

INTRODUCTION

On September 26 1999, at a joint meeting of the World Bank's Development Committee and the International Monetary Fund's Interim Committee (since renamed the International Monetary and Finance Committee), a new version of the Heavily Indebted Poor Country (HIPC) Initiative was adopted. That new (Enhanced HIPC or HIPC II) Initiative offered the possibility of more generous, and expeditiously delivered, debt relief than the earlier 1996 version (HIPC I). However, debt relief would be conditioned on an explicit commitment to allocate the savings (or dividends) from such relief to poverty reduction through an articulated, and approved, Poverty Reduction Strategy (see Box 1). The new initiative was, in effect, the institutional expression of the objectives of the 1999 Köln Debt Initiative launched by the heads of state of the G-8 countries in June 1999. That initiative, in turn, was a response to a vociferous international campaign for forgiveness of the debt of the poorest countries that had been mounted in the preceding months by the Jubilee 2000 Coalition and other civil society organisations.

This (HIPC II) debt initiative remains by far the most broad-based attempt at addressing the debt problems of the poorest countries to date (see Box 2), and only two of the potentially eligible countries (Ghana and Laos) have declined to participate. Though the first year of implementation of the Enhanced HIPC Initiative produced less than spectacular results (out of 25 immediately eligible recipients¹ only 10 had been duly considered), a flurry of activity, and less strict interpretation of pre-requisites, in the latter part of 2000 led to approval of an additional 12 countries.

Yet, despite its obvious superiority to the first HIPC Initiative in the extent and speed of delivery of debt relief, the issues of adequacy, efficacy, and procedural efficiency that dogged the earlier version have not been completely laid to rest. Further, this Initiative's insistence on an explicit link between debt relief and poverty reduction has added new procedural and ethical dimensions. Criticism of the Initiative from both civil society and donor governments, and its spirited defence by the overseeing institutions—the International Monetary Fund and the World Bank—have been well publicised. However, the views and experiences of citizens, non-governmental organisations (NGOs), the private sector, and governments within debtor countries with regard to debt relief in general, and the HIPC Initiative in particular, have received much less exposure.

This *Report* attempts to identify and examine some of the more pertinent lessons coming out of the HIPC debt relief experience of five debtor countries at various stages of the debt relief process: Bolivia, Ethiopia, Mali, Nicaragua, and Uganda (see Appendix 1). To the degree possible, an attempt is made to highlight both the common and differing perspectives of governments, peoples, and organisations within these countries. In that regard, this paper draws heavily on the work of domestic researchers (or research teams) in the five countries whose research was commissioned through a North-South Institute *Study of the Debt of Poorest Countries* (see Appendix 2).²

¹ "Immediately eligible recipients" were countries that had been designated as heavily indebted and poor (HIPCs), were not conflict affected, and whose debt ratios were not likely to reach the prescribed sustainability criteria without HIPC II debt relief. Thus, (other than failing to meet conditions imposed by the program itself), these countries had no immediate impediment to consideration for debt relief.

² The authors of the country reports are: Lykke E. Anderson and Osvaldo Nina (Bolivia); Befekadu Degefe (Ethiopia); Massa Coulibaly (Mali); Ligia María Castro-Monge (Nicaragua); and Peter Mijumbi (Uganda). These studies will be published in a special (June) issue of the Canadian Journal of Development Studies. Preliminary drafts of these papers are available from The North-South Institute.

THE PRE-HIPC INITIATIVE RECORDS

Low and middle-income countries grew much more slowly, on average, in the 1980s than in the 1970s. Four of the five countries considered here—Bolivia, Ethiopia, Mali, and Nicaragua—grew at a slower rate (in the 1980s) than even the low and middle-income country average (Figure 1). In fact, Bolivia and Nicaragua had negative overall growth rates, and Ethiopia and Mali had negative per capita growth rates.

Without exception, this period also marked a fall in domestic savings in these countries and, with the exception of Mali, below average growth in real exports relative to other developing countries (Figure 1). These factors, in the absence of substantial increases in autonomous resource inflows,³ meant that the rapidly increasing external debts and debt service obligations soon outstripped these countries' debt servicing capacity. In fact, as Figure 2 suggests, during the 1980s average debt service payments were at or above 20 percent of exports for four of these countries (Bolivia, Ethiopia, Nicaragua, and Uganda) and above 16 percent for the fifth (Mali). The build-up of arrears over that period suggests that the ratio of scheduled debt service to exports (i.e. debt service payments falling due, as opposed to what was paid) was even higher.

The external imbalance (related to the indifferent export performances in the face of rapidly increasing debt service obligations), and the internal imbalance (related to the low savings rates), resulted eventually in a recourse to stabilisation and adjustment programs and related financing. Bolivia received its first World Bank structural adjustment loan together with an IMF Stand-by Arrangement in 1980, and its first IMF Structural Adjustment Facility (SAF) in 1986. This was upgraded to an Enhanced Structural Adjustment Facility (ESAF) in 1988. The country has since moved through a contiguous sequence of adjustment programs. After Stand-by Arrangements in 1982 and 1983, Uganda submitted to its first Structural Adjustment Facility in 1987. Like Bolivia, it has since been under continuous adjustment through ESAF arrangements (now renamed Poverty Reduction and Growth Facilities—PRGF). Mali received Stand-by support in 1983 and 1988, and its first Structural Adjustment Facility in 1988. It is currently under its third consecutive three-year PRGF arrangement.

³ Autonomous resource inflows refer to financial flows, such as foreign direct investment, that are not related to, or motivated by, the country's immediate need for financing its payments to foreigners (including debt service payments).

BOX 1

The Enhanced Heavily Indebted Country Poor (HIPC) Initiative

Objective:

To provide broad-based debt relief to heavily indebted poor countries beyond that which is available through *traditional debt relief mechanisms*.

Implementing Agencies:

The World Bank and International Monetary Fund.

Country Eligibility:

A country is considered eligible for Enhanced HIPC debt relief if:

- it is eligible for concessional financing from the World Bank Group (through the IDA) and from the IMF (via a Poverty Reduction and Growth Facility (PRGF));
- it faces an unsustainable debt burden after *traditional debt relief*;
- it has established a strong recent record of economic reform and sound macroeconomic policies through an IMF or World Bank adjustment facility.

The Stages to Debt Relief

PHASE ONE:

- At least three years of structural adjustment through an IMF and/or World Bank supported adjustment program;
- Application and receipt of debt relief through traditional mechanisms;
- The development and adoption of a Poverty Reduction Strategy Paper (PRSP).

THE DECISION POINT

- Determination of the country's qualification for further debt relief through a debt sustainability analysis (DSA);
- Approval (by the Bank and Fund) of the country's PRSP (or Interim PRSP).
- Establishment of policy and reform objectives to be met at the decision point.

PHASE TWO

- Development of a further track record, based on criteria established at the decision point;
- Interim debt relief in the form of rescheduling from bilateral and commercial creditors and advance debt reduction from multilateral creditors;
- Completion (and perhaps implementation) of the PRSP and related monitoring and evaluation mechanisms.

COMPLETION POINT

- Up to (and possibly beyond) 90 percent debt reduction from bilateral and commercial creditors;
- Additional debt reduction from multilateral creditors (equitably shared) to bring debt reduction to a sustainable level.

Definition of Sustainable Debt

EXPORT CRITERIA

A country's debt is considered unsustainable if the *net present value*** (NPV) of the country's external debt to export ratio exceeds 150 percent.

FISCAL CRITERIA

A country with an open economy (i.e. with an export to GDP ratio of 30 percent or more) is considered to have an unsustainable debt if the NPV of the external debt to (government) revenue ratio exceeds 250 percent when the revenue to GDP ratio is at least 15 percent.

^{*} *Traditional debt relief mechanisms* refer principally to three ongoing (but relatively narrow) debt relief mechanisms. These are: (1) Paris Club debt reduction; (2) the IDA Debt Reduction Facility; and (3) bilateral forgiveness of ODA debt (see Box 2).

^{**} The sum of all of a country's future debt service obligations (interest and principal) discounted at the market interest rate.

BOX 2

DEBT REDUCTION INITIATIVES FOR POOR COUNTRIES

Initiative	Year Introduced	Nature of Relief Offered	Eligibility
Special Program of Assistance for Africa	1987	Bilateral Debt Reduction Funding for Commercial Debt buybacks IBRD debt service support	IDA eligible African countries
Paris Club: Toronto Terms	1988	Up to 33% debt service reduction on all pre-cut-off date, on non-concessional bilateral debt during a consolidation period	Heavily Indebted Poor Countries
Brady Plan	1989	Stock Reduction on Commercial Debt. Brady restructurings include buyback, debt swaps and debt conversions	Highly Indebted Countries with large amounts of commercial bank debt (mostly middle income)
International Development Association (IDA) Debt Reduction Facility	1989	Financing for the buyback of commercial bank debt	IDA eligible countries
Paris Club: London (on enhanced Toronto) Terms	1991	Up to 50% of pre-cut-off date, bilateral (non-concessional) debt falling due during consolidation period	Severely indebted low income countries (SILICs) ¹
Paris Club: Naples Terms	1994	Up to 67% of pre-cut-off date, bilateral (non-concessional) debt falling due during consolidation period	Countries with per capita income below US\$500 or a NPV debt-to-export ratio over 350%
Heavily Indebted Poor Country (HIPC) Initiative	1996	Stock reduction on all debt (Bilateral, Multilateral and Commercial) up to and beyond Paris Club Naples Terms	All heavily indebted poor countries in non-conflict situations
Enhanced Heavily Indebted Poor Country Initiative	1999	More generous stock reductions than offered in HIPC I, plus an explicit attachment to poverty reduction	All heavily indebted poor countries in non-conflict situations

1. SILICs are officially defined as countries with debt-to-GNP and debt-to-export ratios larger than 80% and 220% respectively, and GNP per capita less than US\$675.

