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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 03/84

10:00 a.m., September 3, 2003

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Executive Board Attendance

A. Krueger, Acting Chair
A. Carstens, Acting Chair

Executive Directors

S. Al-Turki

I. Bennett

K. Bischofberger

M. Callaghan

P. Duquesne

S. Indrawati

V. Egilsson

N. Jacklin

W. Kiekens

G. Le Fort

A. Mozhin

D. Ondo Mañe

L. Martí

P. Padoan

M. Portugal

T. Scholar

A.S. Shaalan

I. Usman

J. Kremers

K. Yagi

F. Zurbrugg

Alternate Executive Directors

A. Alazzaz

C. O'Loughlin

C. Gust, Temporary

M. Kruger, Temporary

S. Wolff-Hamacher, Temporary

W. Cho, Temporary

I. Alowi

B. Anderson

M. Lundsager

C. Josz, Temporary

A. Zoccali

M. Daïri

S. Rouai, Temporary

A. Lushin

L. Rutayisire

M. Beauregard

D. Lombardi, Temporary

R. Steiner

R. Jayatissa

K. Kanagasabapathy, Temporary

M. Brooke

O. Kanaan

P. Ngumbullu

H. Ge

Y. Yakusha

P. Nijssse, Temporary

M. Kitahara

T. Miyoshi, Temporary

W. Szczuka

S. J. Anjaria, Secretary

B. Esdar, Acting Secretary

S. Leite, Acting Secretary

A. S. Linde, Acting Secretary

Y.P. Chia, Assistant

T. Davidson, Assistant

J. Puig, Assistant

S. Soromenho-Ramos, Assistant

Also Present

IBRD: G. Bauche, Advisor; M. Dorfman, Senior Economist; B. Mierau-Klein, Acting Director and Chief Credit Officer; V. Nehru, Manager HIPC Unit; J. Thornton Economist. African Department: A. Basu, Deputy Director; Asia and Pacific Department: D. Citrin, L. Molho. External Relations Department: D. Hawley, S. Nardin, K. Rosser. Fiscal Affairs Department: S. Gupta, P. Heller. Finance Department: E. Brau, Director; B. Arnason, E. Budras, J. Honda, J. Lin, N. Wagner. International Capital Markets Department: A. Bertuch-Samuels, C. Blitzer, C. Medeiros, E. Psalida. Independent Evaluation Office: J. Chelsky. Legal Department: D. Eastman, S. Hagan, Y. Liu, N. Rendak, G. Rosenberg, B. Steinki. Middle Eastern Department: J. Le Dem, A. Milasiute. Policy Development and Review Department: T. Geithner, Director; M. Allen, Deputy Director; L. Cui, T. Dorsey, M. Fisher, J. Gold, M. Hadjimichael, R. Khemani, A. Kireyev, A. MacArthur, M. Mecagni, W. Mitchell, J.-C Nascimento, S. Panth, M. Plant, L. Redifer, Hemant Shah, K. Srinivasan, J.-Y Wang. Secretary's Department: L. Hubloue, P. Ramlogan, J. Stotsky. Western Hemisphere Department: L. Cardemil, P. Dyczewski, O. Gronlie. Advisors to Executive Directors: S. Bah, S. Bakhache, A. Ismael, F. Manno, J. Milton, T. Moser, Y. Patel, K. Sakr, A. Tombini. Assistants to Executive Directors: M. Abbing, R. Gauba, M. Jamaluddin, B. Mamba, D. Prasad, M. Sidi Bouna, J. Sipko, J. Yu.

1. PROGRESS REPORT ON CRISIS RESOLUTION

Document: Progress Report on Crisis Resolution (SM/03/301, 8/26/03)

Staff: Geithner, PDR; Bertuch-Samuels, ICM; Hagan, LEG

Length: 2 hours, 5 minutes

Mr. Reddy submitted the following statement:

We welcome the concise but a comprehensive report prepared by the staff detailing the progress made since the last spring meeting in respect of use of collective action clauses (CACs) and in the evolution of a Code of Conduct. We believe that these developments augur well for crises resolution in a cost efficient and timely manner without serious disruptions to the smooth functioning of markets. Second, they also show that there is a strong tendency for handling the debt restructuring process through voluntary, contractual and market based solutions in preference to any statutory approaches, with a central direction or prescription. Third, even while we find widespread acceptance of the use of CACs, there is a strong element of divergence in practices, though the essential elements like majority restructuring and enforcement provisions have found a place in all issuances. Fourth, the market is also willing to innovate as is evident from the Uruguay's recent bond issues. In a nutshell, we consider these developments as impressive gains and spill over benefits of the extensive discussions initiated by the Fund since November 2001 on various aspects of sovereign bond restructuring. The Fund's initiative has no doubt sufficiently sensitized financial markets and private and public sector participants with regard to this important subject.

The most important and encouraging feature of CACs noted in the report is the dispelling of any fear of premium for the inclusion of CACs. This finding, evident first in the Mexican bond issue, has been further strengthened by subsequent issues in several other countries. While it is true that still there are number of issuances without CACs, and different issuances with CACs followed varied practices, all the issuances met with success, inasmuch as the demand outstripped supply to a significant extent. The fact that there was no uniformity with regard to the adoption of governing law shows some element of market segmentation and preferences. In our view, this must be allowed to continue since it reflects country specific circumstances and that the issuers and investors are comfortable with such differential features.

As regards the design features, we would like to reiterate that the Fund should continue to encourage use of CACs as found appropriate and acceptable to issuing authorities and investor countries rather than promoting any rigid format or models. Therefore, differences in voting threshold in the range of 75 per cent to 85 per cent and majority enforcement provisions

ranging anything from 25 per cent to above 25 per cent should not be viewed as imperfect use of CACs, but a tolerable variance suiting to different issuers and investors. Perhaps, as the market evolves and as the number of issuances with the CACs increased, there could be convergence to one or two major designs of CACs.

We welcome several steps taken by the staff in a proactive manner promoting the use of CACs in sovereign debt issues. We also support the ongoing efforts by the Fund/Bank in improving internal guidance notes on this subject.

Evolving a Code of Conduct for market participants is a recent development. We, therefore, recognize that there are bound to be areas where a greater degree of consensus among the sovereign issuers and private creditors yet to be achieved. However, in this regard there should be no scope for any compulsion from IFIs since the evolution of the code as well as adherence of the code should continue to remain voluntary. We welcome the initiative by the Banque de France and the Institute for International Finance. We would like to reiterate that the process should be purely voluntary and, therefore, before the code is finalized, there should be extensive involvement of both creditors and debtors from industrial as well as emerging and developing markets. We do not believe that the code should be 'prescriptive' enough to offer a useful guide. While we agree that a degree of consensus is important, we do not agree that any kind of prescriptive approach will be desirable. In view of this, we strongly recommend that the first sentence in paragraph 15 should be modified to appropriately reflect this position.

As regards the desirability of increasing the disclosure of information by the sovereign bond issuers, protecting at the same time the confidentiality and sensitivity to market reactions, we reiterate that the information as part of the code should be limited to the claims for which restructuring will apply. Nature of information exchange and the scope of transparency, could be left to the developers of the Code, as acceptable to participating members.

As regards the monitoring mechanism to oversee the compliance with the code, in our view, it may not be desirable for the Fund or any other IFI to directly involve in this effort. The evolution of a monitoring mechanism should be an integral component of the development of the Code and such a mechanism could be agreed to by the signatories to the Code when it is finalized. In countries where the IFIs are directly involved, the application of the 'good faith criterion' is nevertheless important in reaching a collaborative agreement before restructuring.

In sum, the progress has been encouraging and the Fund could continue to monitor and report the developments to the Board. We encourage the staff to continue to explore other issues relating to debt restructuring as

part of crises resolution including aggregation issues and we look forward to the forthcoming paper. We support the publication of the revised version of this paper after the Board completes its discussion.

Ms. Indrawati submitted the following statement:

We thank staff for the paper before us today on the progress in the use and design of collective action clauses (CACs) and on efforts being undertaken by the Fund toward encouraging sovereign borrowers to include CACs in their debt instruments, as well as the progress in developing a voluntary Code of Conduct for sovereign debtors and their creditors.

We note that rapid progress has been made in promoting the inclusion of CACs in international sovereign bond issuances and we believe that the wider use of such clauses could help in building an orderly and timely agreement on sovereign debt workouts and can be considered as part of efforts to strengthen crisis resolution.

