, 1912, 1914-1915, 1917-1923, 1932-1935, 1964-

1971, 1980-1985; Ottoman Empire/Turkey: 1876-1881, 1915-1928, 1931-1932, 1940-1943, 1958-1963, 1965-1967, 1977-1983). This comparatively high proneness to debt crisis can be attributed to the weakness of the national economic and political structures as a result of the peripheralization process the two countries were subject to in the course of the nineteenth and twentieth centuries: the Ottoman Empire suffered from the disintegration and decay of its old world-empire structures, whereas Liberian society became fully dependent from the rule of foreign capital which established an enclave economy. In addition, both countries were largely dominated by state classes and, in the case of Turkey, populist forces, i.e. those two types of political regimes which have been expected to be least successful in handling debt problems.

Expansion of Periphery Indebtedness

As hypothesized, the expansion of periphery indebtedness and of core capital exports coincides, with peaks of global growth cycles (i.e. Kondratieff waves over the whole period and Kuznets cycles over the period of ca. 1860 to ca. 1930). Two indications could be found for the thesis that the expansion of periphery indebtedness is connected with declining profits and market saturation in the core: On the one hand, there is a tendency for declining returns on equity investment within major core countries during the late 1960s and the 1970s. On the other hand, fluctuations of British capital exports and of foreign borrowing by countries belonging to the Atlantic economy occurred parallel to shifts in the profitability of British domestic investments during the period 1870-1913. Cross-national research on the determinants of periphery indebtedness during the 1920s and 1970s suggests that peripheries with a large economic potential were most heavily indebted. In addition, the presence of developmentalist strategies (which are associated with the favorable conditions of the peripheral economy as production site during the late upswing phases of a long wave) and the degree of dependence on foreign direct investment were further factors determining the amount of foreign borrowing during the 1970s.

Outbreak of Debt Crises

The occurrence and duration of global debt crises largely coincide with stagnation phases of global Kondratieff growth cycles. In addition, during the period of ca. 1860 to ca. 1930, periods of widespread debt-service incapacity coincide with stagnation phases of Kuznets cycles of the capital-importing countries integrated into the Atlantic economy. Cross-sectional evidence on the determinants of debt-service incapacity for the global debt crises of the early 1930s and the 1980s suggests previous debt-service difficulties and declining export revenues combined with rising debt-service payments as the most important causal factors. This confirms the basic argument that economic stagnation within the world-economy and adverse development of world trade contribute to the outbreak of debt crises at the periphery. Contrary to the expectations, credit rationing by lenders seems to play only a minor role on an aggregate level.

The case histories of individual debtor countries confirm these findings for the nineteenth century, too. Thus, Peru's debt crises were always preceded by a collapse of export income (e.g. collapse of guano exports during the 1870s). The same applies to the Ottoman Empire and Liberia. Apart from declining export earnings, the inefficient and consumptive use of foreign resources played an important role as well. Likewise, creditor behavior has been found to be of importance. Hard and unfavorable loan conditions (cf. the Liberian and Ottoman loans) on the one hand and the refusal of new credits (cf. the 1930s in general and the Peruvian debt crisis of 1876) on the other were decisive factors for the outbreak of debt-service incapacity in several instances.

Arrangements of Debt Settlements

The conclusion of debt settlements between debtor countries and their creditors occur discontinuously and cluster around the early upswing phase of global growth cycles.

The empirical analysis of debt settlements showed substantial differences between the settlements of defaulted foreign bonds prior to World War II and multilateral reschedulings during the postwar period with respect to the efficacy of the crisis management, the degree of debt relief granted by creditors and the degree of political and economic pressures exerted on debtor countries by creditors. In the case of multilateral rescheduling, creditors have been able to respond quickly to the crisis, to exert pressures on debtor countries to carry out economic adjustment programs and to prevent any far-reaching debt forgiveness. The settlement of defaulted bonds, by contrast, was characterized by long-lasting defaults, relatively favorable terms of the settlement for debtor countries and, with the exception of the period 1871-1925, few political and economic pressures by creditor countries on debtors. This pattern can be explained by the increasing density and institutionalization of creditor cooperation during the postwar era.

The analysis of the three default-settlement periods of 1821-1870, 1871-1925, and 1926-1975 showed that the efficacy of debt settlements and the degree of political and economic control of debtor countries by creditors was highest during the period 1871-1925. The terms of debt settlement were most favorable for debtor countries in the wake of the debt crisis of the 1930s, suggesting that the bargaining power of peripheral borrowers is greatest in phases of hegemonic transition, i.e. when a new hegemony integrates peripheral debtor countries into its newly emerging power system at the expense of the old and decaying hegemony.