Figure 1

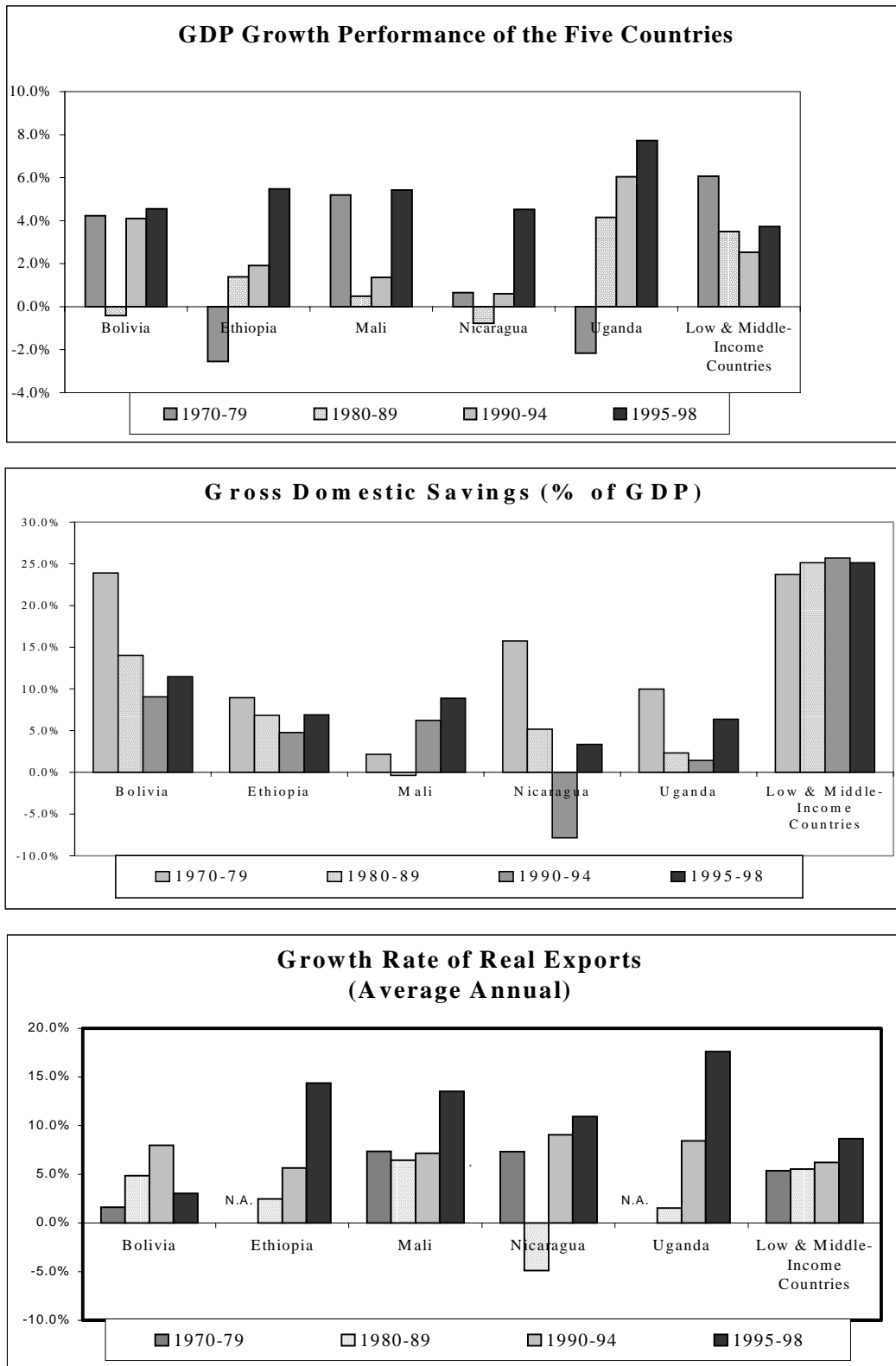
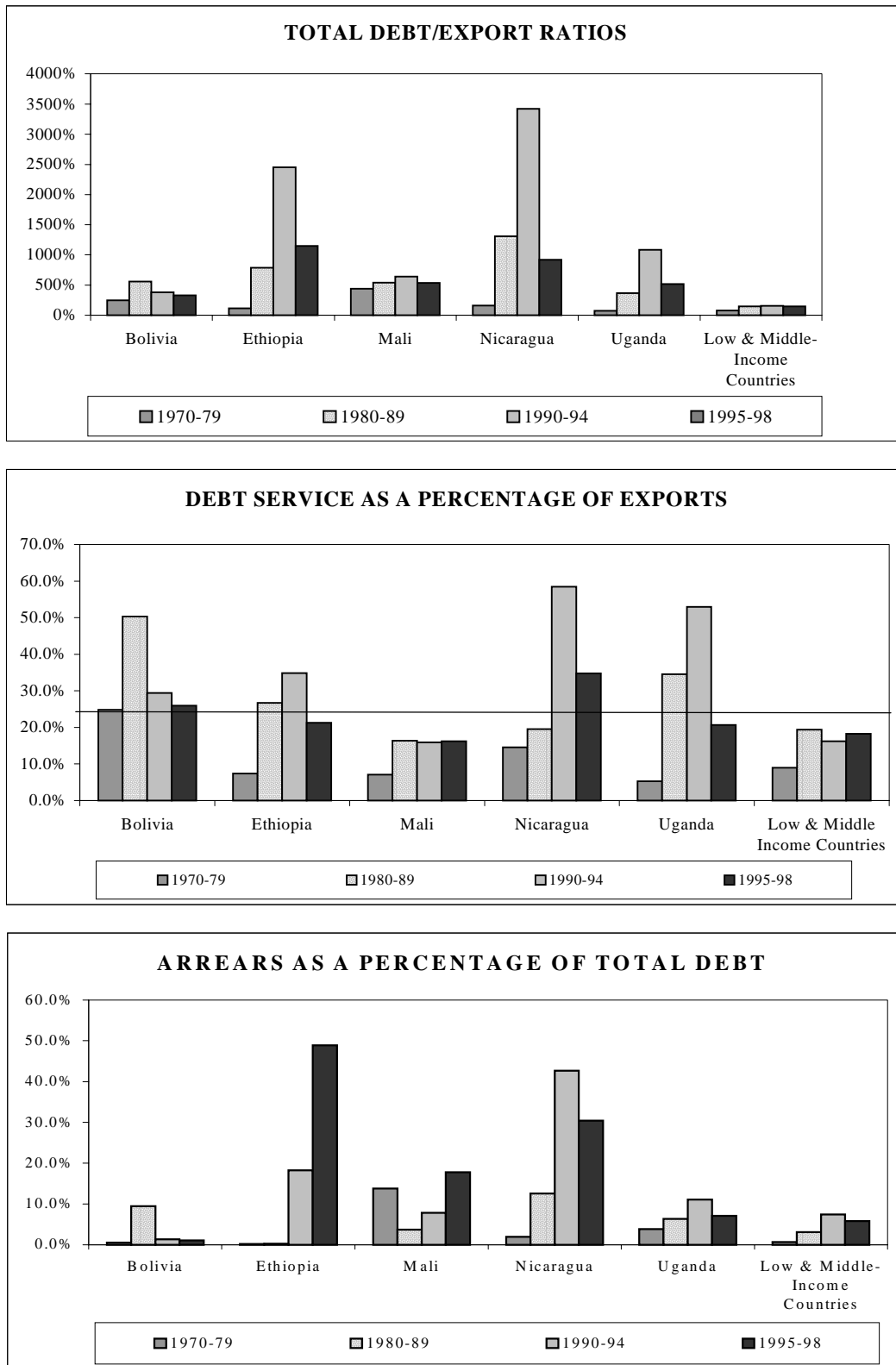


Figure 2



The 1990s witnessed better growth performances for these countries compared to the 1980s. However, that was more true of the latter half of the 1990s than the first half, particularly for Ethiopia, Mali, and Nicaragua, which had performed poorly in the first half (Figure 1). Undoubtedly, the significantly better growth performance of the late 1990s is related to the improved export performances during that period (Figure 1). The exception is Bolivia, whose growth performance is more closely related to a sharp increase in foreign direct investment in the country during the 1990s. Savings rates showed signs of recovery as well, though they remain well below the developing country average. However, despite the resumption of growth, the recovery of exports, subsidence in the rates of growth of debt stocks, less than perfect repayment records, and even some debt relief, debt service to export ratios remained well over 20 percent for four of these countries and over 16 percent for the fifth (Figure 2). This underscores the importance of debt reduction for providing the breathing room these countries need to address their developmental challenges.

THE FLOW DIMENSIONS OF DEBT RELIEF

The Debt Dividend

While debt reduction—if it is sufficient—can have a significant positive effect on the behaviour of economic actors (by removing or reducing the fear of debt-related crises and constraints), the exact magnitude of this (incentive) effect remains conjectural. However, the quantitative (flow) dimensions of debt reduction operations—the debt relief dividend—can be measured. Given that (for the poorer countries) the negative financial impact of a heavy debt burden occurs mainly through its pre-emptive claim on (government) budgetary resources (and equivalent amounts of foreign exchange), it follows that the financial impact of debt reduction will be the reduced size of that claim.⁴ We can thus define the debt reduction dividend as: "the budgetary saving from debt relief " or "the new spending available for other endeavours because of smaller debt service payment obligations."