We welcome the development of the issuance of international sovereign bonds since the beginning of this year without an increase of premium that is associated with the use of CACs. Given these developments, we recognize the fact that a significant stock of current outstanding debt does not include CACs and it would take some time before such clauses are included in most international bonds. In this regard, we welcome staff's proactive role in promoting the use of this provision as indicated in the paper. Nevertheless, we would like to stress that given the contractual nature of CACs, any decisions as to the inclusion and design of CACs should be left to the debtor and its creditors and continue to be on a voluntary basis. The paper also highlights the differences in the design of recent CAC issues. We see the importance for countries to exercise flexibility in designing the CACs and factors such as differences in legal systems, market features and other country circumstances as well as the changes in the global financial markets should be taken into account. Serious consideration should be given to the legal framework of the country concerned that could thwart or delay the necessary action and derail the restructuring process.

We note staff's effort to continue several forms of outreach to encourage the use CACs. Educating the market through dialogues with emerging market issuers, private market participants as well as legal practitioners are important to enhance understanding and should be one of the current priorities. At the same time, priority should also be given to the introduction of CACs in debt contracts in markets where their use is not widespread. As staff points out, a number of mature market countries have taken steps to introduce CACs in their international sovereign bonds, but since March 2003 there were some emerging market issuances that did not contain CACs. However, in the process of educating and encouraging the use of

CACs, the Fund should not promote or endorse any particular model or set of clauses for countries to adopt. It should be left to the relevant parties to discuss and decide the clauses that could benefit both the debtor and their creditors.

On the Code of Conduct (a Code), we appreciate staff's effort in their exploration of introducing a Code. We can agree that a Code could facilitate a continuous dialogue between creditors and debtor, promote corrective policy action to reduce the frequency and severity of crisis and facilitate the orderly and expeditious resolution of crisis. However, we see that the establishment and implementation of a code could be complex and further exploration is needed. Therefore, we support the exploration of difference approaches to consultation and the design of a restructuring strategy. Although the code is intended to be voluntary, it may involve the creation of some forms of institutional infrastructure that has no legal basis. The question of how to ensure that parties comply with the Code and the issue of how non-compliance would be treated requires much further exploration. We wonder how the Fund can play its role in monitoring the compliance beyond the existing mechanism. Staff's further explanation would be appreciated.

Finally, while we see the importance of Fund involvement in promoting CACs and a Code, it is also important to carefully weigh the use of Fund resources and strike an efficient balance between crisis resolution and crisis prevention efforts. We believe that more emphasis should be given to the latter.

Mr. Shaalan made the following statement:

First, I would like to welcome the progress made in promoting the inclusion of collective action clauses (CACs) in sovereign bonds in quite a few jurisdictions where these provisions were not previously included. It is fair to say that the increasing acceptance of their inclusion could well be a by-product of our extensive discussions on the Sovereign Debt Restructuring Mechanism (SDRM) itself. The Fund should continue to encourage countries to include these clauses, particularly as the once-feared premium payments attributed to their inclusion does not appear to have materialized—at least there is no evidence of it so far.

We note that for those countries that have used CACs there are differences in what could be key aspects, and I am not at all sure whether they are important or not. One key aspect is the voting threshold required for majority restructurings, which has in some cases been 75 percent, and in others 85 percent. Does this difference pose any difficulties in practice?

The other point is with respect to majority enforcement provisions. My understanding is that all recent New York law bonds adopted a 25 percent

threshold for acceleration, but they differ on thresholds for deceleration, resulting in some degree of asymmetry. Could these differences give rise to legal difficulties?

On the Code of Conduct, more work is still needed. I see, based in our previous discussions on this issue, the provision of complete data by debtor countries as a major issue in this area. We would like to concur with Mr. Reddy when he underscores the voluntary nature of the process in both the evolution of the code as well as adherence to the code.

Mr. Kruger made the following statement:

I would like to thank the staff for their update on collective action clauses (CACs) and the Code of Conduct. The progress seen on CACs since the spring is very positive. A large number of bonds with CACs issued under U.S. law and the innovative approach taken in Uruguay shows that the market can respond to new situations accordingly. I would like to make two brief comments on recent developments in crisis resolution. First with respect to the design of CACs and second on disruptive litigation.

First of all, our experience with CACs is limited. They have only been used to restructure Ukrainian bonds under Luxembourg law, Uruguayan bonds under Japanese law, and Moldovan bonds under English law. Therefore it is hard to draw general lessons. However, the bonds recently issued under U.S. law represent a departure from pre-existing practice in that the thresholds are calculated with respect to outstanding principal rather than representation at bondholders meeting. In addition, the thresholds are high. The new bonds issued by Mexico, Italy, the Republic of Korea, South Africa, and Uruguay all use a 75 percent voting threshold, while those issued by Belize, Brazil, and Guatemala use an 85 percent voting threshold. While the approach taken by these new bonds may be a useful example of how to apply majority restructuring provisions in jurisdictions that put a high value on individual bondholder rights, it raises a concern with respect to bondholder inertia. In particular, bondholders that for one reason or another fail to vote will be counted as having voted against the restructuring, in effect becoming holdouts. We understand that institutional investors represent a higher percentage of the market in the United States than they do overseas. Nevertheless, an 85 percent threshold could make it difficult to engineer a restructuring either because of bondholder inertia or because it might be relatively easy to obtain a 15 percent blocking minority. Since these issues are emerging, it is difficult to gauge the extent to which restructuring these bonds will be problematic. Nevertheless, we wonder if there are any lessons that we can draw from the corporate context. Is there anything in the voter turnout of corporate bondholders or shareholders that might lead us to believe that bondholder inertia would be an obstacle to restructuring?

Moving to disruptive litigation, in our discussions under the SDRM we devoted a lot of time to thinking about the effects of disruptive litigation and whether or not a stay on litigation should be part of the statutory framework. I wonder what lessons can be learned from the default in Argentina, which took place almost two years ago. I understand that, given the stakes involved, a number of proceedings have been initiated against the sovereign, yet it does not so far appear that these proceedings have been a factor in working towards a restructuring deal. Could the staff update us on who has initiated proceedings against Argentina and what the status of the various cases is? Does the staff think that there are lessons to be learned from the Argentine experience on the extent to which litigation can derail a restructuring?

Mr. Lushin made the following statement:

We join the staff in their assessment that a rapid progress has been made in promoting the use of collective action clauses (CACs) in sovereign bond issuances over the past two years. It is, indeed, encouraging that there is a continuous increase in such issuances by both emerging market and developed countries. Therefore, it is appropriate to say that the international campaign for the promotion of CACs, led by the G-10 Working Group and several international institutions, not least the Fund, has paid off.

Moreover, the main prejudice against CACs that existed in several emerging market issuers, i.e. the belief that the cost of issuance will increase drastically, did not materialize. The capital markets seem to have shown that the acceptance of the country's bonds was based mostly on the strength of the macroeconomic fundamentals rather than on the addition of CACs. Moreover, the inclusion of CACs may have been seen as yet another mechanism that could be beneficial to the investors in the case of debt restructuring.

At the same time, it was interesting to learn that in 2000-2001, or before the initiation of the CAC campaign, the issuance of bonds in New-York with majority restructuring provisions by three countries in the Middle East had gone unnoticed by the international capital markets. If the staff have any explanation to this fact, it would be worth including into the Progress Report. In the same vein, it would be interesting to learn whether the absence of CACs in some issuances after March 2003 reflects just technical aspects, such as the reopening of old bond issues, or signals still cautious attitude of some borrowers and investors to such practice.

The staff mentioned that, while considerable discussion about CACs took place in the markets before the first Mexican issue, market analysts virtually ignored the subject at the time of Korea's issuance. Could this mean that, in the end, investors have become more accustomed to CACs or they have been attracted by the scarcity of Korean debt instruments? We wonder if the staff could provide any thoughts on the specificity of Korean case.

As to the design of recent CACs, we have always seen the CAC process as a market driven one that reflects the interactions between borrowers and investors. Therefore, we trust that the differences in the composition of provisions in CACs emerged from the investors' differentiation between the borrowers and see this as a welcome development.

In regards to the Code of Conduct, we continue to believe that the Fund should refrain from endorsing any set of standards and continue to participate in any discussions on this issue as an observer only. In general, we see value in the existence of such a Code, although in a rather diverse international financial community it is difficult to imagine how it could become binding. In this respect, we recognize that reaching a consensus on the right balance between the debt resolution framework that is flexible enough to be applied to a diverse group of country circumstances and, at the same time, prescriptive enough to be able to orderly guide through restructuring, is a tall order. As there are no easy solutions on how to accomplish this and since many contentious issues are present, we see the only way forward in the continuing dialogue between investors and borrowers. In this context, we see scope for the borrowers to re-examine their investor relations program and for the investors to assist them in this by pointing out the drawbacks. As to the process of consultation and the design of a restructuring strategy, there is room for innovation as well and different options should be definitely explored if there is interest on behalf of all parties involved.