These differences found in the global pattern of debt settlement are reflected in the case studies. Peru, Liberia and the Ottoman Empire experienced political and economic pressures by creditors with respect to the debt settlement concluded in the late nineteenth and the early twentieth centuries (Peru: cedation of state railways to bondholders, Ottoman Empire and Liberia: establishment of debt administrations by creditors). In addition, all three countries considered had to accept economic adjustment programs administered by the International Monetary Fund in the wake of the debt crisis of the 1980s. The terms of debt settlements were most favorable for debtors in the arrangements agreed upon after the debt crisis of the 1930s (particularly in the Peruvian and Turkish cases, where 50-70 percent of outstanding debt had been cancelled), whereas the settlements during the first half of the nineteenth century (only Peru) and the rescheduling agreements of the 1980s brought no substantial debt relief.

Debt Behavior of Political Regimes

On the level of individual country case histories, the specific national pattern of periphery indebtedness has been related to the structure of the dominating political regime. Specifically, I have argued that the degree of dependence on external financial resources, the proneness to debt-servicing difficulties and the handling of debt problems depend in part on the nature of the political regime.

As postulated, state class-based and populist regimes rely heavily on foreign debts and spend them largely unproductively for consumption purposes. Regimes dominated by state classes spent external resources to maintain, expand or enrich the state class. Outstanding examples are the Ottoman Empire during the Tanzimat era (1839-1876) and under Abd ül-Hamid II (1876-1908); Liberia under Roy (1869-1871), Barclay (1906-1912) and Tolbert (1971-1980); and, with some qualifications, Peru during the Balta administration (1868-1872). Populist regimes use financial means borrowed abroad to finance redistributive and integration policies for urban middle and lower classes. Examples are Peru during the governments of Leguía (1919-1930), Belaúnde (1963-1968) and Velasco (1968-1975) as well as, with some reservations, Turkey under Ecevit and Demirel (1973-1980). Populist regimes turned out to be particularly dependent on the mobilization of external financial resources since, as a result of opposition from the powerful oligarchic forces, they often lack an adequate tax base to finance their redistributive and import-substituting industrialization policies (cf. the Peruvian case during the first term of Belaúnde and during the government of Velasco). Capitalist and disarticulated regimes only rarely relied on external debt. No example of heavy external borrowing of these regime types could be found in the cases of Peru, Liberia and Turkey.

Due to their reliance on consumptive use of external resources, regimes based on state classes and populist regimes are those most frequently affected by debt crises. This is shown by the debt history of the Ottoman Empire/Turkey (default 1876-1881, 1915-1928, 1931-1932, 1940-1943); the Peruvian defaults and reschedulings of 1826, 1876 (after Balta), 1931 (after the fall of Leguía) and 1968, 1969-1970; and the several Liberian debt crises during the rule of the Republicans and True Whigs. By contrast, capitalist regimes rarely fell into the debt trap. The Turkish reschedulings during the rule of the Democrats (1959) is the only example. With respect to disarticulated regimes it has been suggested that debt-servicing difficulties may be inherited from previous regimes that resorted more strongly to foreign borrowing. This has been the case in the reschedulings by the governments of Özal in Turkey (1981-1982), Bermúdez and Belaúnde in Peru (1978, 1980, 1983-1984) and Doe (1980-1985) in Liberia.

The empirical material from the three case studies concerning the debt-crisis management shows that defaulted debts were often settled by disarticulated and capitalist regimes. This is demonstrated most clearly by the Peruvian debt settlements of 1849, 1889, 1951/53 and 1978-1984, and the Turkish reschedulings under Özal. Debt settlements agreed to by regimes based on state classes and populist regimes have often proved short-lived, as demonstrated by the frequent debt settlements of Liberia's external debt (particularly between 1912 and 1935 and between 1963 and 1985), of the old Ottoman debt by Atatürk and his followers between 1921 and 1943 or the unsuccessful reschedulings undertaken by the Ecevit and Demirel administrations during the late 1970s.

How do these findings contribute to the explanation of the fluctuations of global debt cycles? The empirical material on the evolution of political regimes discussed in Chapters 8-10 suggests that (at least after a country has been integrated into the world-economy) there is a certain tendency for regime sequences to be of a cyclical nature, too. At a general level this can be explained by the shifting relative strength of social forces over a long wave of economic development at the periphery. A cyclical evolution from capitalist regimes during the upswing, populist regimes at the peak and disarticulated regimes during the downswing of a long wave, together with the systematic behavior of regime types with regard to foreign debt, implies a procyclical behavior of many debtor states concerning global debt cycles: populist regimes at the peak favor the inflow of debts and their unproductive use, and disarticulated regimes during downswing phases permit a conclusion of debt settlements. Part of the global dynamic of debt cycles is thus explained by processes occurring at the national level of peripheral countries.