The term "dividend," in the context of debt relief, suggests an increase in available domestic spending. It can thus be interpreted as the saving on fiscal expenditure from lower debt service payments. It is, in effect, the difference between typical spending on debt servicing before debt relief and spending after relief. We take the average expenditure level in the period 1994-98 as our estimate of average pre-debt relief spending on debt servicing. Thus, debt dividend for each of these countries is defined as the difference between the average expenditure level in the 1994-98 period and the post-debt-relief debt service level.

If a country had been meeting only part of its scheduled debt service obligations (i.e. the government had made a unilateral decision to limit budgetary outlays to levels below what its debt obligations required), the net impact of debt reduction on the budget (the debt dividend) will be smaller than the actual debt service reduction amounts over the relevant debt repayment period.⁵ This is precisely the situation faced by the four countries examined below.⁶

⁴ For a more detailed analysis of the effects of a heavy debt burden see: *Debt Relief for the Poorest Countries: Challenges and Opportunities*, J. Serieux (Ottawa: North-South Institute, 1999).

⁵ However, if debt relief is front-loaded, it is possible for the debt dividend to exceed the average debt service reduction in the initial years.

⁶ The fifth, Ethiopia, has yet to reach the decision point as of early 2001, and thus debt reduction amounts are yet to be determined.

It should be noted that in estimating the debt relief and debt dividend amounts, the period under consideration is the years 2001 to 2015, even though debt relief began earlier for many countries and ends a few years later (usually 2018 or 2019). This is because the year 2015 has tremendous symbolic importance in the context of poverty reduction. It is the target year set by both the OECD (OECD, 2000) and the Millennium Summit (UN, 2000) for the reduction of world poverty by half (as well as the accomplishment of several other human-development related goals). Thus the estimation of debt relief dividends below is made in the context of their anticipated role in providing new resources for poverty reduction over this crucial period.

Bolivia

The debt reduction offered by the combined HIPC Initiatives (HIPC I and II) amounted to US\$1.3 billion in net present value terms, and represented a reduction of approximately 35 percent of the net present value of Bolivia's debt (after full use of traditional debt relief mechanisms) at its decision point in February 2000. Over the next five years (2001-5) debt service relief through the HIPC Initiative (the difference between expected debt service obligations before and after HIPC debt relief) is expected to average US\$158.8 million. The amount falls to US\$113.9 when averaged over the next fifteen years (2001-15). This front-loading of debt relief will cause debt service payments to reach a low of US\$201 million in 2001, but it is projected to rise again to nearly US\$800 million by 2015.⁷

While Bolivia historically serviced all its multilateral debt, it did not service all its bilateral and commercial debts. In fact, its average debt service payment record for 1990-97 was 82.9 percent (Andersen and Nina, 2001). In the 1994-98 period, Bolivia paid an average of US\$415.1 million in debt service payments. Thus, the expected fall in average payments over the next five years (2001-5) means an average debt service payment reduction—and debt dividend—of US\$157.7 million. This is close to the actual size of HIPC debt relief offered for that period (Table 1), but by 2008 debt service payments will have surpassed the previous (1994-98) levels (Figure 3). Thus, when the past payment level is compared to expected average debt service payments over 2001 to 2015, there is no net saving on debt service payments. In fact average debt service payments will be higher by US\$47.6 million (implying a net increase in resource outflows compared to the outlays of the mid-to-late 1990s).

Relative to other flows, the average annual debt dividend similarly fades beyond the next five years. If the expected average annual debt dividend over the next five years of US\$157.7 million was added to total government expenditure in 1999, it would have increased it by 8.2 percent, and increased social expenditure by 16.1 percent. However, the increased average debt service payments over the next fifteen years is equivalent to 2.5 and 4.8 percent reductions in 1999 total and social expenditure levels respectively.

Mali

In September 2000, Mali received the net present value equivalent of US\$121 million in debt relief under the HIPC I framework and was promised a further US\$401 million under the HIPC II framework. Debt reduction from the combined initiatives will result in an approximately 39 percent reduction in the net present value of the country's debt at the end of 1998. This will translate into average debt service relief of US\$48.6 million in 2001-5 and US\$44.3 million in 2001-15. The associated debt dividend, will average US\$25.8 million over 2001-5 and US\$12.5

⁷ These estimates are based on the IMF/World Bank's *Debt Sustainability Analyses* included in the decision point document for HIPC II for Bolivia (IMF/World Bank, 2000) of January of 2000.

million over 2001-15. As Figure 3 shows, the dividend is only slightly more than one-half (53.1 percent) of total debt relief in the early years, but falls sharply thereafter, to average only 28.2 percent of total debt relief over the fifteen-year period.

Figure 3

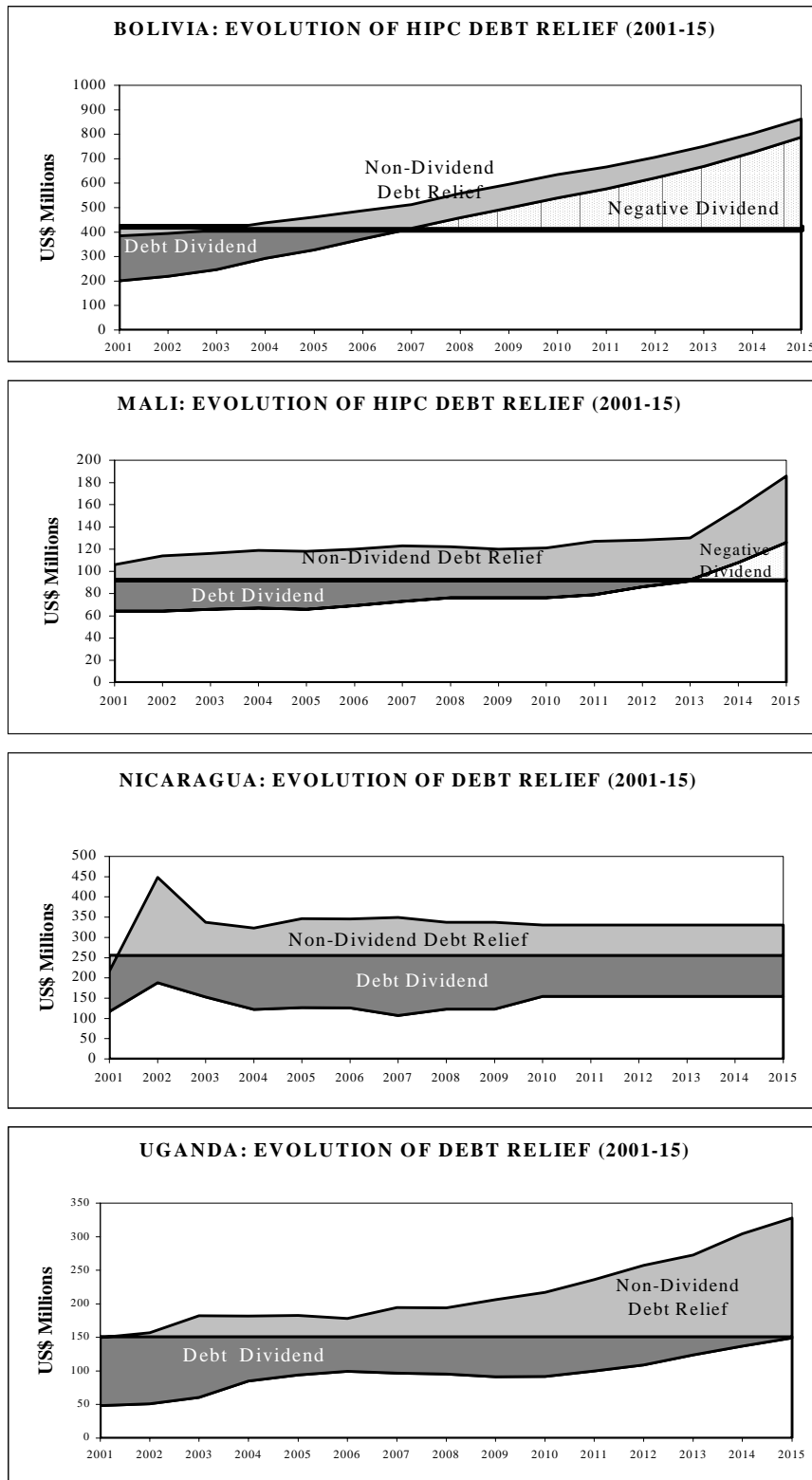


Table 1
Debt Relief Indicators for Four Countries

Aggregates and Ratios for HIPC I and II Combined (Annual Average)	Bolivia	Mali	Nicaragua	Uganda
<u>Estimated Debt Service Reduction (US\$Millions)</u>				
2001-2005	158.8	48.6	193.0	102.9
2001-2015	113.9	44.3	194.2	120.6
<u>Debt Service Reduction as % of IMF/WB Projected GDP</u>				
2001-2005	1.5	1.4	7.2	1.1
2001-2015	0.9	1.1	5.8	1.0
<u>HIPC Debt Dividend (budgetary saving) (US\$Millions)</u>				
2001-2005	157.7	25.8	116.7	83.4
2001-2015	-47.6	12.5	117.2	55.5
<u>Debt Dividend as % of Debt Service Reduction Amounts</u>				
2001-2005	99.3	53.1	60.4	81.0
2001-2015	-41.7	28.2	60.4	46.1
<u>Debt Dividend as % of Total Govt. Expenditure in 1999</u>				
2001-2005	8.2	3.8	15.2	6.6
2001-2015	-2.5	1.8	15.3	4.4
<u>Debt Dividend as % of Social Expenditure in 1999</u>				
2001-2005	16.1	14.5	34.4	19.4
2001-2015	-4.8	7.1	34.5	12.9

Source: North-South Institute

The smaller debt reduction and debt dividend amounts for Mali also mean that debt relief will not, by itself, represent a large potential addition to government spending. The average debt dividend amount for 2001-5 is the equivalent of only 3.8 percent of government expenditure in 1999 and 14.4 percent of social expenditure. The average debt dividend for 2001-15 is the equivalent of 1.8 percent of government spending and 7.1 percent of social spending in 1999.