To sum up, the Fund staff have done a good job in promoting the use of CACs. We encourage them to continue their work along the lines of activities mentioned in paragraph 12. At the same time, we do not see the Fund being involved in the monitoring of the implementation of the Code of Conduct, if such were to emerge. However, if it were to be an agreed Code, the Fund's policy of lending into arrears could be revisited in order to bring more substance into the good-faith criterion.

Mr. Cho made the following statement:

Like previous speakers, I thank the staff for the concise yet very informative report. I also find useful the staff's separate paper on the sovereign debt restructuring issue within the existing framework circulated for the information of the Board. Indeed, there has been much progress on this issue since the last IMFC meeting in the spring. In particular, the progress on collective action clauses (CACs) seems to be quite remarkable. A series of emerging countries, including my own, successfully included CACs in their recent sovereign bond issuance. As the progress report duly acknowledges, Mexico should get credit for breaking the ice for the first time, but I would also like to join Mr. Shaalan in pointing out that this initial success is a by-product of the intensive discussion of the Sovereign Debt Restructuring

Mechanism (SDRM). In this respect, I would like to offer my salute to the management, especially Ms. Krueger, and the staff who worked tirelessly to enlighten some suspicious minds in the international financial community by convincingly raising the need for an explicit mechanism to deal with the sovereign debt restructuring issue.

At the same time, the report also reminds us of the unsettled issues on the subject. For instance, while it is encouraging that the concern about the first mover problem for the inclusion of CACs now appears to be overcome, it is still premature to expect CACs to become an established market practice in sovereign bond issuance. Given that the recent cases of success for inclusion of CACs were appropriately timed with abundant liquidity in the international financial market, it remains to be seen whether investors' risk appetite will continue to ignore the presence of CACs in bond issuances when the liquidity situation turns sour against emerging markets, as the recent issue of the Global Financial Stability Report (GFSR) warns. On their part, emerging issuers do not seem to be fully convinced of the nonexistence of costs of CACs on spreads, as evidenced by the cases that did not include these clauses listed in the report. Most substantially, the recent success in CACs highlights even more challenges ahead; namely, how to deal with outstanding bonds that did not contain CACs, and more seriously how to deal with the aggregation problem as a whole in the actual sovereign debt restructuring, not to mention the concern about disruptive litigation raised by Mr. Kruger. It is true that the case of Uruguay offered some way out on the first issue by accommodating some noble features that are explained in Box 2 of the report, but it is still too early to be certain that the experience is repeatable. The exit consent clause provides an alternative in the existing framework, but it is far from perfect as the aforementioned paper notes. When it comes to the aggregation problem, however, the limitations of the recent progress are more evident.

Certainly, developments in the discussion for the Code of Conduct are promising. The Fund can play a certain role in facilitating the operation of the code by linking its lending into arrears policy with the good faith criterion for negotiations of sovereign states with creditors, but given its voluntary nature, it would be too much to ask for the code to be a reliable mechanism for any sovereign debt restructuring. Finding a solution to this problem is not easy, as we saw during the discussions on the SDRM, but efforts should continue. In this respect, we welcome the staff's assurance that more work is undergoing, especially on the aggregation issue.

To conclude, we welcome the recent progress and encourage management and the staff to continue with the discussion of crisis resolution for further meaningful progress.

Mr. Le Fort made the following statement:

I join other Directors in thanking the staff for a clear and concise paper, and welcome this progress report on the use and design of collective action clauses (CACs) as a mechanism to facilitate crisis resolutions, as well as on the efforts being undertaken to encourage its use in future bond covenants. I think that I can be brief, as I fully concur with Mr. Reddy's preliminary statement, in particular in that CACs are a voluntary, cost-efficient, market-based mechanism for timely crisis resolution which leaves enough room for flexibility in practices, including instrument innovation.

The countries in my constituency are prepared to adopt CACs in new sovereign issues, and as a matter of fact the bonds issued by Uruguay in the recent exchange include novel CAC features. Additionally, the Finance Ministry of Chile recently announced that CACs would be included in future bond issuances. Moreover, and to some extent surprisingly, the adoption of such clauses have been mentioned by major credit rating agencies as a factor for possible upgrading Chile's sovereign debt.

Finally, I join Ms. Indrawati in calling for special attention to be concentrated in the design of Fund facilities aimed at crisis prevention. Indeed, large reserve holdings and a huge gap between what is considered a prudent level of public debt in emerging market compared to that of industrialized economies represent costly self-insurance mechanisms developed for crisis prevention in the absence of an efficient collective insurance process. We believe that the Fund is the one called to fill that gap.

Mr. Al-Turki made the following statement:

I join other speakers in thanking the staff for a concise and informative update on developments regarding collective action clauses (CACs) and the Code of Conduct. I am encouraged that the inclusion of CACs in new international sovereign bond contracts governed by New York law has increased substantially over the past few months, as shown in Table 1. It is also reassuring that there was no evidence of higher interest costs associated with the use of CACs. This would hopefully encourage the inclusion of CACs in all future international sovereign bond issues. This should be further facilitated by the staff's ongoing efforts to promote the use of CACs along the lines detailed in paragraph 12 of the paper.

At this initial stage of including CACs in international sovereign bond issues governed by New York law, it is to be expected that there will be some variation in the design of CACs in differing issues. It is important, however, that, as the CACs gain more acceptance there will be convergence to the provisions recommended by the G-10 working group. This will facilitate comparison between the bonds in the market and guard against the risk of

raising the voting threshold to levels that will render the CACs practically useless.

In addition to the increased use of CACs, a voluntary Code of Conduct could help improve the existing process of restructuring sovereign debt. While some progress has been made, the staff rightly highlights the challenges that remain. In this connection, I agree on the importance of improving the quality of investor relations programs across emerging markets. In view of the voluntary nature of the Code, I do not see a need for a mechanism to monitor compliance.

Ms. Jacklin made the following statement:

We welcome the update on Crisis Resolution initiatives, particularly the details on the use of collective action clauses (CACs).

Collective Action Clauses

We are pleased to see progress made in the adoption of CACs and support the Fund's more active role in promoting better understanding and use of CACs through talks with borrowing countries and market participants. That investment bank representatives now expect New York issues to include CACs as a matter of course demonstrates that a significant hurdle has been cleared. We note (footnote 5) that no bonds with CACs have yet been issued under German law. Could the staff explain the latest state-of-play on this?

We have seen some evolution in the terms used to incorporate CACs and believe it should be left to the market to sort out what terms are most desirable. We expect that over time there may be a convergence on terms.

Code of Conduct

Regarding a voluntary Code of Conduct in debt restructuring, we hope creditors and issuers can agree on a useful framework, but stress that the official community cannot force agreement in this area between the parties to such transactions.

There are several different issues including the relative merits of creditors' committees. While creditors' committees can be a useful mechanism for facilitating discussion between debtors and creditors, we should recognize the need for a case-by-case approach so that the most effective means of resolution are used in each instance. In any restructuring, transparency is essential to promote an equitable resolution of claims.

We believe the Fund is participating appropriately as an observer and agree with the views of many Directors that the Fund should not take on a formal monitoring role for a Code of Conduct.

Going Forward

We appreciate the efforts of the staff and look forward to further consideration at the Board of any future developments, but do not believe that currently any detailed discussion is needed at the upcoming IMFC meeting in Dubai. In considering the focus of Fund efforts, we agree with Ms. Indrawati on the need to emphasize crisis prevention.

Mr. Rouai made the following statement:

We thank the staff for the concise and informative report on recent developments and initiatives to strengthen the toolkit for orderly resolution of crisis, in particular, regarding the voluntary adoption of Collective Action Clauses (CACs) and the design of a code of conduct to improve the process of restructuring.

Our chair continues to support staff's further efforts in promoting the use of CACs by industrial and emerging market economies and in educating market participants. In this context, staff's information regarding greater use of CACs in recent bond issues, without any premium in pricing, is encouraging; and the indication that investment bank representative "expects new sovereign issues governed by New York law to include CACs as a matter of course," is comforting. We welcome staff's preparation of the operational guidance note encouraging member countries in the context of Article IV consultations to use CACs. During the last Article IV consultations with Tunisia, the authorities declared their preparedness to include CACs in future bond issues. Staff are encouraged to pursue this outreach effort during their meeting with the authorities in Dubai. The last CACs staff report contained a proposal of organizing an international seminar to promote the use of CACs; staff may wish to elaborate on this initiative.

