

# Cancelling the debts of poor countries : for what results ?

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Restructuring debt of developing countries began in the 1950s. Argentina was the first country, in 1956, to negotiate the repayment of its debt with bilateral creditor within the framework of the Paris Club (set up for this purpose). Other debt cancellations were then granted unilaterally by the industrialised countries, but it was not until 1988 that such procedures became common practice for low-income countries. However, the sums involved remained limited.

The mechanisms for reducing debt took a new turn in 1996 with the launch of the HIPC initiative (Heavily Indebted Poor Countries) by the International Monetary Fund (IMF), the World Bank and the industrialised countries. Being impulse in 1999, the initiative seeks to extricate the poorest countries from the spiral of poverty through the reduction of their external debt. However, the HIPC initiative differs from the debt reduction mechanisms hitherto granted in that multilateral institutions are now involved financially. In exchange, the recipient countries are required to implement a programme drawn up in conjunction with the IMF. In the light of the recurrent difficulties confronting the beneficiary countries, the G8 member-countries decided in 2005 to go a step further by announcing their wish to fully cancel the debt of the Heavily Indebted Poor Countries contracted with three leading multilateral institutions, namely the IMF, the World Bank and the African Development Bank.

Ten years after the launch of the HIPC initiative, this article sets out to put the debt of the developing countries into perspective, to describe mechanisms relating to the initiative, and to provide a preliminary assessment of its financial impact. At the outset, this initiative undoubtedly constituted a major step forward in the field of debt treatment, but its impact today remains modest. For most

countries, the debt reductions granted have done no more than regularise a situation that already existed without releasing much in the way of supplementary resources. Meanwhile, macroeconomic imbalances problems have not been solved. Therefore, the recent declarations by the G8 countries in favour of both increased aid and debt reduction have not been enough to dispel the uncertainty concerning the long-term debt dynamics of the HIPC.

## Developing countries debt in perspective

### Several forms of development financing

As is also the case with many industrialised countries, the developing countries import capital in order to finance their growth. These multilateral, public and private financing flows break down into four categories: debt flows, direct foreign investments, portfolio investments and grants. Among these instruments, the debt gives rise to future commitments as it implies the payment of interest and reimbursements according to a schedule. Thus, the borrower has to implement an efficient development strategy so as to generate sufficient revenue.

External debt implies a dual constraint: internal as the debtor is forced to make periodic payments and an external constraint as payments are made in foreign currency. While recourse to the international financial markets appears necessary as a means of encouraging growth, the accumulated debt burden may nevertheless become an obstacle to economic development, resulting in extreme cases in default payment situation.

## Country's creditworthiness: key element in its borrowing capacity

"The creditworthiness of a country is the assessment by potential lenders of the capacity of the country to repay its external debt"<sup>(1)</sup>. It is essential for a country to be creditworthy so as to raise more funds to finance its growth.

At the same time, creditworthiness can alter and will essentially depend on political, economic and financial factors. A country's debt repayment profile or its ability to receive external capital are both factors which can aggravate or improve this signature. Thus while creditworthiness is built up over a period of time, it can swiftly deteriorate in the event of failure to carry out contractual obligations. The consequences can be serious and may involve repudiation by the financial markets with loss of access to future loans. But this risk can be avoided and will in particular depend on the state's capacity to negotiate a debt restructuring plan with its creditors. If the negotiations following default payment are engaged on a favourable and voluntary footing, the country's borrowing capacity on the financial market may be restored more easily.

## The debts of developing and emerging countries

According to the World Bank, the total external debt of developing and emerging countries at the end of 2004 amounted about USD 2600 billion, of which USD 2136 billion was medium and long-term debt. Sovereign debt accounted for almost three-quarters of the latter one, with 60% of this sovereign debt contracted with official creditors (multilateral and bilateral).

However, this general picture masks profound disparities. Most of the countries of Latin America, Asia, Eastern Europe and North Africa essentially receive private financing, whereas most of sub-Saharan countries and several poor countries in Asia have recourse to institutional financing. These latter ones have little access to bank loans due to a very limited reimbursement capacity. Similarly, the external debt of the private sector is virtually inexistent. According to the countries, the creditor is different and so the constraint linked to the reimbursement of the loan. The international

