

AFRODAD

The Heavily Indebted Poor Country (HIPC) Initiative

Experiences of implementation in Africa

By Barbara Kalima - 3/13/03

Introduction

With the very high expectations of meeting the Millennium Development Goals (MDGs) by 2015, one of the creditor-designed debt relief initiatives – HIPC, launched in 1996 by the IMF and World Bank, has failed to achieve the promised objective of a “robust exit from the burden of unsustainable debts” for developing countries. As a potential source of development finance, the debt relief through HIPC is not sufficient to guarantee poverty reduction in these countries let alone meet some of the goals of the MDGs. An analysis of key debt indicators shows that external debt and debt-servicing problems and poverty have become most severe and persistent in the heavily indebted poor countries, the so-called HIPC.

Throughout the process, creditors have failed to put sufficient political will, resources and serious analysis into the debt reduction operations. Debt reduction targets have been set and reset arbitrarily rather than based on serious assessments of the needs of each country. Despite claims of success by creditors for debt reduction under the HIPC initiative, the IMF estimated that Africa's debt service payments would only go as low as 17.1 percent of export earnings in 2001 (down from 20.3 percent in 1999), before rising again to 18.4 percent in 2002. This is still economically crippling! Most of this debt is owed to the World Bank and the IMF. But neither the international financial institutions nor the rich creditor countries have given any indication that they were willing to consider more than marginal adjustments to the HIPC initiative.

The process has been much slower than expected and the initiative is suffering from problems of under-funding, excessive conditionality, and restrictions over eligibility, inadequate debt relief and cumbersome procedures.

Key experiences of implementation in Africa

Unsustainability of Africa's debt - The 22 African countries that have so far qualified to receive some relief under HIPC are still required to pay almost \$2 billion each year in debt repayments to wealthy creditor countries and institutions, mainly to the World Bank and IMF themselves. African countries' efforts to address urgent domestic priorities, from poverty reduction to the fighting of HIV/AIDS, continue to be undermined by their persistent debt burden. Most African governments still spend up to three times more on debt repayments than on health care and education combined. Not only are some countries spending more on debt payments after they receive debt relief, but they are also overshooting the World Bank and IMF own definitions of debt sustainability.¹

Uganda, the first HIPC graduate, currently has debts of over 200% of the debt-to-exports ratio. This will be the third time Uganda has exceeded its debt sustainability after reaching Completion Point. Surprisingly, the World Bank and IMF have changed definitions of debt sustainability to include liquidity as the operative criterion. Uganda has conformed to rigid economic conditions

¹ Africaaction, A Critique of the HIPC, www.africaaction.org, June 2002.

imposed by these institutions for ten years and urgently needs financial breathing space. One child in five dies before reaching age 5 in Uganda, yet the government spends \$3 per person on health and \$17 per person on debt repayments. The Ugandan government has anticipated debt relief from HIPC in its current budget plan to be allocated to primary education. Without the promised debt relief it is estimated that 1.7 million children may be sent home from school².

Ethiopia, for example will have its total debt stock reduced by 47% at completion point this year, the benefits of this relief will be felt through reductions in debt service only in the short run. Yet, in the long run, even after HIPC assistance, Ethiopia's debt service will remain high - more than \$74 million per year for the next twenty years, and more than \$100m from 2004/05 onwards, absorbing roughly 5% of government revenues.

In Burkina Faso, it is anticipated that the HIPC initiative will bring down its existing external debt value to below the HIPC sustainability threshold of 150% of exports; its total debt will remain between 180% and 190% of its exports until beyond 2015³. The country still has some of the worst human development indicators, with 45% of its population living below the poverty line and a life expectancy of 46.1 years.

The amount of debt relief released from HIPC is not sufficient to put a country on a sustainable path to debt reduction. There is a need to reverse this form of resource transfer from the South to the North if poverty has to be seriously eradicated.

***HIPC initiative's policy contradictions** - There is no correlation between debt relief and poverty reduction; the two derive from separate motivations. Debt relief is supposed to reflect the repayment capacity of poor countries while there is little evidence that poverty reduction as addressed in the Millennium Summit Declaration explicitly relates to debt relief.*

Since the start of the HIPC process in most of the poor countries, their industrial base has shrunk even further (de-industrialisation). The policy prescriptions under HIPC have negatively affected economic growth, threatened the sustainability of reforms, and prevented the development of a capable and functioning state due to the fiscal crisis that they engender.

In Tanzania, factories that were privatised have been working at lower capacity with fewer staff and a number of them have closed down. One example is the textile industry that was once a flourishing industry that has now completely collapsed. The initial assumption of job creation through privatisation has not proven to be realistic. Privatisation has not really broadened the revenue base through increase in taxes. It has rather meant massive retrenchments and more suffering for the ordinary Tanzanians. A growing income gap, galloping inflation, sky-rocketing prices of basic commodities, illiteracy, diseases such as HIV/AIDS and malaria, and natural disasters have also contributed to Tanzania's poverty.