We welcome recent initiatives for designing a set of principles and best practice to guide the relationship between private creditors and issuing governments during the process of restructuring sovereign debt. We also support this voluntary framework and Fund monitoring of this process. It is premature at this stage to address the issue of monitoring by the Fund of practices against the standards in the code.

Mr. Portugal made the following statement:

I would like to thank the staff for the progress report, which shows good progress on the issues at hand. The nature of our current discussion is

mainly to see if the report adequately reflects that progress, rather than entering into a detailed discussion of the substance of the topic itself. I just have three suggestions, supporting points that were raised by Mr. Reddy and Ms. Indrawati in their preliminary statements.

First, on the point made by Mr. Reddy that differences in voting thresholds for CACs in the range of 75 to 85 percent should not be viewed as an imperfect or an inappropriate use of CACs, but as a normal variance which suits different interests of issuers and investors, I would suggest capturing this idea in paragraph 8 of the report. One way of doing this would be to make a more extensive use in that paragraph of the summing up of the previous Board discussion on CACs. Quoting from that summing up “most Directors noted that it is too early to reach a definite view on the degree of standardization that should be sought in terms of the design of CACs within and across jurisdictions. Several Directors agreed that it would be not advisable for the Fund at this early stage to promote or endorse a single set of model clauses as the exclusive benchmark.”

Second, I would like to support Mr. Reddy’s comments on the Code of Conduct, which should not have any kind of prescriptive approach. There is probably general agreement on the need for the code to be voluntary, as mentioned by a number of Directors in the current discussion, including Mr. Shaalan. In this vein, the word “prescriptive” should be changed to the “descriptive” or “concrete” in the sentence in paragraph 15 stating that there is a balance to be reached between a code which is flexible enough to be applied and one which is still prescriptive enough. In fact, the code will not be prescriptive, but voluntary.

Third, like Mr. Le Fort, I agree with the point made by Mrs. Indrawati asking for further work in order to improve the design of our precautionary facilities.

Mr. Brooke made the following statement:

Like other Directors, we welcome the encouraging progress made on collective action clauses (CACs) since the spring, and especially the actions taken by a number of emerging markets to include CACs in their bonds issued under New York law. We were pleased to note that the inclusion of these CACs has not resulted in a yield premium. This was also the experience for the U.K. Consequently, we strongly encourage the use of CACs by all issuers so that they become standard market practice. We therefore fully support the staff’s continued efforts to encourage the take-up of CACs through discussions with sovereign issuers, private market participants, and in the context of bilateral and multilateral surveillance.

On a more specific note, I would like to echo the question raised by Mr. Lushin asking for more explanation as to why some countries have still chosen not to include CACs. This has happened not only in cases of reissuance of an existing bond, but also in a case of issuance of new bonds. I would be interested to know what were the particular factors in that case and what the staff has done in discussing that instance.

Few CACs have thus far included provisions in respect of litigation proceedings and the sharing of information, as was recommended in the G-10 report. The exceptions were Uruguay and the United Kingdom. The Fund should encourage potential issuers to include these clauses as well as all the other clauses in future bonds, and hope that this is also a part of their dialogue with issuers.

Finally on CACs, it would be helpful if the next Global Financial Stability Report (GFSR) could include some of the analysis presented in the progress report on the price impact of CACs, since it would be important to get as broad a readership as possible of this message.

Turning to the code, we continue to support the development of a Code of Conduct since we feel it will help facilitate crisis resolution and improve the dialogue between creditors and debtors. For a voluntary code to be effective, it needs to have the broad acceptance of all parties. We welcome the recent efforts to push this forward, and we strongly encourage active participation of all issuing countries in the code's development. We also value the Fund's input into the process.

As Mr. Lushin noted, once the code is agreed, the Fund's lending into arrears policy could well need to be adjusted to take this into account. We also believe that it will be important for the code to encompass the role of the Paris Club, and we welcome the ongoing discussions in the Paris Club on this issue.

To conclude, as Mr. Cho highlighted, we feel that it is important that the crisis resolution work commissioned in the IMFC communiqué of the Spring Meetings is delivered in full. In this regard, we continue to feel that aggregation and intercreditor equity considerations, which were core principles of the proposal for the SDRM, deserve further consideration if we are to substantially improve our crisis resolution framework. Therefore, we look forward to the paper on aggregation, which we understand is imminent, and we would urge the Fund to continue to look at innovative ways of promoting aggregation. We would also encourage the staff to continue to explore the options for a debt resolution forum that were provisionally discussed in some of the SDRM papers as part of their ongoing work on crisis resolution issues.

Mr. Beauregard made the following statement:

Like other Directors, I would like to thank staff for preparing a concise but comprehensive progress report on some crisis resolution issues.

The inclusion of collective action clauses (CACs) in sovereign bond contracts has been advancing well and the results are encouraging. The fact that no premium was found in the sovereign bond issues that included CACs augurs a good future for these clauses. But perhaps more importantly has been the fact that a country facing a debt restructuring was also able to include these clauses without penalty and with novel features. These results should be used widely by the staff in promoting the use of CACs among member countries. The voluntary and market friendly nature of CACs also confirm that these two aspects are crucial for their more broadly use among issuers. We concur with Ms. Indrawati that flexibility needs to be maintained in this area and that it is up to debtors to decide which clauses to use. In the same vein, and as we have said in the past, the Fund should promote the use of CACs but without endorsing a particular set of clauses. Differences among debtor countries will certainly be reflected in the particular set of clauses included in the sovereign debt contracts. This flexibility will also work as a promoter for the use of these clauses among debtor countries.

The other area where the staff reports progress has been made is in the development of a Code of Conduct. Like in the case of CACs, this is an area where the participation of debtor countries and creditors is crucial to ensure its viability. We take note that Fund staff has participated as observers in these talks, and we would appreciate it if from time to time they could inform the Executive Board on developments in this area, maybe through the distribution of written notes. I would like to strongly support Mr. Reddy's suggestion to rephrase the first sentence of paragraph 15. Flexibility in this area is also of the essence.

To end, we would like to echo Ms. Indrawati's comments, also supported by Mr. Le Fort, Ms. Jacklin and Mr. Portugal, regarding the need to carefully weigh the use of Fund resources and to strike the right balance between crisis resolution and crisis prevention efforts. Like her, I believe that the Fund ought to devote more emphasis to the latter. In fact, during the last six months that is what has been happening. The Fund has been discussing several crisis prevention issues, while the market and debtor and creditor countries have been working on the important crisis resolution issues covered in today's progress report.

Mr. Egilsson made the following statement:

I would also like to thank the staff for the progress report on crisis resolution. I would in the beginning like to refer to the communiqué from the

last Spring Meeting, where the conclusion was reached that it was not feasible at that time to move forward to establish the SDRM. I would like to emphasize that the idea of the Sovereign Debt Restructuring Mechanism (SDRM) is not dead, even though it has been parked for a while. We will have to see whether it will be necessary to move that idea forward some day.

Having said that, I welcome recent developments with regard to the use of collective action clauses (CACs). What I find important is that we get fairly quickly to a point where there is fairly good convergence on the terms in CACs, because if they develop in a very diverse way, we may easily have a situation where the same country has different clauses in different issues, and then what would happen if these clauses are contradictory? That may cause all kinds of legal confusion. The Fund should put an effort into, if not standardizing these clauses, at least having some kind of opinion on what is the best practice in this area to prevent legal confusion.

As far as the Code of Conduct goes, recent developments are positive. The Code of Conduct should be voluntary, not binding. The biggest contribution of the code would be to establish normal debtor/creditor relations. I would see it as especially valuable if governments that sign up for a code would talk to market participants in a similar way as companies that are listed on the stock exchange. It is strange to think that there has to be a code in order for a country to be marketing itself toward investors, but that may still be the case.

Regarding the role of the Fund in the code, this has to be approached in the context of surveillance, with a focus on evaluating whether governments are approaching the market in a way that is consistent with the functioning of financial markets. This is part of how an orderly financial market functions.

Mr. Yagi made the following statement:

We thank the staff for the progress report on crisis resolution. Concerning collective action clauses (CACs), we welcome the increasing number of inclusions of these in sovereign bonds. We also appreciate the staff's efforts to promote the inclusion of CACs.

Regarding the differences from one issue to another and from one market to another regarding threshold requirements for majority restructurings, it would be better to watch market developments and promote further inclusion of CACs rather than to try to standardize any of these CACs.