## Medium- and long-term debt of developing and emerging countries

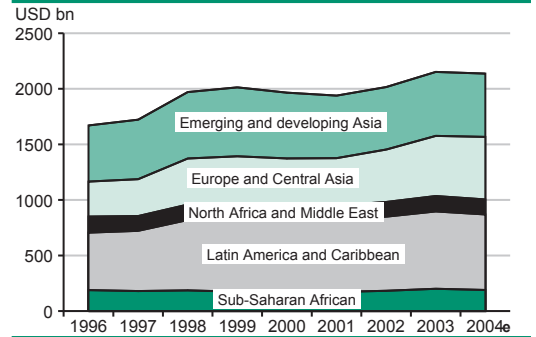


Chart 1 Sources: World Bank, Global Development Finance

## Breakdown of public debt in developing and emerging countries

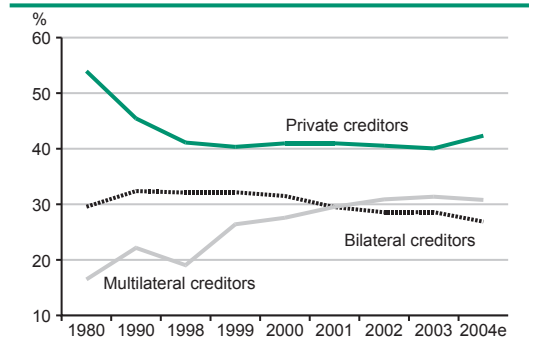


Chart 2 Sources: World Bank, Global Development Finance

financial markets are deeper, but the cost of financing is relatively high and access is more uncertain than for a concessional debt. Nevertheless, the recourse to institutional financing is usually linked to conditionalities, and the constraint is essentially of a political nature.

## The mechanisms of HIPC initiative: a long process ...

### Background

#### First HIPC initiative – 1996

HIPC initiative was launched in 1996 by the IMF and the World Bank in order to find a solution to the debt

## The conditions of eligibility for the HIPC initiative

To be eligible, the applicant country must:

**Show the unsustainability of the debt.** Despite the introduction of the IMF and World Bank programmes and a rescheduling at the most favourable conditions of the Paris Club (\*), the residual debt remains unsustainable, that is to say that its net present value (NPV) exceeds 150% of exports, and/or the NPV/Tax Receipts ratio is in excess of 250%.

**Have formulated a Poverty Reduction Strategic Plan (PRSP)** for which the countries have full responsibility. The plan is financed by the Poverty Reduction and Growth Facility (PRGF) and thus reflects national priorities with regard to poverty reduction and growth. If necessary, the IMF calls on the expertise of the World Bank in order to establish the poverty diagnoses.

**Be eligible only for a concessional assistance** from the IMF (via the PRGF) and the World Bank (International Development Association (IDA)).

**Demonstrate the ability to carry out the reforms and respect the conditionalities concluded with the IMF.** The country must draw up a list of the reforms carried out within the framework of the programmes supported by the IFI and show that a priority is given to poverty reduction.

(\* According to the Terms of Naples: reduction of the commercial debt by two thirds and rescheduling of the remainder over 23 years including a grace period of 6 years.

burden of the poorest countries. A plan was drawn up with a view to providing exceptional assistance to countries in reducing the weight of their external debt to a "sustainable" level, once these countries had applied adjustment programmes, introduced reforms and followed up all the other "classic" debt reduction programmes advocated by the International Financial Institutions (IFI).

Pushed by NGOs and international pressure, the initiative took into account the overall public debt (both bilateral and multilateral) of the countries concerned. It was an important step as multilateral debts was not be considered previously.

### **Second HIPC initiative (reinforced initiative: the debt cancellations are linked to the fight against poverty) – 1999**

Because of the poor results of the first HIPC initiative and growing public criticism, the G8 countries and the IFI launched a reinforced initiative. The selection criterias were relaxed in order to include a larger number of beneficiary countries and increase the volume of debts concerned. Moreover, the determination to speed up the implementation of the initiative and to relate it more closely to efforts to reduce poverty was emphasised. The reform phase became "floating", i.e. a good "pupil" could accelerate the reforms and obtain a debt reduction more quickly.

## Process

### **First stage: analysis of debt sustainability and decision point**

The decision point comes after a period of structural adjustment of variable length (the period has become "floating"). At the end of this period, the IMF and the World Bank pronounce about the country's eligibility for the HIPC initiative. The country can reach the decision point if:

- the application of the standard debt reduction mechanisms (operation carried out in particular by the Paris Club) has not been enough to bring the debt back to a sustainable level (cf. eligibility criteria above)
- the country has made sufficient progress towards meeting the reform criteria adopted by the IFI
- the country has no arrears with regard to the IFI

### **Second stage: the interim period**

The country benefits from a preliminary, so-called "interim" assistance, from all the creditors (bilateral and multilateral) taking the form of a debt service reduction (debt stock is not reduced). The Paris Club, going beyond the Naples Conditions, grants a debt service reduction of up to 90%, while the IMF and the World Bank (and the other multilateral creditors in general)

reduce their debts by an average of no more than 30%. The length of this interim period depends i) on the satisfactory execution of the reforms agreed with the IFI at the decision point, ii) on continued macroeconomic stability and iii) on the adoption and execution of the Poverty Reduction Strategic Papers (PRSP).

