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All Party Parliamentary Group on Overseas Development

Africa's Multilateral Debt: A Modest Proposal

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Overseas Development Institute

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List of Abbreviations

AfDB	-	African Development Bank
AfDF	-	African Development Fund
CCFF	-	Compensatory and Contingency Financing Facility
DRF	-	Debt Reduction Facility
ESAF	-	Enhanced Structural Adjustment Facility
ETT	-	Enhanced Toronto Terms
FSU	-	Former Soviet Union
GDP	-	Gross Domestic Product
GNP	-	Gross National Product
GRA	-	General Resource Account
HMG	-	Her Majesty's Government
IBRD	-	International Bank for Reconstruction and Development
IDA	-	International Development Association
IFC	-	International Finance Corporation
IFI	-	International Financial Institution[1]
IMF	-	International Monetary Fund
LDC	-	Less Developed Country
NGO	-	Non-Governmental Organisation
NPV	-	Net Present Value
oda	-	Official Development Assistance
ODA	-	Overseas Development Administration
OECD	-	Organisation for Economic Cooperation and Development
RAP	-	Rights Accumulation Programme
RDB	-	Regional Development Bank
SAF	-	Structural Adjustment Facility
SDR	-	Special Drawing Rights
SILIC	-	Severely Indebted Low Income Country
SIMIC	-	Severely Indebted Middle Income Country
SPA	-	Special Programme of Assistance (Low Income Africa)
UNCTAD	-	United Nations Conference on Trade and Development

[1] In the context of this inquiry International Financial Institutions consisted of the World Bank, the International Monetary Fund and the African Development Bank.

Acknowledgements

In the course of our inquiries, under the chairmanship of Bowen Wells MP, the Working Party has received evidence from ministers of Her Majesty's Government, representatives of the multilateral institutions, the academic world, non-governmental organisations and the debtor governments themselves. Briefings were held in the House of Commons throughout March, April and May 1994. We are grateful to all who assisted in the inquiry for sharing their perspectives and insights on the sub-Saharan African debt issue, upon which the arguments and conclusions contained in this report are based. We also thank Robert Willis of the Overseas Development Institute for providing research assistance throughout the inquiry and for drafting this report, Charles Kenny for additional assistance and Adrian Hewitt for his role as Research Adviser to the Group.

Box 1: Membership of the Debt Working Party

Bowen Wells	Conservative (Chairman)
John Denham	Labour
Jim Lester	Conservative
Peter Luff	Conservative
Mike Watson	Labour

Box 2: List of Persons Consulted

9/12/93	Ron Johannes, principal author of World Debt Tables 1993/94, World Bank
	Julian Grenfell World Bank
24/1/94	Ken Yagi Director, Development Policy Division, Japanese Ministry of Finance
	Yoshihiro Ikeda Chief, Development Policy Division, Japanese Ministry of Finance
1/3/94	H.E. Alhaji Abubakar Alhaji High Commissioner for Nigeria and formerly Minister of Finance
8/3/94	Matthew Martin
	John Williamson Institute for International Economics
15/3/94	Carolyn Culey Policy Adviser for the Reactive Team and Parliamentary Officer, Oxfam
18/3/94	Susan George Author, *The Debt Boomerang* and *A Fate Worse Than Debt*
22/3/94	Ishrat Husain Chief Economist, Africa Regional Office, World Bank
	N. Susungi Resident Director of the European Office, African Development Bank
12/4/94	Baroness Chalker Minister for Overseas Development
13/4/94	Anthony Nelson MP Economic Secretary to the Treasury
18/5/94	Jack Boorman Head, Department of Policy Review and Development, International Monetary Fund

Introduction

Many sub-Saharan African countries are presently burdened with volumes of external debt they can ill afford to service. Many of the continent's indebted countries are paying more to external creditors than they are spending on domestic public services, and as a consequence social conditions faced by large numbers of Africans are at best stagnating, and in many regions deteriorating. Excessive debt service obligations are threatening the economic prosperity of a substantial number of sub-Saharan African countries, with shortages of domestic capital and foreign exchange impeding the implementation of programmes of economic reform, in turn discouraging inflows of foreign direct investment and resources. As a result, over recent years a substantial proportion of Africa's population have experienced frozen or declining per capita incomes, with the associated poverty, malnutrition and famine emerging as major problems throughout the continent. In addition the inability of many countries to service their external debt stock is also exerting pressure on an already fragile international economy, and in many cases threatens to disrupt diplomatic relations between debtor and creditor nations.

The problems associated with developing country debt are by no means new; the 1980s saw a widespread emergence of countries unable, or unwilling, to honour obligations to creditors, and intense publicity of the hardships and poverty which typically accompanied excessive debt burdens increased worldwide public and political awareness of the difficulties faced by indebted Third World countries. The result was a mobilisation of industrial country resources in an attempt to reduce the debt burdens of some of the most severely indebted developing countries. But whilst many of the efforts assisted the indebted countries of Asia and Latin America, and have encouraged a revival in international investor confidence and the corresponding inflows of foreign direct investment, the situation in a number of sub-Saharan African countries has continued to deteriorate. In initially examining the factors underlying the continued debt dilemma faced by many sub-Saharan African countries, it has become clear to the Working Party that the majority of Africa's external debt is owed to official creditors, and that of these the multilateral institutions are playing a major role as distributors of additional funds, instigators of programmes of economic reform and recipients of large volumes of debt service payments.

This Debt Working Party therefore resolved to examine the issue of sub-Saharan African debt, concentrating on the role of the multilateral institutions as substantial creditors of severely indebted low and middle income countries in this region. Particular attention has been paid to identifying debt-related problems which have resulted from the stance adopted by the International Financial Institutions (IFIs) in approaching debt relief, and possible measures which should be implemented to attempt to resolve the overall debt dilemma of sub-Saharan African countries. In addition the role of bilateral creditors in both contributing to and alleviating the debt burdens of African countries has been examined, concentrating on the activities of Britain within the international donor community, and where possible conclusions in the form of policy prescriptions have been made.

Summary

Introduction

Despite the measures implemented by the international community to alleviate the Third World debt crisis of the 1980s, which overall have proved very successful in addressing the debt-related problems of many Asian and Latin American countries, a large number of sub-Saharan African countries continue to be faced with volumes of external debt they can ill afford to service. Large proportions of African debt are owed to official creditors, with the multilateral financial institutions occupying a prominent role. The All Party Group On Overseas Development (APGOOD) has therefore resolved to examine the issue of sub-Saharan African debt, concentrating particularly on the activities of the multilateral institutions as major creditors of severely indebted low and middle income countries in the region, and to make recommendations for action to address this problem. This report sets out the findings and conclusions of the inquiry.

Method

Towards the end of 1993, APGOOD asked its members to form a Working Party. Between December 1993 and May 1994, the Working Party held discussions with Ministers of Her Majesty's Government, representatives of the multilateral institutions, the academic world, non-governmental organisations and debtor African governments.

Results and Findings

Over the late 1980s large flows of private foreign investment returned to the indebted countries of Asia and Latin America, encouraged by the success of policies of debt relief in reducing external debt burdens and fostering the consequent economic growth. This has not occurred in the majority of sub-Saharan African countries. Declining commodity prices, in many cases combined with irresponsible government policies and difficulties with development assistance, have led to economic stagnation. Public debt service obligations are still absorbing large proportions of government revenues.

Official creditors have been slow to introduce measures of debt relief, and in the case of multilateral institutions have refused to implement programmes of debt reduction and/or official rescheduling. Bilateral creditors, independently and through the operations of the Paris Club, have succeeded in reducing the burden of outstanding bilateral debt on the poorest countries, but much of the resulting benefit has been swallowed by growing debt service obligations to multilateral institutions. Although the bilateral creditors have made a move in the right direction in terms of Paris Club debt reschedulings, the Working Party concludes that the Enhanced Toronto Terms (ETT) are insufficient to resolve the bilateral debt-related problems of many sub-Saharan African countries, and the effectiveness of the Paris Club activities should be increased by incorporating debt stocks as well as debt service obligations in the negotiations.

Nevertheless, the primary emphasis must now rest on the multilateral institutions to review their approach in dealing with indebted African countries.

In insisting on their role as 'preferred creditors' in sub-Saharan Africa, the multilateral institutions have exerted an additional burden on bilateral donors as well as on the debtor governments themselves. Many financially distressed countries are choosing to default on interest and repayments owed to the bilateral creditors in order to remain current with the International Financial Institutions (IFIs). Thus far this situation has been supported by the majority of bilateral creditors, but the Working Party has concluded that patience amongst donor governments is now beginning to wear thin.

When providing debt relief, the multilateral institutions have primarily relied on programmes of concessional lending, often refinancing outstanding non-concessional debt stocks. The concessional lending of the World Bank, via the IDA, has been praised, whilst that of the IMF, via SAF and ESAF, has been criticised for incorporating exceptionally rigorous conditionality with short term repayment schedules. However, it is felt that an adapted ESAF would have a valuable role to play in assisting economic reform and addressing the debt-related problems of sub-Saharan Africa. On the other hand, the negative flow of resources from the IMF during a Rights Accumulation Programme has been questioned for impeding the essential structural reform process and applying pressure on bilateral creditors to assist the indebted developing country.

In funding their concessional lending facilities, the multilateral institutions have placed a considerable emphasis on using finance contributed by member countries, and the Working Party feels that this again imposes an exceptionally high burden on bilateral aid budgets and should therefore be reviewed. In particular the claim by many multilateral institutions that they are already implementing substantial programmes of debt relief via their concessional facilities should be viewed critically in light of the primary role played by bilateral donors in supporting these facilities.

The Working Party feels that the AfDB should listen to criticism suggesting it should stop lending non-concessional finance to the poorest sub-Saharan African countries, since this has been worsening their long term prospects of economic prosperity. The activities of the AfDB require attention immediately. Further difficulties with the Bank would result in the imposition of further hardship on debtor African countries. Steps should be taken to avoid this.

Overall the Working Party has concluded that the efforts of the multilateral institutions in addressing Africa's debt crisis are currently inadequate, and that the need for increased volumes of debt relief, including debt write-offs and rescheduling, is now imperative. This study has found the credit rating and moral hazard arguments proposed by the multilateral institutions in defending their opposition to debt write-offs to be invalid. It has identified substantial reserves which the World Bank and the IMF hold and which could be used effectively in financing additional programmes of debt relief without detriment to the ongoing operations of the respective institution. It is therefore time for the multilateral institutions to follow the lead set by commercial and bilateral creditors in accepting a share of the burden of resolving the sub-Saharan African debt crisis.

Recommendations of the Working Party

The Multilateral Institutions

The Working Party concludes that the multilateral lending institutions should now relax their stance on according debt relief and should consider implementing measures of debt rescheduling and debt reduction for the most severely indebted developing countries in Africa.

In particular the Group recommends that the multilateral institutions join bilateral and commercial creditors at a debt management forum, allowing indebted low income countries to discuss their total external debt stocks, and where the burden of relief could be distributed equitably between creditors.

The Bretton Woods institutions should be pressured to mobilise greater volumes of their own resources in funding their concessional lending facilities (which need to be expanded in size and scope) and additional measures of debt relief. They should join member governments in assisting the AfDB in resolving its current financial crisis. The World Bank could achieve this by using its large financial reserves, and the IMF has the option to sell a proportion of its gold stocks held in the USA (the Working Party concludes that the sale of only 3–4 per cent of IMF gold stocks would allow the Fund adequate finance to implement additional measures of debt relief and concessional lending for all sub-Saharan African SILICs, as well as assisting the AfDB).

The IMF should review the operations of ESAF, taking note of the needs of sub-Saharan African countries, and volumes of concessional lending should be increased to ensure the Fund maintains a positive net flow to sub-Saharan Africa as a whole. In addition positive flows should be maintained to countries undergoing RAPs, increasing the likelihood of successful reform and reducing pressure on bilateral donor aid budgets.

In a similar fashion to programmes of structural reform, the granting of debt relief should be made conditional on recipients adopting rational and responsible domestic policies, with particular attention being paid to expenditure on defence and prestige projects. Responsibility for the emergence of the African debt problem lies partly with the African governments, which in many cases implemented extravagant and misguided policies utilising borrowed funds, and correspondingly responsibility for finding a resolution to the problem must also partly rest with the African governments. Negotiations on debt relief between multilateral institutions and debtor governments should therefore embrace the processes of democratic and economic reform.

We believe that programmes of debt relief and concessional funding should be granted on a case-by-case basis. In addition, the social impact of such programmes should be accounted for throughout the processes of identification, planning and implementation.

Eligibility to the concessional facilities of the Bank and the Fund needs to be extended to include Severely Indebted Middle Income Countries (SIMICs). Also contingency provisions need to be implemented to allow debtors relief from debt repayment under certain unforeseen circumstances.

Both the IMF and the World Bank should adopt 'roll-over' provisions, allowing the rescheduling of outstanding debt under certain predetermined contingencies. Where programmes are deemed to have failed due to errors on the side of the multilateral institution, the eligible portion of that outstanding debt should be written-off by the respective institution.

The multilateral institutions should adopt a more flexible approach in dealing with indebted low income countries, where necessary circumventing time-absorbing bureaucracy to assist deserving countries in need.

The multilateral institutions should join bilateral creditors in contributing to the forthcoming AfDF replenishment. This should be made conditional on the AfDB agreeing to restructure both its operations and management board to the satisfaction of non-African contributors.

Her Majesty's Government

The Working Party recommends that HMG maintain its prominent role in promoting the need for debt relief for severely indebted developing countries, at the same time continuing to support its current programmes of bilateral funding, particularly concentrating on sub-Saharan African Severely Indebted Low Income Countries (SILICs).

Following the decisions made in the recent G7 summit which supported the role of the Paris Club and proposed increasing its scope, Ministers should continue to push for the implementation of improved Trinidad Terms within the operations of the Paris Club, and should advocate a flexible approach for those countries unable or unwilling to implement bilateral debt reductions. We already note a healthy shift in the policies of those governments hitherto adopting an intransigent stance towards increased debt relief, the most notable being Japan, which showed encouraging signs of flexibility at the G7 summit. Such peer pressure now needs to be sustained, not only by the government but by this all-Party initiative.

The abolition of the use of a 'cut off date' in the Paris Club operations is proposed, with relief provided on a country-by-country basis so as to limit external debt to sustainable levels.

HMG should continue to request the multilateral institutions to consider more carefully the need for increased debt relief and debt stock reduction in sub-Saharan Africa. Contributions to the concessional facilities of the International Financial Institutions (IFIs) should be continued on the understanding that the use of the institutions' own funds will increase in the near future.

HMG should introduce an official channel of information between the IFIs and Parliament, recording the votes of and the policy advice given to our Executive Directors. This could be modelled on the mechanisms utilised by the Canadian and Australian Parliaments. This would increase the accountability of the multilateral institutions to the British Government as they come under greater public scrutiny, often from hostile and ill-intentioned groups outside Parliament.

Finally, Britain should join and support the Task Force on the Multilateral Development Banks instigated, in May 1994. This aims to review the activities of the World Bank and the Regional Development Banks (RDBs), and thus will allow an opportunity to influence the policies of some of the major multilateral institutions.

We believe the best moment for HMG to implement these proposals is at the Fall Meeting of the Development Committee and Interim Committee of the Bank and the Fund, to be held in Madrid in the week of 3 October 1994, and we commend these recommendations to all parties.

1

An Overview of the Origins of the African Debt Crisis

It is now more than a decade since the public of the 'industrialised nations' were made aware of the plight of a large number of developing countries which were struggling with volumes of debt which they could no longer afford to service. In 1982 Mexico set a precedent by announcing a moratorium on its debt, to be quickly followed by other developing countries unable, or unwilling, to service the large debts they had accumulated with commercial banks, governments and multilateral institutions around the globe. The ensuing 'debt crisis' held repercussions for both debtors and creditors alike, and also the well-being of the entire international economy, and pressure for an effective resolution to the problem was applied from all sectors. As a result the mid-1980s saw the introduction of a spate of programmes[1] designed to curb the debt burdens of developing countries, with politicians of the industrialised regions joining multilateral institutions in persuading commercial banks to initiate debt reductions and rescheduling. At the same time multilateral institution-inspired programmes of structural reform were implemented within many developing countries, frequently under encouragement from bilateral donors, in an attempt to address the fundamental problems which had originally contributed to the emergence of the debt crisis. In a number of well publicised cases, the reduction in commercial debt stocks which followed, combined with the implementation of programmes of structural reform, led to an easing of debt burdens and a move towards economic growth and viability. Indeed, using Mexico as an example, 12 years after announcing its inability to honour debt service obligations, it is now an 'industrialised nation' belonging to the OECD. Such cases have been championed by multilaterals and western governments alike, and in the late 1980s were taken as proof that economic growth could be restored with the implementation of only limited amounts of debt reduction.

By 1986 it was evident that although the situation in a number of developing countries had improved, the overall debt burden of the developing world had continued to expand[2] following the debt crisis of the early 1980s, and many countries were still faced with the dilemma of being unable afford their debt service obligations. In order to gauge the magnitude of the debt problem, and to assess the performance of both bilateral and multilateral institution operated policies in relieving debt related problems, in 1986 the All Party Group examined the debt issue and published a report of their findings, *Managing Third World Debt* (1987), which concluded that:

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[1] Most notably the Baker and Brady Plans.

[2] The growth in total Third World debt could be attributed to a gradual resurgence in lending to developing countries experiencing economic recovery combined with the substantial accrual of outstanding service payments by the poorest countries which occurred throughout the 1980s.

> Many developing countries cannot service their external debt as scheduled. Piecemeal attempts to rearrange their debt profiles have not worked. New lending has not been forthcoming. Developing countries are now paying back to their creditors more in interest and principal than they receive in new loans. Countries which are already very poor are suffering, imports are being curtailed and world recovery undermined. Yet the markets have discounted much ldc debt long ago.

The report noted that although limited attempts had been made to address the debt-related problems of a number of middle-income developing countries via the implementation of the Baker Plan and similar initiatives, those of the poorest developing countries remained as serious as ever and were in urgent need of an effective resolution. The Working Party went on to recommend that in dealing with developing country debt, the political will should be generated for a more innovative approach, and that once development interests (not just the interests of the developing countries) had been adequately taken into account, the need for public sector initiatives became imperative.

Eight years later, although the issue of developing country debt is no longer considered worthy of the front page media coverage witnessed throughout the 1980s, total debt stocks have continued to grow, reaching approximately $1800bn in 1993, compared to $1200bn in 1986. For the substantial number of developing countries which have benefited from the measures of debt relief and have begun a process of economic recovery, a small number have slipped into deeper financial distress, with the associated problems of poverty, malnutrition and civil strife. Despite a decade of discussion and analysis, the issue of Third World debt is still far from being resolved, and the search for an appropriate and effective solution continues.

Current Third World Debt and its Origins

The overall debt stock of the developing world is by no means evenly distributed between individual countries and regions, as is shown in Table 1.1. Although estimates for 1993 indicate that Latin America accounted for by far the largest proportion of aggregate developing country external debt, followed by Eastern Europe and Central Asia, when compared to the economic activity observed in each developing zone, it becomes clear that although relatively small, the debt stock of sub-Saharan Africa dominates the domestic economies of that region at an overall equivalent of more than two-thirds of the continent's aggregated annual GNP. Indeed, of the 29 severely indebted low income countries (SILICS) categorised by the World Bank in 1993, 23 were situated in sub-Saharan Africa.