On the specific case of Uruguay, we appreciate the constructive initiative to try to address some aspects of the aggregation issue, which could

be particularly interesting initiatives with the swap operation for various bonds at the same time.

Concerning the Code of Conduct, we appreciate the efforts of various institutions or representatives of emerging market economies, major economies, and the private sector. We are particularly appreciative of the efforts of the Bank of France in this area.

Mr. Yakusha made the following statement:

At our last Board meeting on CACs, and I have to admit that the progress on CACs is described in the report very well, we asked the staff to discuss with the World Bank the possibility of including CACs in their own bonds issued under U.S. law, where CACs seem to have quickly become the norm rather than the exception. Perhaps the staff could provide an update on that.

On the Code of Conduct, I agree with the staff on the need to maintain some kind of balance between the voluntary nature of the code and some degree of prescriptiveness. The staff should have some interest in having better structured debtor/creditor relations, so we would support a little bit more ambitious, hands-on approach on that.

Finally, while the report describes the modest progress achieved in the last few months, it is less clear what progress will be made in the coming period on the agreement reached by ministers in the last IMFC meeting to keep working on crisis resolution issues. There is plenty of work to do in this area, including the development of best practices for the use of CACs to facilitate crisis resolution, the inclusion of other types of debt and crisis resolution considerations, the further development and implementation of the Fund's lending into arrears policy, and the need to decide on the balance between fiscal adjustment and the extent of debt restructuring among others. I would be interested in hearing the staff's views on the work on these issues in the period ahead.

Mr. Padoan made the following statement:

We welcome this accurate report and the inclusion of the Global Financial Stability Report (GFSR), as Mr. Brooke pointed out.

We welcome progress in collective action clauses (CACs) and positive market reactions, including no clear premium effects. However, like others, we note that it may be too early to declare our enthusiasm and wait to draw final conclusions on an inevitable shift towards generalized CAC adoptions. We also wait for the rally on emerging markets (EM) to boil down.

We agree with Mr. Reddy, who notes that contractual approaches have spread also as a consequence of widespread discussion on a statutory approach. He also notes that this evolution shows a clear preference for voluntary, contractual, and market-based solutions over a statutory approach. This is hardly a surprise as a statutory approach is not yet available.

However, this also supports the idea that continuing discussion on features such as aggregation, litigation procedures, and the implications of a stay on litigation could provide important input as to the way markets self-organize in dealing with crises. Like Mr. Brooke and Mr. Egilsson, I look forward to further discussion on these issues and perhaps staff could briefly update us on the future agenda in this respect.

I look forward to progress in the development of a Code of Conduct. I wonder to what extent the discussion on the definition and implementation of a Code of Conduct could benefit from looking at other experiences, including in the private sector, of voluntary self-adopted codes in related areas. Staff comments are welcome.

I support Ms. Indrawati's suggestions for further exploration of the legal basis of such a code. I also support Mr. Lushin's suggestion to reconsider our Lending into Arrears Policy once the code is adopted.

Mr. Rutayisire made the following statement:

Like other Directors, we welcome the increasing use of collective action clauses (CACs) in international sovereign bonds. This goes in the direction of market-friendly solutions that many debtors and creditors prefer. We are pleased to note that the use of the clauses has not been accompanied by an increase in premium pricing. We agree that efforts should continue to make the use of CACs a more common practice, but like Ms. Indrawati and Mr. Reddy we think that should be done on a voluntary basis, with each country's specific circumstances taken into full consideration.

On the Code of Conduct, we welcome the ongoing discussions. However, we note that views still differ on several important elements of the code, and we encourage the staff to continue their efforts on this issue as well as on other issues related to the resolution of crisis.

Mr. Duquesne made the following statement:

We welcome recent developments regarding the use of collective action clauses (CACs). In this regard, I share the remarks made by Mr. Padoan and I would add that the G-10 proposal should become the reference for those clauses. Thus, we can accept paragraph 8 as it is.

We welcome involvement by the staff, including area departments as in the recent case of Uruguay, in the promotion of those clauses. We also welcome the work underway to revise the guidelines for public debt management by the Bank and the Fund, and we are waiting for the results of this work. Having said that, like Mr. Yakusha, and being myself a member of the board of the World Bank, I wonder if the World Bank could not include CACs in its own issues under New York law.

On the code, we felt that the meeting that took place in the Bank de France on July 25 between senior officials of issuer countries and eminent representatives of the private sector was a fruitful one. There are still divergences on some critical points, but there was broad consensus on the objectives and principles underpinning such a code, including consultation between debtors and creditors, information sharing, good faith, and fair treatment among others. Participants agreed that a code should be voluntary, flexible and balanced, but I do not see a conflict between the prescriptive and voluntary natures of the code. Prescriptive does not mean mandatory. It just means that subscribers to the code will apply the clear and prescriptive rules under the code even if they subscribe on a voluntary basis. Therefore, I can live with the current drafting in paragraph 15. Against this backdrop, I understand that the G-20 could be seen as the appropriate forum to discuss the different proposals on the table regarding further steps to draft the code. Finally on the code, the Fund can continue to play a useful role in the process of elaborating the code and in its future implementation.

Finally, like Messrs. Brooke and Padoan, we think that more work should be done beyond CACs and the Code of Conduct on the topics that were underlined in the last IMFC communiqué; namely, aggregation, inter-creditor equity, transparency, and debt resolution. Beyond the reference in footnote 1 of the progress report to the two staff papers on these issues that have been or will shortly be circulated to the Board, I wonder if excerpts from these papers could be added in the progress report to update ministers on the substance of developments in these areas.

Mr. Kiekens made the following statement:

I think today's most penetrating questions were raised by Mr. Kruger, concerning the risk of bondholders' inertia and the lessons from Argentina about litigation; and I am looking forward to the answers of the staff.

Second, I think there is a broad consensus in the Board that the Fund should not interfere in the drafting of collective action clauses (CACs). But I think the Fund should not hesitate to point out that we see clauses emerging in practice that risk jeopardizing the possibility of an orderly restructurings and that would fairly balance the interests of all creditors. Mr. Kruger seems to have been the first to point out the emergence of such a clause, which would make an 85

percent majority of bondholders the threshold for restructuring. In my opinion, this threshold is too high. It conflicts with the G-10 recommendations. I think the report should point out the risk of bondholders' inertia, and the risk of paralyzing an orderly restructuring process.

In any case, if the Fund wants to be neutral, I think there is reason to change paragraph 8 of the staff paper, which seems to suggest that the Board or Directors have expressed the view that the majority restructuring provisions should set the voting threshold at 75 percent *of the outstanding principal*. I think it is misleading to say that the Board preferred to set the threshold at either a 70 percent or a 75 percent majority of the outstanding principal. I think it was rather the Board's view that these would be acceptable alternatives to what I consider the better clause, namely the English clause, which specifies 70 or 75 percent *of the bondholders present at the meeting*. As it now stands, the drafting of paragraph 8 seems to suggest to the non-alert reader that the Board prefers the New York practice, at least the limited practice that has emerged so far, to the clause based on English law.

Granted, there is a small footnote that says that regarding bonds governed by English law, but apparently only such bonds, the Board considered it appropriate to continue the practice existing in that jurisdiction. As far as I am concerned, and I think the Board would agree, if tomorrow we see emerging a practice based on New York law, on German law, on Japanese law, on Luxembourg law, whatever law, setting the threshold at 75 percent of bondholders present at a meeting, we would consider that a reasonable and even a preferable practice. I therefore strongly insist to that paragraph 8 be redrafted. Otherwise we will be in conflict with our own preachments of neutrality, by giving the impression that we have a clear preference for a practice that I personally consider inferior to the practice in London.

As to the Code of Conduct, I think the Fund is part of the orchestra. The many colleagues, who were reading the numbered paper on Argentina during this meeting, may have concluded that the Fund is the single most important creditor in Argentina. So even if we are not a private creditor, we take a genuine interest in how a country structures its relations with its debtors. For this reason the Fund should take an active part in discussions between creditors and debtors on how this code should be worked out. And once the code is fairly accepted, I think there is probably a role for the Fund or the World Bank in monitoring compliance with it. This could even evolve into a ROSC, but it is too early to decide. We will come back to that issue later on.

My main point when I spoke just now was that I do not think the report accurately reflects the agreement or the sense of the Board, during the meeting cited by Mr. Portugal, with respect to desirable CACs. Nor am I completely reassured by the reply of Mr. Bertuch-Samuels, who said they will look again at the drafting of paragraph 8. I would like to see the new draft before this paper is

published. I seek reassurance that this paragraph will be drafted so as to avoid giving the impression that the Board favors New York law or New York practice over the law and practice in London. I think it does give that impression now. It conveys a clear sense that the New York practice is superior.