### ***Final stage: the completion point***

When a country has satisfactorily carried out the IFI programmes, it reaches the completion point. The debt stock is cancelled in the proportion determined at the decision point. On a case by case, a cancellation may be topped up in order to allow countries suffering from an exogenous shock to maintain their debt sustainability ratios within the 150% threshold. The calculation and the timetable of the debt reduction are made at the end of this period.

### **Beneficiary countries**

At the beginning of 2006, among the 42 countries qualified by the IMF and the World Bank as “Heavily Indebted Poor Countries”, 38 remained “potentially eligible” for the HIPC initiative. After assessment, Angola, Kenya, Vietnam and Yemen were unable to benefit from the process as their debt level was considering as being sustainable. Moreover, the Laos authorities still do not wish to have access to the debt reductions granted in the context of the initiative, preferring to benefit from capital inflows. In addition, the list of beneficiary countries may be extended to include four new countries: Haiti, Kyrgyz Republic, Eritrea and Nepal. The IMF and World Bank councils will pronounce on the definitive list of eligible countries at the beginning of 2006 after collecting all the data concerning the debts of these countries.

Most of the 32 countries eligible for the HIPC initiative are in sub-Saharan Africa (note that, with the exception of Gabon and Equatorial Guinea, all the Franc Zone countries are included). Among the “eligible” African countries, 23 countries have reached the decision point, of which 14 have already reached completion point. Of the 9 remaining African countries<sup>(2)</sup>, The Republic of Congo seems today best placed to reach the decision

point, although the process continues to be affected by persisting disagreements on arrears with some commercial creditors. The qualification of the other countries is obstructed by a heavy accumulation of arrears with regard to the IFI (sometimes due to a period of conflict) and/or internal political difficulties which have complicated the design and implementation of macroeconomic programme.

## **State of progress of the HIPC initiative: insufficient ventilation for a sustainable development**

### **The financial impacts are by no means negligible but ...**

In practical terms, the reduction of the debt means that, for a period of varying length (10-40 years), the payments which should have been made in repayment of the external debt will in fact be deleted. The relevant indicator for assessing the impact of the HIPC initiative in a country is the annual debt service.

Despite the delays in introducing the process, the HIPC initiative has already relaxed the financial constraint for 28 countries. Overall, debt service (due but not necessarily paid) represented 7.3% of exports at the end of 2004 against an average of 15.7% in 1998-99<sup>(3)</sup>. In terms of budget revenue, the share of debt service came to 12.5% in 2004, i.e. 11 points lower than the average of 1998-1999. Meanwhile, the budgetary resources allocated to the reduction of poverty rose from an average of 6.4% of GDP in 1998-1999 to 8.1% of GDP in 2004. According to IMF and World Bank estimations, the debt service to exports and to budget revenue ratio should continue to fall and would represent only 6% and 9% respectively in 2007, while expenditure on poverty reduction should continue to increase and settle at 9.3% of GDP.

In addition, econometric studies conducted by the IMF (2003) suggest that the gain in growth attributable to the HIPC initiative for the beneficiary countries could be 1.5 percentage points of GDP two-thirds of which would be due to the relaxation of the financial constraint and one third to the rise in public investment expenditure<sup>(4)</sup>.