The aggregated figures also disguise a fundamental difference in the composition of the debt stocks held by developing regions. Over recent years there has been a considerable expansion in the flows of private capital directed to developing countries, but the majority of these flows have been attracted by middle-income countries in Asia and Latin America, plus China (which alone accounted for approximately one third of total

Table 1.1: Total External Debt Stocks of Developing Country Regional Groupings, Percentage of Total Developing Country External Debt and Debt to Annual GNP Ratio, Estimated for 1993

Region	*Total Debt Stock $bn*	*% of Total LDC Debt*	*Debt/GNP %*
Latin America	512	29	41
Europe and Central Asia	351	20	35
East Asia and Pacific	367	21	31
Sub-Saharan Africa	199	11	68
Middle East and N. Africa	195	11	64
South Asia	145	8	38
Aggregate	1770	100	40

Source: World Bank, *World Debt Tables, 1993–94.*

private flows). In many regions, most notably Latin America, the recent repatriation of substantial volumes of flight capital has been a major contributor to the large upsurge in private inflows. In general the most significant recipients of the expanded private capital flows have been those developing countries which benefited from the debt reductions and multilateral structural reform programmes conducted in the mid/late 1980s, initially under the auspices of the 'Baker Plan' and later under the 'Brady Plan'. The strong emphasis on commercial debt reductions incorporated in these programmes clearly favoured countries which at that time owed large proportions of their total debt stocks to commercial creditors, notably countries in Asia and Latin America, and was biased against countries which owed substantial sums to official creditors but had only relatively small commercial debt stocks. This typified the position of a large proportion of sub-Saharan African countries. The reduction in overall debt burdens, combined with the implementation of multilateral institution operated structural adjustment programmes, proved very successful in increasing international investor confidence in the future prosperity of participant countries, and correspondingly encouraged increased levels of both foreign direct and portfolio equity investment. In turn the increased levels of private investment entering these regions encouraged the commercial banks and financial institutions of the industrialised countries to resume lending, and subsequently the majority of the external debt stocks presently held by Asian, European and Latin American countries are owed to private creditors.

The dominance of private capital in the inflows of these regions has had substantial influences on domestic economic performances, for in general private creditors have taken care to ensure that the funds they provide are utilised in viable and productive projects, and often substantial proportions of the resulting profits have returned to the recipient country in the form of investment reflows. In addition foreign direct investments by private creditors have generally been accompanied by inflows of staff training, advanced technology inputs and in some cases an automatic access to markets in the lucrative industrialised North. This has had the overall effect of increasing the skills base and productivity of the domestic workforce, whilst at the same time offering domestic governments an expanded volume and range of potentially taxable products from which to obtain budgetary revenues. Therefore, as a result of the programmes of debt relief, governments in these regions have been able to engage in increased levels of public expenditure, raising both domestic living standards and creating a favourable environment for future economic prosperity.

The Different Situation Confronting Sub-Saharan African Countries

Sub-Saharan Africa has not experienced the upsurge in volumes of private sector investment witnessed throughout Asia and Latin America, with flows of foreign direct investment and portfolio equity funds stagnating throughout the 1980s and early 1990s. Correspondingly commercial creditors have also remained reluctant to offer new finance to sub-Saharan African countries, generally perceiving African domestic economies to be high risk, low return options, and at present more than two-thirds of sub-Saharan Africa's debt stock is owed to official creditors (bilateral and multilateral).

The aversion shown by private investors to involvement in sub-Saharan African economies can be traced back to the pre-debt crisis period, and can be seen to be one of the primary factors behind the relatively high debt exposures of official creditors observed in this region at present. During the 1980s the low levels of private capital entering from abroad, combined with exceptionally small domestic reserves, resulted in many African countries suffering from severe domestic investment deficiencies, and this situation was exacerbated by the high levels of capital flight observed throughout sub-Saharan Africa over recent decades (the World Bank has estimated that in 1991 sub-Saharan Africa's aggregate stock of flight capital held overseas was equivalent to more than 90 per cent of the continent's aggregate annual GDP[3]).

[3] World Bank, *World Debt Tables 1993–94.*

The resulting capital shortages had the effect of impeding the already low levels of industrial activity observed in the more developed sub-Saharan African nations, and correspondingly forced many African governments to become almost solely reliant on the taxation of exports of primary commodities for domestic budgetary finance and foreign exchange reserves. The persistent decline in international primary commodity prices (including oil) witnessed over the 1980s thus resulted in a gradual contraction in the overall export earnings of many African economies, in turn reducing governments' abilities to raise revenues for use in both domestic spending and external debt service. Although faced with limited capital supplies, a number of African governments continued to divert substantial sums of foreign exchange for use in large programmes of defence spending, importing high technology weaponry from industrialised countries, whilst others implemented large scale construction programmes based on factors of prestige rather than economic rationale. The consequent shortage of private sector investment combined with declining levels of low quality public spending, contributed to the low, and in many cases negative, levels of economic growth experienced throughout sub-Saharan Africa over the 1980s, and this correspondingly further discouraged private foreign investors and creditors from becoming embroiled in the African economic dilemma.

The mid-1980s therefore saw the majority of sub-Saharan African countries in need of additional volumes of finance to fund immediate government consumption, undertake domestic investment and service external debt stocks. Although as a result of the widespread economic problems the international capital markets were reluctant to lend directly to sub-Saharan African states, the IFIs, comprising the Bretton Woods 'twins' and the regional development banks, were willing to lend large quantities of finance. The accommodating stance of the IFIs could partly be attributed to the roles designated in their founding charters, notably to assist countries experiencing balance of payments disequilibrium and, in the case of the development banks, to promote economic development, and partly to the need for the IFIs to be seen to be distributing the large volumes of funds which donor countries had contributed for use in developing country assistance. In addition governments throughout the developed regions proved willing to lend substantial sums to sub-Saharan African countries directly on a bilateral basis, with financial agreements between European states and their former colonies becoming commonplace.

Although both multilateral and bilateral loans were in general contracted on terms favourable to those offered by commercial creditors, the returns on officially financed programmes and projects were frequently of insufficient magnitude to generate the funds required to service the official loans. Correspondingly programmes funded by official creditors frequently contributed little in the way of returns to the domestic economy, and thus in many cases failed to encourage future economic prosperity.

By the late 1980s the economic situation in a large proportion of sub-Saharan African countries had deteriorated, with export earnings continuing to fall whilst debt service obligations increased. Governments of the most debt-distressed states were pushed to cut already low public spending budgets, diverting funds for use in debt maintenance, and this had the effect of imposing negative pressures on already fragile economies, and subsequently on domestic living standards. Despite efforts to redirect resources from the domestic economy in a number of countries governments were still unable to honour all of their debt service obligations owed to external creditors.

Debt Owed to Multilateral Institutions

Although at this time the international community had already experienced similar problems of excessive debt burdens during the debt crisis of the early 1980s, and had successfully pressured commercial creditors to engage in wide-scale debt reduction and relief, the same impetus was not applied to official creditors, and African countries were generally not allowed to benefit from the substantial easing of debt burdens witnessed in many debt-distressed Latin American and Asian countries. In response to the inability of many African countries to pay all of their debt service due, the bilateral donors did initiate limited amounts of rescheduling on debt service due to them, both independently and through the activities of the Paris Club, but the IFIs remained inflexible, refusing to engage in programmes of debt reduction or rescheduling, and the small gains incurred from bilateral debt write-offs and reschedulings were swallowed by expanding IFI debt service obligations. Instead the IFIs responded to the debt dilemma by granting additional loans to already severely indebted countries, increasing their debt stocks yet further. The new loans were generally contracted on concessional terms, and their distribution was made conditional on the recipient countries accepting the implementation of rigorous programmes of structural reform, which were intended to correct in-built problems in domestic economies and provide a favourable environment for economic growth. Although many countries showed reluctance in allowing the various IFIs to dictate their domestic economic strategies, a large number were coerced into accepting structural reform programmes and the attached financial packages by bilateral and commercial creditors, which made the granting of debt relief and reschedulings conditional on the implementation of IFI programmes.

The continued allocation of new loans by the IFIs, combined with the capitalisation of arrears, has resulted in the overall sub-Saharan African debt stock expanding substantially over recent years (from $139bn in 1986 to $199bn in 1993), and the proportion of total outstanding debt accounted for by multilateral institutions has increased. Volumes of annual debt service owed to the multilateral institutions continues to grow (from $1.5bn in 1986 to $2.8bn in 1993), and for a large number of African countries repayments made to IFIs presently exceed new disbursements, resulting in negative net flows of resources from countries which are already desperately poor. In addition the implementation of structural reform programmes and the injection of large sums of project-based funds by the IFIs have generally not initiated the significant levels of economic expansion projected, and many sub-Saharan African countries are still enduring low or even negative economic growth rates. This combination has resulted in falling per capita incomes and living standards throughout much of sub-Saharan Africa, and an increasing number of countries which are unable to service their debt stocks, with total volumes of African arrears expanding annually.

It therefore becomes clear that although the concerted efforts made after the debt crisis of the early 1980s to reduce commercial debt burdens and encourage economic growth in the developing regions assisted many of the severely indebted countries in Asia and Latin America, little was done to address the rapidly emerging debt problems of sub-Saharan Africa. The intransigence shown by many official creditors, in particular the multilateral institutions, towards the mounting burden of debt evident in many African countries has contributed to the evolution of a second debt crisis, this time affecting some of the world's poorest and most destitute nations. Unlike the previous crisis though, the overall volumes of debt involved are relatively small and do not threaten the stability of the international financial system, and correspondingly the urgency shown in resolving the debt dilemma of sub-Saharan Africa has been notably less. Nevertheless, pressure is now mounting from many corners of the development arena for the multilateral institutions to review their attitudes to debt reduction and rescheduling. Both commercial and bilateral creditors have been forced to accept the gravity of the debt situation and initiate wide scale debt relief, but without the compliance of the IFIs their efforts have to a large extent been in vain.

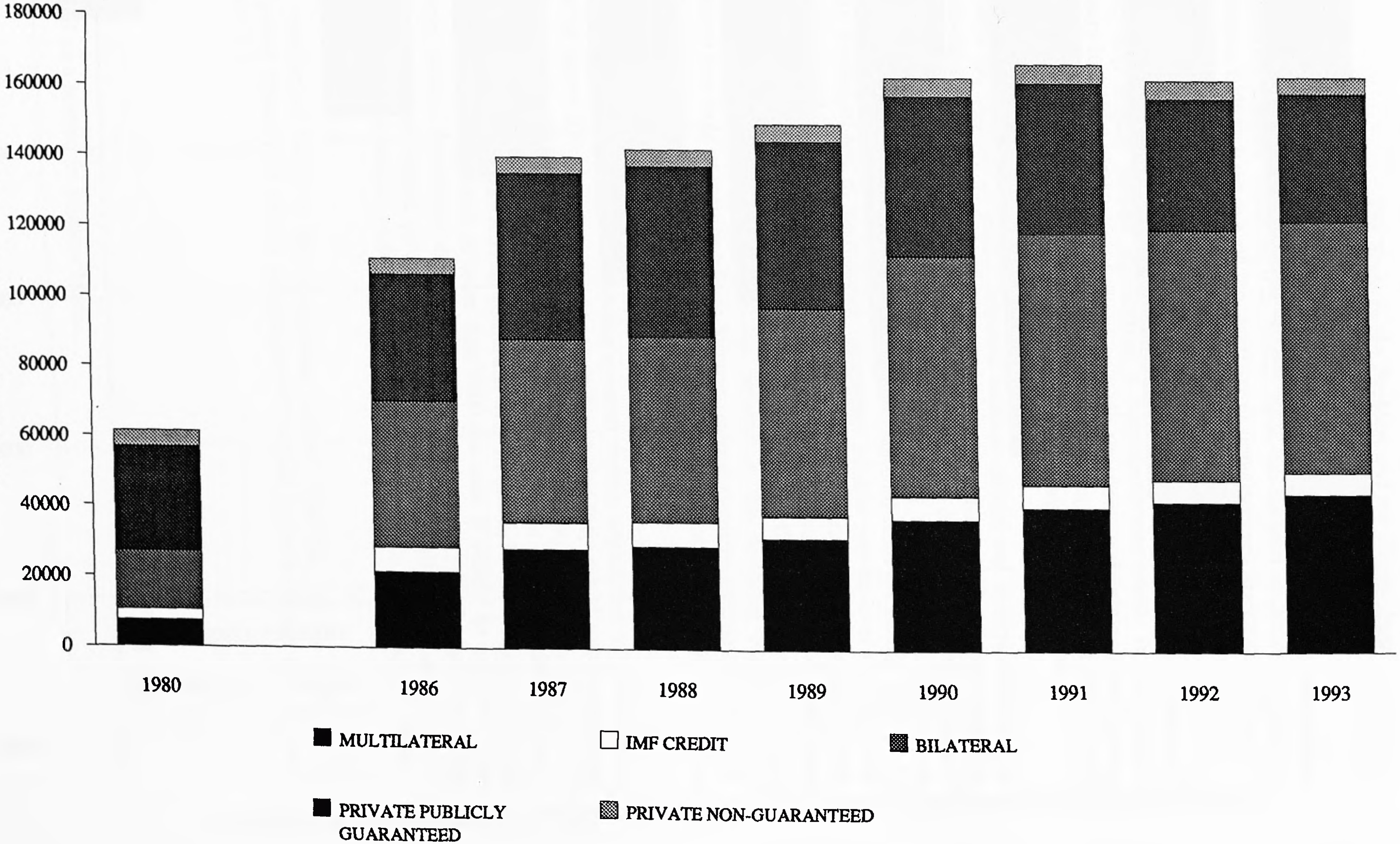
2

Sub-Saharan African Debt: The Scale of the Problem and the Urgent Need For Reform

The combination of declining international commodity prices and a shortage of private foreign investment throughout the 1980s forced many sub-Saharan African countries to engage in wide scale borrowing to fund both domestic expenditure and service due on outstanding debt stocks. As noted in chapter one, commercial creditors and the international capital markets proved reluctant to become involved in African domestic economies, and correspondingly the majority of funds borrowed were provided by official sources, either creditor governments or multilateral institutions. Over the period 1980–93, sub-Saharan Africa's total outstanding external debt more than doubled, with the volume owed to official creditors rising nearly threefold to account for more than three quarters of the total. The World Bank calculated that in 1993 approximately 22 per cent of total sub-Saharan African debt was owed to multilateral institutions, compared to 17 per cent in 1986. When this figure is disaggregated it becomes evident that some African countries owe very large proportions of their external debt stocks to multilateral institutions. Although a substantial proportion of the growth in African debt stocks observed over the last decade can be associated with an increase in overall loan disbursements from official creditors (net flows from commercial creditors have generally been negative over the period), it has been suggested that around a third of present outstanding debt owed by sub-Saharan African countries comprises of interest and principal obligations capitalised on non-payment.

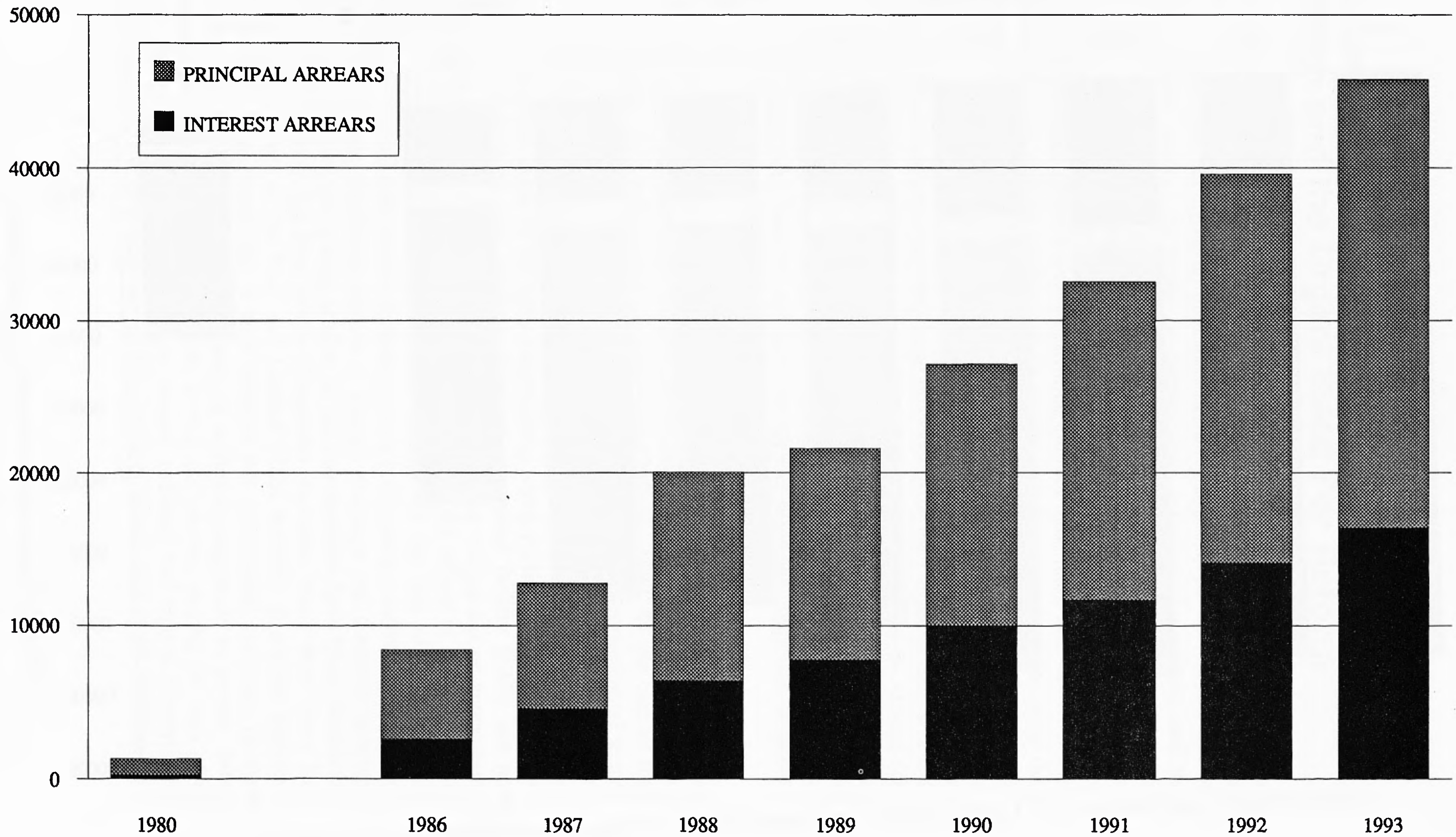
A large proportion of recent lending to sub-Saharan Africa has been disbursed on concessional terms, but substantial volumes of non-concessional official and commercial debt still remain outstanding from the early–mid-1980s (in 1993, 67 per cent of total sub-Saharan African debt was estimated to be contracted on non-concessional terms). An increasing number of these loans are now reaching maturity, and consequently creditors are requesting greater volumes of repayment of both principal and interest charges. In addition many of the early concessional loans, particularly those disbursed by the IMF through its soft window structural adjustment facility (SAF), are now coming to the end of their grace periods, and debt service obligations on concessional funding are rising for many African countries. Despite the efforts of commercial and bilateral creditors to reduce Africa's debt burden via the use of write-offs and reschedulings, overall debt service obligations have remained at consistently high levels over the last decade. Declining inflows of foreign exchange and domestic economic stagnation have meant that a large number of African countries have found themselves unable to honour their full debt service obligations, and over recent years many have been forced to return to the Paris and London Clubs annually to request additional reschedulings of payments due to both bilateral and commercial creditors. In many cases the debt relief granted has not been of sufficient magnitude to prevent debtor countries from having to default on debt service obligations, and by the turn of the decade virtually all sub-Saharan African severely indebted low income countries had entered into arrears with at least one of their major creditors. Indeed the Working Party

FIGURE 2.1: SUB SAHARAN AFRICA, LONG-TERM EXTERNAL DEBT & IMF CREDIT, US$ MILLION



SOURCE: WORLD BANK, WORLD DEBT TABLES, VOL.1, 1993

FIGURE 2.2: SUB SAHARAN AFRICA, INTEREST AND PRINCIPAL ARREARS, US$ MILLION



SOURCE: WORLD BANK, WORLD DEBT TABLES, VOL.1, 1993

was informed that by the end of 1993, the situation had become so severe that despite the 'preferred creditor' status of IFIs, twenty three sub-Saharan countries had entered into arrears with at least one of the multilateral organisations, seventeen of these in arrears to either the World Bank, the IMF or the African Development Bank.[4]

The extent to which individual countries are suffering from debt-related problems differs, with certain nations shouldering a disproportionate share. It is therefore necessary to distinguish between country-specific situations, highlighting those nations which are most seriously burdened by external debt and forming judgements about those which are most in need of assistance in tackling their debt-related problems.

