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Rescue of Less Developed Countries from National Debts and Other Financial Constraint

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Introduction

A less developed country, is a country which, according to the United Nations, exhibits the lowest indicators of socio economic-development, with the lowest Human Development Index ratings of all countries in the world. The concept of LDCS originated in the late 1960s and the first group of LDC was listed by the UN in its resolution 216(XXVI) of 18th November 1971. A country is classified as a less developed country if the following problems prevail

- Poverty
- Human resource weakness (based on indicates of nutrition, health education and adult literacy) and
- Economic vulnerability (based on instability of agricultural production, instability of exports of goods and services, economic importance of nontraditional activities, merchandise exports concentration, economic smallness, and the percentage of population displaced by natural disasters)

LDC criteria are reviewed every three years by the committee for the Development Policy (CDP) of the UN Economic and Social Council (ECOSOC). Countries may graduate out of the LDC classification when indicators exceed these criteria. The United Nations Office of the High Representative for the less Developed Countries, Landlocked Developing Countries and small island Developing states (UN-OHRLLS) coordinates UN support and provides advocacy services for less Developed Countries. The classification as at 1st January 2011 applies to fourth-eight countries.

Since the LDC category was initiated, only three countries have graduated to developing country status. The first country to graduate from LDC status was Botswana in 1994. The second country was Cape Verde in 2007 and Maldives became the third country to graduates to developing country status in 1st January 2011.

The United Nations suggested that Equatorial Guinea, Samo, Tuvalu and Venatu are among countries to be promoted from LDC status to developing countries. At the UN's forth conference in LDCs held in May 2011, delegates endorsed a goal targeting the promotion of at least half the current LDC countries within the ten years.

Less developed countries can be distinguished from developing countries. Some Economists refer LDCs to as third world countries, but many contemporary scholars argue that "third world" is outdated, irrelevant or inaccurate. Others use the term "Fourth World" in referring to less developed countries (although, fourth world is also used to refer to stateless ethnic groups). The term "less economically developed countries (LEDC is also used today).

However, in order to avoid confusion between less developed countries (LDCs) and less economically developed countries (LEDCS)" which may be both abbreviated as LDCs) and to avoid confusion, with landlocked developing countries which can be abbreviated LLDC) "developing countries" is generally used in preference to "less developed country". Less developed countries suffer conditions of extremes poverty, ongoing and widespread conflict (including civil war or ethnic clashes), extensive political corruption and lack of political and social stability. They form of government in such countries is often authoritarian in nature, and may comprise a dictatorship, warlordism or a plutocracy. Acquired Immune Deficiency Syndrome (AIDS) is a major ailment in many of these countries. The majority of LDCs are in Sub-Saharan Africa.

Common Characteristics of Less Developed Countries

Developing nations are characterized by;

i. **Low Levels of Living**: Ademola (1999) Pointed out that developing countries are poverty-riden. The general conditions of living of the vast majority of the people tend to be very low due to low per capital real income (Less than 250 US dollars per annum for most people). This implies that the vast majority of the people are poorly fed poorly-clothed, poorly-housed, poorly education, diseases-redden and with low life expectancy.
ii. **Low Levels of Productivity:** Maidison (1970) observed that developing nations experience relatively low levels of labour productivity working efficiency and productivity are impaired by malnutrition and poor health which are caused by low income.
iii. **Predominance of Agricultural Sector and Primary Product Exports:** According to Ademola (1999) the main occupation of the bulk of the labour force is 60 percent or more of farming. Agricultural practices are characterized by widespread use of primitive technology with the use of cutlasses and hoes resulting in low output and incomes. With the exception few oil-exporting developing

countries (OPEC and non OPEC), most developing countries earn a high percentage (70 percent or more) of their foreign-exchange income through exportation of agricultural products, especially tree crops, the agricultural sector also accounts for a higher proportion of the Gross Domestic Product (GDP) and Gross National Product (GNP) relative to the manufacturing sector.

iv. **Rising Levels of Unemployment and Underemployment:** The problems of unemployment and underemployment especially of human resources are more chronic in the developing countries. This is as a result of rapidly growing population, low capital formation, as well as emphasis on educational courses that are not relevant to the development needs of their economies. Dependency burdens are also relatively high and incidence of international brain drain in common.

v. **Widespread Income Inequality:** The bulk of the national wealth is concentrated in the hands of the majority few, about 20 percent of the population. The gap between the rich and the poor is always on the increase and the poor are hopeless (Ademola 1999).

vi. **Unavailability of Public Utilities:** Oladeji (1980) pointed out that public utilities, that is public sector enterprises which supply public goods and services such as electricity, water transportation and communication services are lacking in less developed countries because of their low level of income and inadequate control.