Nicaragua

Under the Enhanced HIPC Initiative (HIPC I does not apply) Nicaragua is expected to receive debt relief valued (in net present value terms) at US\$3.3 billion. This will amount to a 72 percent reduction (in the net present value) of Nicaragua's debt at the end of 2000.⁸ Because of the nature of its debt obligations, Nicaragua's debt relief will be much less front-loaded than Bolivia's, thus debt service reduction amounts will average US\$193.0 million annually in 2001-5, and a slightly higher US\$194.2 million over the fifteen-year period 2001-15.

Given its extraordinary debt load (over 3400% of exports from 1990 to 1995 and 761% as late as 1998), Nicaragua was never able to meet all of its scheduled debt payments despite average

⁸ The full use of traditional debt relief is assumed.

payment levels of 16 percent of GNP (and over 42 percent of exports) during the 1990s. In fact, it was able to meet only 20.7 percent of its scheduled debt service obligations during 1990-94, and 56.3 percent during 1994-99 (Castro-Monge, 2001). In short, nearly half of Nicaragua's debt was non-performing despite the extremely high resource cost of actual debt service payments. It is, therefore, not surprising that the average annual budgetary saving from debt relief (the debt dividend) will be only 60.4 percent of the debt service reduction amounts over both, the short and long term (Table 1 and Figure 3). The actual (average) dividend amounts are US\$116.7 million for 2001-5 and US\$117.2 million over the 2001-15 period.

However, despite the considerably smaller size of the debt dividend relative to the debt service reduction amounts, the substantial size of the debt stock reduction means that the overall impact will still be substantial. If the average dividend had been added to the government budget in 1999, it would have allowed for an increase in total expenditure of 15.2 percent and an increase in social expenditure of over 34.4 percent (Table 1). The average dividend for 2001-15 would have boosted 1999 total and social expenditure by similar amounts (15.3 and 34.5 percent respectively). In effect, given expected future borrowing requirements, Nicaragua can expect a significant boost to domestic spending over both the short and long term.⁹

Uganda

Having completed debt relief arrangements under both HIPC Initiatives in May 2000, the net present value of Uganda's debt was reduced by US\$1.0 billion, or 50 percent of its original net present value before HIPC relief. Over the next five years, this will translate into average annual debt service relief of US\$102.9 million. Because Uganda's debt is not front-loaded, the average debt service reduction amount increases to US\$120.6 million when the period of reference is 2001-15. Debt service payments will fall to a low of US\$48.1 million in 2001, but are projected to rise steadily thereafter. Like the other countries, Uganda had been unable to service all of its debts, achieving a debt service payment ratio of only 48 percent of debt service due in the 1991-96 period. Thus the debt dividend associated with the above noted debt service reductions reaches a high of 81 percent of debt service reduction for the 2001-5 period, but falls to only 46.1 percent for the 2001-15 period. The related dividends are US\$83.4 million in 2001-5 and US\$55.5 million in 2001-15. The larger size of the debt dividend in the initial years, despite the essential back-loading of debt relief, is due to the relatively steep rise in Uganda's debt service payments after 2010 (Figure 3).

The average (annual) debt dividend for 2001-5 represents 6.6 percent of total government expenditure in 1999 and 19.4 percent of social expenditure in 1999. The average dividend for 2001-15 represents only 4.4 percent of total expenditure and 12.9 percent of social expenditure in 1999.

Comparing Discounts

As noted earlier, the HIPC Initiatives (HIPC I and II) surpass all other debt reduction efforts in terms of coverage of eligible debt. More particularly, they are unique in their explicit inclusion of multilateral debt. However, in terms of the discount offered on eligible debt, HIPC debt reduction

⁹ It should be pointed out that estimates of future borrowing requirements are based on rather optimistic export and growth performances for 2001-15. If these expectations are not fulfilled, borrowing requirements will increase (if there is no net increase in grant flows) and the debt dividend will be smaller because service payments are likely to increase more rapidly. Nevertheless, anything short of a complete economic collapse over the next fifteen years will allow for a significant debt dividend.

does not distinguish itself particularly. All countries considered here have had more generous debt reduction operations with commercial creditors. The discount rates have ranged from a low of 84 cents on the dollar for Bolivia, to 92 cents for Ethiopia and Nicaragua. Non-Paris Club debt reduction operations have also been similarly generous. Nicaragua received a 92 cent discount on the dollar from non-Paris club creditors (Mexico, the Czech Republic, and pre-Paris Club Russia). By comparison, Nicaragua's 72 percent debt reduction is the highest that will be received by the four countries considered here (and the second highest received by the end of 2000).

Table 2
Some Pre-HIPC (and non-Paris Club) Debt Reduction Operations

Country	Year	Type of Debt	Reduction of Eligible Debt (%)	Amount of Debt Written Off (US\$ Millions)
Bolivia	1989	Commercial debt buyback	89	169.2
	1993	Commercial debt buyback	84	170.0
Ethiopia	1996	Commercial debt buyback	92	226.0
Nicaragua	1995	Commercial debt buyback	92	1,099.4
	1995-96	Non-Paris Club bilateral debt reduction	92	4,201.4
Uganda	1993	Commercial debt buyback	88	153.0

Source: Boote and Thugg (1999); Castro-Monge (2001).

Some of these debt reduction operations have also been sufficiently large to compare with HIPC debt reduction amounts. This is particularly true for Nicaragua which received debt relief of over US\$1 billion from commercial creditors and US\$4.2 billion from non-Paris Club public creditors in 1995-96. The combined debt reduction operations resulted in a 50 percent reduction in the nominal value of Nicaragua's debt.

To a certain degree, the supplementary nature of HIPC II—it is supplementary to Paris Club and other debt reduction operations—makes the comparison unfair. However, there is a larger question here. The generous discounts, particularly on commercial debt transactions, suggest something about the perceived repayment value of those countries' debt. If this is the case, it is instructive to ask whether the average discount on all debt, after the last debt reduction operation is completed, is in any way reflective of that perception.¹⁰

The Aid Equivalents of Debt Relief

The explicit requirement that HIPC debt relief must be used for poverty reduction implies a common objective between debt relief in general (and the debt dividend in particular) and much of official development assistance. This 'additionality' factor, when considered in the context of the cost of debt reduction to creditor countries (who are also providers of official development assistance), leads to the concern that debt relief over the coming years may be concomitant

¹⁰ Of course, if we accept what is implicit in the HIPC Initiative itself—the seniority of multilateral debt—the issues become more complicated.

with a drop in aid levels.¹¹ Table 3 compares aid provided on a per capita basis before HIPC debt relief with the level per capita of assistance implied by HIPC debt relief levels and the related debt dividend (as estimated above). The numbers suggest that, on a per capita basis, the average debt relief dividend over the next five years will represent less than a 20 percent addition to recent per capita aid levels in any of the countries considered. When considered over the next fifteen years (2001-15), the debt dividend represents more than six percent of recent (per capita) aid levels for only one country (Nicaragua).

Table 3
Per Capita Aid and Debt Relief Comparisons

	Bolivia	Mali	Nicaragua	Uganda
<u>Aid per capita (US\$)</u>				
1994-1998	90.8	45.3	139.1	36.1
<u>Debt relief per capita under HIPC (US\$)</u>				
2001-2005	18.0	3.9	35.1	4.0
2001-2015	12.0	3.2	35.8	3.9
<u>Debt dividend per capita (US\$)</u>				
2001-2005	17.8	2.1	21.3	3.3
2001-2015	-4.8	0.9	19.0	1.8
<u>Debt relief (under HIPC) per capita/Aid (%)</u>				
2001-2005	19.8	8.6	25.2	11.1
2001-2015	13.2	7.1	25.7	10.8
<u>Debt dividend per capita under HIPC/Aid (%)</u>				
2001-2005	19.6	4.6	15.3	9.0
2001-2015	-5.3	1.9	13.6	5.1

Source: The North-South Institute

These percentages also give us some idea of how large any fall in aid levels would have to be in order to negate the average net flow effect implied by debt relief. It would thus take only a 4.6 percent drop in (per capita) aid levels to Mali to nullify the net flow effect of debt relief (as implied by the debt dividend) over the next five years. It would take a nine-percent drop in Uganda, a 15.3 percent drop in Nicaragua, and a 19.6 percent drop in Bolivia to have the same effect. When considered over the fifteen-year period, it would take even small reductions in per capita aid levels to nullify the net flows effects of HIPC debt reduction. Only Nicaragua would have to sustain a substantial reduction in (per capita) aid levels (13.6 percent) before the net flow effect of debt reduction is negated. For Uganda it would only require a 5.1 percent reduction and for Mali a 1.9 percent reduction. Bolivia, because it will experience a net *increase* in average debt repayment outflows over the next fifteen years would need an *increase* in per capita aid levels of 5.3 percent to cancel out the increase in outflows.

¹¹ Because debt reduction costs are also counted as ODA in OECD country budgets, there is, in fact, a one-to-one substitutability between debt relief and other aid from the donor perspective. Thus, unless donor aid budgets increase, more debt relief will necessarily mean less aid.