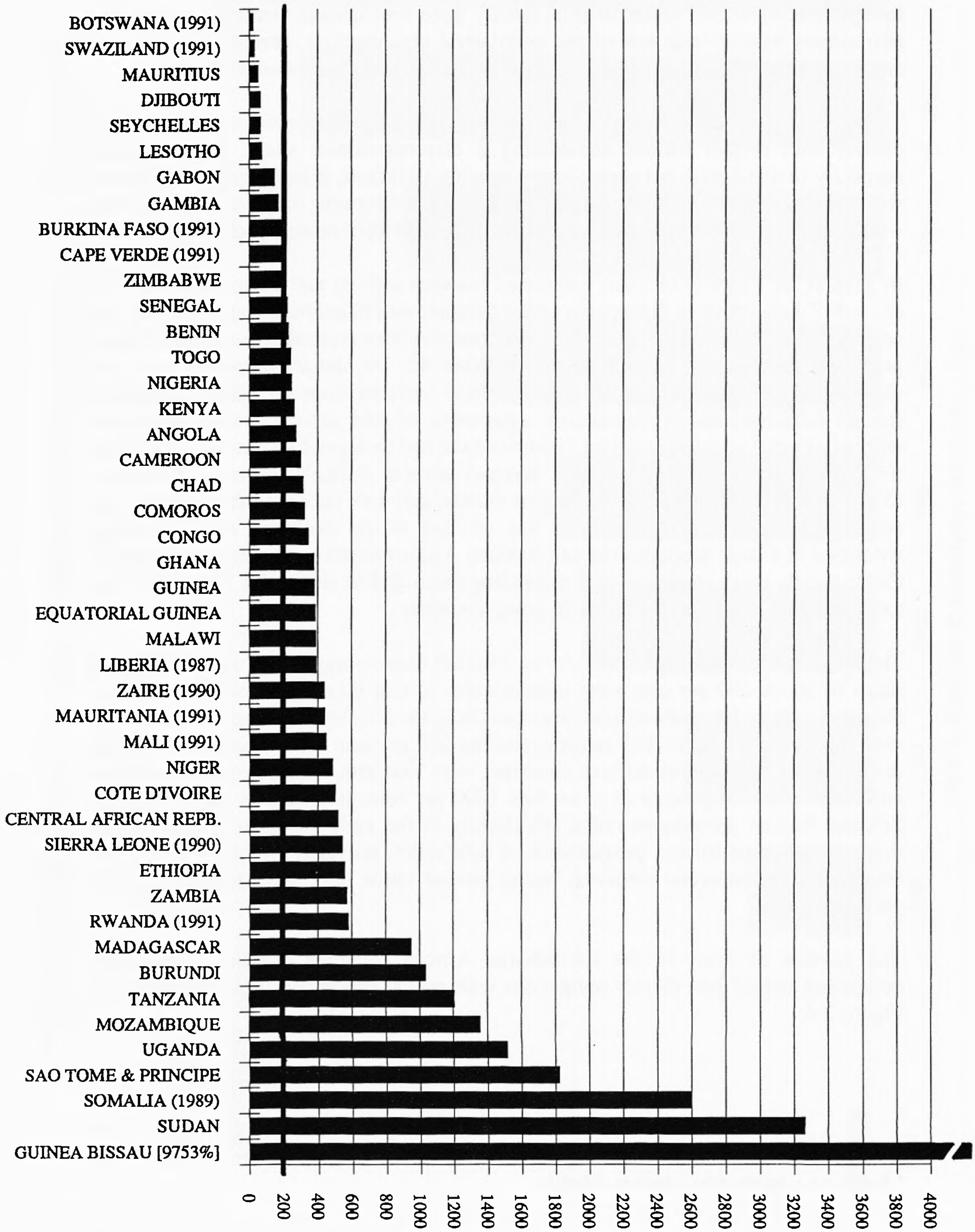
In general the majority of loans contracted between official and commercial creditors and sub-Saharan African debtors have been denominated in international currencies, and correspondingly service due on mature debt has also been repayable in a predetermined primary international currency, in many cases the US dollar. In recent years the majority of sub-Saharan African countries have suffered from dwindling supplies of foreign exchange, and in maintaining repayments of debt service over the long term without external assistance, debtor countries have had to depend on the earnings gained from the exportation of goods and services abroad. Africa's terms of trade have experienced a steady decline over the past decade, and with little growth in productivity and overall economic capacity this has resulted in the declining export earnings witnessed in a large proportion of sub-Saharan African countries throughout the 1980s. Consequently when combined with expanding external debt stocks this has led to rising external debt/export earning ratios in many countries.

The 1991 World Bank report on African external finance argued that total debt/export ratios of above 200 per cent were unsustainable in that they would seriously damage the opportunities for renewed economic growth in the country concerned, but as can be seen from Figure 2.3, in 1991 ratios exceeding 200 per cent were recorded for a large proportion of sub-Saharan African countries, with Tanzania, Mozambique and Uganda and others exhibiting ratios of more than 1000 per cent. It should be noted that sub-Saharan African debt/export ratios fell slightly in the early 1990s as a result of the implementation of limited programmes of debt relief, primarily by bilateral and to a lesser extent commercial creditors, but in general ratios have since returned to their previous levels.

The position of many of the sub-Saharan African countries can be illustrated by comparing annual debt service obligations with annual export earnings, as is shown in Figure 2.4.

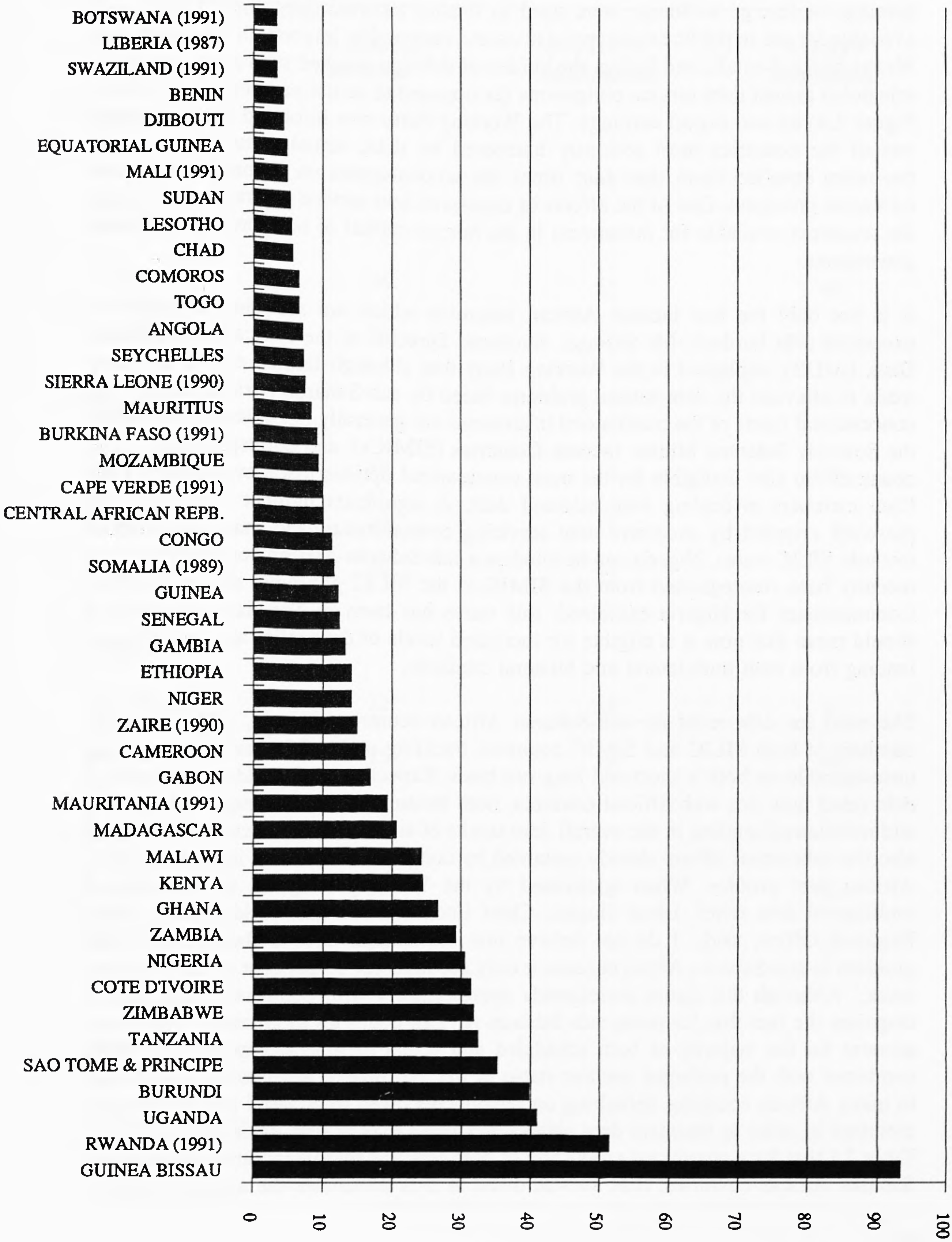
[4] Based on a briefing by Matthew Martin.

FIGURE 2.3: DEBT AS A PERCENTAGE OF EXPORTS, 1992



SOURCE: WORLD BANK, WORLD DEBT TABLES, VOL.2, 1993

FIGURE 2.4: DEBT SERVICE AS A PERCENTAGE OF EXPORTS, 1992



SOURCE: WORLD BANK, WORLD DEBT TABLES, VOL.2, 1993

In 1992 in a large proportion of country-specific cases more than 20 per cent of annual earnings of foreign exchange were used to finance external debt, limiting the funds available for use in public service provisions and commodity imports. In Guinea-Bissau, Mozambique, Somalia and Sudan, the burden of debt has reached such a magnitude that scheduled annual debt service obligations (as opposed to actual payments illustrated in Figure 2.4) exceed export earnings. The Working Party was informed that in Uganda, one of the countries most seriously hampered by debt, actual annual debt service payments equalled more than four times the amount spent on domestic health and education provision. One of the effects of excessive debt service payments is to reduce the resources available for investment in the human capital of both present and future generations.

It is not only the low income African countries which are suffering the strain of excessive debt burdens. Mr Susungi, European Director of the African Development Bank (AfDB), explained to the Working Party that although limited efforts are being made to alleviate the debt-related problems faced by sub-Saharan African SILICs, the concessional funds of the multilateral institutions are generally not extended for use by the Severely Indebted Middle Income Countries (SIMICs), and correspondingly these countries are also ineligible for the most concessional options made available by Paris Club members in dealing with bilateral debt. A significant number of SIMICs are presently crippled by excessive debt servicing commitments, and many are slipping towards SILIC status. Nigeria can be cited as a sub-Saharan African country which has recently been recategorised from the SIMIC to the SILIC grouping, and as the High Commissioner for Nigeria explained, this move has been in Nigeria's favour for it should mean that now it is eligible for increased levels of debt relief and concessional lending from both multilateral and bilateral creditors.

The need for debt relief for sub-Saharan African countries is great, with significant numbers of both SILIC and SIMIC countries buckling under debt burdens which are unsustainable on both a short and long run basis. Expectations for additional levels of debt relief now lies with official creditors, both because of the dominance of bilateral and multilateral lending in the overall debt stocks of sub-Saharan African countries and also the substantial efforts already sustained by commercial creditors in reducing their African debt profiles. When questioned by the Working Party on the viability of multilateral debt relief, Ishrat Husain, Chief Economist of the World Bank's Africa Regional Office, said, 'I do not believe that multilateral debt is the source of the problem in sub-Saharan Africa because it only accounts for 25 per cent of the total debt stock.' Although this figure corresponds approximately with published Bank data, it disguises the fact that for many sub-Saharan African countries multilateral institutions account for the majority of both scheduled and actual debt service payments. When combined with the preferred creditor status of the multilateral institutions, this has led to many African countries defaulting on repayments owed to bilateral and commercial creditors in order to maintain debt service payments due to IFIs. It can be seen from Table 2.1 that for a significant proportion of both low and middle income indebted sub-Saharan African countries, debt service owed to IFIs dominates the aggregate annual

Table 2.1:Debt Indicators of Selected sub-Saharan African Countries, 1992

COUNTRIES	*% TDSTK Bilateral*	*% TDSTK Multilateral*	*% TDSV Multilateral*
SILICs			
Madagascar	49	32	55
Mozambique	62	14	74
Tanzania	54	33	43
Uganda	25	52	86
SIMICs			
Côte d'Ivoire	28	16	49
Congo	55	11	0
Cameroon	48	22	50
MILICs			
The Gambia	22	65	34
Malawi	15	75	49
MIMICs			
Senegal	36	42	40
Gabon	54	9	12

TDSTK : Total Debtstock
TDSV : Total Debt Service

Source: World Bank, *World Debt Tables, 1993–94.*

obligations, so multilateral debt is indeed the source of a large proportion of Africa's debt problems.

While commercial creditors have generally accepted the inevitability of the African debt situation, and rather than waiting for debt to be repaid have been willing to accept substantial volumes of debt reduction, bilateral creditors have on the whole been less generous and have engaged in only relatively low levels of debt write-offs,[5] in general favouring the rescheduling of debt service due via the operation of the Paris Club. Official debt forgiven in 1992–3 reduced total debt stocks by $2.5bn, while rescheduling added an additional $15bn to the total. In terms of annual debt service obligations, the activities of the Paris Club have assisted many financially distressed African countries in reducing net outflows of foreign exchange to bilateral creditors, but the benefits have only been short term in nature, and generally service obligations have returned to previous levels following the expiry of Club contracts. Although many bilateral donors have shown admirable intentions in enroling in the Paris Club, thus far its activities have had only a limited impact on the overall sub-Saharan African debt problem, with the reschedulings implemented of insufficient scale and scope required to initiate a substantial reduction in debtor burdens. Husain estimated that even the region-wide introduction of the full Enhanced Toronto Terms, which so far have only been granted to a relatively small number of severely indebted developing countries, would leave eleven African SILICs with debt/export ratios of over 200 per cent. In the case of Uganda, which owes most of its debt to multilateral institutions, the implementation of the Enhanced Toronto Terms would save just $9m in debt service obligations. The present official approach to debt relief still seems to want to put off the problem to a later date.

It was made clear to the Working Party that a consensus exists amongst official creditors: although a large number of severely indebted low and middle income states which are suffering under substantial debt burdens have made concerted efforts to remain current on debt servicing obligations and initiate economic reform, a small number of 'rogue' nations have done little either to help themselves, their populations, or to honour obligations to external creditors. While both bilateral and multilateral creditors might agree that the former category of country is generally deserving of significant volumes of debt relief (although there exists an unofficial disagreement as to who should bear the major brunt of the relief operation), it is presently neither economically nor politically desirable to offer assistance to the latter group of countries. The group of 'rogue' economies presently consists either of countries in the grips of civil conflict, including Liberia, Sierra Leone, Rwanda, Somalia and Sudan, which generally have little regard for the operations of the international community, or

[5] There have been a number of exceptions to this generalisation, and a number of bilateral creditors (including the Nordic countries and Britain) have proved keen to implement substantial levels of debt-write offs via the use of the UNCTAD inspired Retro-active Adjustment Programme.

countries which are presently deemed to be economically mismanaged or are on the brink of financial collapse, such as Nigeria under the rule of Sani Abachi. The latter case highlights an additional factor underlying donors' decisions to distribute debt relief; many official donors have a policy of spending aid capital in a way which promotes democracy, and when faced by regimes which flout the democratic process, donors have the option to withhold official debt relief, which then acts as a lever to encourage a return to democracy.

3

The Activities of the Paris Club and the Bilateral Donor Approach to Sub-Saharan African Debt Relief

The Paris Club was established in the 1960s as a forum for discussion between indebted low income countries and their OECD bilateral creditor governments. Up until this point, debtor countries which were experiencing difficulties in honouring obligations on outstanding bilateral debt stocks were required to approach each bilateral creditor on an individual basis, with a resulting complex system of relief arrangements which differed substantially between respective creditor countries. The Club allowed representatives of debtor governments to address all of their bilateral creditor governments in one location, and to appeal for a universal programme of assistance which would apply to all bilateral creditors concerned, thus reducing the drain on valuable manpower resources of the low income countries and minimising the complexity of the overall bilateral debt relief arrangements.

Traditionally, low income countries facing short term liquidity problems would be eligible to meet with Paris Club members, and subsequent arrangements would be designed to prevent only immediate default on bilateral debt servicing. Measures of relief would typically be very short term in nature, covering service payments due over a twelve to eighteen month period, and interest would be charged at non-concessional rates on the consolidated debt stock.

The deterioration of the economic positions of a substantial number of low income countries throughout the early 1980s, and the subsequent development of a preferred creditor status by the multilateral institutions, resulted in an expansion in the number of countries facing difficulties in honouring their bilateral debt service obligations, and by the late 1980s it became apparent that the facilities offered by the Paris Club were insufficient to address the needs of the most severely indebted developing countries, particularly those situated in sub-Saharan Africa which were heavily indebted to official creditors. In response to the growing debt dilemma, the Paris Club adopted a series of initiatives designed to allow debt distressed countries greater relief from bilateral service obligations. The original concessional package, known as the Venice Terms, was introduced in 1987, and allowed SILICs extended grace and maturity periods in which to repay the rescheduled debt service payments, although market interest rates were still applied on the consolidated repayments. The implementation of the Venice Terms was made provisional on the acceptance of IMF operated SAF or ESAF programmes of adjustment. In 1988 this facility was extended via the introduction of the Toronto Terms, which offered yet longer periods of grace and maturity for repayments of rescheduled oda debt service obligations. In addition the interest rates charged on the consolidated payments were made concessional. For non-oda debt (i.e. export credits), SILICs approaching the Paris Club were offered a menu of three options; partial cancellation of the rescheduled debt (one third), extended grace and maturity periods (the same as those applied to rescheduled oda debt), or highly concessional interest rates (3.5 per cent below the market base rate, or one half the market base rate, whichever was higher).

A number of donor countries recognised that, although the Toronto Terms were a move in the right direction, they did not go far enough in relieving the non-concessional bilateral debt burdens of SILICs, which in most cases were still suffering from economic stagnation and were unable to honour all of their debt service obligations. In 1990, John Major (then British Chancellor) proposed the implementation of the 'Trinidad Terms', which called for the cancellation of two-thirds of bilateral debt stocks contracted before a 'cut-off' date, with the remaining debt rescheduled to be payed over a 25 year period with 5 years' grace. At the same time the Dutch government proposed the cancellation of total bilateral debt stocks contracted by SILICs implementing agreed structural adjustment programmes. The implementation of either of these proposals would have increased the effectiveness of the Paris Club activities enormously, at the same time setting a precedent in including total debt stocks, rather than just debt service maturities, in the negotiating process.

Both the Dutch proposal and the Trinidad Terms were seen as being excessively generous by a substantial number of Paris Club member governments, and in 1991 a diluted proposal, known as the 'Enhanced Toronto Terms (ETT)', was introduced as an alternative. These Terms are still operational and presently govern the activities of the Paris Club in dealing with low income countries (eligibility to the ETT is restricted to all IDA-only countries). The adapted facility dismisses the recommendation that the Club should include total outstanding debt stocks in negotiations, instead restricting its operations solely to debt service obligations due. In fact, as the name suggests, the ETT are effectively only a moderately extended version of the Toronto Terms, with eligible oda debt being rescheduled on long repayment periods (12 years grace and 30 years and concessional interest rates). In reality under the ETT most major Paris Club members routinely cancel 100 per cent of oda debt.[6] The three options open to SILICs in rescheduling non-oda debt service obligations have been extended so as to allow the equivalent of a 50 per cent reduction in their net present value (NPV), and are now as follows; partial cancellation (one half) and repayment of the consolidated remainder over 23 years (6 year grace period), rescheduling on concessional terms to reduce the NPV of current service obligations by one half with repayment over 23 years, and a combination of reduced interest rates and interest payment capitalisation with repayment over 23 years.

