

banks received strong approval and even encouragement from the governments of the industrialized countries. The U.S. Administration in particular regarded the commercial banks as the best ready-made mechanism for transferring petrodollars quickly to developing countries. Several Canadian banking authorities told the Committee that they were personally aware that U.S. State Department and Treasury officials had urged the international banking community to act and to "accept the responsibility of being the first channel for moving the new petrodollars." (Hockin, 13:7) The U.S. Secretary of the Treasury told a 1979 IMF meeting that "we all recognize that the private markets will, in the future as in the past, have to play by far the major role in channelling financing from surplus to deficit nations." Successive British Chancellors of the Exchequer, including Mr. Denis Healey and Sir Geoffrey Howe, spoke warmly of the useful role the commercial banks were performing in financing Third World deficits. For example, in September 1977, Mr. Healey told the IMF annual meeting that "the commercial banking system has rightly played the main role in financing these developing country deficits until now and has shown immense resourcefulness in doing so".

As a result of the second oil shock of 1979 the OECD countries experienced greatly increased inflationary pressures and renewed balance-of-payments problems. Many of them decided to meet these challenges by introducing restrictive monetary policies. This response in turn caused a severe recession — even a depression, some would argue — leading to low, often negative growth rates in the industrialized world coupled with a dramatic rise in interest rates in 1981 and 1982. The extensive borrowings of developing countries left many of them highly vulnerable as interest rates climbed sharply.

For many Third World countries that had borrowed heavily, these developments provoked economic difficulties from which they have not yet recovered. The demand on world markets for commodities other than oil had slumped. Commodity prices — which for many of the countries represented the major source of foreign exchange — fell, declining 27 per cent in 1981 and 1982. In many cases overvalued currencies caused imports to soar as foreign goods looked deceptively cheap. With exports shrinking and imports expanding sharply, many debtor countries experienced a severe worsening in their balance of payments and it became increasingly difficult to service their debts. Interest charges on past debts were escalating rapidly with the rise of U.S. interest rates to unprecedented heights. Since 80 per cent of the bank debt was denominated in U.S. dollars and much of it on a floating rate basis, debt servicing costs rose in tandem.

In addition to these adverse external factors, there were internal policies and actions in the debtor countries which fuelled the crisis. Bankers and officials recounted to the Committee that a number of debtor governments mismanaged their economies and followed misguided domestic policies, that an overvalued currency in Venezuela over a 20-year period had caused massive capital flight, that inflationary policies in Mexico and Brazil undermined the international competitiveness of their economies, and that both Argentina and Mexico had worsened their problems by supporting inefficient state enterprises. Underestimating the extent and duration of the recession that was beginning, many countries avoided the necessary adjustments in favour of policies supporting continued consumer consumption. Inefficient state-owned or subsidized industries consumed