POVERTY REDUCTION AND DEBT RELIEF

Although there is significant variation in average per capita incomes, the countries considered here are all at the lower end of the income ladder (Appendix 1), and all face urgent poverty reduction challenges. Not surprisingly, the greater focus on poverty reduction demanded by the HIPC debt reduction process has had welcome effects in those countries. However, the authenticity of the consultative process, as well as the sustainability and likely effectiveness of debt reduction programs are still in question, as the three examples below illustrate.

Bolivia

Bolivia has attempted to develop its Poverty Reduction Strategy through a bottom-up process that began with consultations at the municipal level and moved up, through the state level, to a national level roundtable. Deliberations were informed by preliminary Development and Political Agendas prepared by the national government.

The intent was to gain agreement on:

- a development agenda;
- constitutional reform;
- institutional reform; and
- the method of distribution of debt relief dividends.

As a result of that process, it was agreed that municipalities, rather than state or national governments, should be responsible for implementing poverty reduction projects. Municipalities have thus developed plans that propose an average 11-fold increase in public (municipal) investment, at an average annual cost of US\$1.3 million. Reflecting a greater concern with economic opportunities than social services, these projects are heavily biased toward productive sector investments. Projects in transportation (26.2%) and agriculture (15.0%) dominate those in education (13.8%), sanitation (8.8%), and health (5.5%).

Although Bolivia attempted to make the process inclusive of the poor, it did not succeed. The results of a national survey showed that only 5 percent of the poor were significantly aware of the process, and only 31 percent of those in the upper income group knew more than a little about it. The credibility of the process itself is also called into question by the fact that among the low, middle, and high income groups, only 6.8, 7.3, and 15.3 percent respectively thought that the dialogue represented a sincere effort at an inclusive approach to poverty reduction. The majority considered it as little more than a political manoeuvre by the government.

The significant limitations of this consultation effort were clearly evident when disgruntled farmers, coca-growers, teachers, and others, staged widespread strikes and blockades for a period of three weeks after the completion of the National Dialogue because they felt that their perspectives had not been represented in the process. In the end, they may have assured themselves better consideration in the development of the final PRSP because of this rather "unofficial" intervention.

A survey of opinion leaders in the country suggests that views about the HIPC Initiative and the conditions attached to debt relief vary among various sectors. Government respondents see the conditioning of debt relief on a Poverty Reduction Strategy as a useful way to force the government to increase social investment faster than it otherwise would. Private sector and NGO respondents do not support the link, although NGOs concede that the government would have been unlikely to increase social investment otherwise. Private sector respondents, however, generally view the HIPC Initiative as a band-aid approach in the larger context of

international economic relations. In their view, trade access to developed-country markets would prove far superior and have longer-term effects than debt reduction. Individuals, if they were aware of the process, generally indicated distrust of any process orchestrated by the government, and voiced a strong preference for a coordinating role for the church, which in turn argues that it does not have the institutional capacity to do so, although it would be willing to participate in the monitoring process.

Mali

Mali completed its Interim PRSP in July of 2000, and the paper was approved by the World Bank and the International Monetary Fund in September of 2000. Mali anticipates the completion of a final PRSP by June of 2001.

The PRSP will not be Mali's first attempt at a national poverty reduction strategy. In 1996-98, in partnership with the United Nations Development Program, the government of Mali developed a National Strategy for the Fight Against Poverty or *Stratégie nationale de la Lutte contre la Pauvreté* (SNLP). The impetus for the SNLP was the need to improve living standards and reduce poverty while restoring macroeconomic stability and financial credibility through structural adjustment. The strategy was meant to provide a co-ordinating framework for all actions aimed at reducing poverty (Government of Mali, 2000). The strategy envisaged a set of sector-based projects that would cost an average of US\$74.6 million a year, over five years. However, the SNLP was limited in its sectoral and regional coverage as well as the anticipated time frame for implementation. It is thus anticipated that it will form the basis for the PRSP, which will have an expanded scope, reach, and implementation time frame.

The development of the Interim PRSP involved very little consultation with other sectors of Malian society and in fact NGOs have complained that their knowledge and expertise in poverty alleviation has yet to be tapped (Coulibaly and Keita, 2001). In fact, the Interim PRSP is more a blueprint for further action than a preliminary attempt at defining a strategy. It develops a clear program for consulting with civil society, other sectors of the society, and donors, to determine their role in the development of the final PRSP. Some consultations were held in late 2000 and a final meeting was planned for February 2001. However, these meetings are meant to determine the role to be played by these various actors (i.e. it is preliminary to their direct involvement). Given the tight time frame for the development of a final PRSP (the expected completion date is June 2001), it is difficult to conceive of sufficient time for meaningful consultation. It is very likely that, at some point in the development of the PRSP, a choice will have to be made between effective consultation and delay in completion and superficial consultation in favour of deadlines.

The Interim PRSP does not propose the manner in which the debt relief dividends will be directed to poverty reduction, however, it does state that the National Directorate of Planning is responsible for managing the PRSP and the co-ordination of programming and monitoring of investments related to poverty reduction. Thus, unlike the case of Bolivia, a highly centralised implementation matrix is anticipated.

Nicaragua

Nicaragua has chosen to develop its poverty reduction strategy in three stages:

1. An intra-government consultative process through joint meetings of the economic and social cabinets;

2. Civil society participation through the National Council for Economic and Social Planning;
3. Meetings with donors, international organisations, and specialised United Nations agencies.

Table 4
Nicaragua: Short and Long Term Goals in the PRSP

National Goals	Short Term Targets (Year 2005)	Long Term Targets (Year 2015)
Poverty Reduction	Reduce extreme poverty by 25%	Reduce extreme poverty by 50% by 2015 with respect to 1995
Raising access to primary education by 90%	Increase net primary enrolment rate to 85% from 75% in 1999	Universal access to primary education
Reduction in maternal mortality rate	Reduce maternal mortality rate to 129 per one-hundred-thousand live births from 148 per one hundred-thousand born alive in 1999	Reduce maternal mortality rate by three-quarters by 2015 with respect to 1994
Reduction in infant and child mortality rate	Reduce infant mortality rate to 32 per thousand live births from 40 per thousand in 1998 Reduce mortality in children less than five to 37 per thousand live births from 50 per thousand in 1998	Reduce infant and under five mortality rates by two-thirds by 2015 with respect to 1994 levels
Access to reproductive services	Reduce to 25% by 2003, the unsatisfied demand for family planning among women with partners in the 15-19 age group from 27.1% in 1998 Reduce to 17.9 % by 2003 the unsatisfied demand for family planning among women with partners in the 20-24 age group from 19.7% in 1998	Provide Access to reproductive health for all individuals of appropriate age
Implement national strategy for sustainable development	Have the National Strategy for Sustainable Development implemented by 2005	Have a sustainable development strategy implemented by 2005
Reduce Chronic Malnutrition	Reduce chronic malnutrition in children under 5 to 13% from 19.9% in 1998	Reduce chronic malnutrition to 7% by 2015
Increase access to water and sanitation	Increase national coverage of access to water to 75.5% from 66.5% in 1999 Increase national access to sanitation to 50.2% from 36% in 1999 Increase access to sewage in urban areas to 47.3% from 33.6% in 1999	Increase to 100% national water coverage Increase to 87% national access to sanitation
Reduce Illiteracy rate	Reduce illiteracy rate to 17% by 2002 from 19% in 1998	Decrease illiteracy rates to 10% by 2015

Source: A Strengthened Poverty Reduction Strategy (Government of Nicaragua, August 2000).

The process remains top-down and has been roundly criticised by several civil society participants for its failure to include the poor and rural segments of the society (Castro-Monge, 2000). Though further community-level consultations are planned, it is not clear to what degree these consultations can lead to amendment of the present PRSP, where a clear set of goals and approaches have already been determined.

The Poverty Reduction Strategy that has been developed rests on four pillars:

1. Promoting economic growth;
2. Investing in human capital;
3. Developing a social safety net for the poor; and
4. Good governance and institutional reform.

From the consultative process, nine specific national targets and a number of indicators for the PRSP were generated. A monitoring and evaluation system (directed by the recently created National Council for Social and Economic Planning) will provide measurable information of progress, and will facilitate timely adoption of corrective actions. The long-term targets aim, at a minimum, to meet those set out as objectives by the OECD-DAC for the year 2015 (DAC, 1996 and OECD 2000), and are complemented by additional goals and targets that resulted from the consultations and reflect country-specific characteristics.

Project and program implementation is expected to take place through existing government structures, which remain very centralised. Thus, at least in the initial period, poverty reduction initiatives are likely to be highly centralised and top-down as well.

Opinions on conditionality between various sectors in Nicaragua are much the same as in Bolivia. Government officials, for example, strongly support the PRGF preconditioning as a means to a healthy economy. Surprisingly, however, the private sector views the PRGF-related conditions as biased against private investment and detrimental to competitiveness—the exact opposite of these programs' intent. This sector, like its counterpart in Bolivia, sees debt relief as a poor and inadequate substitute for a more effective solution to the debt problem: free access to Northern markets. Civil society representatives see the process largely as a performance put on by the government to meet conditions set by a donor community that is itself uncoordinated and inconsistent in meeting its stated responsibilities.