**Foreign debt service by countries having reached decision/completion points**

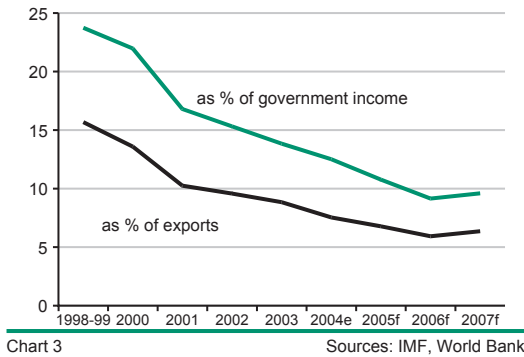


Chart 3 Sources: IMF, World Bank

**Debt service and poverty-reducing expenditure by countries having reached decision/completion points**

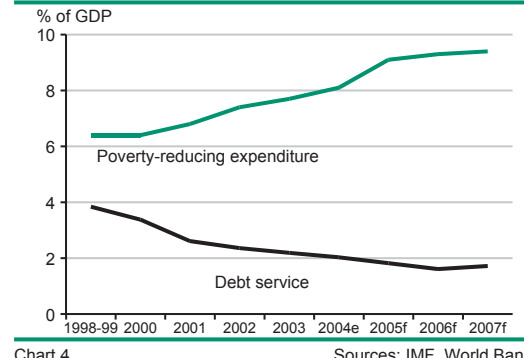


Chart 4 Sources: IMF, World Bank

The total amount of reductions granted to the 28 countries involved in the initiative should reach USD 38.2 billion in net present value (NPV), i.e. a reduction of the external debt stock of about 65%. The total cost of assistance is likely to be divided roughly equally between bilateral creditors, assuming 45% of the reduction, and multilateral creditors (half of which is at the charge of the World Bank). The outstanding amount is supported by private creditors. In addition, the cost of assistance could increase by USD 21.7 billion in net present value, if the 9 remaining countries were to reach the decision point, to which could be added USD 1.3 billion if the 4 new countries mentioned above were to become eligible.

... many limits remain

**A process which is still too slow...**

A study conducted by the Bank of France<sup>(5)</sup> reminds that, while 40 countries were declared “potentially” eligible for the HIPC initiative, only 18 of them have benefited from complete and irreversible reduction of their debt. The fact is that it is so difficult and complex for a country to respect the series of eligibility criteria required by the IFI. Therefore, the interim period has had to be lengthened. When the reinforced initiative was introduced in 1999, it was expected that the Heavily Indebted Poor Countries which had reached the decision point in 2000 would reach their completion point in less than three years. In actual fact, only 6 of the 12 countries concerned have so far managed to reach the completion point.

... and too limited

The ongoing debt cancellation processes only concern about 40 of the poorest countries, owing “no more than” about USD 180 billion (the equivalent of the debt of a single country like Brazil or Mexico) out of a total debt for the developing countries amounting to USD 2500 billion. The debt of emerging countries is not concerned, although this sometimes gives rise to considerable problems. The governments of these countries do not request a cancellation of their debt but rather greater and stabilised access to the international capital markets.

**The regularisation of an existing situation leading to a rise of debt service in the short term**

Before the initiative was introduced, most of the countries concerned paid no more than 50% of the debt service due. Part of the debts contracted by the Heavily Indebted Poor Countries was not in fact reimbursed. Thus, on the whole the reduction does no more than regularise a situation which already exists. In this context, the debt service reductions presented above appear to overestimate the impact of the initiative and partly concern these irrecoverable debts. This explains why the reduction of the effective reimbursement levels

of the Heavily Indebted Poor Countries remains low in comparison with the debt stock reductions announced. According to IMF forecast, debt service payments for the 28 countries mentioned above should increase regularly to reach USD 3 billion in 2007 compared to USD 2.6 billion in 2004. Therefore, the decrease of debt service to exports ratios remains closely linked to IMF assumptions, that is to say an average annual growth of exports by 10% between 2005 and 2007.

**Slowdown in “traditional” Official Development Aid (ODA) for beneficiary countries**

All in all, the amounts of ODA have continued to increase since 1997, the year in which the initiative was introduced. This upswing in aid is all the more remarkable that it also concerns long-term aid and assistance programmes, which do not include debt reductions and emergency aid. However, while debt reductions represented on average only 17% of ODA over the period between 1990 and 1996, this share increased substantially to 34% between 2001 and 2004. Although the traditional aids still constitute the bulk of ODA, the decrease of their share in aid budget since the launch of the initiative illustrates the tendency of bilateral donors to substitute them by debt cancellation measures.

**Difficult financing for donors**

The financing of the initiative has already give difficulties for the multilateral organisations. While the countries have annual budgets for financing their aid programme alongside debt cancellations, this is not the case for the multilateral development banks. As a matter of fact, the financing capacity of these IFI is closely correlated to the loan reimbursements made by the debtor countries. In this context, each dollar cancelled as part of the HIPC initiative means one dollar less for their future loans. The World Bank has on several occasions accumulated heavy deficits (on this initiative), which have been covered by donor countries during periodical meetings (every three years). De facto, most of the debt reduction to be reimbursed to the multilateral banks is financed by bilateral donors, which in most of cases are already engaged in the HIPC initiative. These financial