The low per capital income of less developed countries is due to the low level of national income and high rate of population growth. They are therefore relatively poor countries (Oladeji 1980)

According to Oladeji (1980), less developed countries are regarded as poor because of their general characteristics discussed above. Poverty is a relative term in the sense that the population that will be regarded as poor in America may have a level and pattern of living that would be regarded as materially well-off in many of the less developed countries. It is difficult to give a precise definition of poverty but the poor in any society stand out sufficiently clear in terms of their economy, cultural, social and psychological condition. Poverty is a condition of life so degraded by diseases, illiteracy, malnutrition, etc, as to deny its victims basic human necessities. More than 40 per cent of the people of developing countries mostly in Africa and South Asia are in this type of condition.

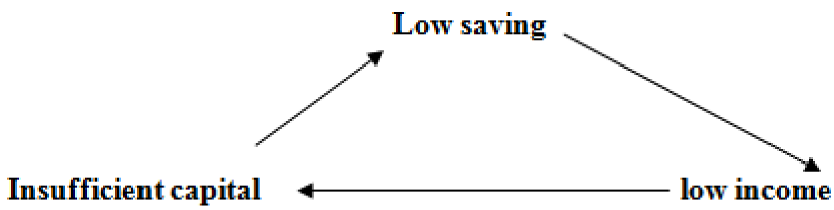
Baker, Peter, Dugger and Celis (2009) stated that poverty is the state of one who lacks a certain amount of material possessions or money. They also enunciated that absolute poverty or destitution refers to the deprivation of basic human needs which include food, sanitation, clothing, shelter, health care and education. Relative poverty defined according to these writers, Baker et all (2009), is economic inequality in the society in which people reside.

Historically, poverty was considered largely unavoidable as traditional modes of production were insufficient to give an entire population a comfortable standard of living. After the industrial revolution, mass production in factories made wealth increasingly more inexpensive and accessible. More importantly, is the modernization of agriculture, such as use of fertilizers to provide enough farm produce yield to feed the population. The supply of basic needs can be restricted by constraints on government services such as corruption, tax avoidance, debt and loan conditionality and the brain drain of health care and educational professionals. Oladeji (1980) asserted that the causes of poverty among less developed countries can be identified as insufficient capital, lack of resources, over population, value system of the people, ignorance, colonialism, lack of law and order and incompetent economic policies.

Vicious Circle of Poverty

The phrase vicious according to Oladeji (1980) is often used to explain why less developed countries are economically backward or poor. It simply means that a country is in object poverty. A circular related can be traced from any of the characteristic of underdevelopment which are responsible for the poverty of underdeveloped countries. For instance, in underdeveloped nations, there is little capacity and capability to save resulting from low level of real income which is due to lack of capital.

Vicious Circle of Poverty



Similarly, circular relatives can be traced from any other characteristics of underdeveloped countries such as high population growth, lack of resources and poor resource distribution and control Oladeji (1980) also noted that any less developed nation which is trapped in a vicious circle of poverty can break the circle through capital accumulation, discovery of new resources, improvement in skill and technology, introduction of new and better techniques of production, institutional changes and complement economic policies. He also suggested that the vicious circle of poverty can be broken through balanced economic growth. The United Nations argued that fundamentally, poverty is a denial of choices and opportunities, a violation of human dignity. It means lack of basic capacity to participate effectively in the society. It means not having enough to feed and clothe a family. Not having a school or hospital to go to, not having the land on which to grew one's food or a job to earn a living, not having access to credit. It also means insecurity, powerless and exclusion of individuals, households and communities. It means susceptibility to violence, and it often implies living in marginal or fragile environments without access to clean water or sanitation.

The World Bank defined Poverty as a pronounced deprivation in well-being, which comprises many dimensions. It includes low incomes and the inability to acquire the basic goods and services necessary for survival with dignity. Poverty also encompasses low levels of health and education, poor access to clean water and sanitation, inadequate physical security.

