not been solved. In 1986, \$2.6 billion in interest and \$3.7 billion repayments are due, although the total export earnings for 1985 amounted to only \$6.2 billion. In the past, most of the repayments (and even a large proportion of the interest payments) have been dealt with by reschedulings and fresh credits, because the troubled régime is too politically vulnerable to be able to risk the workers' unrest that would be the unavoidable result of a severe deflationary squeeze. Even so, since 1983 there have been modest balance-of-trade surpluses—an indication that there has been some attempt to force exports and curb imports.

It is difficult to avoid the conclusion that Eastern Europe and Latin America were "exploited" far more effectively by Western finance capital in the 1980s than Czarist Russia in the 1890s. The existence of the concept of "the Sovereign Borrower" not only meant the massive and potentially destabilising build-up of international debt, but also that the costs of adjustment were borne for the most part by the borrowing countries. The existence of the State as Borrower ruled out the easiest, and the most equitable, way of sharing the burden of large investment programmes that had been catastrophically misconceived.

By trying to reduce risk, the international financial system had produced an outcome whereby the way in which risk was distributed became a major political theme. Every possible solution seems to impose a one-sided sacrifice, and becomes bitterly controversial. *Should the borrowers continue to pay?* In that case the austerity programmes they would need to impose might easily become politically unacceptable. *Should the borrowers refuse to pay?* In that case the international banking system would be faced with the likelihood of a collapse that would certainly endanger the industrial countries. In the 19th-century railway defaults, on the other hand, the damage was much more limited. A small handful of railway directors and a larger number of European investors paid a price that seemed, in the short term, very high. In a longer term the economic cost was small, and in addition no great political issues seemed to be raised by the distribution of risk. It would have been pointless to see those crises in terms of "North-South" dialogues, Third-World arguments or conflicts.

It is very hard to see a way out of the growing political crisis that the imposition of austerity will engender. It may be that, in the longer run, there is no possibility of some of the Latin American public borrowers repaying their loans, and that new King Philip IIs will have no alternative except to declare some form of public bankruptcy that will endanger the future credit of the borrower.

Is any optimism at all possible here? The immediate catastrophe on world financial markets would be horrifying; and no one can be in a position to predict any outcome with any degree of security. So the following crumb of comfort might not, in the end, amount to very much at all. In the aftermath of such a disastrous collapse there would be scope for raising new money for Latin America and Eastern Europe only by invididual borrowers (i.e. *not* states), who would offer marketable goods or services to provide for the amortisation and interest on the borrowed sums. The privatisation of assets, or a redistribution of risk away from the public sector, will become attractive as a way out of the debt crisis and as a way to encourage new lending.

The debt problems of today arise directly out of a fallacious assumption that risk is avoidable, and can and should be "socialised", or taken over by the state. It is an international version of the domestic story of Keynesian-style "crisis avoidance". In both cases, the system of crisis-response actually generates political problems. This is because states are tempted to take on themselves risks and burdens which they cannot, in the long run, sustain. This may well have an effect on the way in which citizens think about states: the moral authority of a state is weakened when it attempts to perform something that is, quite simply, impossible. States cannot take the risks and the uncertainties out of development. They should not try to escape small crises, and small bankruptcies, that are immeasurably less painful than large ones, and have the highly therapeutic function of distributing sacrifice more or less equitably.

Not only does the ambition of removing risk and avoiding crisis produce large-scale economic snarl-ups, often rather misleadingly described as "profound structural crises"; it also transfers the crisis into the sphere of politics. This is because it makes people conscious of choices (which can rarely be made on the basis of any rational criteria) about how unpleasant sacrifices should be allocated. One of the most attractive features of the small therapeutic crisis is that it does not raise such difficult political issues as the large traumatic crisis. Shouldn't we really be a little fonder of small crises?

Neonatal

Thick snow conceals recumbent cars under
showroom wraps. The oak-trees in the grounds show off
their sale-price minks. Wires sag towards the city
awaiting messages of joy or grief.
Sparrows pioneer patterns where paths have gone.
The whole thing's counterfeit and soundless.
In here a high-pitched blip signals something.