**Costs for multilateral and commercial creditors (for the 28 countries having reached the decision point)**

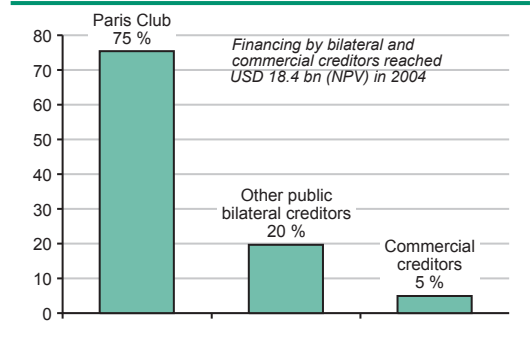


Chart 5 Sources: IMF, World Bank

**Costs for multilateral creditors (for the 28 countries having reached the decision point)**

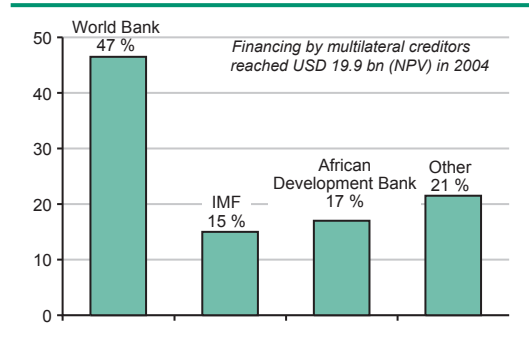


Chart 6 Sources: IMF, World Bank

difficulties do not endanger the financing of the HIPC initiative but they do directly alter the IFI’s ability to act, and have an indirect impact on the aid budgets of the donor countries. Thus, the debts of various countries are too high to be cancelled owing the initiative’s current level of financing. This is the case, for example, for Liberia and Sudan, both hit by civil strife in the last few years. Therefore, the IMF and the World Bank recently decided to put back the cut-off date until the end of 2006 so as to provide more time for current non-eligible HIPCs to become eligible for debt relief under the HIPC Initiative.

**The initiative has not yet mobilised all the creditors**

The purpose of the HIPC initiative was to bring together all the creditors of the debtor countries around a

process of shared debt reduction. It was not its intention to release resources for the reimbursement of certain creditors, once the country in question had offloaded this charge onto another group of creditors. However, this sharing out is still not complete. There is very little participation in debt reduction from creditors who are not members of the Paris Club. It should, however, be pointed out that China has announced a reduction programme on the African countries, but under the principle of free choice which is not compatible with the principles approved at multilateral level. The Gulf countries have often refused to grant reductions despite the fact that they are major creditors of the eligible Heavily Indebted Poor Countries. The same question arises (though in different terms) for those "poor" creditors who are themselves eligible for the initiative – for Honduras on Nicaragua, for example.

**The HIPC initiative: a mechanism for the permanent restructuring of the debt of the poor countries?**

Unless to consider the HIPC initiative as a procedure for permanent debt restructuring, the process (as defined) allows the sustainability of the debt in the short term, but cannot guarantee it in the medium or long term. Thus, terms of trade fluctuation and the choices made by the beneficiary countries, particularly with regard to new debt, (e.g. the implementation of certain capital-intensive projects which cannot be secured by grants) may affect long term debt dynamic.

**Bilateral ODA allocated to HIPC**

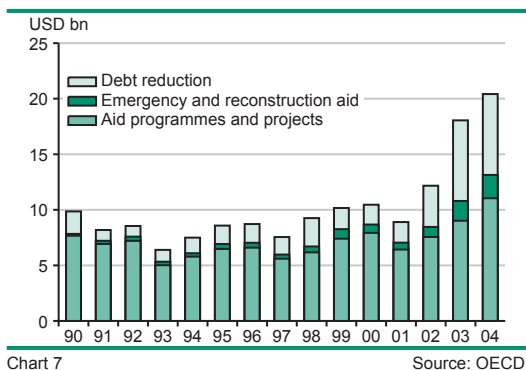


Chart 7

Source: OECD

**Breakdown of ODA (in %)**

	1990-96	1997-00	2001-04
Aid programme and project	79.0	72.4	57.2
Emergency aid and reconstruction	4.1	6.7	9.1
Debt reduction	16.9	20.9	33.7

Table 1

Source: Development Assistance Committee (OECD)

**The HIPC initiative has helped to reduce debt... but will the debt remain sustainable in the medium term?**

External public debt (in % of GDP)	Before completion point	After completion point (year)	End 2004
Mozambique	149	102 (2001)	72
Ghana	98	75 (2004)	75
Uganda	65	59 (2000)	61
Benin	56	44 (2003)	43
Mali	90	75 (2003)	69

Table 2

Source: Fitch

## Beneficiary countries for the MDRI

Immediately	<u>HIPC countries</u> : Benin, Bolivia, Burkina Faso, Ethiopia, Ghana, Guyana, Honduras, Madagascar, Mali, Mozambique, Nicaragua, Niger, Uganda, Rwanda, Senegal, Tanzania and Zambia. <u>Non HIPC countries</u> : Cambodia, Tadjikistan.
Between 6 and 18 months	Cameroon, Democratic Republic of the Congo, Gambia, Guinea, Guinea-Bissau, Malawi, Mauritania, Sao Tome, Sierra Leone and Chad.
Later	Burundi, Central African Republic, Comoros, Congo-Brazzaville, Côte-d'Ivoire, Liberia, Somalia, Sudan, Togo, Laos and Myanmar.