Combining Different Types of Cycles and Trends: The Three Stages in the Evolution of Periphery Indebtedness

Despite the presence of cyclical patterns in periphery indebtedness, no homogeneous sequence of cycles throughout the period of industrial capitalism can be established. Rather, different types of cycles, i.e. Kondratieff waves, Kuznets cycles and world leadership cycles, and trend movements (e.g. increasing institutionalization) appear to interact mutually. If these different world-system forces are combined, the long-term evolution of periphery indebtedness during the period of industrial capitalism can be divided into three stages.

During the first phase, which covers the first half of the nineteenth century, the institutional base of industrial capitalism was still weakly developed within the world-economy. This applies particularly to the political sphere. Thus, at the periphery of the expanding world-economy the international state system was not yet strongly established. The material presented within the framework of the country case studies indicates that the formation of the structures of modern nation-states within peripheral societies was largely financed through foreign loans (e.g. financing of liberation wars in Latin America). Similarly, external debt played an important role for the dissolution of world-empire structures and the incorporation of previous world-empires as peripheries into the capitalist world-economy (e.g. the case of the Ottoman Empire, but also of the Spanish world-empire in Latin America). The only limited relevance of Kondratieff and Kuznets cycles during the first half of the nineteenth century (e.g. the weak empirical evidence for cyclical fluctuations in core capital exports) may be explained by the low level of expansion of industrial capitalism. During those years the industrial segment of the world-economy was just emerging, and its influence on the dynamics of the total economy and society was, therefore, still limited. Similarly, the long period of disrupted financial relations during the first half of the nineteenth century can be attributed to the low degree of institutionalization of international financial relations, which is related to the low level of integration of peripheries into the world-economy during this initial phase.

The second stage of periphery indebtedness covers the second half of the nineteenth and the first decades of the twentieth centuries (i.e. the period of the second and third Kondratieff cycles). This period saw the rise of the Atlantic economy dominated by the dynamic of Kuznets cycles. According to Lipietz (1984), this phase has been characterized by extensive capital accumulation. Limited state activities, demographic forces (e.g. increase in population, migration movements), territorial expansion and the establishment of communication and transportation infrastructure were of great importance for the development dynamic of extensive capitalism. The pattern of periphery indebtedness during this phase shows a shift from promoting the establishment of the institutional base of nation-states to the financing of large infrastructural investments, notably railroad construction. The cyclical dynamic of global debt is characterized by a combination of Kondratieff and Kuznets cycles, with the latter type of long swings being most clearly visible within the area integrated into the Atlantic economy. Due to the British hegemony prevailing during the second half of the nineteenth century and the beginning institutionalization of creditor cooperation (establishment of national bondholder committees), the debt crises of the mid-1870s and the 1890s were settled comparatively efficiently (e.g. short duration). The particularly severe debt crisis of the 1930s which fell into a period of intense core rivalry marks the beginning transition to the third stage of periphery indebtedness.

After World War II, when the model of intensive capital accumulation succeeded (centralized production, active role of the state and the institutional arrangement of rising real wages parallel to productivity increases), cyclical fluctuations of the Kuznets type lost their influence. Periphery borrowers employed external financial resources to finance redistributive and import-substituting industrialization strategies which may be considered as an attempt by the periphery to initiate a development model based on intensive capital accumulation. Caused by the institutionalization of international financial relations that resulted in strong cooperative networks among creditors, a relatively long period of few debt-service difficulties occurred during the postwar period. The formation of international institutions (e.g. International Monetary Fund, World Bank, OECD) and strong cooperative structures (e.g. multilateral rescheduling techniques) has rendered the international financial system more resilient to adverse developments and helped to prevent an open outbreak of the debt crisis during the 1980s. Although growing institutionalization has thus reduced the destabilizing forces associated with the decline of the hegemonic power, it has not contributed to a liquidation of periphery indebtedness. As a consequence of these developments, a long-term and durable solution of the present crisis has become more difficult to realize than during earlier debt cycles.

Looking Ahead: Prospects for Future Debt Settlements

The analysis of the debt-crisis management during the nineteenth and twentieth centuries has shown that the present settlement strategy of multilateral rescheduling is able to respond much more quickly to crisis situations than the settlement of defaulted foreign governmental bonds. Yet, it is confined to dealing with short-term symptoms on a provisional basis. This raises the question about the future of the rescheduling strategy and the prospects for a long-term solution of the present crisis. In this final section the different debt proposals suggesting ways out of the present debt crisis will be discussed in the light of the historical experiences from settlements of earlier debt crises.