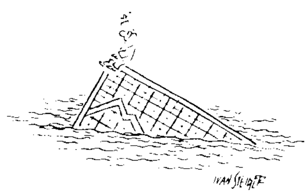
I emerge with a thud, rooting for the pap
and hard-faced with exhaustion. My head
is fibre-glass, shaped and left to set. Bruised, blue
and filmy, I spit into voice. My yell
protests at the light, rising and falling
like ink on graph paper. Indigo fingers
claw at the breast, their nails already long.

Adrian Blackledge

Walter Eltis

The Borrowing Fallacy

On the World Debt Crisis



MUCH OF Latin America's debt has become unfinanceable, and in addition the government debt of several Western developed countries has increased massively in the 1970s and the 1980s. Several of these are rapidly approaching a condition where drastic corrective action will be needed if they are to avoid financial destabilisation. This recent growth of government debt in Latin America, North America, and Europe can be explained in two broad ways.

First, government expenditure is often popular, and it helps governments to realise many of their promised social and political objectives. Taxation, in contrast, always weakens popularity and reduces political support. Politically weak governments are therefore tempted to buy short-term popularity by raising public expenditure through borrowing—it allows them to reward their supporters and fulfil their objectives more rapidly. This borrowing will involve significant costs in due course; but a different group of politicians will often have to face the unpopularity involved in paying the interest, often to foreign countries, on debt which financed originally popular expenditures. A disregard for the eventual cost of policies which are popular in the short term is a feature of the politics of many countries.[1]

But this has always been a feature of the politics of democracy, for electorates are widely believed to have very short memories so that there are overwhelming pressures on politicians to spend more and to tax less as elections approach. And authoritarian governments are also often under overwhelming pressure to boost their popularity, or at any rate to reward the supporters of the régime.

So why is it that government debt has grown so overwhelmingly in the 1970s and the 1980s, when this pattern of causation has always been present?

An important explanation of why 19th- and early 20th-century governments often resisted the political pressure to borrow is that electorates then believed that this was incorrect economics, with the result that deficit financing was not the political asset it subsequently became. Britain ran enormous Budget deficits in the great wars of 1793-1815 and 1914-18, for the need to borrow heavily to finance international conflict has always been accepted. But the economics of Adam Smith took over immediately peace was declared, and public debt fell year after year in relation to the national income. Disraeli was castigated by Gladstone for the expedients he resorted to to balance the British Budget of 1852, and his Budget proposals were defeated in the House of Commons. Ramsay MacDonald's Labour government ran a modest deficit of £120 million in the 1931 world slump (just over 3% of the national income), but the May Committee advised that the Budget be balanced via reductions in unemployment benefits and only half the Labour Cabinet was prepared to support this. King George V urged Ramsay MacDonald to form a National Government in order to balance the Budget, and those members of the Parliamentary Labour Party who believed in deficit financing won only 60 seats at the subsequent general election. So far from being an election asset, *peacetime* deficit financing was actually a recipe for electoral catastrophe less than 60 years ago.

Part of the explanation of the growing debt of many Western countries since the Second World War is that the Keynesian Revolution reversed orthodox economists' analyses of the desirability of deficit financing. Electorates—which had previously regarded peacetime government borrowing as a politically disreputable expedient which only weak governments resorted to—were gradually educated to believe that deficit financing was *correct* economics whenever domestic demand was deficient.

KEYNES'S SOLUTION to the unemployment problem of the inter-War years involved the generation of sufficient effective demand to sustain full employment. He argued that if the private sector failed to spend enough, it then became incumbent on the state to spend what the private sector would not. He accepted that most of this additional government expenditure would need to be financed by borrowing.

Keynes did not envisage that government borrowing would be necessary all the time to sustain full employment; for he believed Budgets should be balanced over a period of years. This optimism is reflected in the celebrated *White Paper on Employment Policy* after the Second World War which the British government published in 1944:

> ". . . to the extent that the policies proposed in this paper affect the balancing of the Budget in a particular year, they

[1] This line of argument is developed in James M. Buchanan and Richard E. Wagner, *Democracy in Deficit* (Academic Press, New York, 1977).