Table 3

### What next?

The countries have yet to meet the serious challenge consisting of keeping the current level of debt at a sustainable level. Meanwhile, countries seeking the additional financing required to move towards the Millennium Development Objectives (whose main goal is to halve the number of people living in poverty by the year 2015). It is to be noted that few flows of private capital towards the Heavily Indebted Poor Countries has been recorded since the initiative was launched. The countries concerned are very vulnerable to external shocks, emerging or suffering as they are from a conflict.

### Further progress? The G8 and the Paris Club become more closely involved

Obviously the HIPC initiative depends on the multilateral donors for its application, but also on bilateral and commercial creditors. If the member-countries of the Paris Club are now closely involved in the process, but the non-member countries are still passive and only partially meet their commitments with regard to debt cancellation. The commercial creditors (as part of the London Club<sup>(6)</sup>), who play only a minor role in this assistance to the Heavily Indebted Poor Countries, have up to now made few effort in the context of this initiative.

### The multilateral debt reduction initiative or financing by the G8 countries

In September 2005, the 184 shareholders of the IMF and the World Bank validated the measure adopted in July at the Gleneagles Summit (Scotland) by the G8 countries to wipe out all the multilateral debts contracted by the 18 countries reaching the HIPC completion point with the IMF, the World Bank and the African Development Bank. Unlike the HIPC initiative, the Multilateral Debt Relief Initiative (MDRI) does not envisage the cancellation of debts to the public or private bilateral creditors, or to other multilateral institutions<sup>(7)</sup>. This does not mean that the poor countries are going to find themselves relieved of all debt (some of their creditors are not in fact members of the Paris Club (China, the Arab countries, certain developing countries). The total amount of debt concerned by the MDRI represents about USD 57 billion. In concrete terms, the G8 countries are committed to guaranteeing, "dollar for dollar", the cost of the debt cancellation. 70% of which is owed to the World Bank and the rest to the IMF and the African Development Bank. Thus, the MDRI joined the HIPC initiative in December 2005. It is planned to extend this mechanism to 20 other countries.

Nevertheless, the decision to grant a debt cancellation remains of the responsibility of each IFI. The scope and details of application may vary from one IFI to another.

For its part, the IMF has decided that as far as the MDRI is concerned:

## ***The Paris Club: a determining role within the international financial community***

*The Paris Club was set up in 1956 in the form of a club bringing together major creditor countries, when Argentina's debt was restructured for the first time. Since then, it regularly meets to find solutions to bilateral public debt repayments issues.*

*Nevertheless, in the 80s, the debt position of the majority of developing countries has worsened given the capitalization of rescheduled interest. The solvency crisis affecting some countries called for a new definition of debt management. As a result, since 1989, Paris Club introduced debt rescheduling systems at longer term by notably including cancellation element for the poorest countries. Nowadays, Paris Club has a decisive role for debt restructuring within HIPC initiative and in collaboration with IFI.*

- All countries whose per capita income is less than USD 380 per year, HIPC or not, will benefit from a debt reduction financed out of the IMF's own resources

- Heavily Indebted Poor Countries whose per capita income is more than USD 380 per year will benefit from a debt reduction financed by the G8 countries

The debt reduction with respect to the MDRI concerns debts contracted until the end of 2004. The IMF plans to implement the MDRI in the beginning of 2006. The exact date at which a particular member country will benefit from the cancellation of its debt regarding the MDRI will be decided on a case by case basis. The IMF has already determined that 19 countries will benefit from a debt reduction (see table below), representing a total of USD 3.3 billion.

For the World Bank, the debt cancellations – contracted before the end of 2003 – could come to USD 40 billion and may become effective in July 2006. The African Development Bank has not yet decided on the methods for applying this new mechanism.

This debt cancellation measure has, however, prompted some concern about its feasibility, particularly with regard to its financing. "Insofar the debts concerned are long-term; the substitution of rich countries for poor countries for reimbursement implies a long-term commitment"<sup>(6)</sup>. However, many governments, including the USA, have not committed themselves over such a long period. Therefore, the weight of this cancellation may be supported by a minority of countries. Meanwhile, the G8 countries have agreed to double the amount of their Official Development Aid to the beneficiary countries (see above).