The World bank anchored absolute poverty line as 1 US dollar per day in 1990 and was revised in 1993 and through 2005, absolute poverty was 1 US. of a day for all countries on a purchasing power parity (PPP) basis, after adjusting for inflation to the 1993 US dollar. In 2005, after extensive studies of cost of living across the world, The World Bank raised the measure for global poverty line to reflect the observed higher cost of living. Now, the World Bank defined extreme poverty as living on less than USS1.25 (PPP) per day.

Debt and Financial Crisis in Africa

The global financial and economic crisis has had a negative impact on African economies and the main challenge facing these countries now is how to position themselves for post-crisis recovery as well as ensure that policy responses to the crisis do not lead to medium and long term problems of debt sustainability.

Laeven and Valencia (2010) examined the situation in Africa over the period 1970-2011 and effort to strengthen financial systems in the continent. In general, economies that have experienced financial crises are characterized by a mix of weakness such as: balance sheet fragilities, inadequate regulation and supervision, negative fiscal balance, current account deficit and a perceived failure to mobilize an effective policy response. These issues and their interactions influenced both the beginning of the crises. In some cases, balance sheet fragility in the financial sectors has been the cause.

The Theory of Systemic Financial Crises in Africa

A systemic risk is the threat of disruption to the flow of financial services that is caused by an impairment of all or parts of the financial system. Form the view of the international monetary Fund (IMF) an assessment of "systemic importance" requires the identification channels of systemic risk in the financial system. These are components that are critical to the system as a whole and are not easily substitutable (banks, clearing, payment and settlements systems): direct inter-linkages between components, common or correlated exposures and indirect linkages among components.

In the context of financial systems, there are strong linkages between currency, banking and debt crises, especially for emerging and developing economies hit by all the three at the same time.

Reinhart and Rogoff (2010) suggested that subsequent causality, private sector default precede banking sector crisis that coincide with or precede public debt defaults. At the same time, the opposite may also occur with public debt default leading to banking crises either when banks are the main owners of government debt or the government accumulates large payment area ending up weakening the private sector. A banking (and/or currency) crisis may trigger a debt crisis, in which, case the valued effect of debt crisis on contemporaneous output growth could be seen as the lagged influences of banking (or currency) crisis episodes. It is particularly difficult to separate the effect of debt crises and real output. Banking and debt crises and also lead to currency crises. For instance, third generation crisis theory (Krugma 1999) Stated the role of maturity mismatches and currency disequilibrium in private sector.

Causes of Banking Crisis in African Countries

Evidence suggests the prevalence of crises in countries with pronounced government ownership of banks. For instance, the database indicates that government ownership explained directly more than 30% of the banking crises, particularly in CFA Franc zone. During the 1980, 30 banks encountered structured weakness (servant 1991), among them, 27 collapsed, state owned banks represented on average 56% weighted as followed: 50% in Benin, 100% in Burkina-Faso, 75% in Cote d'voire, 67% in Niger, 43% in Senegal, and 25% in Togo (Maidison).

What comes out of the analysis of African financial crisis above is that there are strong linkages between currently, banking and debt crisis. However, underlying causes prior to banking crises include:

i. Weak macroeconomic background: negative fiscal balances, current account deficit, devaluation, high inflation and high interest rates and

ii. Structural weakness: inadequate regulation and supervision, poor governance, high non performing loans ratio, high government ownership of banks, loss of value due to competition from new entries, contagion between banks, (liabilities highly liquid but assets have longer maturity), insolvency (large shock to balance sheet relative to capital: large exposure or little capital)