The Working Party was informed by a number of speakers that the revisions included in the ETT are still inadequate in addressing the problems of the most severely debt distressed low income countries, and in sub-Saharan Africa it has been observed that

[6] Martin, M. (1994), *Official Bilateral Debt: New Directions for Action.* EURODAD Policy Paper, Brussels.

a large number of countries have been forced to return to the Paris Club year after year to continually reschedule their service obligations. Clearly the present activities of the Paris Club have the effect of delaying the inevitable problem of low income countries being unable to repay their bilateral creditors, and are not assisting in resolving the core issues underlying the current debt dilemma faced by sub-Saharan African SILICs. Indeed, it was pointed out that the benefits resulting from recent Paris Club reschedulings have been of such small magnitude that in most cases they have not reduced the actual debt service payments made by low income countries, but instead have only released funds for use in repaying other creditors and outstanding arrears.

Baroness Chalker, Minister for Overseas Development, and Anthony Nelson MP, Economic Secretary to the Treasury, both indicated to the Working Party that the British Government feels there still exists an urgent need for the implementation of full Trinidad Terms, and that a total debt stock reduction of up to 80 per cent on a case by case basis to countries which have a 1–2 year track record of economic reform would be entirely justified. This view was mirrored by representatives of academia, NGOs and the multilateral institutions, who felt that the Paris Club should now go beyond the Trinidad Terms. As a result, pressure from a number of international forums and member governments alike have prompted the Paris Club to initiate discussions on how improved Trinidad Terms might be implemented. It has been suggested that the 100 per cent debt stock reduction proposed by the Dutch administration would perhaps be counter-productive, in that this would damage the debtor countries' credit worthiness with the international financial community, whilst limited debt reduction would enhance confidence and thus boost levels of foreign direct investment into sub-Saharan African SILICs.

Thus far the move towards greater concessionality and actual debt stock reduction through the operations of the Paris Club have been opposed by a small number of member governments. The Working Party was informed that the US government has shown great courage and commitment in pushing the issue of debt stock reduction through Congress, which was initially reluctant to sanction such a facility (although actual volumes of US debt reduction accorded to date have been exceptionally low). On the other hand the Japanese government is continuing to encounter substantial difficulties in agreeing to the introduction of programmes of debt contraction. In receiving evidence on the position of the Japanese government, the Working Party was told domestic legislation within Japan forbids the writing-off of debt, and that to be seen to be operating within a different legal framework when dealing with foreign debt would be both inconsistent and politically damaging. In addition it was pointed out that Japanese oda loans come partly from a general government account and partly from a Post Office account which has to be reimbursed. It is therefore easier for the Japanese government to assist severely indebted countries using additional grant aid rather than actual debt cancellation. It would appear that if there were to be a groundswell of international official creditor opinion in favour of taking improved Trinidad Terms seriously, the Japanese would be unable to respond beyond approximately two thirds debt reduction, and this they would achieve by extending maturities into the future almost to infinity.

In light of the perceived restrictions governing the Japanese administration in implementing debt stock reduction, the Working Party welcomes the shift in the Japanese stance on debt relief signalled at the recent G7 summit, where the Japanese administration joined other G7 nations in declaring:

> We encourage the Paris Club to pursue its efforts to improve the debt treatment of the poorest and most indebted countries. Where appropriate, we favour a reduction in the stock of debt and an increase in concessionality for those countries facing special difficulties.

An associated 'On the Record' press release explained that the softening of the Japanese position was partly prompted by a reluctance to be 'left behind the other countries', a point which was emphasised by the Working Party when meeting Japanese representatives.

Although previous objectors are now showing signs of reviewing their attitudes to bilateral debt stock reduction, the Working Party feels that in extending the scope of the Paris Club operations, rather than implementing a proposal within which certain Club members are either unwilling or unable to operate, a more flexible approach should be adopted, wherein creditor countries would be able to choose between offering debt stock reductions, disbursing additional grant assistance, or applying a combination of both of these options. The extent of the measures required could be determined using NPVs, as are currently utilised in the operations of the ETT, with country specific NPVs of both debt service obligations and total debt stocks being reduced to levels deemed sustainable by an external monitor (these levels could be determined using such information as annual debt service to export earning ratios, annual economic growth rates and inflows of foreign direct investment). This would suggest dealing with debtors on a country-by-country basis, taking into account their respective situations, a move that has been advocated by a number of speakers.

It has been suggested to the Group that the implementation of a 'cut-off date' within the operations of the Paris Club, after which any bilateral flows contracted are ineligible for relief initiatives, has resulted in certain countries suffering excessive burdens from bilateral debt stocks. The case of Uganda was highlighted as being particularly serious, with the cut-off date set when Paris Club negotiations commenced in 1981. The Working Party therefore suggests that the Paris Club should relax its emphasis on cut-off dates, instead concentrating on the implementation of sufficient measures of debt relief to attain an overall sustainable debt stock in each particular case.

The annual nature of the Paris Club operations has also been criticised by a number of speakers addressing the Working Party. Traditionally severely indebted countries approaching the Paris Club have been granted relief on debt service obligations due to mature in the following year. If the country's economic situation has not improved sufficiently by the following year it is required to return to the Club and negotiate a new package of rescheduling. It has been suggested that these annual meetings represent a substantial burden on ministers and governors of central banks of both the debtor and the creditor countries, and often reduce the quality of the internal decision making processes in developing countries. Correspondingly the Paris Club should be pressured to adopt longer term rescheduling and debt write-off strategies, with external monitors being employed to ensure that the debtor countries are behaving 'responsibly' and are deserving of continued assistance. This would reduce the drain imposed by numerous negotiations on scarce managerial resources and at the same time have the effect of increasing the consistency of Paris Club operations over a period of time.

Finally the Working Party feels that rather than negotiating reductions and rescheduling of solely bilateral debt obligations, the scope of the Paris Club should be extended to cover the total debt stock and service requirements of low income developing countries. The Paris Club has been proved to be an effective forum for the discussion of debt relief, and multilateral creditors should now be pressured to join governments and private creditors (via the merger of the London Club) in allowing the discussion of aggregate debt stocks for each severely indebted country. This is a move the multilateral institutions are likely to oppose vigorously.

4

The Role of Multilateral Creditors in Sub-Saharan Africa and Their Response to the Debt Dilemma

During the initial emergence of sub-Saharan Africa's economic crisis the multilateral institutions were seen by the international community as being ideally placed to offer a potential solution to the continent's problems, being in the position to lend substantial volumes of funds without the requirement to amass profits for distribution between shareholders. Correspondingly the multilaterals were pressured to assume a role of 'lender of last resort' for low income African countries, providing large volumes of funds to countries in which both commercial and bilateral creditors were loath to become heavily involved. This influenced the respective roles of the multilateral institutions, and effectively ensured that they became embroiled in the overall African debt scenario.

Multilateral financial institutions engaged in lending to sub-Saharan African countries can be grouped into three distinct categories:

i) The International Monetary Fund
ii) The World Bank
  a) IBRD (non-concessional)
  b) IDA (concessional)
  c) IFC (commercial)
iii) Regional Multilateral Lending Agencies (in this case the AfDB)

One of the original intended roles of the IMF designated at its foundation at Bretton Woods was to assist in correcting temporary economic disequilibrium in both developed and developing countries, and in this function it has provided short term liquidity at non-concessional rates to a large number of countries experiencing balance of payments difficulties. Borrowing countries accepting IMF short-term liquidity assistance have generally been obliged to begin repayment of loans after only short grace periods, and repayment periods have usually been relatively short with high unit instalments. The World Bank and the Regional Development Banks have concentrated their activities solely on developing countries, and were originally primarily concerned with providing funds and expertise for use in projects which promoted economic development and sectoral growth. Although most of the World Bank and AfDB lending to sub-Saharan African countries throughout the 1970s and early mid-1980s was contracted at interest rates only marginally below those observed in the international markets, debtors were given longer grace periods than those offered by the IMF before initial repayments of principal and interest were due, and repayments were generally spread over a greater period of time, allowing the long term returns to projects to materialise before debt servicing obligations began.

The multilateral institutions have also differed in terms of their primary capital sources used for funding traditional 'hard window' non-concessional lending. In lending for short run economic stabilisation programmes, the IMF has generally used funds gained from quota increases paid in by 'shareholder' countries. As Jack Boorman of the IMF explained to the Working Party, quotas held by the IMF are officially counted as international reserves by contributor countries, and must be available for withdrawal by the respective governments at as little as three days notice. The IMF therefore argues that in order to maintain the Fund's ability to honour requests for a release of member governments' reserves, loans contracted using these funds must correspondingly be short term in nature, with the overall exposure of the Fund at any one time restricted to an acceptable level. In financing their non-concessional lending, the World Bank and the Regional Development Banks have depended on both capital subscriptions from member countries and the international capital markets, using the financial guarantees of member governments as collateral in securing funds at favourable rates. This has allowed scope for longer payback periods for developing country debtors as private creditors have been confident of the banks' abilities to repay.

In response to the deteriorating economic situation and dwindling inflows of foreign exchange witnessed in many sub-Saharan African countries through the early mid-1980s, pressure was applied by both debtor and creditor governments for the multilateral institutions to engage in programmes of lending to developing countries outside their usual framework of objectives. Rather than being reserved for use in the attainment of specific economic goals, untied multilateral loans were utilised by many low income African countries for general domestic expenditure purposes, including the purchase of imports for immediate consumption and large programmes of defence spending, which provided no perceptible economic return. Lending by the IMF was particularly unsuitable for such functions because of the short term nature of the Fund's financing operations, but this did not deter a substantial number of desperately underfinanced low income countries from utilising IMF and other IFI provided finance in roles which gave very low or even negative rates of return. In addition a large proportion of the short term IMF lending directed towards balance of payment relief in sub-Saharan Africa was failing to attain its objectives, and the Fund now admits it was as guilty as the rest of the world in judging the economic problems of Africa to be caused by insufficient volumes of liquidity, rather than a lack of solvency. At the same time a significant proportion of development bank projects implemented in sub-Saharan Africa were failing to reap positive returns, but although these were being officially recognised as failed initiatives the recipient African countries were still being held liable for servicing the full debt stocks resulting from these projects. Clearly the repayment of principal plus interest on loans which had been unproductive put additional stress on diminished domestic budgets, and rising debt servicing requirements contributed to the economic decline of many sub-Saharan African countries throughout the mid-1980s.

The Preferred Creditor Status of the IFIs

The multilateral institutions were aware of the onerous task faced by many financially distressed countries in honouring debt service obligations, and in order to ensure that repayments were maintained in an environment in which numerous other creditors were also pressuring debtor countries for debt maintenance, they fostered the concept of a 'preferred creditor' status for multilateral institutions in general, and notably for the IMF and the World Bank in particular. With the support of bilateral donors, the multilateral institutions made it clear that any country failing to honour debt servicing obligations on multilateral loans would become automatically ineligible for further credits from these institutions, and in the case of non-payment to the IMF would lose access to the Paris Club rescheduling mechanism. In addition in certain circumstances the automatic suspension of bilateral aid flows would follow.

The case advanced by the multilateral institutions to support their preferred creditor status centred around the need to protect their 'AAA' credit ratings on the international capital markets, proposing that if multilateral institutions were seen to be allowing debtors to default on loans they would no longer be given access to international funds at below market interest rates. It has been suggested to the Working Party that this argument is not entirely valid in that much of the confidence held in the multilateral institutions' ability to repay stems from the callable capital guarantees offered by donor governments, rather than the security of the loans outstanding.

The Arguments Against Debt Write-Offs

Although the multilateral institutions maintained their preferred creditor status, the overall debt service to export earnings ratios of a number of sub-Saharan African low income countries reached such serious levels by the late 1980s that even obligations to multilaterals were at risk from default. Anticipating this, and partly because of pressure applied by bilateral creditors, who were experiencing increasing volumes of debt defaults as a result of the IFIs' preferred creditor status, the multilateral institutions began to review their strategies in approaching the needs of severely indebted low income countries. The IFIs as a group refused to implement either debt write-offs or official debt rescheduling, saying that, similar to allowing non-payment of debt service obligations, such actions would jeopardise the multilaterals' favourable access to the international capital markets. They also advanced the 'moral hazard' argument, suggesting that allowing countries which are suffering severe economic problems a reduction in debt stocks and servicing obligations owed to the multilateral institutions would create the impression that a failure to undertake adjustment can result in a more favourable treatment by some of the most significant creditors of developing countries. Indeed some of the strongest advocates of this argument have been those developing countries which have successfully, although often painfully, achieved economic reform, and see no reason why severely indebted countries should now be accorded preferential treatment and drain the overall funds available for use by developing countries.

Nevertheless, it became clear to the multilateral institutions that to continue to lend large volumes of non-concessional funding to the most severely indebted African countries would only serve to exacerbate the debt crisis in the long run, and would increase the risk of a wide scale default on outstanding IFI loans at a later stage.

Concessional Facilities

In response to the deteriorating economic situation facing many Third World SILICs, the multilateral institutions have each devised systems through which the poorest nations are able to borrow money on concessional terms. In addition the major multilaterals have also instituted programmes to assist in relieving the debt burdens of some of the countries most severely affected by debt; this has not involved debt reductions or rescheduling, but has been attempted through new rounds of refinancing. Access to the resulting 'soft window' lending and assistance options has generally been limited to nations officially categorised as being low income, which in 1993 the World Bank defined as countries with annual per capita GNPs of less than $675,[7] and to those governments following prescribed economic and financial reforms.

The IMF

The Structural Adjustment Facility

In 1986 the IMF launched the Structural Adjustment Facility (SAF), which provided concessional loans to severely indebted low income countries on the proviso that they engage in a Fund designed programme of structural reform. The founding of the SAF marked an official change in the IMF's role in the international economy, establishing it as a donor institution committed to promoting economic development rather than solely the macroeconomic facilitator and adviser which its founding charter had originally envisaged. The operation of the SAF was centred upon the allocation of a concessional loan which was generally disbursed in tranches, with the release of each additional tranche being conditional on the country having successfully fulfilled a number of Fund-specified economic criteria. Typical targets included a reduction of budget and trade deficits and a squeezing of inflation. The original round of lending conducted within the SAF was funded using the revenues from sales of small amounts of IMF gold stocks in the late 1970s, combined with capital contributions from member state governments, but subsequent replenishments relied solely on the generosity of donor governments.

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[7] World Bank, *World Debt Tables, 1993–94*

The Enhanced Structural Adjustment Facility

In 1988 the operations of SAF were complemented by the formation of the Enhanced Structural Adjustment Facility (ESAF), which allowed countries to borrow larger sums of concessional finance but imposed tighter conditionalities than SAF. In a similar fashion to SAF, ESAF is financed using contributions from Fund member governments. The use of donor funds has allowed the IMF to extend the repayment schedules contracted on SAF and ESAF loans relative to those available on non-concessional Fund loans, with grace periods of 5.5 years and repayment of 10 years, and an overall interest rate of 0.5 per cent per annum. Following the expiry of SAF in 1992 the use of ESAF has been expanded to cover all IMF concessional programme lending to developing countries. Using SAF and ESAF the IMF has managed to maintain a positive net flow of funds to sub-Saharan Africa as a whole over recent years, and a large proportion of debt owed to the Fund is now contracted on a concessional basis. Nevertheless, country specific situations have differed considerably, with some of the world's poorest states burdened by net outflows of finance to one of the world's richest institutions.

Some criticisms of the operations of both SAF and ESAF in sub-Saharan Africa have been made. Non-Governmental Organisations concerned with Third World issues told the Working Party that the rigorous nature of the conditionalities attached to SAF and ESAF lending, combined with the relatively short run repayment schedules, have made both adjustment facilities unsuitable for use in sub-Saharan Africa. It was proposed that the adoption of SAF and ESAF programmes had done more harm than good in some of Africa's most indebted countries, and a lack of social orientation in many of the conditionalities had resulted in a deepening of the poverty of the poorest sections of society. In a number of recipient countries difficulties with SAF and ESAF programmes have been associated with a change in circumstances between the planning and implementation stages. A number of speakers addressing the Working Party have been critical of the Fund for not adopting a special contingency facility, wherein debt contracted through a structural adjustment programme would be either rescheduled or, in the extreme case, written-off in the event of an adverse change in pre-specified circumstances. Indeed, Carolyn Culey of Oxfam suggested that African countries are in general very reluctant to engage in ESAF programmes because of the harshness of the conditionalities and the associated lack of flexibility, and she pointed out that in 1993 $4bn of ESAF funds remained undisbursed due to a shortage of willing borrowers.

In defence of the operations of the Fund's adjustment policies, Anthony Nelson MP, Economic Secretary to the Treasury, suggested that both SAF and ESAF had fulfilled vital roles in encouraging economic reform in sub-Saharan African SILICs, roles which by their nature automatically prove to be unpopular both domestically and internationally and would not be adopted by other creditors. Mr Nelson felt that although many of SAF's and ESAF's critics feel duty bound to object to their operations, in reality it is likely that they believe both facilities have made positive contributions to the economic well being of recipient countries. He maintained that SAF and ESAF had allowed many domestic governments to implement essential economic policies whilst effectively using the IMF as a scapegoat for the social pressures resulting. However a significant number of IMF member countries showed some considerable reluctance in contributing to the ESAF II replenishment in early 1994. The UK pledged only an additional £50m to the ESAF extension (it has pledged £327m to the interest subsidy account over the lifetime of the facility), and the US has adopted a hard line in dealing with the replenishment, initially withdrawing the pledge of $100m for ESAF planned for the 1995 fiscal budget. The Senate appropriations committee has recently restored $25m of this pledge, but even the US Treasury is quoted as saying this is 'a meagre share for the largest economy in the world' (Financial Times, 15/6/94). Although the Fund has championed the fact that the largest number of countries yet contributed to this replenishment, including a significant number of developing countries which are themselves 'graduates' of earlier SAF and ESAF programmes, it was forced to cut the initial replenishment requirement from $6bn to $4.5bn because of a lack of donor support. While reluctance to contribute may be associated with recession and pressure on oda budgets in many of the developed countries, it also indicates a degree of dissatisfaction with the ESAF mechanism as a whole, which some critics claim is mirrored by many of the developing countries targeted for ESAF programmes.

Rights Accumulation Programme (RAP)

Despite the provision of additional volumes of concessional lending via the operations of SAF and ESAF, over recent years net flows from the IMF to sub-Saharan Africa have been only marginally positive, and for a number of severely indebted countries have in fact been negative (it was suggested to the Working Party that in 1994 aggregate net flows from the Fund to sub-Saharan Africa will be negative to the magnitude of $0.2bn). Partly as a result of strong outflows of capital from already financially stressed domestic economies, the Fund has been faced by the threat of default in debt servicing from an increasing number of sub-Saharan African countries. The Working Party was informed that by 1991 SILIC debtor countries, of which a large majority were situated in sub-Saharan Africa, had accrued SDR 3.6bn of unpaid debt service to the IMF, with this figure falling to SDR 3bn by 1993 following the clearance of arrears owed by Peru. Although the IMF has consistently refused to consider either the write-off or rescheduling of outstanding debt service and arrears, it has accepted that a number of countries unable to honour their debt servicing obligations are deserving of assistance. It was with the aim of enabling countries in arrears to clear their overdue debts to the IMF that the Rights Accumulation Programme (RAP) was initiated in May of 1990. The RAP requires countries in arrears to commit to a three year structural adjustment programme, similar to that entailed in the implementation of an ESAF programme. If the programme is deemed by the IMF to be successfully completed over the designated period, the Fund agrees to disburse substantial sums of additional funding to the country with which it can repay the majority of its arrears. However the net flow of transfers from the Fund to the indebted country is negative during the three year adjustment period, as no new disbursements are released from the IMF, whilst interest charges on the arrears and current debt servicing maturities still apply.

