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Opening Remarks by the Staff on Issues and Developments
in Multilateral Debt and Financing for the Heavily
Indebted Poor Countries - Preliminary Considerations
Executive Board Meeting 95/19
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Thank you, Mr. Chairman. I thought it would be useful to deal with some of the points raised in Directors' Gray statements at the start of the meeting.

In approaching this topic, the staff took the line that the first thing to do was to lay some of the facts out in order to get a handle on the size of the problem. Is there a looming multilateral debt crisis? Are the multilaterals withdrawing resources from the poorest countries? Can we continue to lend without overburdening these countries? Where should we concentrate our attention? In looking at these issues and giving some answers, we have sparked a new round of questions which touch on the prospects and conditions for growth and for resource transfers to the poorest countries over the next two decades. These are very important questions, but they lay beyond the scope or purpose of the current papers or of what could be done in the time available.

Our conclusions are limited but moderately reassuring. That after reaching a hump, the burden of multilateral debt service will be declining for most poor countries, partly as a result of the switch during the last decade to lending on more concessional terms. This is true even if the multilateral institutions continue the current level of support for the development process through their lending providing it is on concessional terms. That there are some countries, however, where a continuation of current multilateral lending policies will create an unserviceable debt burden: these include some of the cases of protracted arrears, and seven or eight others where borrowing even on current concessional terms is too burdensome. These countries financing needs will have to be met by financing from bilateral or multilateral sources on even more concessional terms.

In coming to some of these conclusions, have we used optimistic assumptions?

The first assumption in the "new multilateral disbursement" scenario is that real exports grow by 3 percent annually over the period. This is clearly significantly better than recorded by these countries over the last decade. But in defense, I would note that exports do respond well to good policies. For the group of low-income countries, which includes countries with widely different fortunes, real export growth in the second half of the last decade over the first half was 6 percent a year, which can plausibly be related to the general improvement in the policy environment in many

countries. Some countries where exports peaked around 1990, such as several of the CFA franc countries, have rather good export prospects at present. Countries that have successfully completed ESAF programs have generally shown subsequent export growth at a much faster rate than 3 percent. Of course, our adjustment program ought to show this sort of result, and one of the lessons of this paper might be the crucial importance of strengthening the link between conditionality and export growth.

What would sensitivity analysis have shown? We took a standard 3 percent real export growth for our projections. Even if this turns out to be the average, some will do better than this, and some worse. This might alter the composition of the group of countries we note as having potential problems, with some additional ones falling into it and some now in escaping. But this wouldn't alter the general picture. If we took 2 percent real export growth as standard, export earnings by 2014 would be some 20 percent less. While this would certainly worsen the ratios, the vast majority of countries would still fall well below the 10-12 percent level.

Another assumption that has been questioned is that inflows are maintained over the period in real terms. Strictly speaking, we have not assumed this. What we have done is to answer the question of whether the countries involved would face a growing problem of multilateral debt service if inflows from the multilaterals remained constant in real terms. But implicitly we are assuming that these countries will continue to get the external financing they need to support their development. Some Directors have questioned this assumption in the light of growing stringency of aid budgets. If aid is reduced, it could be a very serious problem for these countries. I would thus underline the importance of protecting the poorest countries from the worst effects by redirecting assistance to them. This may be possible over the twenty-year perspective taken in this paper, since some of the larger recipients of ODA may gradually need less support than they now get and some may even become providers of aid. Directors will have an opportunity to discuss aid flows in some depth on the basis of a staff paper to be circulated in March.

Directors are certainly raising an important question. The countries discussed in these papers rely on average on concessional multilateral and bilateral flows to the extent of 80 percent of their export earnings. If these flows are substantially cut, the countries will face a very serious adjustment problem. Mr. Autheman notes that actual debt service for these countries averages about 20 percent of export earnings. In the event of a major cut in aid flows, the amount of debt service payments might suffer, but the scope for this offsetting a sharp cut in disbursements is clearly limited.

Finally, Mr. Chairman, I would like to say a few words about the assumption that future assistance to these countries be on concessional terms. We have assumed the implementation of Naples terms on existing bilateral debt and that new bilateral aid flows to the poorest be highly

concessional. This is in accordance with international policy. For the Fund and the World Bank, mechanisms have been in place for some time to ensure that new assistance to these countries is on concessional terms. One message of the paper is that the need for such concessional mechanisms for Fund assistance will continue for the foreseeable future. It is true that some of the regional multilaterals do not yet have in place the means to put their assistance onto a concessional footing. But our message is that some of the poorest countries cannot continue to finance themselves through multilaterals unless this is done.