Tanzania's debt has also increased rapidly from US\$2 257 million in 1980 to more than US\$5 billion at the beginning of the 1990s.⁴ Although Tanzania is spending more on education than on debt service, its budgetary allocation for health is less than what it is paying back to creditors⁵. This has serious implications, particularly for a country where 40% of the population dies before

² Halifax Initiative, Update and Action Alert. March 2002.

³ Jubilee 2000 Research: Profile Burkina Faso Analysis.

⁴ Mwanza, 1991 SAPEM vol 4 No. 9. p18

⁵ Melly.P. and Ette. M. (2001) Debt Relief in News Africa magazine, March 12, 2001.

the age of 35. In April 2001, several donors under the guidance of the Bretton Woods institutions asked Tanzania and many other African countries to prepare a Poverty Reduction Strategy Paper (PRSP), which is based on policy prescriptions, contained in Structural Adjustment Programmes.

Exclusion of other eligible countries - According to the UN Secretary General's report of 2000 there are 18 least developed countries that are not included in the HIPC category, and some of them are considered severely or moderately indebted according to the World Bank classification. For instance, most of the debt-distressed African countries are classified, as moderately indebted middle-income countries such as Zimbabwe while Gabon and Nigeria are both severely indebted yet excluded from the HIPC initiative⁶. The criteria by the Fund and Bank to classify countries as low, middle and /or high income have not succeeded in providing real solutions to the debt problems in these various countries simply because their definitions are purely based on economics.

HIPC ignores the illegitimate debt issue - The HIPC Initiative obfuscates the illegitimacy of most of Africa's debt thereby fundamentally undermining the strong imperative for debt cancellation. It sanctions the continued exploitation of indebted countries by rich creditor nations and institutions. Many of the loans that are being re-paid were made during the Cold War to repressive regimes and corrupt leaders, who used the money to strengthen their power or to fill their own pockets. Many more loans were made without attention to the viability of planned projects or to the capacity of the recipient country to make repayments.

No foreign loan granted to South Africa during the apartheid years could have been legitimate because the apartheid state was immoral; and any attempt to claim ignorance of this fact would not be credible.

Lack of Creditors' commitment - In most cases multilateral creditors have failed to provide sufficient relief and have thus violated 'the burden of sharing' approach to the HIPC initiative. For example Burkina's completion point document shows that when calculating the additional relief to be provided, the World Bank and IMF included the additional bilateral conditions committed by creditors such as the UK, US, Germany and France, openly violating 'the burden of sharing' approach⁷.

The experiences outlined above show serious flaws in the implementation of HIPC in Africa. We have the issues of a) unsustainability of debt, which has propelled and permutated other socio-economic problems; b) the policy contradictions in the HIPC initiative which are more poverty and debt creating than they would be for achieving the MDGs; c) lack of creditor commitment to burden sharing and d) insufficient debt relief through HIPC which undermines the strong imperative for debt cancellation when considered under the illegitimacy of the debt.

Conclusion

In an attempt to implement the Monterrey consensus, it would be important to consider that the solutions to tackle the debt crisis must move beyond debt relief and conditionality, to consider debt within the wider context of equitable and sustainable development. It should address socio-economic and developmental relations between debtor and creditor countries. If global efforts to

⁶ UN A/55/422 General Assembly 26 September 2000

⁷ Halifax Initiative, Update and Action Alert. March 2002.

reduce poverty as stipulated in the MDGs are to succeed, third world's debt must be cancelled outrightly and unconditionally.

In addition, a fair and transparent arbitration mechanism on debt must be established within the UN in order to seek redress of illegitimate debts for these countries.

Reform of the international strategy regarding official debt of poor countries should address the problems of debt distressed low-income countries that are not currently eligible for special treatment accorded to the HIPC.

Third world governments should be given the chance to determine their own approaches to poverty reduction, in consultation with civil society groups and other partners - not to have such forms of participation prescribed to them by external powers as is currently evident under PRSPs. Civil Society's participation in the PRSP process in Africa has been necessary and meaningful but not sufficient to guarantee effective policy change that would make a significant difference in the lives of the poor people. Instead, the call for civil participation by the Fund and the Bank has merely increased conditionality.

It is well understood that the economic policy conditions attached to the HIPC process mirror the same prescriptions that have been imposed by the World Bank and IMF on African countries for the past two decades through SAPs, with their disastrous results. There must be a delinkage between debt relief and PRSPs and HIPC, otherwise the policy conditions enshrined in these initiatives will continuously undermine Africa's efforts to prioritise and develop initiatives that take into account the peoples local aspirations and needs.

The political and economic motivations for creditors to give loans must be seriously examined at the global level. Debt has continued to be used by creditors as an instrument of domination of the South by the North. Debt relief granted through HIPC has been more successful in protecting the interests of creditors than those of debtors, particularly in terms of re-financing of loans.

Input into the UN FfD Follow-up to Monterrey – NGO/ECOSOC Hearings: Coherence and Coordination in Development Finance – 20th March 2003, New York.