It is generally during periods of structural adjustment that indebted countries are most in need of positive flows of external finance, and countries which have accrued large volumes of arrears with the IMF are likely to be in an extremely desperate balance of payments position and will therefore have little in the way of reserves to fall back upon. Countries which have thus far been recipients of RAPs have been forced to request bridging loans from sympathetic bilateral creditors with which they can finance the charges due to the IMF and also fund the adjustment process. This has meant that the debt financing burden falls on bilateral aid budgets, reducing the funds available for other, possibly more productive, bilaterally funded lending programmes. Indeed the RAP implemented in Zambia failed primarily because of a lack of funds during the period of adjustment. It was indicated to the Working Party that HMG is concerned about the operations of the RAP and the demands it imposes on Britain's ODA budget, but when questioned Mr Boorman felt that it made very little difference whether the bilateral donors contributed directly to countries undergoing RAPs or via their contributions to the ESAF fund, which would be the alternative source of finance if the IMF was pressured to engage in additional lending during the adjustment period. It was imperative that the IMF was seen to be collecting current payments due from all debtor countries, irrespective of their economic positions, and economic rationale demanded that in the short term it should not disburse additional volumes of lending to countries which were unable to service debt stocks already held.

The World Bank

The initiatives implemented by the World Bank over recent years in attempting to ease the debt-related problems of sub-Saharan African SILICs have been praised by a number of individuals consulted by the Working Party, both for their innovation and their efficiency. The Bank has consistently refused to implement debt write-offs or official programmes of rescheduling, and large stocks of non-concessional IBRD loans still remain outstanding throughout the African continent, with debtor countries obliged to honour their full service obligations on these debt stocks.

IDA

In the late 1980s the World Bank, like the IMF, realised that continued lending on non-concessional terms to severely indebted countries would jeopardise the chance of service payments being maintained on IBRD debts already outstanding, and would seriously hinder the prospects of economic growth in countries which were already burdened by debts they could not afford to service. Subsequently the Bank increased its lending operations through its concessional affiliate, the International Development Association (IDA), disbursing large quantities of funds to low income countries at highly concessional rates of 0.75 per cent per annum. IDA loans have typically been contracted on more relaxed repayment terms than those disbursed through SAF and ESAF, with 10 year grace periods followed by 30 year repayment periods. This has allowed severely indebted countries to utilise IDA provided funds in programmes of spending which have only low immediate returns, but over the long run contribute significantly to the economic prosperity of the domestic economy, so fitting in with the overall objectives of the World Bank to promote economic development. The broad lending objectives of the IDA received praise from a wide variety of individuals addressing the Working Party, and it was suggested that the World Bank should be pressured to increase the volume of IDA loans it disburses over the near future.

Access to IDA lending is presently restricted to low income countries, and is financed using contributions from World Bank member governments. Although the last replenishment round conducted in 1992, IDA–10, raised generous contributions from donors, many recipient low income countries are already approaching the ceilings on funds allocated for their use, and are thus facing the prospect of having insufficient funds to finance ongoing long term development programmes. In addition, increased pressure is being applied on IDA resources as more developing countries slip into the low income classification and become eligible for IDA lending. There is correspondingly a need for IDA funds to be increased, and with donor countries experiencing severe pressures on aid budgets, an additional source of income is required. At present relatively small volumes of IBRD profits and reflows are transferred to IDA accounts (between 1981–93 the IBRD transferred only $2,342m to IDA and the Special Fund for sub-Saharan Africa), and many commentators have suggested that these transfers should be expanded in future to represent the primary source of IDA funds, rather than making further calls on bilateral aid budgets.

Although the overall objective of IDA lending has been widely praised, it has been suggested to the Working Party that there remains considerable room for improvement in the actual implementation of both IDA and IBRD lending programmes. The Bank's own Wapenhans report concluded that 37.5 per cent of projects completed in 1991 were judged unsatisfactory. Furthermore, the Bank's 'non-project' lending (loans used in Structural Adjustment Programmes, SAPs) has accounted for 21 per cent of its lending over the early 1990s, and the most recent World Bank report on Africa admits that there has been only a weak correlation between structural adjustment lending and policy change. This suggests that the performance of Bank lending could be worse than quoted in the Wapenhans report. The Working Party's concern is that this puts exceptional pressure on recipient countries which remain obliged to repay both principal and interest on the poorly performing loans.

Net Flows

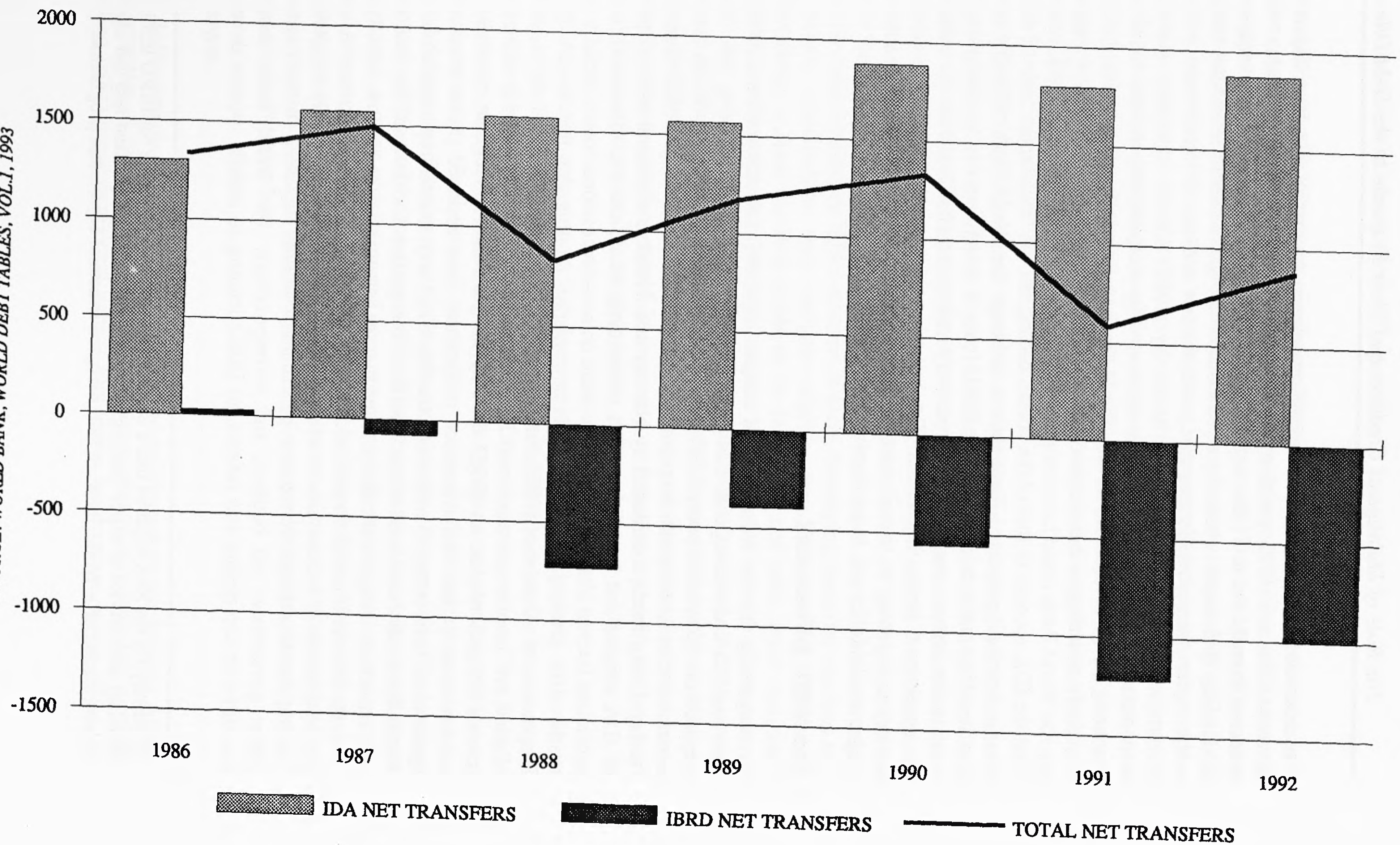
Despite disbursements of large volumes of concessional finance to sub-Saharan Africa via the activities of the IDA over recent years, the existence of substantial sums of outstanding IBRD non-concessional debt in this region has to some extent offset the gains accrued from the increased concessional flows. As can be seen from Figure 4.1, between 1986 and 1992 positive net flows of IDA funds to sub-Saharan Africa increased from $13bn to $19bn, with only very low levels of service being required on outstanding IDA loans, whilst for all but one of the years overall IBRD net transfers to the region were strongly negative, with the net outflow of interest and principal repayments increasing to around $10bn by 1992. Clearly therefore significant proportions of the IDA disbursements were used by recipient low income countries in honouring IBRD obligations to the World Bank during this period, with the funds effectively returning to their source in Washington. A number of critics have suggested that the World Bank could have simplified its operations by transferring funds internally from the IDA account to that of the IBRD, cutting out the 'middleman' role of the low income developing country. Nevertheless, although the World Bank officially refuses to write-off or reschedule outstanding IBRD loans, it recognises that by disbursing IDA loans to low income countries it is effectively refinancing IBRD debt stocks with loans on concessional terms. The use of IDA loans in such operations assists the recipient country in lessening its overall debt burden, but clearly the concessional finance is no longer available for use in productive projects.

The 'Fifth Dimension'

In recognising that the refinancing of outstanding IBRD non-concessional debt using increased IDA disbursements has only partially assisted in reducing the burdens imposed on the world's poorest developing countries, since 1988 the World Bank has attempted to reduce the interest payments due on IBRD debt using its 'fifth dimension' facility. Using funds contributed by Norway and Sweden, combined with 10 per cent of IDA reflows and income on IDA outstanding loans, the fifth dimension scheme subsidises interest charges owed to the Bank on non-concessional loans. Initially access to the fifth dimension was limited to countries eligible for the Bank's Special Programme of Assistance (SPA) for Africa,[8] but this was soon extended to all IDA eligible low income countries, and by 1990 the scheme was effectively reducing the interest obligations due on IBRD debt by 90 per cent for recipient countries. The achievements of the fifth dimension programme have received praise from a wide spectrum of commentators addressing the Working Party, and its implementation by the World Bank has been heralded as unofficial recognition for the need for multilateral debt reduction, though it should be noted that the impetus for the scheme initially came from the Nordic bilateral donors, and large contributions from these countries are still required for the fifth dimension to operate effectively. It has been widely suggested that funding for the scheme should now be increased without imposing further burdens on donor government aid budgets, and correspondingly the World Bank should be pressured to use profits and reflows on IBRD lending to middle income developing

[8] Eligibility for the SPA required that a country was officially ineligible for IBRD lending, had an annual debt service to export earnings ratio of greater than 30 per cent and had agreed the implementation of a World Bank or IMF designed structural adjustment programme.

FIGURE 4.1: IBRD, IDA AND TOTAL WORLD BANK NET TRANSFERS TO SUB SAHARAN AFRICA, US $MILLION



SOURCE: WORLD BANK, WORLD DEBT TABLES, VOL.1, 1993

countries to subsidise both interest and principal repayments due on low income country IBRD debt stocks. In addition, Mr Susungi of the AfDB suggested that access to the fifth dimension programme should be extended to middle income countries which are struggling under exceptionally large debt burdens, a large proportion of which consist of non-concessional IBRD debt.

The Debt Reduction Facility

The World Bank has not only concentrated on alleviating the debt burdens imposed by its own outstanding loans in low income developing countries. Using the net income from IBRD lending operations, in 1989 the Bank established the 'Debt Reduction Facility (DRF)', more commonly known as the 'sixth dimension'. This facility has concentrated on disbursing grants to IDA-only eligible low income countries for use in reducing the debt stocks owed to commercial banks, which has generally been achieved by performing debt-buyback operations on the recently emerged international secondary markets for debt. By late 1993 five countries had taken advantage of the sixth dimension (three of which, Mozambique, Niger and Uganda, are situated in sub-Saharan Africa), and the Working Party was informed that in Uganda the use of the facility had assisted in creating a favourable environment for increased foreign investment and reflows of flight capital. Indeed by 1994 virtually all of Uganda's commercial debt stock had been eliminated, reducing total debt stocks by 6 per cent. However, in most countries eligible for assistance from the DRF large proportions of service due on commercial debt stocks are not being honoured, and commercial creditors are generally resigned to the inevitability of having to write-off much of their outstanding capital. The World Bank should be encouraged to continue operating its sixth dimension facility for countries heavily indebted to commercial creditors, providing this does not take precedence over initiatives designed to reduce the burden imposed by multilateral debt stocks.

The African Development Bank (AfDB)

The AfDB has lent much less to sub-Saharan African countries than either the IMF or the World Bank, but is emerging as a key player in the evolution of the present sub-Saharan African debt crisis, receiving a large proportion of the debt servicing payments of some of the continent's poorest nations. The AfDB is facing the threat of default from several severely indebted African countries, and many commentators predict a bleak future for the Bank if changes are not implemented.

The core of the AfDB's problem stem from the high proportion of non-concessional funds held in its portfolio of outstanding loans, a substantial volume of which are now reaching maturity and are requiring repayment. During the late 1980s, when the Bretton Woods 'twins' were finally accepting the severity of Africa's debt dilemma and were suspending their disbursement of non-concessional finance to the poorest countries, the

AfDB continued to lend substantial volumes of finance through its 'hard window' non-concessional facility. For low income countries, the offer of finance from either the Fund or the Bank was made conditional on the implementation of an official programme of structural reform, and as a result rather than lose control over their domestic economies many governments turned to the AfDB for assistance, receiving loans with very little in the way of conditionality but which were contracted on hard terms.

In a similar fashion to the World Bank, the AfDB has an affiliate organisation, the African Development Fund (AfDF), which engages in programmes of lending on concessional terms to the poorest African countries (typically on an annual interest rate of 0.75 per cent with a 10 year grace and 50 year repayment period). Unlike the World Bank though, the AfDB has been relatively unsuccessful in using AfDF loans to unofficially refinance non-concessional debt stocks. The AfDF is financed by donor government contributions, which have been of an insufficient volume to meet all the requests for finance made by Africa's low income countries over recent years. Subsequently, rather than refuse severely indebted countries much needed funding, the AfDB has agreed to disburse additional volumes of non-concessional hard window finance on relatively short term contracts, often to countries which are uncreditworthy and have generally been recognised as such by the international community. As a result a significant proportion of the AfDB's outstanding debt stock is of low quality, and it was indicated to the Working Party that a large number of member governments, the UK included, are very concerned as to the future of the AfDB, and are forcing the Bank's management to review their lending criteria before fresh contributions are made.

It was suggested that the most practical course of action to relieve the dilemma faced by the AfDB and maintain its credit rating on the international capital markets would be for the AfDF to engage in a round of concessional lending in countries most troubled by AfDB debts, and for the AfDB to implement a facility similar to the fifth dimension of the World Bank for use by the poorest and most severely indebted African countries. The former action would require a large amount of donor government generosity in the forthcoming AfDF replenishment, and the latter would require a supplemental source of funding to compensate for the exceptionally low returns earned from AfDB non-concessional lending, again exerting pressure on governments to dip into their already hard-pushed bilateral aid budgets.

5

Options Open to the IFIs in Implementing Further Debt Relief

Although the multilateral institutions have implemented a number of measures aimed at reducing the debt burdens of some of the poorest and most severely indebted developing countries, it is evident that these initiatives have not gone far enough, and a large number of poor countries in sub-Saharan Africa are still being drained by high outflows of foreign exchange paid to creditors, a substantial proportion of which are going to multilateral institutions.

Representatives of the IMF, the World Bank and the AfDB all agreed that there was now a requirement for both debt stocks and overall debt servicing obligations to be reduced for the sub-Saharan African SILICs. There was also a strong consensus of opinion as to how this should be achieved, namely via bilateral and commercial debt reschedulings and write-offs, particularly through the operations of the Paris and London Clubs. This line of thinking is by no means a recent development. The multilateral institutions have consistently been prepared to shift the burden of debt reduction and relief on to bilateral and commercial donors, either through their preferred creditor stance or their requirement that concessional lending operations be funded using donor contributions.

It was explained to the Working Party that the patience of many bilateral donors in supporting the multilateral institutions is now beginning to wear thin, particularly in light of the efforts made to initiate substantial debt relief via the Paris Club, only for the benefits resulting to be engulfed by growing debt service commitments to IFIs. Indeed, it was felt that HMG is not prepared to allow large proportions of its bilateral aid budget to be used in financing multilateral debt stock maintenance for very much longer, and the recent generosity shown by Britain and other bilateral donors towards both debt relief and multilateral inspired operations has effectively been intended to shame the multilateral institutions into initiating their own programmes of debt reduction. Pressure is therefore being applied for the multilateral institutions to relax their stance on debt relief.

The Moral Hazard Argument

Here we examine the validity of the factors used by the IFIs to support their reluctance to implement debt write-offs and reschedulings. One of the core issues proposed by the IFIs against debt reduction has been the moral hazard argument, wherein the introduction of debt reductions for those countries most seriously burdened by debt stocks would appear to be rewarding a failure to implement economic reform. Although the moral hazard argument receives widespread support from both IFIs and numerous member governments, it has been shown to be invalid when dealing with developing country debt stock reductions. In the early 1980s commercial banks widely cited the moral hazard argument in supporting their reluctance to write-off outstanding loans, but following the substantial commercial debt stock reductions of the mid late-1980s (which in many cases resulted from pressures exerted by the major IFIs) it was seen that recipient low income countries had not generally been encouraged by the initiatives to engage in irresponsible borrowing and economic mismanagement.

The Preferred Creditor Status

The other primary factor promoted by the multilaterals in supporting their inflexible stance has been the need to maintain their flawless credit ratings on the international capital markets. It was suggested to the Working Party that if the multilateral organisations lost their access to credit on favourable terms as a result of a perceived increase in the risks associated with lending to the IFIs, developing countries as a whole would have to shoulder the burden of higher interest rates on multilateral lending programmes. As previously noted though, the confidence held by international investors in the multilateral institutions can primarily be associated with the callable capital guarantees offered by member governments, rather than the abilities of debtor countries to honour their obligations. It has also struck the Working Party that the recognition of a bad debt and its corresponding write-off or rescheduling is standard banking practice in the commercial sector, and to be seen to be acting in a responsible fashion by identifying debtors which are unlikely to remain current on their service requirements, and consequently responding in a positive manner, should enhance the IFIs' standing on the international capital markets. The present practice of insisting that all obligations are honoured, irrespective of the debtor country's ability to pay, appears to be both irresponsible, and in banking terms, foolhardy, and if anything should have the effect of suppressing investor confidence in the IFIs' overall creditworthiness. In addition, it has been pointed out to the Group that although the multilaterals have already initiated limited measures to relieve the debt burdens of the poorest developing countries, this has done little to affect their standing on the international capital markets, indicating that international investor confidence has been more resilient than the managements of the IFIs generally suggest.

The Working Party is increasingly persuaded, therefore, that rather than being unable to implement debt write-offs and rescheduling as they suggest is the case, the multilateral institutions have instead been taking advantage of their dominant position in the international economy, and may be shirking their responsibility to accept a share of the burden in assisting the world's poorest countries. Although the multilaterals are 'owned' by member governments, in reality the opposite situation has emerged, wherein the IFI managers have manipulated bilateral donors into bearing too much of the burden of the present sub-Saharan African debt crisis. As bilateral donors begin to tire of this, the time has come for the multilaterals to review their attitudes to debt reduction and rescheduling.

In receiving evidence from representatives of the major multilateral institutions, the Working Party concluded that although the IFIs officially opposed the idea of implementing debt rescheduling and reduction, in practise each institution was providing debt relief through their concessional facilities. Jack Boorman of the IMF told the Working Party that ESAF lending to a severely indebted low income country was equivalent to the IMF granting one third debt stock relief on a net present value basis. The activities of the IDA and the AfDF were similarly advanced as examples of refinancing of multilateral non-concessional debt stocks on concessional terms. But, although the multilateral institutions are keen to take credit for these measures, when designing programmes of debt relief, most notably concessional lending facilities such as ESAF, IDA and AfDF, the IFIs have traditionally placed a great deal of emphasis on funds contributed from donor countries, arguing that the implementation of special programmes of assistance for severely indebted countries should not reduce the volumes of funds available for use in programmes of lending to other developing countries. This has correspondingly exerted pressure on donor aid budgets, which have been concurrently squeezed by domestic constraints. While pressing for the introduction of additional measures of debt relief, both through debt reductions and expanded programmes of concessional lending, the multilateral institutions should be pushed to consider making a first call on their own resources.