## **Involvement of the Paris Club outside the framework of the HIPC initiative**

In October 2003, the Paris Club adopted a new approach for dealing with the debt of countries which do not meet the HIPC criteria but which nonetheless are confronted with an unsustainable debt. This approach was approved by the G7 heads of state and government at the Evian Summit. The Evian Approach seeks to define a response adapted to the situation pertaining in each country and no longer based on standard terms as was previously the case with the Paris Club. The agreements on debt reduction or cancellation on the part of the Paris Club came into effect following the positive results observed in the implementation of the IFI programmes.

## **Debt sustainability and the fight against poverty: synergy or dilemma?**

In recent years, debt reduction measures in favour of the Heavily Indebted Poor Countries have helped to normalise the situation<sup>(9)</sup>, and at the same time have relaxed the financial constraint of the beneficiary countries. However, although these measures alleviate the debt burden in short-term, they do not guarantee the sustainability of the debt in longer term. Successful debt reductions depend on governments' ability to implement medium-term reforms. For all of that, their room for manoeuvre remains limited. With the link-up between HIPC initiative and the Poverty Reduction Strategic

**Debt reduction treated by the Paris Club for countries not eligible for the HIPC initiative**

	Last treatment of debt	Amounts treated	Reimbursement profile
<b>Angola</b>	July 1989	US\$ 446 million	On standard terms - rescheduling of commercial debts treated over 14 years including 3 years of grace - rescheduling of ODA debts treated over 14 years including 3 years of grace
<b>Djibouti</b>	May 2000	US\$ 16 million	On standard terms
<b>Eritrea</b>			Not concerned
<b>Gabon</b>	June 2004	US\$ 858 million	On standard terms
<b>Georgia</b>	July 2004	US\$ 161 million	On Houston terms - rescheduling of commercial debts treated over 15 years including 5 years of grace - rescheduling of ODA debts treated over 20 years including 10 years of grace
<b>Iraq</b>	November 2004	US\$ 37 billion, including US\$ 30 billion cancelled and US\$ 7 billion rescheduled	Specific programme with IMF emergency post-conflict aid
<b>Kenya</b>	January 2004	US\$ 535 million	On Houston terms
<b>Nigeria</b>	October 2005	US\$ 30 billion (global treatment of debt to Paris Club creditors)	This agreement, introduced after IMF approval of a Policy Support Instrument, includes a debt reduction on eligible debts according to Naples terms and a buyback with a discount at market prices on the eligible debts remaining after the reduction. In all, this enables Nigeria to obtain a 60% cancellation of its debt stock owed to the Paris Club. The exceptional treatment of the debt provides a definitive solution.
<b>Dominican Republic</b>	October 2005	US\$137 million	On standard terms
<b>Zimbabwe</b>			No debt treatment

Table 4

Source: Club de Paris

Papers implemented under the trusteeship of the World Bank and the IMF, governments have in fact few alternatives in the choice of their reform programme. The increased expenditure on health and education imposed by the international financial institutions is essential in these countries affected by extreme levels of poverty. However, efficiency of the poverty alleviation programmes is uncertain as the positive effects will only really be felt in the long term. The question is all the more pressing since many beneficiary governments stand accused of endemic corruption. In these circumstances, alleviating the debt would lead to maintain this corruption. At the same time, debt restructuring would give these countries less incentive to reimburse their debts in view of the fact that they are constantly wiped out (hazard moral). Therefore, the view is expressed in many quarters that it would be better to replace the debt reduction measures by aid programmes, essentially in the form of grants.

Thus, covering their financing requirements with the aid programmes, debt dynamics of the HIPC remains a matter of concern. On one hand, there has been a succession of commitments in favour of increased international aid. On the other hand, the pressure on the public finances of the recipient countries will increase. For all of that, there are doubts about the capacity and willingness of the donor states to release sufficient resources to enable the HIPC to reach the Millennium Objectives, while the narrow tax bases and the difficult access to the international financial markets constraint the governments' ability to act. Thus the HIPC initiative is not a panacea, even complemented by the MDRI. Even if the external debt of the beneficiary countries were to be entirely cancelled, many of these countries would still need a substantial concessional external aid since the aid they receive has for many years far exceeded the payments made for servicing their debt. The Heavily Indebted Poor Countries will continue to be vulnerable to

financial, economic and political external shocks, and this will fuel the risk of a new debt crisis.