Now, I observe that the July 8 guidance note for the staff, which was not published and was not discussed, has the same flaws. Paragraph 5 of the guidance note to staff contains almost the same wording that is found in the paragraph 8 of the progress report. For instance, it informs the staff is informed that the Executive Board encouraged the use of those CACs in New York. It does not say that the Board encouraged using these CACs all over the world. It says in New York. Those that have been used after the first issue, those are encouraged. But note that this is not what we encouraged. We said only that this is reasonable. We expressed a view as to whether this was a clause that would achieve the objectives of these clauses, namely reasonable coordination among creditors, but that was all. Accordingly I also think we should also redraft paragraph 5 of the guidance note. I am seeking, now, a response to my concern from the staff. This is why Board meetings are useful.

I had a second point, which is that the Fund should not shy away from pointing out that some of the practices that we see emerging not only risk failing to achieve the objectives of CACs. We have now seen the emergence of majority thresholds that are higher than the Board considered reasonable, to wit higher than 75 percent. I now ask the Board if we should not point out, when examining market practices, the risk that excessively high thresholds will impede the restructurings that are the objective of CACs. This is a progress report, but in a progress report we can comment on developments that we observe in the markets.

When I suggested redrafting, it is to ensure that it is made clear that the Board is pointing out the risks of certain very high thresholds, and not the risk that coordination among creditors during the restructuring process will be more difficult, that is what I want to obtain.

Now, Mr. Portugal asks where it is written that the Board has ever expressed a view on the threshold? Well, I see in the summings up that we are all the time referring to 75 percent. That was also the recommendation of the G-10. I do not mean to say that we should explicitly say that 76 is too high, but we can point out in a carefully drafted way that setting excessively high majority thresholds creates a risk, and I think that Mr. Kruger was the first to report on this problem.

Ms. Wolff-Hamacher made the following statement:

Like other speakers, we welcome the progress report on crisis resolution. I have only a few brief observations.

First, we particularly like the detailed discussion on the pricing of bonds with collective action clauses (CACs) issued under New York law in Box 1. It is encouraging that there is no evidence of a huge premium for bonds with CACs thus far. We support Mr. Brooke's proposal to include this discussion in the GFSR.

Second, we appreciate the clarification in footnote 5 on page 7 regarding the validity of CACs under German law. It is true that legislation is being prepared to dispel any remaining doubts on this question.

Third, like other chairs, we support the Fund's proactive role in promoting the use of CACs. In particular, we welcome the active dialogue of staff with emerging market issuers that have so far not included CACs in their international bond issues. I would like to join Mr. Duquesne in saying that we would like to see the G-10 recommendations adopted as a reference. I also agree with Mr. Duquesne's remarks on the voluntary and prescriptive nature of the Code of Conduct.

Fourth, we recognize that the discussion on the Code of Conduct is still ongoing. We feel there is already broad consensus that in post-default cases there should be a strong presumption that as a rule the debtor country would enter into formal negotiations with its creditors rather than just conducting informal consultations. The rationale for this would be the general requirement for a debtor country to negotiate in good faith. This still leaves room for possible exceptions where, under intense time pressure, informal consultations might be followed by an exchange offer. I also join Mr. Egilsson in his remarks on the code and surveillance by the Fund.

Finally, Mr. Egilsson made a valid point on the issue of the SDRM, and I also would like to associate myself with Messrs. Cho and Padoan on the need for ongoing efforts in this area.

Mr. Zurbrügg made the following statement:

I thank the staff for the concise report. I personally would have liked to see a somewhat more beefed-up report, especially on crisis resolution issues, as mentioned by other Directors. A discussion on the aggregation paper would have rounded off the progress report quite nicely in terms of giving at least a token indication that work on this area has not totally come to a halt. In any case, I look forward to the paper on aggregation, which will certainly be reflected in our next progress report.

Only two comments on collective action clauses (CACs). The presentation of the welcome progress made in the use of CACs will be of great interest to ministers and it is appropriate. The staff should focus going forward on how the specific implementation of these CACs in the various

jurisdictions and cases will pan out, particularly in terms of how they relate to what has already been defined as best practices and possible negative developments should CACs deviate too strongly from these.

In terms of Code of Conduct, the report adequately reflects the many still open questions. I noted that the Fund has taken a hands-off role in terms of being solely an observer, and this should continue to be the case.

Mr. Ge made the following statement:

We thank the staff for the concise paper. It is encouraging that the Fund's work in promoting orderly and predictable sovereign debt restructuring has finally led to the broader use of collective action clauses (CACs). The rapid progress in their use has so far not caused risk premiums to rise. Meanwhile, the private sector has been developing a Code of Conduct to facilitate the restructuring of debt. In general, we welcome these developments and will comment on the following issues for emphasis:

First, the contractual approach is a decentralized and market-based method toward debt restructuring. Hence, it must be adopted on a voluntary basis. Debtors and creditors will jointly decide the timing and format of its use. The IFIs, however, should not promote the use of CACs through any formal modality.

Second, the introduction of CACs may involve some changes in legislation in certain countries. In this vein, the best method could be to provide technical assistance and, as indicated by Ms. Indrawati, educate the market. This process may still take some time.

Third, we note the attempts to develop Codes of Conduct. In this area, we share the view that all international bond issuers are encouraged to participate in the discussions. The Fund, however, should not establish any formal mechanism to monitor compliance.

Mr. Ngumbullu made the following statement:

We also thank the staff for the good progress report. At this stage of the discussion, we welcome the work done on both collective action clauses (CACs) and the Code of Conduct. My authorities are fully supportive of the inclusion of CACs in bond contracts, and South Africa in our constituency has already included these clauses in their recent bonds contracts.

Finally, like others, we believe that the Code of Conduct should be market driven and, as a result of that, voluntary.

The Director of the Policy Development and Review Department (Mr. Geithner), in response to questions from Directors, made the following statement:

First, let me acknowledge that this paper provides a rather limited treatment of the broad range of initiatives underway to help improve the framework for crisis prevention and resolution. We welcome the admonitions from the Board to continue work on those initiatives, and we are committed to continuing to explore the appropriate level of self-insurance by countries, the definition of a prudent debt level, the path of policies consistent with sustainability, and the role of Fund surveillance, Fund programs and Fund facilities in general in helping countries deal with those challenges.

Second, we regard the progress on the adoption of collective action clauses (CACs) as very promising, despite the fact that we are still not at the point where all issuers in all jurisdictions are using CACs and despite the fact that we do not have, and may not expect, complete convergence in the standard of clauses that come to pass across all jurisdictions. It is important to acknowledge, though, that it will take some time before the full stock of outstanding external law claims on sovereigns held by the private sector will be populated by such clauses, and it is also important to acknowledge that we have not yet had a test, and we probably will not have a test for sometime, of the impact of these products on how members deal with a restructuring.

Third, let me say a few things on the code. First, there have been no significant new developments since the progress report was drafted, except for the informal consultations among a limited number of actors since the July 25 meeting that Mr. Duquesne referred to. It is unlikely that there is going to be anything concrete, even an indicative proposal, before the 2003 Annual Meetings in Dubai. It is therefore unlikely that we will come back to the Board with any factual update or the basis for a substantive discussion until after those meetings.

We do not envision at this stage a monitoring role for the Fund. If a code is developed and has broad support among issuers and investors, then we will have to consider the potential implications of that code for the Fund and for how we think about applying, interpreting, and potentially modifying our policies. Therefore, the code will not be irrelevant for the Fund, it will be quite relevant in terms how we approach a number of policy issues, but we have not at this point envisioned a formal role for the Fund in monitoring adherence to the code.

I do not believe that there is a contradiction between describing the code as prescriptive and as voluntary. Nevertheless, I am open to suggestions on how we can be as careful as possible in how we frame the language in these reports. This is a semantic issue, as every code has some degree of

prescriptiveness to it, even when it is completely voluntary, but we will consider Mr. Portugal's suggestion to use the word "concrete" in the report.

It is important to say that, in the absence of a broad consensus on the elements of the code at this stage, issuers should not wait before making further progress in improving investor relations programs. This will include improving the broad quality of disclosure; designing and applying in the context of restructurings a framework for broad-based consultations among creditors, including consideration of the merits of various approaches, like credit committees; and resolving a set of complicated issues related to inter-creditor equity concerns. It is important to underscore the fact that, as this process of trying to develop a broad consensus among issuers and investors on a code continues, the world should not wait for that consensus to exist before making progress with any improvements that can be introduced at this stage.