Debt and Financial Crisis in Nigeria

Nigerian economy is on the stranglehold of debt (Oxfam 2003) At the national, sub-national, corporate and individual levels, debts owed to banks have held the economy to be a stranglehold, impending **r**eal economic growth, though, policy markets are not admitting same. Since the financial crisis of 2008, corporate indebtedness has almost wiped out the assets of companies in the country. Many of the companies operating are more paper companies living on borrowing. The concern of economists today is the cost of servicing this huge debt. Nigeria has one of the highest interest rates in the developing world and if there are high levels of debt, the debt servicing will become very expensive. The Federal Government is attributing the rise in the nation's debt profile to wage increase and the government's intervention to curtail the impact of the global economic and financial crisis of 2008. This implies that the debt is for consumption and not for productive activities. This makes the matter worse for the economy. Besides the oil price which Nigeria depends upon has encouraged development of U.S., Shale oil, some of which now compete with OPEC'S crude oil. OPEC members had dismissed it as of little concern a year ago. But Nigeria's minister of petroleum Resources, Diezani Alison-Madueke, has said it will have a major impact on Nigeria's finances. Nigeria along with Algeria, has already felt the heat from the US. Oil boom, losing ground in its most lucrative export market and diverting sales to Asia. Violence, unrest and investment hurdles are making Nigeria the weakest supply link, helping prop up oil prices to the benefit of the group's strongmen led by Saudi Arabia.

Oil supply in Nigeria has been underperforming for some time whereas growth is expected in the medium term. This development has pushed many Nigerians into ravaging poverty that has affected the nation. Recent official figures show that 112 million Nigeria live below poverty line on less than S1 or N160 a day. Nigerians have come to the hard reality that the various government policies since 1980, have contributed to the rising level of poverty in the country despite claims that the economy has been growing. The poverty data released by the National Bureau of statistics revealed that 100 million people are in absolute poverty, while 12.6 million are moderately poor.

With rising national and corporate debt that has cost, decline in crude oil production and high costs of servicing domestic debt, the nation's economy is hanging on a debt cliff. It can fall off the cliff if necessary steps are taken.

African development Bank was established by the Articles of Agreement signed in Khartoum, Sudan, by the Finance Ministers of 30 independent African countries on August 4, 1963 (Ademola 1999). It commenced business at its headquarters in Abidjan, Ivory Coast (new Cote D'voire) in July, 1996. The authorized shares capital of the bank was initially fixed at N250 milion units of account (U.A), which was equal to 5 million US dollars membership of the bank is opened to all independent African states. Now the member nations include the 51 independent African states and 25 non-African member nations admitted following an amendment to the African Development Board (ADB) charter in 1982. The non-African members include U.S.A, Canada, Britain, France and Japan. The ADB allocates two-thirds of the voting power to African nations to reflect the shareholding, while policy decision requires a majority of 51 percent of the votes.

Objectives of African Development Bank

As outlined by Ademola (1999) the following are the objectives of ADB.

i. To finance investment projects and programmes of its members, using its resources

ii. To mobilize resources from outside Africa especially from developed countries for the financing of such investment projects and programmes.

iii. To undertake or participate in the selection, study and preparation of projects, enterprises, and activities contributing to development.

iv. To provide technical assistance required in the selection, study, preparation and execution of development projects or programmes.

v. To promote investment of public and private capital in projects or programmes designed to boost economic development or social progress of its members.

In pursuit of its policies to eradicate poverty and promotion of equitable growth in the continent, the bank has granted a number of loans to its African members especially for projects and programmes which foster regional cooperation and integrated development within the member countries.The bank is currently based in Tunis, Tunisia after relocating from its headquarters in Abidjan, cote d' voire because of instability there. It employs approximately 1,020 employees in 2007, and has 78 members, 53 countries in African and 25 American, European and Asian countries. One of the emerging views, repeatedly cited by African Development Bank, ADB'S Board of Directors and management is that the ADB should be more selective and country focused in its operations. Though this policy still need to be clearly defined as it appears to be driving certain lending priorities.

The infrastructure sector, including power supply, water and sanitation, transport and communications, has traditionally received the largest share of ADB lending. This focus was re-affirmed in the ADB'S 2003-2007 strategic plan, which identified infrastructure projects for approximately 982 million US dollars which totalled 40 percent of ADB approvals that year Given the increased attention to infrastructure development in Africa from donors and borrowers, it is likely that ADB'S infrastructure lending will increase significantly in the coming years. Servant (1991) stated that another key area of concentration of ADB's support is the fight against HIV/AIDS. The ADB has five policies towards securing Africa's future through health findings.

- ✓ Institutional capacity building through assistance of policy/strategy formulation and implementation
- ✓ Human capital development to create an environment for the operation of national AIDS strategies through training and technical assistance support.
- ✓ HIV/AIDS multi-sectional responses with emphasis on prevention and control interventions which includes Information, Education and Communication (IEC), Sexually Transmitted Infections (STI) control, voluntary counseling and testing (VCT) Infrastructure support for the establishment of laboratory and blood transfusion facilities, and provision of equipment and supplies, including antiretroviral drugs
- ✓ Advocacy through participation in international and regional forums to raise political commitment and leadership towards a collaborative effort in the fight against the pandemic among member countries and development partners.

