

## **ECOSOC - NGO DIALOG on FFD Follow up** **Coherence and Coordination in Development Finance**

*“Future reviews of debt sustainability should also bear in mind the impact of debt relief on progress towards the achievement of the development goals contained in the Millennium Declaration.”*

**Monterrey Consensus of the International Conference on Financing for Development - March 2002 [pa 49]**

This short issues paper argues that: the international community is now being faced with a stark choice between either ensuring low-income countries achieve the Millennium Development Goals or adhering to the World Bank and IMF’s notion of debt sustainability as set out in the *Heavily Indebted Poor Country* (HIPC) Initiative. It calls for a recasting of official debt sustainability to take account of the resourcing needs required to enable countries to achieve internationally agreed poverty reduction goals as set out in the UN’s Millennium Declaration. Without such a change to criteria in current debt sustainability analyses, a large group of countries – including most of sub-Saharan Africa – will miss the Millennium Development Goals (MDGs) altogether.

### **Some benefits of enhanced HIPC Initiative**

Before setting out how we have arrived at a choice between pursuing current HIPC debt sustainability objectives or meeting the MDGs, it is worth taking a brief look at what HIPC is achieving.

As a result of the HIPC framework:

- Social spending in HIPCs is estimated to have risen by between 20-50%;
- Mozambique has introduced a free immunisation programme for children;
- User fees for primary education have been abolished in Uganda, Malawi and Tanzania, as have fees in rural areas of Benin;
- Mali, Mozambique and Senegal are due to increase spending on HIV/AIDS prevention;
- Uganda and Mozambique, among the early beneficiaries of debt relief and enhanced aid flows, have consistently sustained annual GDP growth rates over 5% and, in some periods, up to the 7% growth reckoned by the UN’s ECA as necessary to reducing by half the number of people living in absolute poverty;
- The requirement to engage in a consultation process in designing Poverty Reduction Strategies has helped to increase the potential for poor people to influence national resource allocation processes.

While the HIPC Initiative has made some advances in increased social sector spending, these are highly precarious and modest gains when set against the scale of human development challenges facing low-income countries.

For example, in Zambia, the Government there will have to increase by a third the number of primary school teachers just to make up for those dying with HIV/AIDS. Zambia faces this mounting disaster at the same time as the HIPC Initiative’s debt servicing regime is set to increase, rather than decrease, its debt repayments.

For many, if not all, HIPC countries, the twin objectives of achieving a notionally sustainable level of debt repayments and pursuing poverty reduction goals are mutually exclusive – and this stems from the failure at the heart of the HIPC initiative,

to finance poverty reduction strategies and, at the same time, to produce “a robust exit from the burden of sustainable debt.”

### **HIPC’s failings**

Amongst the HIPC’s initiative other failings are:

- The non-participation of some creditors will mean that 20 out of 26 HIPCs will never reach debt sustainability.
- Even assuming full creditor participation, 5 countries will be paying about the same and 4 will actually be paying more than when they first entered the HIPC Initiative.
- The continuing commodity price slump will mean that 14 out of 24 countries will be unsustainable again in the medium term.
- And the post-Completion Point “topping up” facility will not produce a radically changed sustainability outcome. Burkina Faso, the first country qualifying for topping up, will not reach sustainability until the year 2016!

These poor outcomes stem from the central weakness of the HIPC Initiative, that is: its over-reliance on an inappropriate debt-to-export sustainability criterion – one that has no financing linkages with HIPC governments’ poverty reduction obligations or objectives.

HIPC economies are characterised by a high concentration of exports in one or two commodities. As a result they have been vulnerable to the vagaries of rain-fed agricultural production and the slumps in commodity prices. Exports are highly volatile variables and, as such, poor indicators and predictors of short term, let alone, medium term debt sustainability.

But there is an added argument for debt sustainability analyses to be reshaped around a broader set of human development objectives. At this moment, the international community is at crossroads in the provision of development finance for low-income countries. It faces a choice between the pursuit of HIPC’s faulty conception of debt sustainability or achieving the MDGs. The problem is exemplified by the recent cases of Rwanda, Niger, and Ethiopia. These three countries have poverty reduction strategies that official donors are keen to fund and need to be funded if they are to meet the MDGs. The problem is that to do so, with current sources of development finance, will take these countries above their notional debt sustainability thresholds.

While the level of grant aid available for supporting governments’ budgets remains relatively small as a proportion of total flows, those countries are required to finance their poverty reduction plans with new loans. But even with additional flows from the most concessional forms of finance available to these countries – the World Bank’s IDA facility – they will not be able to fund their poverty reduction strategies without overshooting their sustainability thresholds.

So the choice we are faced with in these cases – and a further cluster of countries will soon be faced with the same dilemma – is that either HIPC’s conception of debt sustainability is maintained or they benefit from the donor inflows necessary to meet the MDGs.

### **Alternatives**

We argue that the HIPC Initiative needs to recast sustainability criteria around an alternative set of sustainability, or payability, criteria. If we accept that the “gold

standard” of international development cooperation is the achievement of the Millennium Development Goals, then debt sustainability analyses need to include some analysis of the relationship between the goal of debt sustainability and broader poverty reduction goals. At present, the Bank and Fund are attempting to pursue the elusive objective of a purist notion of debt sustainability with absolutely no assessment of the finance required to meet poverty reduction goals or the MDGs.

If the international community – and Bank and Fund – are to be taken seriously in their stated desire to see HIPCs achieve the MDGs, then, we would argue, all financial and development instruments should be made coherent with analyses of the resources required to achieve those goals. We would argue that assessments of the level of sustainable debt repayments should view debt servicing as a residual obligation after financing needs for poverty reduction have been taken care of. It is not acceptable to argue that payable debt servicing levels are separate from social and economic objectives established within those countries.

In other words, debt sustainability analyses need to be expanded into poverty reduction sustainability analyses, where the financing needs of countries are examined in relation to their attaining the Millennium Development Goals and with assessments of how to mobilise such financing. If debt sustainability analyses do not include the full range of MDGs, then there needs to be at least some analysis of the relationship between resources released from debt servicing obligations and the impact that this will have on key goals, such as the GDP growth rates needed to halve poverty.

According to CAFOD’s preliminary calculations, with 100% debt cancellation for all low-income countries in Africa\* – 8 HIPCs would be in a position to achieve the 7% growth rates the UN’s Economic Commission for Africa reckon is needed to halve the numbers of people living in absolute poverty. It is precisely this calculus that needs to be factored in to analyses of sustainable debt burdens.

Under current criteria, it is theoretically possible for countries (whether HIPCs or MICs) to achieve sustainable debt burdens while not having a single cent for poverty reduction. To us, this is nothing less than an abuse of the term of “sustainability”.

Henry Northover – CAFOD/CIDSE  
March 2003

---

\* According to the NEPAD Secretariat’s assessments this would cost only \$6 bn spread over 5 years.