Mr. Kiekens used the analogy of an orchestra for discussions on the code. Building on this analogy, I would say that the Fund is not really part of this orchestra in the same sense that other participants are, but we are certainly not simply sitting in the audience. We are trying to hide behind the more general euphemism that we are participating as an observer, watching carefully, being supportive and constructive, but of course not indifferent to the evolution of the code.

Mr. Kruger asked about the lessons that can be learned from developments in Argentina to date. Looking at the causes of the delay since Argentina went into default, it is hard to attribute the delay to the existence of litigation, the complications in dealing with the quite formidable degree of intercreditor equity issues, or to other issues involved in designing the restructuring strategy. We will not have a test of this until Argentina has put in place a medium-term framework that provides the basis for beginning a more substantive process of discussions with creditors on the restructuring framework. At that point we will be able to say more about any lessons learned.

We have had discussions with the World Bank about the merits of including CACs in a broader array of their debt issues, and that issue is now under consideration internally in the Bank, but the Bank has nothing more to offer in terms of news on the status of those discussions at this stage.

Regarding the drafting suggestions made by Directors, we will look at them, including on paragraph 8, to make sure that the language is consistent with past summings up.

In terms of next steps, the paper on aggregation issues will be circulated to the Board as soon as it is completed and we would hope to discuss the paper after the Dubai 2003 Annual Meetings. We will come back

to the Board at the appropriate time to have a substantive discussion about the content of the Code of Conduct and its implications for the Fund. We are looking at a range of other issues that relate to the difficult substantive questions that countries face in designing economic policies in the face of restructuring, including how to address challenges in the banking sector and how to design the fiscal path. We are committed to advance the debate on how to improve the broader framework for crisis resolution. There are additional issues worth exploring in more detail and we are completely open to come back to the Board and provide a basis for that discussion.

The staff representative from the International Capital Markets Department (Mr. Bertuch-Samuels), in response to questions from Directors, made the following statement:

I would like to address two main questions. First, the reception given by markets to collective action clauses (CACs) and, second, the issue of standardization. At the end I would like to make one forward-looking comment on the use of CACs.

On market reception, we have been in intensive contact with capital market participants between the IMFC Spring Meetings and the summer recess, and it was striking how virtually everybody clearly confirmed that they expected CACs to be here to stay, both for so-called investment grade issuers and for noninvestment grade issuers.

Mr. Lushin asked a more specific question on the case of Korea and whether the scarcity of Korean debt instruments dominated investor assessments of the recent issue of bonds with CACs. That certainly played a role, as this was the first issue after a considerable time, but there were also no CAC-related market comments or questions in the cases of Belize and Guatemala, for example, so we think the good market reception of bonds with CACs really is a reflection of the tide having turned. It remains to be seen whether we are yet at the point, as Mr. Cho said, to declare victory. The real test may come when the international capital markets environment turns less favorable. But, at this time, the picture is certainly encouraging. Issuers were surely given advice by their financial and legal advisors to also look at the investor base they are targeting and take into account their particular circumstances, but the general acceptance of bonds with CACs indicates that they are becoming a market standard.

There was another specific question on the lack of market comments on bond issues with CACs by Egypt, Lebanon, and Qatar in 2000 and 2001. There is a widely held view that the increased use of CACs is sort of a by-product of renewed discussions in this area triggered by the Fund's Sovereign Debt Restructuring Mechanism (SDRM) initiative. The flip side of that coin is that before the discussion was prominent there was not much attention paid to

the use of CACs, and it simply did not register market commentary that a country like Qatar or Egypt came to the market with CACs because there was really no intensive, public discussion of these issues.

Turning to the issue of standardization, Mr. Portugal has reminded us that there was considerable consensus at a previous Board discussion that it is too early for the Fund to be seen as pushing one particular set of CACs, as the contractual and voluntary nature of such clauses means that it should ultimately be left up to the issuer to decide the terms of its bonds. We will revise the language in paragraph 8 to fully reflect the outcome of that Board discussion on CACs.

Regarding Mr. Egilsson's question, the use of various types of CACs in different issues of a single country does not seem to be a concern at the moment. Brazil, for example, has issued four bonds successively with the same type of CACs. A problem may arise when different bonds are issued under different laws, for example London versus New York law. We do not have any practical evidence to assess at this moment how complicated the use of different CACs under different laws would make the process of restructuring. One interesting case was Uruguay, where most of the bonds did not have CACs, but part of the bonds, those issued under Japanese law, did have CACs. The end result was positive, as it was possible to restructure Uruguay's debt with a high participation rate of over 90 percent. That is all we can say at this stage, anything else would be highly speculative.

I tend to agree with Mr. Yagi's point that we should continue with our outreach efforts, encouraging countries to include CACs in their bonds. That is where we want to focus our main attention, rather than pushing strongly for standardization at this point. This does not mean that we do not have an idea of what terms are reasonable for the clauses, as described in the summing up of the last Board discussion on CACs. This can also be seen in the guidance note to the staff on CACs, which provides a basis for the Fund's outreach activities.

In terms of why some countries have not issued bonds with CACs yet, we have been in touch with debt management representatives of different countries, and each one of them showed strong commitment and interest in using CACs. However, when we talked to some of them at the time of the Spring Meetings, there was also an undertone of concern about taking a pioneer role in this area, and they would like to see developments continue for a little longer before taking the next step. In this context, their preference has been to reopen old issues or, when the investor base they targeted was not, for example, mainly institutional investors in the United States, to issue out of London. In a few cases, because of uncertainties about potential success or non-success of the issue, a few countries in the end decided not to use CACs

when they issued in New York. We were proactive discussing with these countries, but in the end it was up to the country to decide what to do.

Finally, looking forward, there is an important point to make that despite the uptick in interest rates in the United States, the environment for emerging market debt as an asset class is still relatively favorable. We still have rather low spreads and yields compared to five-year averages. In this context, we would encourage—not only from the point of view of using CACs but also from the point of view of proactively managing their liabilities—member countries to use the opportunities provided by the current environment to conduct debt management operations to prefinance their needs and improve the structure of their debt.

Mr. Beauregard asked the staff representative about the possibility that countries that did not include CACs in their bonds could end up having to pay a premium.

The staff representative from the International Capital Markets Department (Mr. Bertuch-Samuels) responded that, based on conversations with market participants, there were already some comments about countries having some explaining to do if they came to the market without CACs. Nevertheless, it was still early to reach any conclusions and further monitoring and analysis of country experiences would be needed.

Mr. Egilsson considered that it would be important to develop fairly quickly best practices for the design of CACs, as difficulties could arise from the use by the same country of different clauses in different bond issues.

The staff representative from the International Capital Markets Department (Mr. Bertuch-Samuels) clarified that the staff was not refraining from taking a proactive approach in discussions about the design of CACs. ICM and the Legal Department had made considerable efforts in briefing representatives from member countries on what were considered to be best practice for the design of CACs. However, and based on the Summing Up of the last Board discussion on CACs, the final decision on the specific design of those closes was for each member country to make.

Ms. Jacklin did not share Mr. Egilsson's concerns about differences in the majority voting thresholds in CACs under different jurisdictions. In fact, requiring a standard threshold across jurisdictions could lead to the highest threshold being adopted if such a standard were to be acceptable to all jurisdictions. Aggregation across bond issues should also not necessarily be a concern, as bond issues should be looked at individually with their own rules. In the corporate world, it was common for the same company to issue bonds with different clauses depending on the investors targeted in each case. Majority voting thresholds often varied even under the same jurisdiction, including under London law. The fact that corporations were able to deal with restructurings and reschedulings without a significant level of confusion despite the lack of uniformity indicated that uniformity should not be such a big concern. Issuers should focus on improving their knowledge of their investor base through good data and tracking systems, and the lack of uniformity in the market, even with

respect to bonds issued by a single country, should not be seen as essential to allow CACs to play a significant role in substantially improving the current framework for sovereign debt restructurings.

Mr. Portugal agreed with Ms. Jacklin on the desirability of avoiding the imposition of standardization requirement for the design of CACs, as different market preferences should be reflected in those clauses. In any case, the current Board discussion should focus on assessing whether the progress report to the ministers adequately reflected the progress made and the understandings reached by the Board thus far in the area of crisis resolution. This was not the adequate time to discuss the different views on the need for more or less standardization, or on the need for the Fund to be more or less involved in this area. Using language from the summing up of the relevant Board discussions would be the best way to ensure that the progress report reflected the substance of those discussions. In particular, most Directors had noted at the time of the last Board discussion on CACs that it was too early to reach a definitive view on the degree of standardization required in terms of the design of CACs, and that the Fund should not endorse or promote any single set of models of clauses.

