

# Why some countries are in debt

Countries



## **What is debt?**

On an international scale, debt is the owing of money from one country to another or an international organisation as a result of previous borrowing because of need.

Why are some countries in debt?

Countries can be in debt for different reasons:

- Trade deficit

When a country's imports are worth more than a country's exports, the country loses money and therefore it is forced to borrow money from other countries or international organisations to try and cover the losses.

- Natural disasters and tied aid

After a natural disaster, a country may become dependent on the aid of another country for a short period of time. However sometimes the aid given is tied aid where the country receiving aid may have to pay back the money given (possibly with interest). They are therefore in debt to the donor country/organisation.

- Money mismanagement

If a country mismanages their use of money (most likely through the government) and spends money unnecessarily while taking out loans to cover the cost, the country can end up in debt.

## **The Effect of Debt on Development**

When a country is in debt, a majority of the money it generates is used to pay back money to the donor country. This means that there is little money being invested into the social infrastructure of the country, so healthcare and education levels remain the same or get worse overall slowing down or sometimes even reverse developing a country as literacy rates may fall and not enough money could be invested in improving healthcare.

## **Ways of solving debt problems**

### **Cancelling debt - What are the advantages and disadvantages?**

#### **Advantages**

The advantages of cancelling debt are that it can allow a poor country to start investing the money it gains into its development/ social infrastructure rather than paying back debt to developed countries. This can overall help to fight poverty and reduce the development gap. In 2005, Zambia had \$4 million of debt cancelled and in 2006 it had enough money to pay for free healthcare for millions of people living in rural areas, improving the quality of life.

In Tanzania, money saved from debt cancellations allowed the government to abolish primary school fees in 2001. As a result, the number of students that go to primary school doubled. These examples show that by cancelling debt, it allows money to be invested in education which can lead to more people getting jobs, overall contributing to a country's economy, improving the GDP and by investing in healthcare, the life expectancy and infant mortality rate can also decrease.

**Summary**

- a country can invest in its development
- It reduces poverty and can reduce the development gap
- examples include Zambia and Tanzania

**Disadvantages**

Although cancelling debt can help a country to develop, there are also some disadvantages. Firstly, the donor country loses a significant amount of money which can slightly damage its economy. Developing countries which have had their debt cancelled could start taking out more loans, in the hope of having debt gained from that cancelled as well (This however is unlikely as eventually developed countries will eventually see when a country is not worth giving money to and in a time of crisis, nothing will be given) When a loan is taken, the money should be returned and if it is not, it could give the country which did not pay back, a bad reputation.

**Summary**

- The donor country loses money
- Countries could take out more loans
- A loan should be paid back if taken in the first place

**Debt for Nature Swaps**

Deforestation largely takes place for economical needs of a country to try and pay off debt. A debt for nature swap is an agreement between a developing nation in debt and one or more of its creditors. In a debt for nature swap, the country or organisation owed money, writes off an amount of debt in return

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for a certain amount of environmental protection. They were first established in the 1980s in the attempt of solving two problems with one agreement: 1) to minimize the debt of developing nations and 2) to minimize the environmental destruction that frequently takes place in developing countries.

A company called WWF (world wide fund for nature) which cooperates with countries such as UK and USA has helped to structure and design many debt for nature swaps. In 2008 they helped to structure and facilitate one of the largest debt for nature swaps in Madagascar's history in which 20 million dollars was committed to preserve the country's rich biodiversity. Also in 2008, the USA reduced Peru's debt by \$25 million in exchange for conserving its rainforests.

Debt for nature swaps are extremely beneficial because they not only cancel the debt of a country allowing them to invest in development, but it helps to protect the environment and conserve some of the world's rainforests. This makes it better than just cancelling debt.