During the 1980s numerous plans and debt proposals have been made. For instance, Bergsten et al. (1985) alone discuss 24 specific alternatives for private bank debts. Particularly in the beginnings of the debt crisis there was a surge of innovative new schemes. Towards the mid-1980s the rescheduling approach was generally considered as more or less successful and the discussion of more far-reaching solutions became less lively.[1] It is indicative for the present state of debt-crisis management that the discussion of proposals focusing on long-term solutions has revived during the past years.[2] I do not intend to give a detailed survey on the various debt proposals here. Rather, the following discussion will be confined to the four basic schemes to which most debt proposals may be attributed. These ideal-typical scenarios may be characterized as the scenarios of debt repudiation, debt release, debt repayment, and debt increase.[3]

(1) The scenario of *default or debt repudiation* aims at reducing the debt burden by liquidating a substantial part of indebtedness. Debt repudiations are declared unilaterally by debtor countries without the creditor's consent and represent thus a violation of contractual obligations. As discussed in detail in this study, default on foreign debt was the usual strategy before World War II. While default was declared only by individual countries so far, joint repudiations by the most heavily indebted countries coordinating their policies in a debtors' cartel appear possible in the future.[4]

(2) Like debt repudiation, the scenario of *debt release* intends to reduce a substantial part of the outstanding debt. Yet, contrary to debt repudiation this reduction is achieved by joint actions of debtors and creditors.

Debt release implies substantial write-offs for losses by commercial banks and/or a socialization of these losses by the governments of creditor countries. One of the most paradigmatic versions of this scenario has been advanced by the German economist Wilhelm Hankel (1984: 90-93). The approach of debt release is supported, of course, by debtor countries and their political leaders. Fidel Castro (1985), for instance, proposed to finance the liquidation of outstanding debts by a 12 percent reduction of military expenditures by creditor countries. Elements of debt release are also included in the "debt discounting" proposals suggested by prominent bankers and economists, who recommend the transfer of frozen assets from banks to existing or newly established international organizations.[5]

(3) Under the scenario of *debt repayment*, debtors have to meet their obligations in full. This means that the borrowing countries have to carry the whole burden of the liquidation of indebtedness. Since most peripheral debtor countries do not have enough international reserves, the only way to repay their debts is to earn foreign exchange by producing export surpluses. This can be realized by increasing exports and/or reducing imports. Hence, the debtors' economies have to finance this real transfer by internal adjustment processes. This implies that savings are increased by cutting back on private and government consumption and that a substantial part of savings are not invested but transferred abroad. In the context of the present debt crisis a policy of debt repayment is usually pursued under the guidance of the IMF. Stabilization policies promoted by this organization intend to curb internal demand by policy measures primarily in the fields of price liberalization.[6] An alternative way for debtor countries to earn foreign exchange is to sell parts of their property (e.g. state-owned companies) to foreigners. The consequences of such schemes are the privatization and denationalization of debtors' economies.

(4) The scenario of *debt increase* is based on a global Keynesian model. Advocates of this proposal, like the Brandt Commission (1980, 1983), recommend a massive increase of financial flows to developing countries to free frozen assets and overcome economic recession. As in the case of debt release, this proposal intends to strengthen international financial institutions. The required financial resources may be raised by increasing real transfers from developed countries (e.g. increase in official aid, taxes on international trade or arms production) or by creating international liquidity (e.g. increasing the Special Drawing Rights, or SDRs, of the IMF). Insofar as the latter strategy is carried out this scheme may be called "debt inflation."

Debt-settlement patterns of the earlier debt crises contain elements of all of these four ideal-typical scenarios. Thus, a unilateral suspension of debt-service payments at least for some years was common practice although a permanent debt repudiation rarely happened. The empirical material has shown partial debt release granted by bondholder's representatives during all debt crises before World War II. Debt repayment, of course, also occurred, among others in the form of cedation of property rights to creditors. However, compared to the other three scenarios there were -- apart from capitalization of arrears of interest payments -- only few instances of debt increase before World War II. Obviously, it proved rather difficult to convince individual bondholders to invest fresh money insolvent debtor countries.

Although historical evidence for all of the four ideal-typical scenarios may be found, the models actually realized in the wake of the past debt crises were always a combination of them. Specifically, one may discern a certain temporal sequence in the occurrence of the four basic scenarios. Thus, during the initial stages of an impending debt crisis, debtor countries usually tried to mobilize new loans on capital markets (element of debt increase). If this proved to be impossible they were forced to implement some adjustment measures (element of debt repayment) or to suspend debt-service payments (element of debt repudiation). The settlements eventually negotiated between debtor countries and creditors after a period of default usually contained some debt relief, e.g. reductions in interest rates or outstanding debts (elements of debt release) as well as elements of debt repayment.