ADB Financial Terms

Loan Type	Sovereign Guaranteed	Non sovereign Guaranteed
Interest Rate	6 months	6 months
Liquidity Premium	250bp	Project specific + Risk Premium
Final Maturity	Up to 5 years	Up to 5 years
Grace Period	Up to 3 years	Up to 3 years
Front end fee	0.5 5% flat	1% flat
Disbursement	Single or multiple	Drawdown
Repayment	Semi-annual after	Grace period
Payment	Encouraged – No Prepayment	Penalty charged

Source: African Development Bank Bulletin, 2012

The ongoing financial crisis, coming on top of the recent oil and food price relatively, poses a challengesfor regional member countries (RMCs) of the Bank. Already, its impact is being felt on African equities, currencies, exports and difficulties in accessing capital and trade finance, low revenue, fiscal retrenchment and capital projects which risk being suspended. The impact will increase as the full extent of the global showdown becomes evident. The gains of the past decade are at risk.

The financial and business implications for African countries resulting from the direct and indirect effects of the financial crisis are yet to be entirely obvious. The current situation is characterized by reduced private capital flows, lower foreign direct investment as investors and lenders face liquidity shortages and avoid markets that are perceived to be risky, and widening credit spreads in the international capital market making it difficult to issue bends, and remittances will decline.It should be noted that some regional member countries that fix capital formation and infrastructure development in particular is being delayed or neglected as a result of liquidity crunch.

Rationale for an Emergency Liquidity Facility.

Perry 1994 observed that the sharp reduction in international financial flows, resulting from the global loss of confidence has led to the emergence of urgent liquidity needs in many less developed countries in Africa. Presently, international debt capital markets are almost closed although financing is available with steep premiums over laborers.

Many governments are facing disruptions in the development prospects of their economics and yet must continue to sustain growth rate, domestic financial institutions have seen their foreign credit lines dry up, thereby significantly affecting their ability to participate in project financing with government and private sector. Existing projects are projects currently under preparation, particularly large scale infrastructure projects, are exposed to potential financial difficulties with the withdrawal of some commercial partners. Yet, infrastructure remain a key development priority of LDCS, not only for the previous of basic services and equity markets; ideally, this instrument will bridge funding gaps until normal funding conditions are resolved.

New Initiatives: Unlike other MDBs which have established similar emergency crisis lending instruments to meet urgent liquidity requirement of their member countries during previous crisis, this is the first time that the Bank is considering an emergency liquidity facility to address unprecedented challenges. This facility will not only complement the Banks insight from the experience of others MDBS, whose facilities have either been recently reviewed or are currently undergoing a review to better deal with the current crisis. Perry (1990) also pointed out some other emergency liquidity Facilities instruments which include:

i. International Monetary Fund (IMF) Short-term Liquidity facility
ii. The international Bank for Reconstruction and Development (IBRD) special Development Policy Loan
iii. The Asian Development Bank (ASDB) Special Programme Loan.
iv. The Inter-American Development Banks (IADB) programme for Growth Sustainability.
v. International Finance Corporation (IFC) Facilities Promotion of a Competitive environment but also as an engine of economic growth.

The Following are the reasons why African Development Banks needs Emergency Liquidity Facility

a. Challenging Environment: The magnitude and debt of the global finance justifies the need for an emergency liquidity facility at the Bank. Africa will progressively be adversely affected by falling demand for commodities, reduced foreign investment, remittances, tourism and taxes. ADB has estimated that African will grow at an estimated rate of 3.2% in 2014 from an average of 6% in recent years, with sub-Sahara Africa (SSA) growing at 2.6%. The ELF will enhance ADB's credibility as a partner in a position to provide support to countries, institutions and projects in Africa in the face of a severe liquidity crunch. The Bank will learn lessons from the establishment of these facilities and will prepare to deal with future market disruptions.

b. **Need for New Instrument:-** the ADB has numerous financial instrument which enable it to assist eligible borrowers to obtain finance under normal funding conditions However, it needs to have in its repertoire innovative instrument which would allow it to meet LDCS's request for support under extraordinary crisis situation. This new facility result of the withdrawal of international investors, cancellations of credit lines, closure of debt.