When questioned regarding the practicalities of using their own funds in programmes of debt relief, representatives of the multilaterals responded with unanimity in claiming that the reserves held by the IFIs were essential to the day to day operations of the respective institutions. This has been disputed by a number of independent commentators briefing the Working Party, who have suggested that the Bretton Woods twins hold capital reserves of a sufficient magnitude as to enable them to initiate large scale programmes of debt relief without compromising their roles in the international economy. At the same time it has been widely accepted that the AfDB's finances are in too perilous a state to be able to afford either debt write-offs or reschedulings. It is therefore helpful to examine the resources available to the IMF and the World Bank for potential use in debt relief, and to determine the validity of the reasons proposed by the respective institutions for not mobilising these resources in this role.

The IMF

The IMF holds substantial volumes of capital in its General Resource Account (GRA), but it was explained to the Working Party that these resources essentially represent capital reserves held by the IMF on behalf of specific contributing countries. These reserves remain the 'property' of the country in question, and must be available for withdrawal from the Fund at as little as three days notice. Correspondingly, the use of GRA funds in financing debt relief would effectively place the burden upon member countries rather than the Fund itself, and would be strongly opposed by domestic central banks.

In addition to the GRA, the Fund also holds a volume of reserves for unofficial use in a provisioning role. Jack Boorman argued that the utilisation of these resources in debt relief would set a precedent for the IMF, and as a consequence the institution's board would insist on an expansion in the reserves held for provisioning, primarily to cater for the perceived increased risk of non-payment of outstanding debt. The replenishment of the Fund reserves would have to be achieved by either lending on less concessional terms or reducing the remuneration paid to creditor countries. The latter is unfeasible under the present Fund articles, which state that remuneration to creditors must not fall below 80 per cent of the SDR interest rate, which is the level currently being applied. Correspondingly the burden of replenishing the Fund reserves would fall on countries heavily reliant on IMF lending, notably those in the developing category, thus nullifying the effects of the initial measures of debt relief.

It has been suggested to the Working Party that an effective option open to the IMF in funding additional measures of debt relief would be the distribution of a one-off SDR allocation to low income countries. This was dismissed as impractical by the Fund representative, who explained that under its present articles, the Fund allocates SDRs on a country specific quota basis, with the size of the respective quotas being determined by the contributions payed in by that country. Correspondingly, low income countries, particularly those in sub-Saharan Africa, typically hold only small quotas, and would thus receive a very limited proportion of any SDR allocation. In addition, when a country utilises SDRs in an international transaction, it is immediately charged interest at market rates on the outstanding funds. The use of SDRs under the present Fund statutes would therefore have the effect of refinancing outstanding IMF debt with non-concessional lending, thus further exacerbating the sub-Saharan African debt dilemma in the long run.

In addition to the capital reserves held for use in GRA lending and unofficial provisioning roles, the IMF holds a substantial stock of gold, estimated to be approximately 100m ounces (40bn SDRs). Over recent years widespread pressure has been applied on the Fund to sell a proportion of its gold stocks and use the revenues in funding programmes of debt relief. The governments of Britain and the United States have featured amongst the most ardent advocates of such a measure. It was in this area that the Fund's arguments opposing mobilisation of its own resources were judged to be weakest. Jack Boorman suggested that the gold stocks represent a substantial source of confidence in the financial stability of the IMF, and that during the 1980s, when the problem of arrears to multilaterals initially emerged, the only thing which persuaded central banks not to withdraw their holdings in the Fund was the substantial volumes of gold held in reserve in the Washington vaults. Other speakers found this argument invalid, proposing that confidence in the Fund's financial standing is maintained on the basis of donor governments' callable capital guarantees, rather than its reserves of gold. Indeed, the use of gold sales in funding IMF operations would by no means be setting a precedent; in the late 1970s substantial quantities of Fund gold were sold, the revenues being used to finance the establishment of the Trust Fund, and more recently, the first SAF round. Nevertheless, it was questioned as to whether now would be the right time for a depletion of the Fund's gold stocks. International gold prices are presently low, and could depreciate further. In addition, Jack Boorman pointed out that the IMF is presently being pressured by donor governments to adopt a substantial role in assisting Eastern Europe and the Former Soviet Union (FSU), primarily through the use of GRA lending. Without the financial security provided by the large gold stocks, the Fund would be reluctant to engage in large programmes of non-concessional lending.

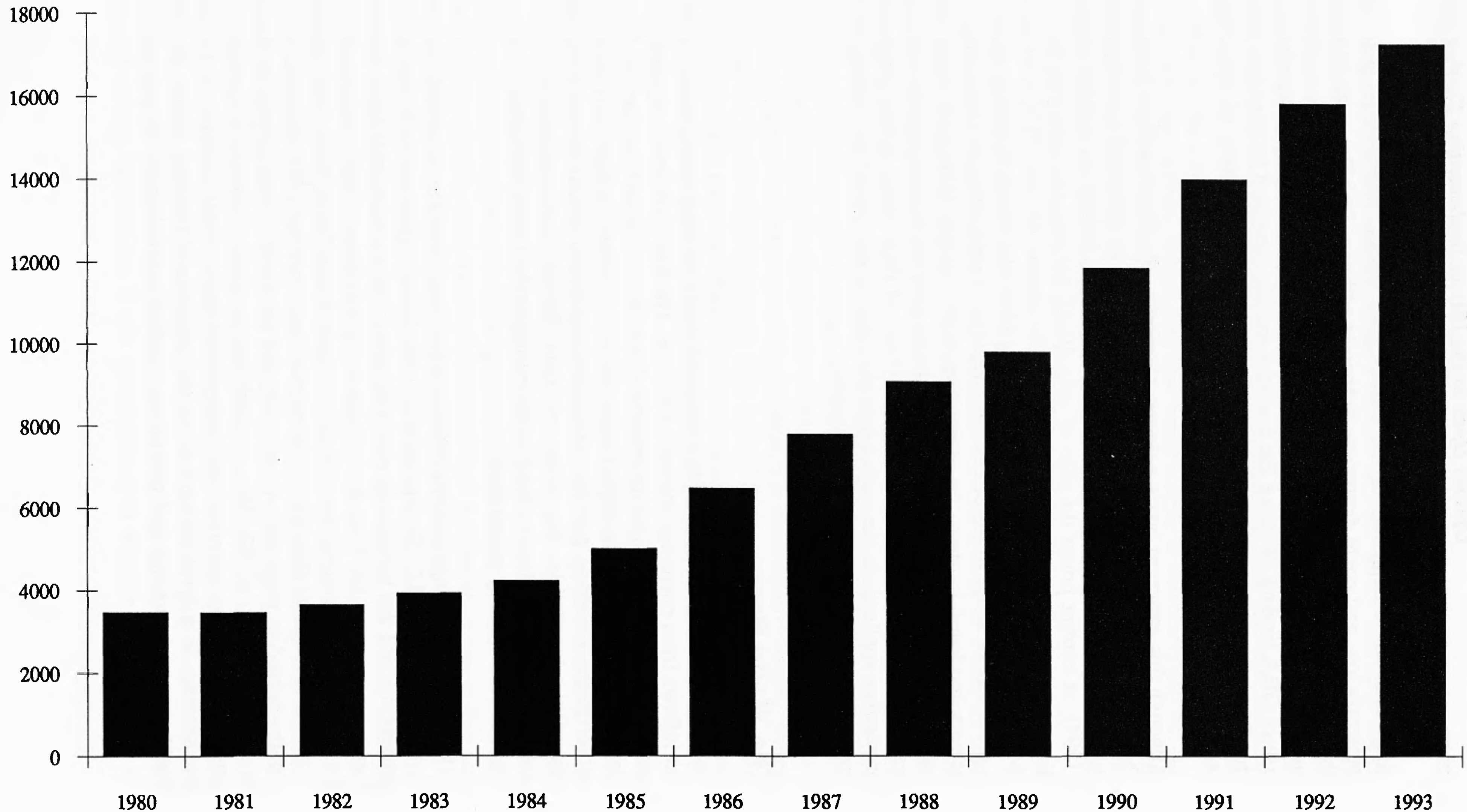
Although this argument holds a degree of validity, the Working Party believes that the IMF gold stocks are of such a volume as to be able to withstand a moderate reduction without reducing the Fund's overall capital security. Indeed, as pointed out by Mistry (1994), at current prices the sale of only 10–12 per cent of Fund gold stocks would finance a total write off of all outstanding sub-Saharan African SILIC debt owed to the IMF. Even a relatively small reduction in gold stocks would therefore allow the IMF a great deal of scope in implementing measures of debt relief for those countries most heavily burdened by debt. An alternative would be that IMF gold stocks should be utilised in a productive role, rather than being hoarded in Washington vaults, with the resulting revenues being used in programmes of debt relief. It was pointed out that productive applications for such substantial gold stocks would be limited, but that the proposition holds a great deal of potential.

The World Bank

The World Bank presently holds substantial assets which are continually bolstered by net inflows from numerous sources of income. The Bank's defences against insolvency and default include principal repayments due each year, annual income, the Special and General Reserves, paid-in capital subscriptions, outstanding loans and callable capital subscriptions. Reserves, paid-in and callable capital and annual income alone are worth approximately double the value of total World Bank outstanding loans, and correspondingly the Bank's 'AAA' credit rating on the international money markets can be regarded as firmly guaranteed.

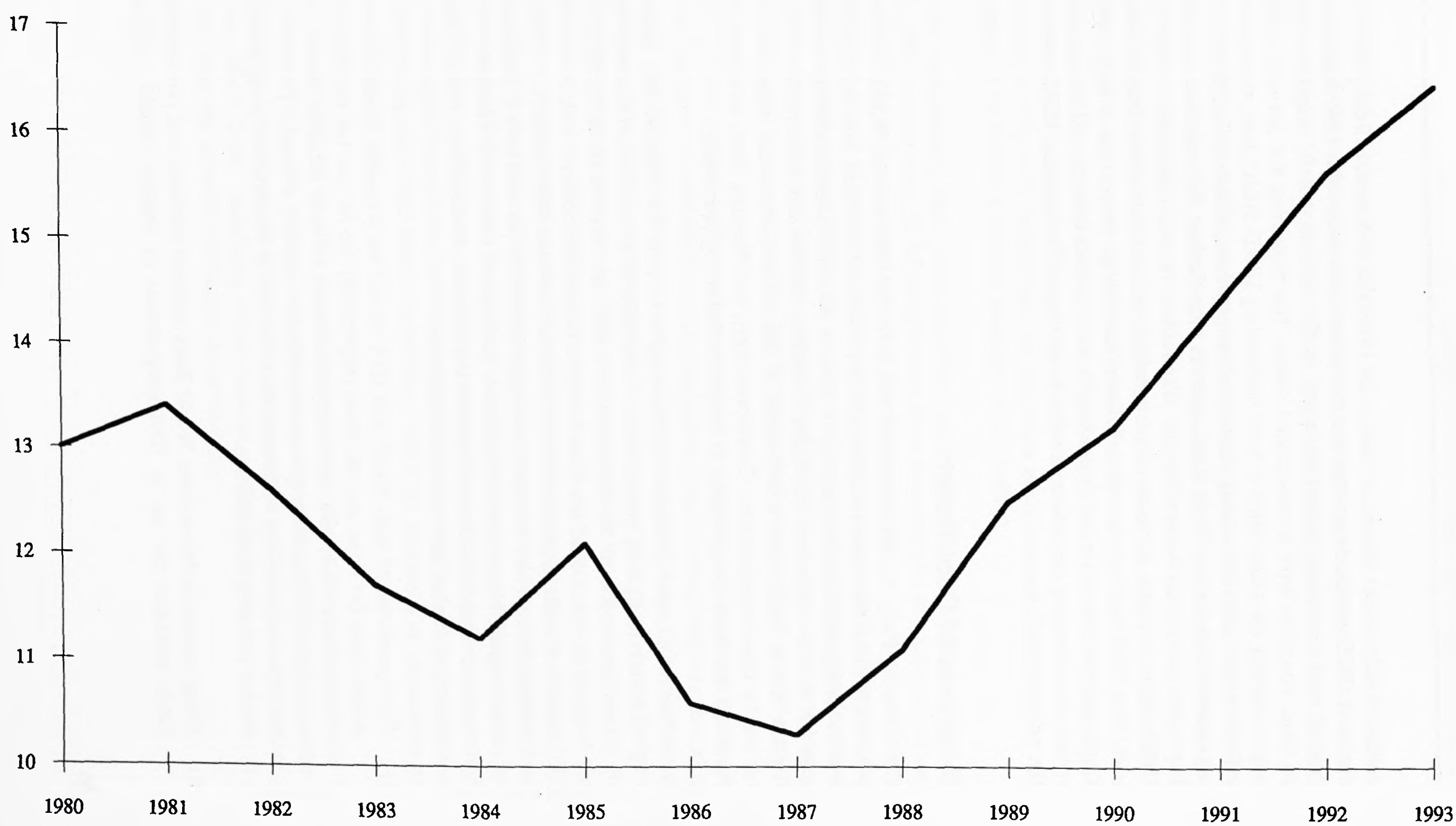
IBRD retained earnings and provisioning have risen since the mid-1980s as illustrated in Figures 5.1 and 5.2. To an extent this has been in response to an expanding loan programme and the increase in countries placed on a non-accrual basis because their loan repayments to the Bank have fallen more than three months behind schedule. On the other hand, no country has officially defaulted on a World Bank loan, and only two of the eight countries placed on a non-accrual basis between 1985–90 are still over three months behind in payments – suggesting that the Bank is usually paid in the end. To have provisioning of $3.15bn, in addition to huge reserves, to cover principal outstanding to those countries on a non-accrual basis of just $2.50bn, or 126 per cent provisioning, is a level unheard of in the commercial banking sector. In 1986, the Bank's retained earnings and provisions equalled approximately 10 per cent of total

FIGURE 5.1: WORLD BANK CUMULATIVE RETAINED EARNINGS AND PROVISIONS FOR BAD DEBT, US $MILLION



SOURCE: WORLD BANK, ANNUAL REPORT, VARIOUS YEARS

FIGURE 5.2: WORLD BANK CUMULATIVE RETAINED EARNINGS AND PROVISIONS FOR BAD DEBT AS A PERCENTAGE OF TOTAL LOANS OUTSTANDING



SOURCE: WORLD BANK, ANNUAL REPORT, VARIOUS YEARS loans, already a high margin of safety. By 1993, this had risen to 16.4 per cent of total loans. If IBRD retained earnings and provisions returned to the 1986 level of 10.1 per cent of total loans, they would still stand at 420 per cent of total principal outstanding to those countries with a non-accrual status. The remaining 6.4 per cent, $6.58bn, is approximately the same value as total outstanding IBRD SILIC debt, and could thus be effectively utilised in financing substantial programmes of debt relief. There are strong arguments for reducing World Bank reserves even further. The rationale underlying the huge provisions must be to allow for all possible 'forced forgiveness' of debt that the IBRD believes might be required of it, which leaves the reserves free for alternative uses. The Working Party therefore believes that a large proportion of the $14bn World Bank reserves should be put to productive use in either funding additional volumes of concessional lending, or where possible in writing-off outstanding IBRD debt owed by the poorest sub-Saharan African countries.

Measures of Debt Relief

The Working Party therefore believes that both the IMF and the World Bank are in a position to fund measures of debt relief for the most indebted low income countries without compromising their respective roles in the international economy. In addition, it is felt that the emphasis on bilateral funding for the soft window facilities of the Bretton Woods Institutions is unjustified in light of the substantial resources available for use by these organisations. Correspondingly, the Working Party advocates that the Fund and the Bank be pressured to adopt the following proposals:

i) The multilateral institutions should agree to join the bilateral and commercial donors in instigating programmes of official debt write-offs and rescheduling. The total debt stock of SILICs, most of which are situated in sub-Saharan Africa, should be considered at a forum of all creditors and debtors, with the overall debt burden of each respective country reduced to a sustainable level (e.g. a maximum annual debt service to export earnings ratio of 20 per cent) via a combination of multilateral, bilateral and commercial packages of debt relief. The burden of these measures should be divided between the creditors in accordance to their respective shares of annual debt service obligations.

ii) The operations of both ESAF and IDA should be primarily funded by finances drawn from the Fund and the Bank respectively. So far this has occurred on only a very small scale, and recent replenishments of both facilities have relied on contributions from donor governments for the majority of funds. This would have the effect of releasing additional funds for use in bilateral aid programmes, thus further reducing debt burdens.

iii) Using resources drawn from World Bank retained earnings and provisioning, the funds available for use in IDA programmes of lending should be expanded considerably. This would both allow for an increase in the number of countries eligible for the soft window facility and an increase in concessional disbursements to the original IDA recipients which are presently approaching their funding ceilings.

iv) It is widely accepted that in low income countries structural reform is necessary to create a favourable environment for economic development, but although the operations of ESAF have been shown to be effective in achieving structural adjustment in both Asia and Latin America, the facility is clearly too short term for effective use in sub-Saharan Africa. Correspondingly the IMF should be pressured either to extend the period of grace and maturity on ESAF lending to African countries, thus allowing time for the medium and long term returns to economic reform to materialise, or run down the operations of ESAF in this region to be replaced by IDA programmes of lending.

v) The exceptionally tight conditionalities attached to ESAF lending should be relaxed so as to make ESAF programmes more acceptable to sub-Saharan African SILICs. It has been suggested to the Working Party that the Fund should allow a greater degree of recipient country involvement in the planning of programmes of adjustment, particularly when dealing with social and political considerations. In addition volumes of lending through ESAF should be increased so as to ensure that the IMF maintains positive net flows to sub-Saharan Africa as a whole.

vi) In a similar fashion to the implementation of a structural adjustment programme, the provision of debt relief by both multilateral and bilateral creditors should be made conditional on debtor countries adopting responsible and rational domestic policies, most notably concentrating on defence and public construction budgets. African governments can be held partly responsible for the emergence of the present African debt dilemma, as a result of extravagant and misguided past policies which utilised expensive borrowed funds. Correspondingly responsibility must partly rest with African governments to work towards resolving debt related problems. Debtor governments should fulfil their role in providing a stable and democratic environment in which sustainable economic growth is strongly encouraged. Negotiations between multilateral institutions and debtor governments concerning debt relief should therefore embrace the processes of democratic and economic reform.

vii) The operation of the fifth dimension programme of the World Bank should be extended to include principal repayments on outstanding IBRD debt. In addition both the fifth and the sixth dimension programmes should be entirely financed by the World Bank, mobilising either reserves or IBRD profits and reflows, thus reducing the pressure on Nordic donor budgets.

viii) Eligibility for the soft window facilities of both the Fund and the Bank should be extended to include severely indebted middle income countries (SIMICs) experiencing economic stagnation as a result of excessive debt service obligations.

ix) The IMF should mobilise the resources gained through the sale of small proportions of its gold stock to provide concessional bridging loans to countries implementing RAPs (Mistry calculated that the sale of 10–12 per cent of stocks would allow the write-off of all sub-Saharan African debt owed to the IMF, and on this basis the Working Party therefore suggests that the sale of 3–4 per cent of stocks would allow the Fund ample capacity to implement substantial debt relief for sub-Saharan African SILICs). The IMF could then maintain credibility by insisting that current maturities are honoured by the debtor country during the rights accumulation period, whilst sufficient funds would be made available in the domestic economy to successfully implement measures of structural reform. In effect the Fund would be adopting the role presently filled by bilateral donors, and would correspondingly reduce pressure on bilateral aid budgets.

x) Both the IMF and the World Bank should be pressured to adopt 'roll over' provisions for use in ESAF and IDA operations, wherein upon the implementation of a specific programme of lending a number of contingencies would be identified, under which the debt repayment obligations of the low income country would be subject to a roll over clause, and the period of maturity would automatically be extended. Such a provision would be in the spirit of the original Compensatory and Contingency Financing Facility (CCFF) operated by the Fund in the 1980s. If the programme is deemed to have failed or is recognised to be severely flawed, additional disbursements should be cancelled. In dealing with the outstanding funds resulting from previous disbursements, the IFIs should examine the criteria under which the original loan was made (concentrating particularly on the process of programme/project identification, planning and implementation) and where it is apparent that at any stage the IFIs made erroneous assumptions, they should accept responsibility for the failure and correspondingly write-off all debt resulting. Such a procedure would have a salutary effect on the respective IFI executives, making them accountable for their errors and providing an effective incentive for an improvement in the quality of future programmes of lending. Where it is clear that a combination of unforeseen circumstances contributed to the programme/project failure, the IFIs should share the burden with the recipient country and agree to reschedule the outstanding debt on highly concessional terms.

xi) Programmes of multilateral and bilateral debt relief and concessional funding should be granted on a case-by-case basis, and donors should ensure that the social impact of all such programmes is adequately accounted for throughout the processes of identification, planning and implementation.

xii) The Washington Institutions should adopt a more flexible stance in disbursing funds to developing countries. The case of Uganda was highlighted to the Working Party, where approximately $100m of multilateral institution allocations presently remain undisbursed because of domestic money supply constraints designed to control inflation. The system should be relaxed so that these funds can be used to service outstanding multilateral debt, without actually passing through the domestic economy.

xiii) The Bank and the Fund should be pressured to contribute to the forthcoming AfDF replenishment using mobilised reserves and proceeds from gold sales. In particular the Bretton Woods twins should be pressured to join bilateral creditors in financing the implementation of a fifth dimension type programme for use in reducing the burden of outstanding AfDB non-concessional debt stocks on African SILICs. Although such a move would be unprecedented for both multilateral institutions, the extent of the problems presently faced by the AfDB require an unorthodox approach, particularly in light of the very low reserves held by the AfDB itself. It has been pointed out to the Working Party that although the problems of the AfDB have largely been caused through internal mismanagement, both donor governments and other multilateral institutions were guilty of encouraging the Bank to continue in its activities, and correspondingly must accept a degree of responsibility for the situation that has arisen. However, any such generosity by multilateral and bilateral creditors should be matched by a commitment from the AfDB board to implement a rigorous restructuring of the Bank's operations and management, placing more emphasis on the role of the AfDF in sub-Saharan Africa. Such a restructuring should be designed so as to be agreeable to all the non-African contributors to the Bank and the Bretton Woods institutions.