The reasoning above suggests that the question about the prospect of future debt settlements is not a matter of pure debt repayment, debt increase, debt repudiation or debt release but rather one of combining elements from different basic scenarios. In terms of the four basic scenarios the strategy of multilateral rescheduling applied to the present debt crisis may be characterized as a combination of debt repayment (partly postponed to the future) and debt increase (as far as new credits were extended and/or interest payments were capitalized) -- a model that was very exceptional before World War II. Moreover, our analysis of developments within the rescheduling culture since the onset of the present debt crisis suggests changes in the combination and importance of the different basic scenarios. Thus, during the first two years elements of debt repayment clearly prevailed. The "Baker plan" proposed in 1985 recommending a strengthening of international institutions as well as a massive expansion of the disbursements of new credits by the World Bank (an increase of 50 percent for 1986-1988) and by private banks ($20 billion for 15 heavily indebted countries for three years) in addition to structural adjustment processes of debtor countries represented a shift from debt repayment to debt increase. Yet, in reality the Baker plan never became effective due to the complete failure of private banks to mobilize the required amount of fresh money.[7]

During the second half of the 1980s new debt relief techniques were implemented indicating a gradual shift from the combination of debt repayment and debt increase to a combination of debt repayment and debt release. Three measures or techniques of debt release have been of special importance. First, a secondary market of Third World debt evolved where debts were traded at discounts ranging from 20 percent to 90 percent. Second, several rescheduling agreements included the possibility of debt-to-equity swaps. In such swap transactions investors buy debt at a discount from the banks and receive the countervalue of the credits as investment capital or shares in existing local firms in the debtor countries.[8] The recently initiated debt-for-nature swaps refer to the same basic idea: A conservation organization acquires debt titles at a certain discount, converts them into local currency and uses the proceeds for the financing of conservation programs in the respective country.[9] Third, official creditors at the Toronto summit of the seven major industrial countries in 1988 decided to grant debt relief to the heavily indebted low-income countries, particularly of sub-Saharan Africa. The techniques recommended included concessional interest rates, longer repayment periods and partial write-offs of debt-service obligations.

The Brady plan adopted in 1989 extended this debt reduction strategy to the heavily indebted middle-income countries on the one hand and to international private banks on the other.[10] It represents, therefore, a further and more decisive step towards the scenario of debt release. Under the Brady plan private creditors can choose among three options, namely, reductions in outstanding debt or in interest rates, or granting new loans. As in the case of the Baker plan, the Bretton Woods institutions are to play an important role in the new debt strategy by financing or guaranteeing debt reduction.[11] The Mexican rescheduling of February 1990 which served as a test case of the realization of the Brady plan illustrates, however, the (yet) limited degree of debt release: This agreement, which covered external debts of $48 billion owed to some 500 private banks, brought the Mexican government a reduction of $1.7 billion in interest payments (corresponding to 10 percent of total debt service due) and a reduction of $6.7 billion in outstanding debts (amounting to 7 percent of total outstanding debt).[12] Only 10 percent of all banks involved agreed to offer new loans, indicating, thereby, their lack of support for the scenario of debt increase. Compared to the settlements of defaulted foreign governmental bonds after the global debt crisis of the 1930s, where 65 percent of arrears of interest were cancelled, outstanding debts were lowered by 25 percent and interest rates were reduced by an average of about 35 percent, the degree of debt release granted to Mexico by the Brady plan rescheduling has to be judged as rather low.

In sum, the developments of the debt-settlement strategy during the past decade show a shift away from pure debt repayment. In the middle of the 1980s an attempt to combine debt repayment and debt increase largely failed, facilitating, thereby, a movement towards the scenario of debt release by the end of the decade. Yet, historical evidence suggests that the elements of debt release have to be considerably strengthened in the future to reach a long-term solution to the present global debt crisis, particularly if the feasibility of debt increase further deteriorates.

Implications for the Future Working of Debt Cycles

The still-pending settlement of debt-service incapacity after ten years of crisis suggests that the long-term cyclical dynamics discussed in this study might be substantially modified in the future. The growing institutionalization of international financial relations and the consequent increased capability of creditors for a more controlled response to the debt crisis raises the question about the future prospect for financial cycles and long cycles in general. In what follows I discuss the implications, first, of the case that an open crisis is averted and, second, of the possibility that the present debt-settlement strategy outlined in the previous section simply defers the breakdown of the system.