Uganda

Though Uganda's growth performance under its first two adjustment programs (1987-92) was good (the economy grew at an average rate of 5.7 percent), there was little evidence that the poor were benefiting from that growth. On the contrary, there was some concern that some of the policies related to these programs (particularly the ongoing policy of fiscal austerity) meant the loss or dilution of services commonly relied on by the poor. Thus, Uganda's third adjustment program was developed together with a concomitant Program to Alleviate Poverty and the Social Costs of Adjustment. However, Policy Analysts within the (then) Ministry of Planning and Economic Development¹², felt that this program was too limited and pushed for a more explicit and universal poverty reduction plan (Mijumbi, 2001). Their efforts, through the intervention of the President of Uganda, led to the establishment of a taskforce in 1996 which formulated Uganda's first Poverty Eradication Action Plan (PEAP) in 1997. The development of the PEAP

¹² This Ministry has since been absorbed into the Ministry of Finance.

involved a consultative process that involved extensive national debate and consultation with district authorities, line ministries, NGOs, academics, and donors.

Despite this extensive level of consultation, it was recognised, quite early on, that the process (of developing the PEAP) still retained an urban bias and did not involve the poorest of the poor (Asea and Makaka, 2000). As a result, a Uganda Participatory Poverty Assessment Program (UPPAP) was developed. The core activities of the UPPAP are Participatory Poverty Assessments (PPA) that attempt to determine, through a consultative process at the district level, the nature and causes of poverty at that level. The information and perspectives gathered are to be used to improve information on poverty at the district level and thus the planning of action aimed at poverty eradication (Asea and Makaka, 2000). One example of the usefulness of this approach has been the increased priority given to the provision of clean water because of the high priority given to that item by the poor themselves.

The Poverty Action Fund (PAF), another institution related to poverty reduction, was established by the government of Uganda in 1997 to direct savings from the HIPC initiative and other development assistance to poverty reduction while raising the profile of social sector expenditure, and ensuring transparency in the governments' poverty reduction efforts (Mijumbi, 2001). Transparency is ensured through the publication of PAF resources and the requirement that recipients of PAF resources publish the amounts received. Accountability is realised through audits of PAF funded programs by the Auditor General and quarterly review meetings involving all major stakeholders ranging from local government representatives and NGOs to donor agencies. The funds provided by the PAF are additional to that provided within the government budget, and five percent of these funds are allocated to programs and activities aimed at enhancing accountability and monitoring of the PAF.

The PEAP of 1997 was updated, through an even wider participatory process, into the PEAP 2000 which also stands in as Uganda's Poverty Reduction Strategy Paper. Like its predecessor, the PEAP 2000 has four main objectives:

- (i) Creating a framework for economic growth and transformation;
- (ii) Ensuring good governance and security;
- (iii) Directly increasing the ability of the poor to raise their incomes, and;
- (iv) Directly improving the quality of life of the poor (Mijumbi, 2001).

The overall poverty eradication strategy is guided by the following principles:

- Comparative Advantage - public sector intervention only to replace or improve poorly function markets or to improve equity;
- Efficiency - when it chooses to intervene, the public sector should use the most cost-effective method available;
- Partnership - poverty eradication should involve the closest possible partnership between the government and its development partners;
- Multifaceted - all government policies should reflect the importance of distribution, gender concerns, children's rights, and environmental impact;
- Planning - public action should be guided by the formulation of desired outcomes and the design of inputs and outputs to promote them.

It is anticipated that the PEAP 2000 will guide sector specific plans that will, in turn, form the framework for district plans. Thus, local authorities will ultimately be responsible for the implementation of the poverty reduction strategy with the necessary modifications to ensure that

it fits local conditions. However, as of early 2001, district plans were still in the early stages of development (Mijumbi, 2001). It is thus not clear whether district level planning and implementation in Uganda will have the autonomy that is implied in Bolivia's PRSP.

Table 5
Summary of Uganda's Poverty Action Fund (PAF) Budget
 (Billions of Ugandan Shillings)

	Actual		Projections	
	1999/2000	2000/2001	2001/2002	2002/2003
Directly increasing incomes of the poor	52.9	50.1	53.8	59.4
Rural roads	24.5	30.5	32.9	37.2
Land Act	3	3	3.3	3.7
Agricultural extension	6.1	6.3	6.8	7.7
Micro finance/restocking	19.3	10.3	10.8	10.8
Directly improving quality of life of the poor	268	371.1	410.4	486.3
Primary health care	28.2	51.1	70.1	92.1
Water and sanitation	17.4	37.6	39.5	44.6
Primary education	222.4	281.4	299.8	348.4
Adult literacy	0	1	1	1.2
Studies for implementation of PEAP	0	1	1.1	1.2
Other district grants	2	12	13	14.4
Accountability	11.3	15.7	17.2	20.3
Total budgeted expenditure	334.2	449.9	495.5	581.6

Source: Mijumbi (2001)

THE COST OF POVERTY REDUCTION

The increased attention paid to poverty reduction by debtor governments through the articulated Poverty Reduction Strategies is a clear consequence of having made debt relief conditional on poverty reduction. The insistence on this new obligation has also brought renewed focus to larger global objectives, such as the Organisation for Economic Co-operation and Development commitment to halving world poverty by 2015. The net effect of both these factors is that poverty reduction programs have more precise, better articulated, and more ambitious objectives than before.

What this means in terms of financing is that budgets for social programs will exceed current and historical levels. These programs have been promoted on the proposition that savings from debt service reductions—the debt dividends—will bridge the financing gap. However, since funding estimates are based on the nature of the poverty problem rather than available funding, there is little reason, *a priori*, to expect additional funding requirements to match debt service savings. Further, as has already been noted, the savings on actual debt service payments will be significantly less than the savings on *scheduled* debt service payments—implying smaller dividends than debt sustainability analyses suggest. Both these factors anticipate the likelihood of a financing gap for poverty reduction programs, and indeed there is evidence of this in the poverty reduction estimates presented for Bolivia, Mali, Ethiopia and Nicaragua.

Bolivia

As noted earlier, it is anticipated that Bolivia's Poverty Reduction Strategy will be implemented through municipal development plans. The average cost of five-year plans submitted so far is US\$6.692 million. Aggregated over 314 municipalities, the estimated total cost of the National Poverty Reduction Strategy will be US\$2,101 million or US\$636 million per year. Identified (potential) sources of funding and the ensuing deficit are shown in Table 4.

Table 6
Aggregate Annual Budget for the Municipal Development Plans of Bolivia
(2001-2005)

	US\$ Million	Percent (of costs)
Annual costs of MDPs (2001-2005)	636	100
Total funding for MDPs	527	83
Debt relief	159	25
Municipalities' own income	94	15
Regular transfers (not including debt relief)	204	32
Natural gas royalties	70	11
The Poverty Reduction Deficit	109	17

Source: Andersen and Nina (2001).

Note: Numbers are extrapolated to cover all municipalities.

Ethiopia

Though Ethiopia has not yet prepared a Poverty Reduction Strategy, Degefe (2001) used the approximate historical relationship between economic growth and poverty reduction to estimate the resource requirements for meeting poverty reduction targets in the coming years. He argues, in the first instance, that the OECD/DAC (OECD, 2000) and the Millennium Summit (UN, 2000) targets of reducing world poverty by half by the year 2015 are not realistic objectives at the domestic level in Ethiopia. The extent and depth of poverty in the country puts this goal out of reach. Taking a less stringent target of halving domestic poverty by the year 2020, his model suggests that it would require a per capita growth rate of at least 5.6 percent per annum over that period (assuming no change in income distribution). This level of per capita growth, given current population growth, would translate into an overall GDP growth requirement of 8.5 percent. Ethiopia's historical capital-output ratio suggests a corresponding investment requirement in the range of 40 to 44 percent of GDP per annum.

Setting aside the issue of absorptive capacity, this level of resource mobilisation is well beyond anything that Ethiopia has ever managed to achieve, and would still remain well beyond reach with even 100% debt forgiveness. As Table 6 below indicates, Ethiopia's savings rate during the 1990s was only 5.7 percent of GDP per annum, ODA amounted to 17.0 percent and foreign direct investment to 5.4 percent. These internally and externally mobilised resources (which actually or potentially contribute to investment), amount to only 28.1 percent of GDP—leaving a financing gap of 12 to 16 percent of GDP if the poverty reduction objective were to be pursued. Debt service payments have averaged only 2.6 percent of GDP in the 1990s. Thus the removal of the entire debt burden would only mean a saving of 2.6 percent of GDP and a reduction of the financing gap from 9.4 to 13.4 percent of GDP.

Table 7
Resource Mobilisation Levels in Ethiopia

Economic Aggregates	Percent of GDP
Gross Domestic Investment	14.8
Gross Domestic Savings	5.7
Official Development Assistance	16.0
Foreign Direct Investment	0.1
Total Debt Service	2.6

Source: Degefe (2001)

Though these figures are hypothetical, what they succeed in demonstrating is that the poverty reduction challenge that Ethiopia (one of the poorest countries in the world) faces, requires resources well beyond what can be mobilised through debt reduction. This limitation is magnified by the fact that Ethiopia has never managed to service more than a small fraction of its debt over that last decade (debt service averaged only 10.5 percent of debt service due from 1992 to 1998). Thus, even the most generous debt reduction offer would not provide the wherewithal for the degree of poverty reduction that is generally envisaged by current global objectives.

Mali

Mali does not yet have a costing of its Poverty Reduction Strategy but had, in fact, developed cost estimates for the much narrower *Stratégie nationale de la Lutte contre la Pauvreté* (SNLP). It was estimated that the sectoral projects anticipated by the strategy would cost US\$373 million over a period of five years. This would imply an average annual cost of US\$74.6 million. Given that the estimated (average) debt relief dividend for Mali in the first five years is only US\$25.8 million, debt relief alone would certainly not provide the necessary resources for funding such a program, despite the fact that it offers much less (and costs much less) than the final PRSP will.

Uganda

Uganda's PEAP admits to a current financing gap of US\$700 million. Government and donor spending on PEAP projects for the year 2000/01 was approximately US\$1,250 million. However, the planned activities will only cover a fraction of planned PEAP activities. If all planned activities were implemented, spending would need to increase to US\$1,950 million. This gap exists even after the debt relief dividend is accounted for.