**Notes :**

(1) *Paris Club*: [www.clubdeparis.org](http://www.clubdeparis.org)

(2) *Central African Republic, Comoros, Republic of the Congo, Côte-d'Ivoire, Liberia, Malawi, Somalia, Sudan and Togo.*

(3) *According to a study conducted by UNCTAD (2004), the IMF and the World Bank would appear to have overestimated the impact of debt service reductions. Their calculations overlook the fact that the debt service payments in the years immediately preceding the decision point were higher than in the years before, since the Heavily Indebted Poor Countries were not authorised to accumulate arrears before reaching the decision point.*

(4) *Assuming that half the margins of manoeuvre released are in fact recycled in public investment expenditure.*

(5) *Arnaud Manas: "Pays Pauvres très endettés, mécanismes et éléments d'évaluation", Bulletin de la Banque de France, August 2005.*

(6) *The London Club is an ad hoc institution without a governing charter. It is charged with the restructuring of sovereign bank debts.*

(7) *This means that the measure's impact differs according to the countries with similar debt burdens and according to the regions.*

(8) *Richard Hiault, "La dette des pays pauvres reste bien réelle", Les Echos, August 2005.*

(9) *In theory, the countries benefiting from a decrease of risk premium and improved access to the international financial markets.*

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**Summary table: Appraisal of the HIPC initiative and the agreements with the IMF (February 2006)**

Eligible countries	HIPC		IMF arrangements			
	Decision	Completion	PRGF <sup>1</sup>		SMP <sup>2</sup>	
			Agreement	Expiry	Agreement	Expiry
Benin	7/00	3/03	8/05	8/08	...	...
Bolivia	2/00	6/01	4/03 <sup>3</sup>	3/06	...	...
Burkina Faso	7/00	3/02	6/03	8/06	...	...
Burundi	8/05	Est.2007	1/04	1/07	...	...
Cameroon	10/00	Est.2006	...	...	...	...
Central African Republic	...	...	...	...	1/06 <sup>4</sup>	2Q/06
Comoros	...	...	...	...	1/05	2Q/06
Democratic Republic of the Congo	7/03	Est.2007	...	...	...	...
Republic of the Congo	Est.1Q/06	Est.2007	...	...	...	...
Côte d'Ivoire	...	...	Outside programme		...	...
Ethiopia	11/01	4/04	11/01	9/05 <sup>5</sup>	...	...
Gambia	12/00	Est.2007	...	...	10/05	04/06
Ghana	2/02	7/04	5/03	10/06	...	...
Guinea	12/00	Est.2007	...	...	04/05	03/06
Guinea-Bissau	12/00	Est.2007	...	...	04/05	2Q/06
Guyana	11/00	12/03	9/02	9/06	...	...
Honduras	6/00	4/05	2/04	2/07	...	...
Laos	...	...	...	...	...	...
Liberia	...	...	...	...	10/05 <sup>4</sup>	2Q/06
Madagascar	12/00	10/04	3/01 <sup>5</sup>	3/05 <sup>5</sup>	...	...
Malawi	9/00	Est.1Q2006	9/05	9/08	...	...
Mali	9/00	3/03	6/04	6/07	...	...
Mauritania	2/00	6/02	Outside programme		...	...
Mozambique	4/00	9/01	7/04	7/07	...	...
Myanmar	...	...	Outside programme		...	...
Nicaragua	12/00	1/04	12/02	12/06	...	...
Niger	12/00	4/04	1/05	1/08	...	...
Uganda	2/00	5/00	9/02	2/06	...	...
Rwanda	12/00	4/05	8/02	2/06	...	...
Sao Tomé and Príncipe	12/00	Est.3TQ2006	8/05	7/08	...	...
Senegal	6/00	4/04	4/03	4/06	...	...
Sierra Leone	3/02	Est.3Q2006	9/01	6/05 <sup>5</sup>	...	...
Somalia	...	...	Outside programme		...	...
Sudan	...	...	Outside programme		...	...
Tanzania	4/00	11/01	8/03	8/06	...	...
Chad	5/01	Est.1Q.2006	2/05	2/08	...	...
Togo	...	...	Outside programme		...	...
Zambia	12/00	4/05	6/04	6/07	...	...

Source: IMF

1-The PRGF (Poverty Reduction and Growth Facility) i.e. a 3-year disbursement programme allocated by the IMF.

2-The SMP (Staff Monitored Programme) is an economic policy assessment programme giving access to the PRGF for the poorest countries.

3-Bolivia benefited from stand by agreement, i.e. a temporary aid for countries experiencing balance of payments difficulties.

4-Emergency aid programme for "post-conflict" countries. Intended for the introduction of economic reforms and reconstruction efforts.

5-Negotiation of a new PRGF in progress.

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