In the context of the simplified model of global debt cycle and Kondratieff waves described in Chapter 3, I have argued that a new cycle is initiated when enterprises begin to invest in the production of basic innovations. Since this kind of investment is risky and, conversely, profit rates are uncertain, the production of basic innovations requires that no other profitable outlets for capital exist. In the past, these outlets have, at least in part, been barred by the outburst of an international economic crisis comprising a collapse of international financial relations. Historically, defaults by sovereign borrowers erased international indebtedness and thereby removed the strains imposed on the world-economy by the frozen assets. The resulting low profit rates were then a powerful motive for enterprises to invest in the production of new basic innovations. During the 1980s, however, the relative profit rates of financial assets were as high as ever before, perhaps precisely because the financial system did not break down so far. Reschedulings require a large amount of capital, and the structural problems associated with the declining hegemonic status of the United States manifesting themselves in large fiscal and current account deficits can be rolled over in part on international financial markets. The high interest rates associated with this new situation may discourage investment in basic innovations. As a consequence, the initiation of a Kondratieff growth cycle may be retarded or even prevented by the present approach to resolve the debt crisis mainly through reschedulings.

It may also be, however, that the present debt-settlement strategy only retards the outbreak of an open crisis. It has been mentioned that the institutionalizing trend has been confined to the creditor side of international financial relations. This implies that the interests of the periphery are rather weakly represented in the present approaches to deal with the debt problem. If the pressure exerted on Third World countries by the core makes itself felt in further declines in living standards, the present interest harmony between the elites of the core and the periphery will increasingly come under legitimatory pressure from the marginalized sectors of the periphery. In the long run this may lead to the emergence of political regimes in the Third World that are based on the support of the marginalized sectors and have only a slight commitment to the internationalized sectors of the society. These new political regimes may repudiate external claims and pursue a new, predominantly inward-oriented development policy. This happened in many Latin American countries during the 1930s. The consequence of this would simply be a deferment of the outbreak of an open global debt crisis and a protraction of the initiation of the beginning of a new Kondratieff wave.

Some tentative evidence for the deferring effect of the trend towards greater institutionalization of international financial relations is visible in the fact that the delay between the end of the upswing of a Kondratieff cycle and the outbreak of a debt crisis has progressively increased since 1800. Insofar as the present crisis is concerned, the recent shift towards the debt-settlement scenario of debt release described in the previous section suggests that the institutionalizing forces are sufficiently strong for the maintenance of international financial relations until the (protracted) beginning of a new Kondratieff cycle.

It can be concluded that the increasing coordination and regulation of international financial relations may protract the initiation of a new Kondratieff cycle by deferring or avoiding a crisis without contributing to a long-term solution. To end on a speculative note, one may conjecture that the world-economy will be characterized by more damped long cycles with less disruptive crises in the future but be burdened with a heavier load of unsolved structural problems.

Notes

1. This may be illustrated by the rhetorical question "Debt: Are we at the end of the crisis?" raised by Michel Camdessus (1986), managing director of the IMF and former chair of the Paris Club.

2. E.g. Bird (1987), Pastor (1987), Feinberg and Ffrench-Davis (1988), Dornbusch (1989), Griffith-Jones (1989), O'Neill (1989), and the contributions in the *Journal of Economic Perspective* 1990, 4 (1) and in *International Environmental Affairs* 1990, 2 (2).

3. Cf. Suter et al. (1988) for a more detailed discussion.

4. Cf. Kaletsky (1985), Hojman (1987), Holler (1989).

5. E.g. Kenen (1983, 1990), Sachs (1990).

6. See Killick (1984).

7. Cf. Pastor (1987).

8. Cf. Parhizgari (1988). The so far rather limited relevance of debt-to-equity swaps is illustrated by the fact that they amounted to less than 1 percent of total outstanding indebtedness by the end of 1987 (World Bank, *World Debt Tables*, 1987/88).