6

Recommendations for the British Government in Alleviating the Debt Burden of Sub-Saharan Africa

Over recent years the British Government has adopted a lead role in promoting the need for debt relief for severely indebted developing countries, and has taken a particular interest in the plight of low income sub-Saharan African countries burdened by excessive debt servicing commitments. Indeed HMG has been at the forefront of the drive to include actual debt stocks, rather than just debt servicing obligations, in the negotiations of the Paris Club, with the proposal of the Trinidad Terms in 1990 breaking new ground in the general movement towards increased non-concessional bilateral debt reduction.

The British Government's emphasis on debt write-offs as a valuable tool in development assistance may be intended to compensate for a reluctance to sanction increased volumes of aid. The Working Party feels that in the short term HMG should at least maintain its current programmes of bilateral funding of low income countries, concentrating its efforts on those countries which are attempting to address their problems arising from bilateral and multilateral debt. As Baroness Chalker explained, in a large number of sub-Saharan African countries where substantial proportions of export earnings are swallowed by debt service commitments, grant assistance from bilateral donors is one of the primary sources of funding through which domestic governments can implement programmes of structural reform and continue to finance essential public services.

In the long term British Ministers should continue to push for the implementation of improved Trinidad Terms within the operations of the Paris Club, and should propose that for those members countries which feel unable to implement debt write-offs, a programme of increased grant assistance of an equivalent magnitude be introduced. Partly as a result of a growing perception of isolation in the international donor community, Japan is now showing signs of relaxing its intransigent stance towards debt reduction, and the Working Party feels that HMG should build on this opportunity and continue to pressure the Japanese government to review its attitude to the possibility of extending the operations of the Paris Club.

HMG should emphasise the need to treat debtor countries on a case-by-case basis in the operations of the Paris Club, with bilateral debt relief being tailored so as to limit each recipient country's overall debt servicing obligations to an externally determined sustainable level. In particular the implementation of a 'cut-off date' within Paris Club negotiations should be questioned in light of the difficulties faced by Uganda and numerous other sub-Saharan African SILICs. In addition HMG should press the Club to review the annual nature of its rescheduling agreements, proposing the introduction of long term contracts of debt relief under the surveillance of external monitors. The

British government should join with other bilateral donors in persuading the multilateral institutions to participate in the operations of the Paris Club so as to allow debtor countries to discuss total debt stocks at a single forum.

In dealing with multilateral institutions, the Working Party proposes that the British Government take a leading role in applying pressure on both the World Bank and the IMF to implement official programmes of debt rescheduling, which in time could be developed into facilities providing debt write-offs for the poorest sub-Saharan African countries. The multilaterals should assist the AfDB in introducing a fifth dimension programme and in replenishing the AfDF. This would most effectively be achieved by orchestrating a consensus between member governments, although difficulties may be encountered in dealing with the conflicting views of donors such as Japan, Germany and the United States. HMG should push the Washington Institutions to mobilise their own resources in funding soft window facilities. It has been suggested to the Working Party that Britain should withhold its contributions to both the Fund and the Bank until such a mechanism is implemented, but the Group agrees that this would prove to be counter-productive in that the primary casualties from this approach would be those countries most reliant on soft window lending, i.e. the sub-Saharan African SILICs. Instead HMG should continue to provide funding for SAF, ESAF, IDA and AfDF in the short run, whilst making it clear that the continued provision of funding would be made conditional on the IFIs contributing substantial volumes of funding from their own reserves. The Government has already made a move in this direction during the recent ESAF II replenishment, when it proposed that the IMF sell a proportion of its gold stocks to provide additional funds. Both the IMF and the World Bank should also be pushed to expand their concessional lending operations so as to ensure they maintain positive net flows to the most seriously indebted developing countries.

The Working Party has considered the proposition that the policies and operations of the multilateral institutions are insufficiently accountable to member state parliaments, and that as a result the quality of the decision making processes in implementing programmes of lending has been allowed to deteriorate, with recipient countries forced to shoulder the entire burden of failed projects. When questioned on this matter, representatives of the IFIs indicated that they are very accountable to the respective donor country representatives, and that in both the Washington Institutions the Board of Executive Directors play an important 'hands on' role. It is therefore the responsibility of the governments themselves to offer themselves to a mechanism through which the respective Executive Directors report back to Parliament. A number of countries, including Canada and Australia, have such a mechanism in place, and the Working Party feels that these could be taken as models upon which a British system should be based. The formation of an official channel of information from IFIs to Parliament would be preferable to the present system, under which the Executive Directors of the respective institutions report back directly to the Treasury. This has frequently resulted in the withholding of information which would be of great interest and relevance to both Parliament and British taxpayers.

Finally, Britain should join and support the Task Force on the Multilateral Development Banks, instigated through the Development Committee by US Treasury Secretary, Lloyd Bentsen, in May 1994. The task force aims to investigate whether the World Bank and Regional Development Banks perform overlapping activities, and if so, identify measures which would eliminate the inefficiencies. A report will be published in time for the IMF-World Bank Fall Meeting of 1995, and will offer an ideal opportunity to influence the policies of the major multilateral institutions.

Appendix: The Problem of Multilateral Debt: An ODI Survey of the Views of Official and Semi-Official Institutions*

* A study commissioned by the World Bank in 1993 and carried out at ODI by Edward Mountfield, with the collaboration of John Howell, Tony Killick, Sheila Page and Adrian Hewitt. Reprinted with permission. This report was commissioned by the World Bank but neither it nor any of the persons or institutions cited is necessarily in agreement with the analysis and the views expressed here.

1. Introduction

The case for substantial commercial and bilateral debt relief is widely accepted. But only more recently has the argument that the 'debt overhang' is self perpetuating been applied to multilateral exposures. Over the past few years, a number of official and semi-official institutions have developed and expressed opinions on the multilateral debt problem and how it might be resolved. This short study summarises these increasingly forthright statements.

The survey is divided into seven sections. Section 2 outlines the component issues of the multilateral debt problem, and the various policies pursued in dealing with them to date. Subsequent sections survey recent statements of opinion on these issues, from official and semi-official institutions. Section 3 considers the problem of existing multilateral arrears, and the issue of multilateral debt relief. The next two sections consider how arrears arise, and how the emergence of new arrears might be stemmed. Section 4 considers the net transfers issue: the debate as to whether the International Financial Institutions (IFIs) ought to adopt targets of more positive (in some cases, less negative) net transfers from themselves to certain countries and regions highly indebted to them. Section 5 considers the issue of the balance between concessional and non-concessional multilateral debts. Section 6 briefly draws attention to statements regarding a number of other questions of relevance to the multilateral debt problem, including systemic issues and conditionality. The Tabulation of institutional positions in Section 7 should be read in conjunction with the text.

1.1 A Note on the Sources

Due to the allegedly sensitive issue of the maintenance of high credit ratings, the bulk of official institutional debate about multilateral debt has not been conducted in public. References to the multilateral debt issue in official documents tend to be terse and lacking in detail, seldom extending over more than a few pages, and frequently occupying only a few lines. Except where noted, the opinions outlined below are taken from public declarations, or from annual reports published by the institution in question. Full details of the documents cited are given in the bibliography.

Due to the proportionately greater significance of multilateral debt in Africa, a significant number of the opinions cited are with specific reference to that continent. In each case, this is clearly indicated.

2. The Problem of Multilateral Debt

Multilateral (IFI) debt comprises three distinct components: (i) debt owed to the International Monetary Fund; (ii) debt owed to the World Bank, in both its non-concessional (IBRD) and concessional (IDA) windows; and (iii) debt owed to other multilateral lending agencies, such as the African Development Bank (AfDB), the International Fund for Agricultural Development (IFAD), etc. Multilateral debt has become increasingly significant, growing both as a percentage of total debt and in absolute terms. Between 1980 and 1991, the stock of multilateral debt owed by all developing countries increased by a factor of more than four, from $61.6bn to $264.7bn, reaching 18.6 per cent of the total debt stocks.[1] In 1990, some 20 per cent of the

[1] World Bank (1992), p.160. These figures are for multilateral debt including IMF credits.

total debt service of all developing countries was to multilateral institutions, and 28 per cent in the case of sub-Saharan Africa.[2]

At present, multilateral debts to the IFIs must be serviced in full. With the support of the major shareholders, debts are never formally renegotiated, and cannot be written-off. One justification given for this is the 'moral hazard' argument. To write off multilateral debts at this stage in the debt saga, it is argued, would create a perverse incentive, by rewarding those who have failed to undertake adjustment.

A second argument held (questionably) to be a justification for such a policy is the 'AAA credit rating' argument. The generally untarnished record on repayment of the Bretton Woods institutions has been vigorously defended. This record, it is alleged, facilitates access to capital markets on the most favourable terms, an advantage which can be passed on to developing country borrowers. Such creditor status in practice, however, is less a function of the Bretton Woods institutions' reputation on financial markets than of the capital guarantees furnished for IFIs by their member governments.

Whatever the reason, the established operational practice is consequently not to lend to countries which are in arrears on an earlier multilateral loan. By not servicing multilateral debts, countries automatically become ineligible for further credits from these institutions, and in the case of arrears to the IMF, also lose access to Paris Club rescheduling. The partial suspension of bilateral aid may also follow. Partly as a consequence of this, debtor governments have generally tried to keep up payments on their multilateral obligations. Multilateral debt accounts for a large and increasing proportion of the total of debt service payments actually made in recent years.

Nevertheless, arrears with IFIs have grown dramatically, from a total of less than $1bn in 1982 to over $9bn in 1991. In March 1993, they stood at approximately $7bn, with a total of 40 countries in arrears to one IFI or another.[3] Most of these arrears were not with the Bank or the Fund. Just as debtor countries prefer to accumulate arrears with commercial and bilateral lenders before falling behind with payments on multilateral debt, arrears are usually accumulated with the perceptibly lower-rated IFIs (the regional development banks) in preference to arrears with the more powerful Bretton Woods institutions. Still, at the start of 1993, eleven countries were overdue more than six months on payments of principal and interest to the IMF, by an amount totalling over $4.6bn.[4]

Almost by definition, a country going into arrears with a leading multilateral lender is in an extremely desperate balance of payments position. Yet the problem of multilateral debt is not limited to those countries actually in arrears with an IFI. There are ten countries whose scheduled multilateral debt service in 1992–94 exceeds 20 per cent of their 1991 export earnings. Eight of these ten countries remain current on their payments to the IFIs. Net transfers

[2] OECD (1991), p.42.

[3] UNCTAD (1993), p.178.

[4] IMF (1993), p.16.

from IFIs were actually negative during 1987–89, and averaged around zero in 1987–92.[5] For low income developing countries, whether in arrears to the IFIs or not, the problem of multilateral debt is seen as an increasingly serious one, even if hard evidence on currently deteriorating levels of debt outstanding and debt service ratios is not conclusive.

2.1 Strategies Pursued

To date, a number of strategies have been pursued by the IFIs and the bilateral creditors, in dealing with multilateral arrears. In May 1990, the IMF introduced an arrangement whereby countries in arrears commit themselves to a three-year programme of the type which usually would accompany drawings from the Enhanced Structural Adjustment Facility (ESAF) or the Extended Fund Facility. The Fund monitors this process, and 'rights' to future IMF lending are deemed to accumulate which, at the end of the three year period, can be used to clear part of the arrears. However, during the programme itself, the net transfer is negative: the country receives no new disbursements and has to pay interest on arrears and current maturities.

During such a 'Rights Accumulation Programme' (RAP), bilateral creditors are sometimes prevailed upon to provide bridging loans to countries with arrears to the IFIs. These loans are used to clear arrears. This in turn enables the Fund to resume lending. The bilateral creditor can then be repaid out of the money the Fund supplies. This was the strategy pursued during Zambia's RAP starting in April 1991; in March 1993, the US and Japan financed jointly a $860m loan to Peru, enabling the repayment of IMF arrears, and hence access to the Extended Fund Facility. By such a mechanism, rescheduling is not formally discussed at the negotiating table. Instead, it occurs *under* the table. However, it relies on the good will and cooperation of a consortium of bilateral lenders.

Similarly, the IDA's 'fifth dimension', providing interest rate subsidies on originally non-concessional World Bank (IBRD) loans, is a form of IFI debt-reduction in effect if not in name. The scheme is funded by 10 per cent of IDA reflows, the investment income on IDA donor funds, and special contributions from Norway and Sweden. The proportion of interest obligations covered was 60 per cent when the scheme began in 1988, with the coverage expanded to 90 per cent in 1990.

Some bilateral donors have recently allocated aid to certain countries with the specific intention that they be used to clear arrears with the IFIs. For example, in December 1992, donor countries agreed to repay on behalf of Cambodia over 80 per cent of the $61m she owed to the IMF. However, such instances are few and tend to be limited to countries of special political importance. Increasingly, it is felt that the solutions on offer are piecemeal, insufficiently institutionalised and out of proportion to the scale of the problem.

Additionally, a number of strategies have been followed by the IFIs to prevent the emergence of arrears (as opposed to dealing with them after they have emerged). The Structural Adjustment Facility (SAF) and the subsequent Enhanced Structural Adjustment Facility (ESAF) have been the IMF's attempts to ease the multilateral debt problem, and to increase the flow of concessional finance to Severely Indebted Low-Income countries (SILICs), through a shift from non-concessional towards highly concessional adjustment lending for SILICs. However, the

[5] UNCTAD (1993), p.177–8.

extremely tight conditionality attached means that ESAF disbursements have been few, and they have not been large enough to reverse the negative net balance of financial flows from the IMF to sub-Saharan Africa. Furthermore, ESAF expires in November 1993, and an 'ESAF-2' has yet to be negotiated.[6]

The World Bank has a substantial concessional window in the form of the IDA. But IDA-10 resources were frozen in real terms at the level of IDA-9, whilst demands for IDA disbursements are growing daily. The soft windows of the regional IFIs are yet more inadequate, with the African Development Bank having to make non-concessional loans to the poorest and most indebted of sub-Saharan African countries.

3. Multilateral Debt Relief

Ought the IFIs to change their articles of agreement so as to be able to write-off, reschedule, or reduce interest payments on some of their multilateral debt, supplementing the debt relief by the bilateral and commercial creditors envisaged in the Brady plan? Until recently, the issue of multilateral debt relief has been something of a taboo issue. However, in the past few years, the NGOs have been joined by a number of major international institutions in calling for action on existing multilateral arrears. A number of official institutions have begun to call, in effect, for Paris Club terms (i.e. enhanced Toronto terms) to be applied to the IFIs.

3.1 The United Nations and UN Agencies

The call for multilateral debt relief was taken up by the UN Secretariat under Secretary-General Perez de Cuellar.[7] The Final Report of the **UN Secretary-General (1991)** on the UN Programme of Action for African Economic Recovery and Development (UNPAAERD) called for 'bolder measures and exceptional treatment' for African debt. Ways should be found substantially to reduce the debt owed to multilateral institutions, with help from donor countries, the report stated.

However, the **UN New Agenda for the Development of Africa in the 1990s (1991)**, adopted by the UN General Assembly in December 1991, did not include the call for multilateral debt relief which figured in the Secretary-General's draft Agenda. The US representative, Edward Marks, expressed fears that such action risked undermining the credit ratings of the multilateral institutions. On US insistence, the reference to multilateral debt relief was replaced by a diplomatic but hollow call for 'a growth-oriented solution of the problems of African developing countries with serious debt-servicing problems, including those whose debt is mainly to official creditors or to multilateral institutions.'

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[6] Discussions are currently under way in the IMF's Executive Board for a *temporary* successor to ESAF. Michael Camdessus is in favour of an ESAF successor. However, financial support, to date, has not been secured (*Financial Times*, 24 September 1993, p.6.), and the UK Chancellor of the Exchequer has indicated the UK's preference for debt relief *rather than* an ESAF replenishment if maintained in real terms.

[7] Secretary-General Boutros Ghali has also spoken of the 'crippling problem of debt', in his first address to the UN General Assembly. The UN Secretariat continues to draw attention to the multilateral debt issue in its annual World Economic Surveys (UN 1991, 1993), although these reports are not prescriptive.

The UN agencies have been prominent in calling for action on multilateral debt. One of the most recent statements on multilateral debt made by an official institution is that of **UNCTAD (1993).**[8] UNCTAD argues that arrears hurt not only the debtor but the IFIs (and all their members) too. Whilst backing calls for increased disbursements from IFIs, UNCTAD argues that these alone will not be enough. Debt or debt service reduction will also be required, from the regional development banks and from the Bretton Woods institutions.

The report goes to some lengths to emphasise that the preferred creditor status of the IFIs should not be endangered in the pursuit of such a strategy. The multilateral debt relief proposal is limited to SILICs, which account for a minor share of the IFIs' portfolios, and yet where multilateral debt forms the bulk of the country's debt overhang. Nevertheless, UNCTAD calls for the preferred creditor principle to be applied in a 'flexible, pragmatic manner', involving 'more comprehensive indirect rescheduling and, in exceptional circumstances, an effective, rather than formal debt reduction'. The strengthening of the major Latin American economies (and the removal of their debt overhang), the report argues, has improved the quality of the major IFIs' portfolios. This could make it feasible for the World Bank to finance debt reduction schemes for multilateral debt, as the IDA currently does for commercial debt through its Debt Reduction Facility. Such proposals, it is argued, are 'unlikely to have a negative impact on IFIs' credit ratings and financial position.'

The report builds on current Bank and Fund approaches to the problem of multilateral debt. UNCTAD's call is essentially for a very substantial expansion and enhancement of the 'indirect' rescheduling and 'effective rather than formal' (p.182) multilateral debt reduction that the World Bank and IMF have been experimenting with in recent years. Multilateral debt or debt service reduction, the report argues, is required on a more extensive scale than is currently achieved through IDA's 'fifth dimension'. The 'fifth dimension' should be expanded to cover principal as well as merely interest. On the Fund's part, Rights Accumulation Programmes should be improved, by ensuring that net transfers are non-negative during the programme; and by making such programmes available to all countries with protracted arrears, and not only those who had protracted arrears in 1989, as is currently the case. It is argued that, in addition, the regional development banks – in particular, the African Development Bank – should instigate similar strategies.