Policy Implementation of Emergency Liquidity Facility In African Development Bank

a. ***Implementation Modalities:-*** The proposes ELF will be implemented by operational complexes in collaboration with the finance complex under the oversight of operations committee (OPS COM).

b. ***Appraisal Process***:- in order to abide with ELF's eligibility terms, a pre-crisis evaluation of the borrowers (for both sovereign guaranteed and non sovereign guaranteed) operations should be undertaken. The evaluation should include sovereign borrowers and analysis of the macroeconomic and financial framework. For non sovereign transactions, the structure and financial situation of the borrower, prior to the start of the global financial crisis and identification of key areas of the borrower will be analyzed. In principle, there should not be any need for an appraisal mission for existing clients.

c. ***Approval Procedures***: approval would be by the board of directors of the bank. Given that the ELF would be a quick-disbursing facility, it is proposed that the approval process be fast- tracked by reducing the period for distribution of document draw down from the approved envelop in trenches.

d. ***Coordination Mechanisms***: the emergency assistance to countries and central banks should to the extent be possible provided within a framework of an IMF led international financing package involving other donors and financial institutions including the World Bank.

e. ***Monitoring and Evaluation:-*** the Proposed rapid response nature of the ELF will require appropriate streamlines process for proper monitoring and evaluation.

f. ***Legal Procedure***:- Due diligence with regard to the ELF would focus, among others on eligibility of the borrower as well as the proposed used of the resources. The transaction would be documented as sovereign guaranted or non-sovereign guaranteed transaction depending on the type of borrower. It should be noted that the proposed tenure of the loans, which will not exceed five (5) years would be a departure from the Bank's policy of providing long term debt, but is justified by the exceptional nature of the facility and the use of the resources.

g. ***Staffing and Systems Implications:-*** the proposed facility is not expected to have major staffing or systems implications.

Measures Militating Against the Objectives of Emergency Liquidity Facilities

1. ***Underutilization of the facility*:-** Given the depth of the financial crisis and increasing volatility of the relative process of key commodities and African currencies, it is improbable that the ELF will be underutilized. However, if countries either find the financial terms too difficult to bear or the crisis subsides earlier than currently terminate the facility at any time during the initial 18-month availability period.
2. ***Insufficient Size*:** the ELF is tentatively set at 1.5 billion USD, with a country cap of USD 150 million. Given the magnitude of the crisis and the broad range of eligible beneficiaries, the facility could prove insufficient.

This showed prompt a review by the Board consideration with a view to increase the size of the facility, as well as country and project limits.

3. ***Crowding out Effect on Bank Normal Activities***:- the ELF could have Potential adverse effect on mainstream Bank operations. To ameliorate this, the terms and conditions are determined to encourage a rapid return to normal funding consideration.

RECOMMEDATIONS

Less developed countries in Africa and Africa Development bank have long been conscious of it that the growing debt levels of poor countries impede development and perpetuate poverty.

National debt in Nigeria is deeply rooted, as such, an effective poverty reduction strategies and development plan must come in place:

- Governments of these countries should ensure commitment in the areas of fund allocation for provision of social services that are beneficial to the prior, fostering efficient macro –economic and sectoral policies and the provision of an enabling environment to facilitate private sector economic framework.
- They should undertake a comprehensive study on the causes of poor implementation of development policies and strategies to develop a plan of action to address this critical and persistent problem.
- There is also need to develop long-term strategic plans that address unemployment, taking into consideration the educational curriculum and the needs of the labour market as well as strengthening the human and financial capacity of poverty alleviation institutions in less developed countries.
- Government of less developed countries can also reduce their national debt by deregulating their economics. Deregulation of the economy is the removal of government controls from an industry or sector to allow a free an efficient market place.

CONCLUSION

There is no economic problem that receives greater global attention than poverty. In less developed countries in Africa, poverty with its associated multiple deprivation appeared to be the greatest degrader of the economy amongst other contemporary socio-economic problems. Also persistent national debt in these countries engenders economic stagnation. Hence, deregulation of these economies is urgently needed in order to experience great debt relief.

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