9. Cf. Hansen (1989), Jaeger (1990).

10. Cf. Frenkel (1989).

11. Cf. *IMF* (1989), Sachs (1989).

12. Cf. World Bank (*World Debt Tables*, 1990/91, Vol. 1: 58).

Appendix: Time Series of Data on Global Debt Crises, 1823-1989

Year	Number of Countries in Default[a] Interest[b]	Total[c]	%Int.[d]	%Tot.[e]	Share of Defaulted Debt[f]	Reschedulings[a] Number[g]	%N.[h]
1823	0	0	0.0	0.0	0.0		
1824	1	1	2.0	2.0	7.6		
1825	1	1	2.0	2.0	7.8		
1826	8	8	15.7	15.7	16.1		
1827	9	9	17.6	17.6	18.6		
1828	15	15	29.4	29.4	21.9		
1829	15	15	29.4	29.4	21.0		
1830	14	14	26.9	26.9	18.1		
1831	13	13	25.0	25.0	14.9		
1832	14	14	26.9	26.9	18.1		
1833	14	14	26.9	26.9	17.1		
1834	14	14	26.9	26.9	16.5		
1835	13	13	25.0	25.0	9.8		
1836	13	13	25.0	25.0	9.2		
1837	15	15	28.8	28.8	18.7		
1838	15	15	28.8	28.8	18.3		
1839	15	15	28.8	28.8	18.2		
1840	15	15	28.8	28.8	18.8		
1841	13	13	25.0	25.0	18.1		
1842	12	12	23.1	23.1	21.0		
1843	11	11	21.2	21.2	19.7		
1844	12	12	23.1	23.1	22.8		
1845	11	11	20.8	20.8	14.8		
1846	10	10	18.9	18.9	13.5		
1847	10	10	18.5	18.5	12.8		
1848	11	11	20.4	20.4	14.5		
1849	10	10	18.5	18.5	13.4		
1850	12	12	22.2	22.2	15.9		
1851	11	11	20.4	20.4	11.0		

Year	Number of Countries in Default[a] Interest[b]	Total[c]	%Int.[d]	%Tot.[e]	Share of Defaulted Debt[f]	Reschedulings[a] Number[g]	%N.[h]
1852	11	11	20.4	20.4	9.7		
1853	11	11	20.4	20.4	8.8		
1854	12	12	22.2	22.2	10.6		
1855	12	12	22.2	22.2	9.6		
1856	11	11	20.4	20.4	8.6		
1857	9	9	16.7	16.7	7.1		
1858	8	8	14.8	14.8	6.3		
1859	8	8	14.8	14.8	5.5		
1860	8	8	16.0	16.0	5.0		
1861	7	7	14.0	14.0	4.9		
1862	6	6	12.0	12.0	3.8		
1863	5	5	10.0	10.0	3.0		
1864	5	5	10.0	10.0	2.7		
1865	5	5	10.0	10.0	2.1		
1866	6	6	12.0	12.0	4.7		
1867	7	7	14.0	14.0	4.5		
1868	6	7	12.0	14.0	3.7		
1869	6	7	12.0	14.0	3.4		
1870	6	7	12.2	14.3	3.2		
1871	5	5	10.9	10.9	3.1		
1872	7	7	15.2	15.2	7.3		
1873	9	10	19.6	21.7	9.3		
1874	11	11	23.9	23.9	8.6		
1875	12	12	26.1	26.1	8.2		
1876	17	17	37.0	37.0	23.3		
1877	17	17	37.0	37.0	22.9		
1878	17	17	34.0	34.0	22.6		
1879	15	15	30.0	30.0	21.8		
1880	15	16	30.6	32.7	20.2		
1881	14	15	28.6	30.6	15.8		
1882	11	12	22.9	25.0	6.3		
1883	10	11	20.8	22.9	2.9		
1884	10	10	20.4	20.4	2.8		
1885	10	10	20.4	20.4	2.7		
1886	7	7	14.6	14.6	1.3		
1887	7	7	14.6	14.6	1.2		
1888	7	7	14.6	14.6	1.2		
1889	5	5	10.4	10.4	1.1		
1890	5	5	10.4	10.4	2.1		
1891	5	5	10.4	10.4	2.5		
1892	8	8	16.7	16.7	2.8		
1893	7	7	14.6	14.6	2.7		

Year	Number of Countries in Default[a] Interest[b]	Total[c]	%Int.[d]	%Tot.[e]	Share of Defaulted Debt[f]	Reschedulings[a] Number[g]	%N.[h]
1894	9	9	18.8	18.8	1.4		
1895	9	10	18.8	20.8	1.7		
1896	7	7	14.6	14.6	1.3		
1897	7	7	14.6	14.6	1.3		
1898	7	7	14.3	14.3	1.5		
1899	7	7	14.3	14.3	1.6		
1900	7	7	14.0	14.0	1.6		
1901	7	7	14.0	14.0	1.6		
1902	6	7	12.0	14.0	0.4		
1903	6	8	11.8	15.7	0.4		
1904	6	8	11.8	15.7	0.4		
1905	5	6	9.6	11.5	0.3		
1906	5	6	9.6	11.5	0.3		
1907	5	6	9.4	11.3	0.3		
1908	4	5	7.5	9.4	0.2		
1909	4	5	7.5	9.4	0.2		
1910	4	5	7.5	9.4	0.2		
1911	5	5	9.4	9.4	0.2		
1912	3	4	5.7	7.5	0.1		
1913	3	3	5.7	5.7	0.1		
1914	4	5	7.5	9.4	1.2		
1915	7	9	13.2	17.0	2.8		
1916	8	9	15.1	17.0	3.1		
1917	8	10	15.1	18.9	3.1		
1918	8	10	14.5	18.2	21.8		
1919	9	10	15.8	17.5	21.8		
1920	8	9	14.0	15.8	21.8		
1921	9	10	15.5	17.2	22.2		
1922	9	9	15.0	15.0	21.2		
1923	8	8	13.3	13.3	20.0		
1924	6	6	10.0	10.0	18.9		
1925	4	4	6.7	6.7	18.4		
1926	3	3	5.0	5.0	18.0		
1927	3	3	4.8	4.8	17.6		
1928	4	4	6.5	6.5	18.1		
1929	4	4	6.5	6.5	16.4		
1930	4	4	6.5	6.5	16.1		
1931	8	9	12.9	14.5	17.6		
1932	19	22	30.6	36.0	21.9		
1933	23	25	37.1	40.3	27.4		
1934	21	23	33.9	37.1	24.5		
1935	21	22	33.9	36.0	24.5		