UNICEF (1993) has also called for multilateral debt relief, in a recently circulated 'Call for Urgent Action' on African debt. It argues that the conversion of outstanding multilateral loans to IDA terms should continue to take place, 'whenever changes in country circumstances dictate', with such concessional terms also being extended to African Development Bank loans. It is suggested that such conversions could be financed out of increased donor contributions, and from the profits of the IFIs. UNICEF calls for the IMF to institutionalise the special concessional facilities – SAF and ESAF – and apply such terms to all forms of IMF lending in Africa. UNICEF suggests that the interest subsidies entailed by the adoption of such a policy by the IMF could be financed through further special donor contributions, an easing of IMF guarantee fund requirements, further sales of IMF gold, or 'in extreme cases, the reduction of loans for countries making fresh policy starts.' Such debt relief, UNICEF argues, should be linked to enhanced support for human development.

[8] UNCTAD (1988) includes an earlier but less detailed call for action on multilateral debt.

Multilateral debt relief for Africa was earlier called for in a major **UNICEF** study by **Cornia, van der Hoeven and Mkandawire (1992)**. The alternative of increasing aid levels by a commensurate amount they dismiss as unrealistic. Debt to multilateral organisations should not, they argue, be excluded from debt relief initiatives, but should be 'an integral part of a debt reduction package'. They suggest that part of an increase in SDRs should be used for debt reduction in sub-Saharan Africa. The **UNDP (1992)** explicitly included multilateral institutions in their brief mention of the need for 'a global debt bargain' (pp.89–90), to involve a major write-down of debts by all involved.

3.2 Governments

For some years, 'moral hazard' arguments against multilateral debt relief have been current in the Group of Seven (G7) Financial Ministries. However, the official positions of G7 governments appear to be in a state of flux. In the US, the Clinton administration recently sought Congressional approval to enable it to reduce debt, and any softening of US policy towards official debt might include multilateral debt.[9] The official position of the UK Treasury is that, where 'low income countries owe much of their debt ... to the multilateral financial institutions', it is 'increasingly the responsibility of government to alleviate the plight of these countries'.[10] The Japanese, traditionally the main opponents of multilateral debt relief, might shift position in the near future. The new Hosokawa coalition government is pledged not to change foreign and defence policy. However, were debt issues deemed to be a financial rather than foreign policy issue, and assuming the coalition survives, Japanese objections to multilateral debt relief might conceivably be amended.

SIDA (1992) assign responsibility for the multilateral debt crisis to the IFIs themselves, who have 'erred in their judgements in conjunction with lending'. They argue that any damage to the hitherto unblemished creditor status of the IFIs has already been done, and so discounted by the bond markets. Consequently, 'measures should be taken to reduce the burden of debt of the poorest, most severely indebted countries' (p.84). The 'fifth dimension', whilst 'an important initiative', represents only 'a step in that direction'. Greater multilateral debt restructuring should be allowed, financed out of a fund in each respective IFI, consisting of development banks' profits, reflows, and aid funds. All SILIC debt to the IBRD should be converted to IDA terms. The regional development banks should be persuaded to soften their non-concessional claims on SILICs. New borrowing should not be included.

SIDA provides an estimate of the cost of their proposal. Converting the SILICs' debts to the IBRD to IDA terms, they estimate, would cost $538m per annum (i.e. the average interest paid to the IBRD over the past five years). Offering debt relief on amortisations would cost an additional $520m a year. The inclusion of non-SILIC countries, such as Vietnam or Nicaragua, would increase the cost. Assistance funds, they argue, should be contributed in proportion to donors' quotas in the multilateral institutions. The Nordic countries should not remain the sole contributors to the 'fifth dimension'.

[9] See for example the keynote speech of Lawrence Summers, Under-Secretary of the US Treasury for International Affairs, to the African Development Bank annual meeting, Abidjan, May 1993.

[10] Speech of the Economic Secretary to HM Treasury, Anthony Nelson MP, to the Environmental and Energy Study Institute, Washington, 15 July 1993.

3.3 Inter-Governmental Groupings

Multilateral debt relief is a significant part of the agenda of institutions in Africa, and in other parts of the 'South'. The Memorandum of the May 1991 meeting of the **Economic Commission for Africa Conference of Ministers (1991)** called on the international community to commit itself to an amendment of the Articles of Agreement of the IMF and the World Bank to permit rescheduling of African multilateral debt. The **Abidjan Declaration (1991)**, organised by the **African Development Bank**, the **Forum on Debt and Development (FONDAD)** and **Parliamentarians for Global Action**, called for the IMF's exposure in low-income Africa to be wound down. The declaration suggests that a one-time emission of a small amount of Special Drawing Rights (SDRs), or a sale of a small part of the IMF's gold reserves, would permit a write-off of IMF claims in Africa.

The **Non-Aligned Movement (1993)**, in a memorandum taken by its chairman, President Soeharto, to the Tokyo summit of the G7, calls for consideration of more flexible treatment of multilateral debt. It argues that the IDA's 'fifth dimension' programme and the RAP approach of the IMF are inadequate. Therefore, 'consideration should be given to the use of SDRs as a means for reducing multilateral debt stocks.' It also calls for consideration of the conversion of a part of multilateral debt into equity investments. It calls for a common pool of funds to be established by bilateral donors, to facilitate the alleviation of multilateral debt burdens. More extensive use of the profits and reserves of the IFIs for multilateral debt relief could be considered.

3.4 The NGOs

Such issues are also an established part of the agenda of the NGOs. The Final Statement agreed by the 43 international NGO participants at the **UN-NGO Workshop (1988)** on Debt, Adjustment and the Needs of the Poor, meeting in Oxford in 1987, asserted (p.74) that: 'Governments should also agree to change the rules of the IMF and the World Bank to allow a rescheduling of the loans where these are made on commercial terms, and a subsidy for the interest charges.'

EUROSTEP (1993), a consortium of 22 NGOs from 15 European countries, also calls for multilateral debt relief for Africa. The consortium calls for an acceleration of the 'fifth dimension' programme, through the provision of additional resources. Donor contributions should also be used to extend concessional terms to African Development Bank loans. EUROSTEP calls for the financing of debt relief by a new issue of SDRs, or through the sale of gold stocks, which they assert would be 'both economically and politically feasible.'

The British NGO **Oxfam (1993)**, in its latest report on Africa, takes a position on the issue of multilateral debt relief. In countries such as Uganda, it argues, where 74 per cent of the total stock of debt is to the Bank or the Fund, only multilateral debt relief can achieve a sufficient reduction in the debt overhang. A major theme of the analysis is the notion of the IFIs' own substantial responsibility for the emergence of multilateral debt arrears. The report argues that the IMF's 'increasingly damaging role in sub-Saharan Africa' is a direct consequence of the Fund's policy mistakes in the early 1980s: treating 'what was a problem of insolvency as one of short-term liquidity, extending short-term loans (repayable over 18 months) at high interest rates to cover structural trade and budget deficits' (p.15).

Oxfam argues that current policies for dealing with countries in arrears are inadequate. The IMF's Rights Accumulation Programme is criticised for perpetuating negative resource transfers during the course of the programme, and for failing to guarantee fresh concessional finance when arrears have been cleared. The IMF must be either reformed fundamentally or extricated from Africa. 'In either case,' Oxfam argues, 'measures to write off obligations due to it from low-income African countries are long overdue.'

Oxfam rejects the arguments that such write-offs would be inflationary or would erode the IMF's credibility. It suggests it would be relatively simple to finance a write off of the IMF's exposures in Africa, through a sale of the Fund's 'largely redundant' gold stocks, or through a new issue of Special Drawing Rights (SDRs).

4. Net Transfers

Many of the official and semi-official statements on multilateral debt focus on policies to prevent the emergence of arrears (as opposed to dealing with them after they have emerged). It is widely argued that the balance of financial flows from IFIs to highly indebted developing countries is excessively negative or insufficiently positive, and that consequently multilateral debt is proving more burdensome than it need do.

The **South Commission (1990)** emphasised this issue, calling for the soft windows of all IFIs to maintain a minimum annual real increase of 15 per cent in their lending to developing countries; and for the doubling of concessional transfers of resources to developing countries by 1995, priority being given to transfers through multilateral institutions (IDA and the soft windows of regional development banks). The **African Development Bank**-sponsored **Abidjan Declaration (1991)** called on the IMF Member Governments to adopt a policy of 'zero net transfers' to Africa for at least the 1991–1997 period.

The first report of the **Independent Group on Financial Flows to Developing Countries (1989)**, chaired by Helmut Schmidt, called for the mobilisation by the multilaterals of 'substantially greater funds than those now flowing to developing countries.' The **UN Secretary-General's Advisory Group on Financial Flows to Africa (1988)** made an earlier call for multilateral resource flows to sub-Saharan Africa to be expanded, and estimated that a minimum of $5bn a year was necessary to meet the region's immediate financial requirements.

UNCTAD (1993) calls for IFIs to help avoid the emergence of arrears by increasing their net transfers substantially. This will require replenishment of IFI soft windows by member countries, if necessary through SDR allocations and IMF gold sales. The **UNICEF** study by **Cornia et. al. (1992)** calls for the net flow of resources to Africa from the IFIs to be vastly expanded.

SIDA (1992) proposes that a ceiling – perhaps 20 per cent – be imposed on the debt service ratio. The negative net transfers from the IMF should be compensated for by a greater volume of IDA loans, or through 'some other, collective measures on the part of the donor community.'

Oxfam (1993) repeats the call for an 'African Marshall Plan', and a halt to the net transfer of resources to the IMF. It also criticises the decreasingly positive net transfers from the World Bank, in the second half of the 1980s. It argues that African recovery will depend on 'substantial inflows of foreign capital', and that official development assistance must supply this. **EUROSTEP (1993)** argues that resources must be found to stem the 'perverse transfer of resources from the world's poorest region', a task which the RAP approach fails to address.

5. The Balance between Concessional and Non-Concessional Lending

Official and semi-official statements emphasise the need for a greater proportion of future IFI credits to be extended on concessional terms. The **South Commission (1990)** attached particular significance to the relative enlargement of the concessional component of multilateral assistance, as well as calling for the refinancing on concessional terms of the non-concessional multilateral debt, of all low-income debtors. The World Bank, the Commission argued, should revive the Third Window instituted for a short period in the 1970s to provide loans on terms intermediate between those applicable to IDA loans on the one hand and regular World Bank loans on the other.

The **Non-Aligned Movement (1993)** calls for the concessional resources of the IFIs to be expanded to cope with the growing burdens of multilateral debt. It notes that this is particularly true in the case of the regional development banks. The **Abidjan Declaration (1991)** included a call for 'an expansion of IDA resources commensurate with Africa's urgent needs for expanded concessional financing from external sources.'

The **UNDP (1992)** reaches similar conclusions to the South Commission, calling for an Intermediate Assistance Facility (IAF), to help countries 'ready to graduate from the extremely concessional IDA terms but not yet sufficiently robust to meet the tougher terms of the IBRD'. The UNDP suggests that India and Pakistan, for example, might fall into such a category. This would allow the IDA to concentrate its highly concessional resources on the long-term development of Africa.

UNCTAD (1993) calls for the 'raising of the concessionality of the hard window/soft window blend.' The inadequate financing of the soft windows of the regional development banks, particularly the African Development Bank, has left these institutions lending hard window funds to low-income countries. UNCTAD argues that this is exacerbating the multilateral debt problem, and that the regional development banks need to increase the scale of their concessional operations.[11]

SIDA (1992) argues that the poorest countries should receive access to the IMF with a greater degree of concessionality than currently applies to SAF/ESAF. The grant element should be at least the 67 per cent of the original Trinidad terms. This could be achieved by an extension of the term of repayment. The regional development banks should cease extending non-concessional loans to the poorest, most severely indebted countries, and should be assisted by the international community in doing this.

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[11] Babacar N'Diaye, head of the African Development Bank, favours a shift from non-concessional to concessional lending. His plan is that African Development Fund (AfDF – the AfDB's soft window) lending should double to \$2bn a year, with AfDB (non-concessional) lending contracting by \$1bn. However, this might require a 62 per cent increase in the replenishment of AfDF funds, a target which western governments have dismissed as unrealistic. (*Financial Times*, 24 September 1993, supplement p. XXII.)

Oxfam (1993) notes that the IDA-10 agreement, whilst allowing a small increase in concessional resources over IDA-9 in absolute terms, was in *per capita* terms considerably less generous than its predecessor, allowing for the probable diversion of resources to some republics of the former Soviet Union. It argues that non-concessional lending is inappropriate to Africa, and calls for new concessional facility to replace non-concessional IMF lending in Africa (see section 6.1, below).

6. Other Issues

6.1 Systemic Issues

Some emphasis has been given to systemic issues in recent official and semi-official statements on multilateral debt. Many institutions and organisations have expressed the opinion that the current institutional framework for coping with multilateral arrears is insufficient for the task.

The **South Commission (1990)** called for an International Debt Conference, involving debtor governments, creditor governments and IFIs, with responsibility for proposing an international solution to the crisis. The statement does not, however, explicitly call for the IFIs to grant relief on multilateral debts. **The Independent Group on Financial Flows to Developing Countries (1989)** recommended that a new facility be created, sponsored by the Bank and the Fund. **Cornia, van der Hoeven and Mkandawire (1992)**, in their study for **UNICEF**, call for the various official and unofficial forums of discussion on debt relief (the Paris Club, IMF drawing, bilateral assistance) to be merged, with multilateral debts being forgiven alongside bilateral and commercial debts.

Oxfam (1993) argues that the IMF is an institution inappropriate to African needs, not being an instrument for providing long-term concessional development finance (p17). It notes that even ESAF has a low take-up rate, because repayment must begin after five years, whereas IDA loans repayments do not start for twelve, and because of the stronger conditionality attached to ESAF borrowing. It calls for the IMF to be withdrawn from Africa, and its role taken over by 'a more appropriate agency', unless there can be fundamental reforms to the terms and conditions of IMF lending.

6.2 Conditionality

Finally, it is impossible to ignore the widespread belief that the policy conditionality attached to multilateral lending has exacerbated rather than alleviated the problem of multilateral debt. A large number of the official and semi-official institutional views on the problem of multilateral debt include lengthy criticism of current multilateral lending conditionality. **UNICEF's** stance on these matters (e.g. **Cornia, Jolly and Stewart 1987**) is broadly representative.

Such arguments are not summarised here. They will be familiar to most readers. This is not in any way to belittle their significance. On the contrary, a lasting solution to the problem of multilateral debt will surely have much to do with getting economic strategy right, as well as with financial engineering.

Perhaps the most significant change overall is that whereas non-official pressure groups have always tended to be in favour of debt relief, in the last few years some of their more radical proposals are being considered, and in some cases adopted as institutional proposals, by the official bodies and agencies themselves.

7. Summary in Tabular Form of Institutional Positions, as revealed in the preceding textual survey[12]

Issue Addressed / Body or Grouping	A Multilateral Debt Relief	B The Net Transfers Issue	C The Balance of Concessional and Non-concessional Lending
UN and Agencies			
1. United Nations Secretary-General (1991)	Final Report 1991 (Peres de Cuellar) 'ways should be found to reduce debt to multinational institutions' – by means of help from donor countries.		
2. United Nations Secretary-General's Advisory Group on Financial Flows to Africa (1988) (Wass Report)		Multilateral resource flows to sub-Saharan Africa to be expanded (minimum of $5bn extra p.a. needed)	
3. UN General Assembly 1991 New Agenda for the Development of Africa	Multilateral debt relief not advocated, 'growth-oriented solution' called for.		
4. UNCTAD, especially Trade and Development Report (1993)	1988 call for 'action on multilateral debt' 1993 increased disbursements would be insufficient; debt or debt service reduction required	To avoid emergence of arrears IFIs need to increase net transfers; IFI concessionary loans to be replenished through SDR allocations and gold sales	Need to increase soft loan ratio for regional development banks, particularly African Bank.

[12] This table should be read *only* in conjunction with the text which precedes it and from which it derives. A blank box does not necessarily mean that the institution has no position or view; a full box, even in including a quotation, may only be ilustrative of an institution's possibly more rounded position on the issue concerned.

Issue Addressed Body or Grouping	A Multilateral Debt Relief	B The Net Transfers Issue	C The Balance of Concessional and Non-concessional Lending
5. UNICEF (1993)	Conversion of outstanding multilateral loans to IDA terms should continue to take place		
6. UNICEF (1992) Cornia *et al.*	Multilateral debt relief for Africa. Multilateral organisations should be an integral part of debt relief package. Increase in SDRs for debt reduction in sub-Saharan Africa.	Net flow of resources to Africa to be vastly expanded.	
7. UNDP Human Development Report (1992)			Need for an intermediate World Bank Concessional Category between IDA and IBRD; IDA could then concentrate on long-term African development.
Governments			
8. USA	1993 Any softening of US Policy towards official debt might included multilateral debt.		
9. UK	Responsibility of government to alleviate plight of low income countries' debt including to multilateral institutions.		Cautious on ESAF replenishment (1993)
10. Japan	Traditionally opposes multilateral debt relief		

Issue Addressed / Body or Grouping	A Multilateral Debt Relief	B The Net Transfers Issue	C The Balance of Concessional and Non-concessional Lending
11. Sweden	SILIC debt to IBRD should be converted to IDA terms. Multilateral debt restructuring should be allowed from special fund in each IFI. Non-Nordic countries should also contribute to 'fifth dimension'	Ceiling on debt service ratio; negative net transfers from IMF to be compensated by greater IDA loans volume.	Poorest countries to have more access to IMF through greater concessionality than current SAF/ESAF. Achieve relief of at least 67% (cf. original Trinidad Terms).
Inter-governmental Groupings			
12. UN Economic Commission for Africa-Ministerial Conference (1991)	Amendment of the Articles of Agreement of IMF and World Bank to permit re-scheduling of African debt needed.		
13. Non-Aligned Movement (1993)	Use of SDRs as means for reducing multilateral debt stock; conversion of part of debt to equity investments; common pool by bilateral donors and use of IFI profits and reserves.		Concessional resources of IFIs to be expanded, particularly regional development banks.
Hybrids			
14. Parliamentarians for Global Action/ADB/FES/FONDAD: Abidjan Declaration (1991)	IMF's exposure in low income Africa to be wound down. Emission of SDRs or sale of IMF gold would permit write off for Africa.	IMF should adopt policy of zero net transfers to Africa for 1991–97.	Expansion of IDA resources commensurate with Africa's needs.

Issue Addressed Body or Grouping	A Multilateral Debt Relief	B The Net Transfers Issue	C The Balance of Concessional and Non-concessional Lending
15. South Commission (1990)	Call for an International Debt Conference (though not for indiscriminate or generalised debt relief).	Minimum annual real increase of 15% in lending by IFIs. Concessional loans and doubling of concessional transfer of resources to developing countries by 1995.	Relative enlargement of concessional component of multilateral assistance. World Bank should have an intermediate rate between IBRD and IDA.
16. Independent Group on Financial Flows to Developing Centres (Schmidt Report, 1989)		From multilaterals 'substantially greater funds than those now flowing to developing countries'.	
NGOs			
17. UN–NGO Workshop (1988)	Rules of IMF at World Bank to be changed for re-scheduling; also subsidies for interest charges.		
18. EUROSTEP (1993)	For African relief a new issue of SDRs and sale of gold reserves; acceleration of 'fifth dimension'.	Stop the transfer of resources from the World's poorest regions.	
19. OXFAM (1993)	New issue of SDRs and sale of gold stocks to write off IMF's exposures in Africa.	African 'Marshall Plan' to halt net transfer to IMF and erosion of positive transfers from World Bank.	Non-concessional lending inappropriate to Africa. IMF should have concessional facility for Africa.

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Many African countries now see the lending policies of the World Bank and the IMF as an impediment to development rather than a help. What is the truth behind this perception?

Should the international financial institutions now reverse their policy of refusing to reschedule or write off bad debts? Are our own governments bailing out the IMF and the World Bank with scarce bilateral aid to keep debts current, and if so should the donors be prepared to continue?

The Working Party has drawn up a framework of recommendations after meeting representatives of all points of view – banks, creditor and debtor governments, as well as the international financial institutions and independent experts.

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