Whether Uganda is able to bridge this funding gap over the next decade (and thus come closer to meeting poverty reduction targets) will depend on the performance of the economy over the next few years, the rate of increase in tax revenue, and the rate of growth in aid receipts. Table 8 below presents two scenarios (reflecting pessimistic and optimistic assumptions) and their implications for the funding gap. The low scenario (which assumes only modest GDP growth and the continuation of the current rate of increase in ODA receipts) would leave Uganda with a poverty funding gap of US\$661 million after five years and US\$191 million after ten years. The more optimistic scenario (which anticipates an increase in growth levels and a doubling of the rate of growth in ODA) would still leave Uganda with a funding gap after five years (of US\$455 million) but a surplus of US\$398 million after ten years. Thus, even with an acceleration of growth in both per capita income and ODA receipts, Uganda still does not expect to be able to meet the annual expenditure requirements of its poverty reduction program within five years. It hopes to do so in ten years only if the most optimistic expectations are met.

Table 8
Alternative Resource Mobilisation Scenarios for
Financing Poverty Reduction in Uganda

Condition	Low Scenario	High Scenario
GDP Growth Rate (%)	5.0	8.0
Annual Increase in Tax Revenue as a Percentage GDP	0.2	0.2
Rate of Increase in (Real US\$) ODA (%)	2.5	5.0
Expected New Resources in:		
5 years	353	559
10 years	824	1,412
Expected Financing Gap in:		
5 years	661	455
10 years	190	-398

Source: Mijumbi (2001).

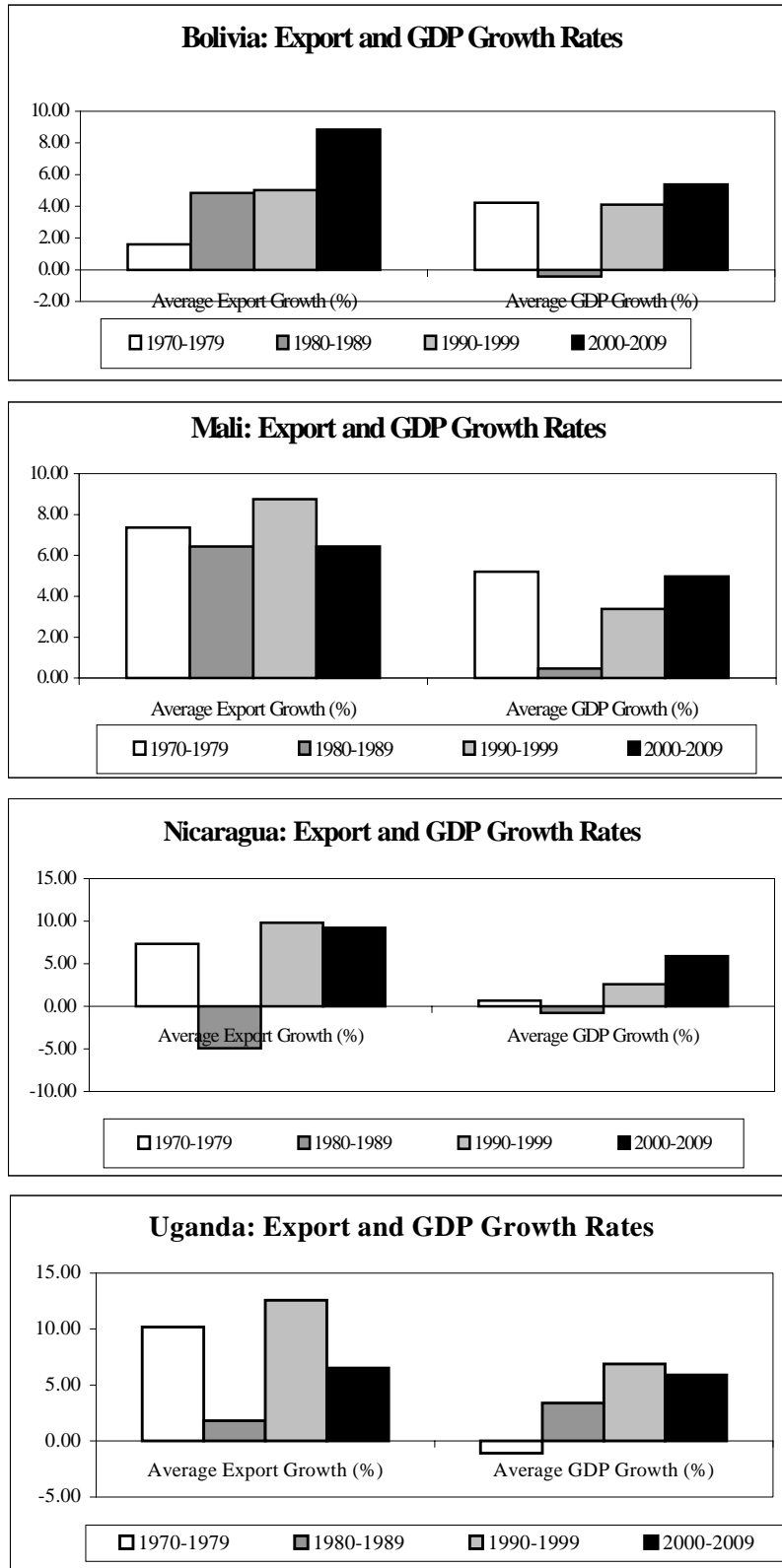
Note: Exchange rate used is 1700 Ugandan Shilling per dollar US.

DEFINING A POST-DEBT REGIME

It is clear from the country research evidence that, though HIPC debt relief will do less in terms of increasing budgetary space than the numbers might suggest, it will, nevertheless, significantly reduce debt service obligations, particularly in the first few years after the decision point. In fact, for the four countries for which debt reduction amounts have already been determined (Bolivia, Mali, Nicaragua, and Uganda), the average reduction in scheduled debt flows in the 2001-5 period is 46.6 percent and 40.8 percent in the 2001-15.¹³ However, the initial decline in scheduled debt service payments will be fleeting and debt service will resume its rising trend almost immediately. In fact, after a 26.1 percent drop in debt service in 2001, debt service payments are expected to increase at an average rate of 7.8 percent up to 2015 and beyond (see Figure 5). These countries will be expected to avoid a return to unsustainable debt levels only through rapid growth of both output and exports. The rate of growth in the real value of exports anticipated for Bolivia, Mali, Nicaragua, and Uganda for the first decade of debt relief (2000-9) ranged from 6.4 percent for Mali to 9.2 percent for Nicaragua. The rate of output growth anticipated ranged from 5.0 percent for Mali to 5.9 percent for Uganda and Nicaragua. These averages are similar to those anticipated for other HIPC countries past the decision point, but are exceedingly optimistic.

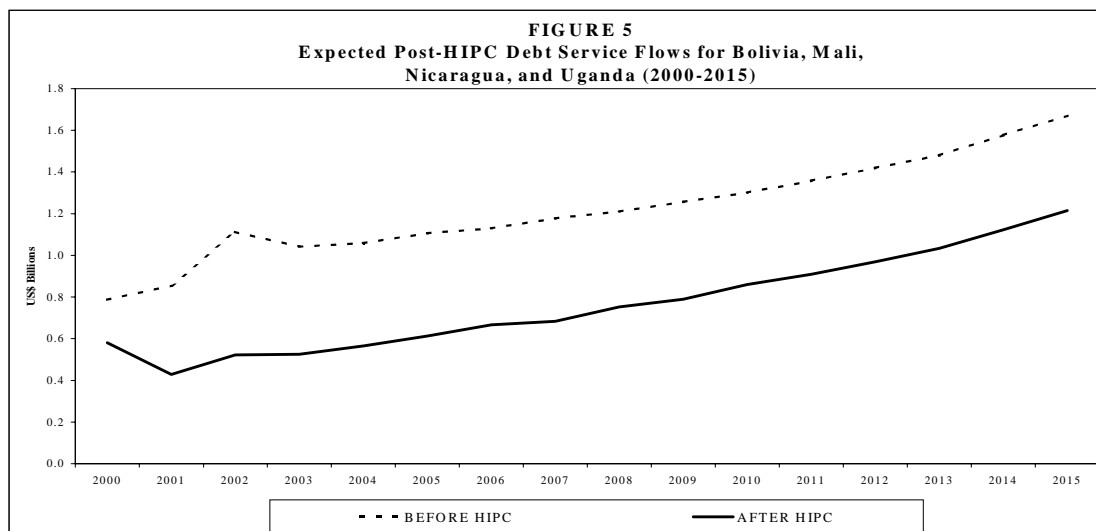
¹³ The base value is scheduled debt payments after the use of traditional debt relief mechanisms.

Figure 4



As Figure 4 clearly indicates, expected output growth rates are well above the average of the past three decades for all countries, and anticipated export growth exceed, or are close to, the highest level achieved over the last three decades for two of the four countries. While such high expectations (particularly for output) may not be unacceptable for a single country, extending such optimism to several countries invites victimisation by the fallacy of composition--several countries can be expected to replicate their best historic performances (or indeed surpass them) but it is extremely unlikely that the majority will. In short, the post-HIPC debt stock figures do not provide any great assurance that we may not again be faced with pervasive over-indebtedness among the poorest countries.

Source: Global Development Finance 2000 (World Bank).