Year	Number of Countries in Default[a] Interest[b]	Total[c]	%Int.[d]	%Tot.[e]	Share of Defaulted Debt[f]	Reschedulings[a] Number[g]	%N.[h]
1936	20	21	32.8	34.4	24.8		
1937	19	20	31.1	32.8	26.5		
1938	20	20	32.8	32.8	26.0		
1939	19	19	31.1	31.1	22.3		
1940	23	23	37.7	37.7			
1941	24	24	38.1	38.1			
1942	25	25	39.1	39.1			
1943	24	24	37.5	37.5			
1944	22	22	34.4	34.4			
1945	20	20	29.9	29.9			
1946	20	20	29.0	29.0			
1947	16	16	22.5	22.5			
1948	15	15	20.5	20.5			
1949	15	15	19.7	19.7			
1950	15	15	19.7	19.7			
1951	14	14	18.2	18.2			
1952	13	13	16.9	16.9			
1953	9	9	11.7	11.7			
1954	8	8	10.4	10.4			
1955	8	8	10.4	10.4			
1956	7	7	8.8	8.8		1	1.3
1957	7	7	8.6	8.6		0	0.0
1958	7	7	8.4	8.4		0	0.0
1959	6	6	7.2	7.2		1	1.2
1960	7	7	7.1	7.1		1	0.1
1961	7	7	6.9	6.9		3	2.9
1962	8	8	7.3	7.3		3	2.8
1963	7	7	6.3	6.3		3	2.7
1964	7	7	6.2	6.2		2	1.8
1965	7	7	6.1	6.1		4	3.5
1966	7	7	6.0	6.0		4	3.4
1967	7	7	6.0	6.0		3	2.6
1968	6	6	5.1	5.1		4	3.4
1969	6	6	5.1	5.1		4	3.4
1970	6	6	5.1	5.1		4	3.4
1971	6	6	5.1	5.1		4	3.4
1972	6	6	5.0	5.0		6	5.0
1973	6	6	5.0	5.0		5	4.2
1974	6	6	5.0	5.0		5	4.2
1975	6	6	4.9	4.9		4	3.3
1976	6	6	4.9	4.9		4	3.3
1977	6	6	4.9	4.9		5	4.1

Year	Number of Countries in Default[a] Interest[b]	Total[c]	%Int.[d]	%Tot.[e]	Share of Defaulted Debt[f]	Reschedulings[a] Number[g]	%N.[h]
1978	6	6	4.9	4.9		7	5.7
1979	6	6	4.9	4.9		7	5.7
1980	6	6	4.9	4.9		9	7.4
1981	5	5	4.1	4.1		15	12.3
1982	5	5	4.1	4.1		17	13.9
1983	5	5	4.1	4.1		32	26.2
1984	5	5	4.1	4.1		33	27.0
1985	5	5	4.1	4.1		31	25.4
1986						33	27.0
1987						32	26.2
1988						30	24.6
1989						33	27.0

[a]Countries with a population of less than 1 million in 1980 have been excluded.

[b]Number of countries in default on interest payments of foreign bonds.

[c]Number of countries in default on interest and/or amortization payments of foreign bonds.

[d]Number of countries in default on interest payments of foreign bonds as a percentage of all sovereign nation-states.

[e]Number of countries in default on interest and/or amortization payments of foreign bonds as a percentage of all sovereign nation-states.

[f]Share of foreign bonds in default relative to total foreign investment of major core countries.

[g]Number of countries involved in multilateral reschedulings.

[h]Number of countries involved in multilateral reschedulings as a percentage of all sovereign nation-states.

Sources: Suter (1990: 235-284, 306-310) for 1823-1986, with minor modifications for Latin American countries according to the figures given by Marichal (1989); World Bank (*World Debt Tables*, 1990/91) for 1987-1989. For more details see Suter (1990).

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