What this serves to illustrate is that there are larger systemic issues here that are not necessarily addressed by the HIPC Initiatives. One clue to the underlying problem is the apparent negative correlation between economic status and debt status suggested by Table 9 below. In effect, a country is much more likely to be severely (or heavily) indebted if it is poor and/or among the least developed, than if it is an upper middle-income country. To put it more directly, debt flows, as a means of development financing, remain heavily biased against poorest countries. They are more likely to have difficulty meeting debt repayment obligations, and are thus more crisis-prone.

This proposition is not new. The deployment of the IMF's Enhanced Structural Adjustment Facility (now the Poverty Reduction and Growth Facility), the separation of the World Bank's more generous International Development Association's (IDA) lending window from the International Bank for Reconstruction and Development's (IBRD) window, and the move by OECD donor countries to provide more aid in the form of grants rather than loans, are merely formal acknowledgements of the fact that poorer countries simply cannot sustain borrowing at anything near market determined rates. However, universal application of this concept has been slow in evolving. The evolution of interest rates on official credit over the last 30 years (Table 8) clearly illustrates that. Interest rates on official credit to HIPCs rose during the 1970s and early eighties and have only fallen consistently (though rather gradually) since the late 1990s. The grace periods (before loan repayments become due) have, however, not shown an increasing trend. It is not at all clear that the current level of differentiation (in terms of degree of

concessionality) is sufficient. Nor is it a given that debt flows to vulnerable countries can be made independent of the larger global economic context. Even the most modest debt service levels may be problematic for a poor country facing a decline in its terms of trade.

Table 9
Average Interest Rates and Grace Periods on Official Credit for HIPC's

Period	Average Interest Rate (%)	Average Grace Period (years)
1970-74	2.5	7.8
1975-79	3.1	7.8
1980-84	3.6	7.2
1985-89	2.7	7.8
1990-94	1.9	7.8
1995-99	1.2	7.2

Source: Global Development Finance 2000 (World Bank)

The results of the country studies clearly indicate that the residents of those countries are acutely aware of the limitations of debt relief with respect to long-term economic growth and poverty reduction. Several ideas furthering these goals beyond the HIPC process have been brought to light by the country studies. The dominant proposal was for freer trade. In the view of many opinion survey respondents--particularly from the private sector--greater access to developed countries' markets held greater potential for long-term economic growth and poverty reduction than debt relief. One respondent in Bolivia even commented that he would support a return of debt relief funds in favour of greater market access. Related to this, was a Nicaraguan suggestion for an Export-led Poverty Reduction Program that would promote diversification, South-South trade, and rural development, by promoting small-scale non-traditional exports.

Table 10
Debt Status by Country Group

	% Severely Indebted	% Moderately Indebted	% Less Indebted	Total by Country Group
Least Developed Countries	59.1	22.7	18.2	100.0
Low Income Countries	54.0	30.2	15.9	100.0
Lower Middle Income Countries	20.0	27.3	52.7	100.0
Upper Middle Income Countries	9.7	29.0	61.3	100.0
All Low and Middle Income Countries	32.2	28.9	38.9	100.0

Source: Global Development Finance 2000 (World Bank)

More directly related to the nature of financial flows was a proposal for a High-Risk Trust Fund for Nicaragua, to be used to promote investment—akin to a similar fund used for Chihuahua State in Mexico. There were also proposals for more complete multilateral debt relief for Mali through debt swaps involving expatriate nationals, greater co-ordination of aid flows among

donors, and domestic control over the nature and extent of technical assistance to reduce potential negative consequences with respect to human capital development.

CONCLUSION

While the experiences of the five countries reviewed in this report cannot be unquestioningly generalised, they do provide some clues as to the range of likely experiences during the debt relief process, some perspectives on that process, and some likely outcomes. These countries' experiences undeniably differ, but there are several commonalities that can perhaps give us some perceptions of the present and future effectiveness of debt relief in general and HIPC in particular. Some of these are:

- The insistence on a link between poverty reduction and debt relief has been *operationally* useful. It has encouraged a greater focus on poverty reduction, and increased public sector spending on human development and poverty reduction at a faster rate than would otherwise have been the case. However, it remains *procedurally* problematic. There is an inherent tension between developing fully owned, indigenous, and inclusive Poverty Reduction Strategies and preparing PRSPs to meet perceived deadlines. There is already some evidence that the need for speed more often wins over ownership and inclusiveness.
- HIPC debt relief will effect significant reductions in scheduled debt payments, but its most significant impact will be limited to the next five years. After an initial decline in 2001, debt service levels will resume growth.
- Given increasing debt payment levels, it will require consistent export and output growth performances to avoid a return to overindebtedness. But these countries are heavily indebted precisely because they have never been able to sustain growth. It is not clear what will make the future different.
- The budgetary impact of debt relief—the debt dividends—will be significantly smaller than the size of debt relief flows and represents only a modest addition to development assistance. Thus even a modest decline in development assistance over the next few years could negate the net positive flow effect of debt relief.
- The new attention to poverty reduction engendered by HIPC has also generated budgetary requirements that cannot be fulfilled by HIPC flows. A substantial funding gap remains that needs to be addressed through other flows or more debt relief.
- Debt Relief can be part of, but is not by itself, a long-term solution to the problem related to non-autonomous North-South flows. The fact that the majority of least developed and poor countries fall within the HIPC group suggests that overindebtedness is neither purely self-imposed nor accidental. Without a more complete solution that addresses the modalities for delivery of development financing, HIPC debt relief may simply succeed in providing a respite between crises.

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Appendix 1 Country Profiles and Traditional Debt Relief Experiences					
	Bolivia	Ethiopia	Mali	Nicaragua	Uganda
Main Attributes					
Population (millions – 1998)	7.9	61.3	10.6	4.8	20.9
GDP per capita (US \$ - 1998)	1,087	107	254	418	324
GDP per capita (PPP\$ - 1998)	2,269	574	681	2,142	1,074
% of population below 1\$ a day ^b	11.3	31.3	72.8	3.0	36.7
Human Poverty Index (1998)	17.4	55.3	51.4	24.2	39.7
Rank	27	83	81	41	67
Average rate of growth 1990-98 (%)	4.2	4.9	3.7	4.1	7.4
Debt Situation (million US\$)					
Total external debt (1998)	6,077	10,352	3,201	5,968	3,935
Total Debt/Exports (%)	448	998	500	784	621
Debt/GDP (%)	71	158	119	297	58
Total debt rescheduled (1990-98)	1,461	416	93	3,943	484
Total debt reduction (1990-98)	1,173	359	454	5,328	342
HIPC debt relief (NPV equivalent)					
Original framework	448		128		347
Enhanced framework	854		401	3,267	656
Debt Relief Experiences					
Paris Club	Relief covering US\$2.3 billion from 1986-98: US\$1.3 billion cancelled and the rest (US\$1 billion rescheduled)	Relief covering US\$538m: US\$142m cancelled and the rest (US\$396m) rescheduled	Relief covering US \$230m from 1988-96. Cancellation of US \$413m in 1994	1991 - 50% NPV reduction (London terms); 1995&1998 - 67% NPV reduction (Naples terms)	Has signed agreements with all Paris Club members
Non-Paris Club	n.a.	n.a.	Rescheduling—China and ex-USSR. Cancellation—Morocco, former Yugoslavia, Germany and Qatar (CFA\$3,744 m)	1995-96: rescheduling and reduction from Mexico, Czech Republic and Russia (92% NPV reduction)	Rescheduling of arrears and current maturities with Rwanda and Tanzania
Commercial debt buyback	Concluded in May 1993 at 84% discount. Principal extinguished: US\$170m	Concluded in January 1996 at 92% discount. Principal extinguished: US\$226m		Concluded in December 1995 at 92% discount. Principal extinguished: US\$1099m	Concluded in February 1993 at 88% discount. Principal extinguished: US\$153m.

a Bolivia Data refers to 1996

b Bolivia (1990), Ethiopia (1995), Mali (1994), Nicaragua (1993), Uganda (1992)

**Appendix 2: A Study of the Debt of the Poorest Countries:
A North-South Institute Project**

Implementing Institution: The North South Institute, Ottawa, Canada

Objectives: The examination and analysis of issues pertaining to the debt problems of the poorest countries—with particular reference to the HIPC Initiatives and the perspectives and experiences and experiences of debtor countries—with a view to engendering dialogue among relevant actors.

Research Output:

Reducing the Debt of the Poorest: Challenges and Opportunities.

Serieux, John

The North-South Institute (November, 1999)

Study of the Debt of the Poorest Countries: The HIPC Initiative in Bolivia.

Andersen, Lykke E. & Nina, Osvaldo

The Canadian Journal of Development Studies, Vol. 22, No. 2 (June, 2001)

Ethiopia's External Debt: Impact and the way Forward.

Degefe, Befekadu

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Nicaragua and the HIPC Initiative, the Tortuous Journey to Debt Relief

Castro-Monge, Ligia Maria

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Étude sur l'endettement des pays les plus pauvres - Le cas du Mali.

Massa Coulibaly, Amadou Diarra, and Sikoro Keita

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Uganda's External Debt and the HIPC Initiative

Mijumbi, Peter

The Canadian Journal of Development Studies, Vol. 22, No. 2 (June, 2001)

The HIPC II Initiative from a Developing Country Perspective: Uganda Case Study

Asea, Patrick K. and Andrew Makaka

The North-South Institute (August, 2000)

Debt of the Poorest Countries: Anatomy of a Crisis Kept on Hold

(February, 2001)

Serieux, John

The Canadian Journal of Development Studies, Vol. 22, No. 2 (June, 2001)

A Non-structural Response to a Structural Problem: Putting the HIPC Initiative in Perspective

Serieux, John

The Canadian Journal of Development Studies, Vol. 22, No. 2 (June, 2001)

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