Mr. Kiekens considered that the progress report did not accurately reflect the sense of the Board discussion on CACs to which Mr. Portugal was referring to. He requested seeing the revised drafting of paragraph 8 before the publication of the progress report. The paragraph should be drafted in such a way that there could be no perception that the Board favored the practice under New York law over the practice under London law, as that was not the sense of the Board. Paragraph 5 of the guidance note for the staff issued on July 8, 2003, which had not been published, had the same flaws as the current draft of paragraph 8 of the progress report. The staff was informed in that note that the Board encouraged the use of CACs under New York law. The Board's view was that these clauses were acceptable, but not that they should be encouraged over those under other laws. Therefore, the language in the guidance note should also be revised in line with the requested revision for paragraph 8 of the progress report.

Mr. Padoan considered that the Board was not in a position to endorse a particular clause at this stage. It should be clear in the progress report that the Fund was not endorsing any particular clause when encouraging the use of CACs, and Mr. Kiekens was right in requesting careful redrafting of paragraph 8 to dispel any ideas in that respect.

Mr. Kiekens stressed that the Fund should not shy away from pointing out when some of the emerging practices were seen as failing to achieve the objectives of CACs. It would be appropriate to inform in the progress report on the Board's concern regarding market trends like the use in recent bond issues of majority thresholds above the 75 percent threshold judged by the Board as reasonable to achieve the objectives of CACs.

Mr. Portugal observed that the Board had not expressed a view that a majority threshold of 85 percent would be excessively high. The summing up of the relevant discussion stated that it was too early to decide on the specific design of CACs, and that the

Board should not endorse any single model at this stage. In addition, Mr. Reddy had made a similar point in his preliminary statement.

Mr. Egilsson considered that it would be entirely appropriate to comment in the progress report on the views of the Board regarding recent developments in the use of CACs and whether these were considered to represent progress in the right direction or not. In any case, the adoption of best practices would not imply a need for total convergence on a single set of clauses, as a range of options could be incorporated as best practices.

Mr. Kiekens indicated that the Board had referred in the last discussion on CACs to 75 percent as a desirable majority threshold, as could be seen in the summing up of that discussion, and that had also been the recommendation of the G-10. The progress report could be drafted in a way that the concerns of the Board regarding the risks posed by excessively high majority thresholds could be made explicit. Mr. Kruger had also referred to this issue in his statement.

Mr. Duquesne agreed with Mr. Egilsson that the discussion on CACs was evolving and that the progress report should not necessarily repeat the view that the Board had already expressed in a discussion held several months earlier. It should be possible to reflect in the progress report the satisfaction of the Board with the progress made in some cases, including the case of Uruguay, and the concerns regarding the use of high thresholds in certain other cases.

The Acting Chair (Ms. Krueger) encouraged the staff to come up with some wording to appropriately reflect the views of Directors on the issue of majority thresholds used in recent bond issues.

The staff representative from the Legal Department (Mr. Hagan), in response to questions from Directors, made the following statement:

Without going into specific drafting suggestions at this stage, let me respond to some of the substantive questions on the design of CACs. Clearly, we should not look at any single feature of collective action clauses (CACs) in isolation when considering the optimal design of CACs. We need to look at how provisions interact with each other and also at the market in which bonds are being issued. From that broader perspective, dealing first with the majority restructuring provision that allows for the amendment of key terms, the question is to what extent there is a significant risk that moving from a 75 to an 85 majority voting threshold would increase the leverage of holdouts and therefore undermine the restructuring process. The answer to that question is that the degree of risk depends on how that threshold is calculated. Is it based on the outstanding principal or is it based upon the claims of bondholders present at a duly convened meeting? This is important because if the threshold is based on the outstanding principal, a non-vote—in other words a retail investor who did not open his mail because he was on vacation—ends up becoming an unconscious holdout. It is for that reason that in the G-10

recommendations it was specifically stated that if the threshold is based on an outstanding principal approach, it is important not to set a threshold that is higher than 75 percent. The Board has expressed a positive view of the G-10 recommendations, even if no exclusive standard or model has been endorsed because we are still going through a transitional process. The degree of risk also depends on the market targeted by the issuer. If bonds are issued to retail investors, an 85 percent voting threshold based on the outstanding principal amount is more risky than if those bonds were issued to institutional investors.

On the majority enforcement provision, and specifically the point raised by Mr. Shaalan, the staff is less concerned about existing variations between 50 percent and 66 2/3 percent in the threshold for the reversal of acceleration, partly because that is within the norm that has evolved in the market and which has proven to be successful in restructurings, including in the case of Ecuador. This is not consistent with the proposals of the Institute of International Finance and the Emerging Markets Creditors Association which recommend a 75 percent threshold. Perhaps a more important provision is the use of a trust structure. In this regard, as Mr. Brooke has said, the most significant development is Uruguay's use of a trust indenture because the trust structure is a much more powerful weapon to deal with holdouts prior to a restructuring than a reversal of acceleration.

On German legislation, Ms. Wolff-Hamacher has already responded to Ms. Jacklin's question.

On the question of corporate bonds, this is an intriguing issue. The first point to make is that in many countries corporate bonds do not include CACs because restructurings take place in the context of the insolvency law. In the United States, for example, the Trust Indenture Act precludes the use of such clauses and restructurings have to take place under the insolvency law. In countries where such clauses are allowed, for example in the United Kingdom, our understanding based on a survey is that they have used the quorum approach.

Turning to the question on litigation raised by Mr. Kruger, there has been litigation in both the United States and in Europe, and it is fair to say that Argentina has had mixed success in defending those cases. Most of the litigation has been initiated by distressed debt purchasers or retail investors. Large institutional investors seem to have adopted a wait and see approach and they have generally not sought recourse to the courts thus far. In the United States there have been summary judgments in favor of three individual plaintiffs, but these are relatively small claims. Perhaps more troubling is a claim by a holder of \$700 millions in bonds that is pending in front of the same court. We are awaiting the decision by the New York court on that one. Additionally, two class actions have been filed in New York, one representing bonds worth \$30 billion. Fortunately for Argentina, in both cases the court has

decided not to certify those as class actions because they would be unmanageable. We understand, however, that one of the class actions has been filed again with a smaller class. There are also about 30 lawsuits pending in Germany, but we do not think that they have been successful in attaching any assets yet.

Going forward, it is difficult to predict what the strategies of bondholders will be, but based on patterns to date there is a risk that creditors will seek to obtain a judgment because they have a certain degree of seniority in the restructuring process. That means that those creditors will be immune in Argentina from the use of any contractual provisions, whether it be exit consents or CACs, because they do not bind judgment creditors. That is one of the limitations of the contractual approach. Secondly, looking at the litigation strategies used to date in other contexts, given the difficulty of attaching assets of a sovereign, one of the strategies has been to use as a form of blackmail judgments to get an injunction which precludes the debtor from paying other creditors. That is one potential strategy.

Ms. Jacklin observed that the lawsuits filed in the case of Argentina probably had a lot to do with the failure of the authorities to hold bona fide discussions with creditors—she referred to these as “is-anybody-home?” lawsuits. It was certainly appropriate by any standard of good conduct for creditors to try to enforce their private contracts with sovereign issuers. Nevertheless, the favorable resolution of some of the class action precedent issues was a welcome development for a smooth restructuring of debt.

Mr. Kruger asked the staff to clarify if the current situation was that judgments had been made against Argentina, but that no assets had been attached thus far.

The staff representative from the Legal Department (Mr. Hagan) confirmed that that was the case.

Mr. Kruger also asked if the staff would agree with Mr. Kiekens’s point that a CAC based on 85 percent of outstanding principal presented a higher risk that debt would not be successfully renegotiated.

The staff representative from the Legal Department (Mr. Hagan) confirmed that that was the view of the staff. The risk posed by higher majority thresholds based on the outstanding principal amount had been admirably put in the G-10 report on CACs. The question was whether the staff and the Board were in a position to mandate a particular threshold of 75 percent at this stage.

The Acting Chair (Ms. Krueger) proposed the publication of the paper taking into account the revisions in light of the current Board discussion and following its circulation to members of the IMFC.

2. EXECUTIVE DIRECTOR

The Acting Chair bade farewell to Mr. Yaga V. Reddy on the completion of his service as Executive Director for Bangladesh, Bhutan, India, and Sri Lanka.

Length: 15 minutes

3. POVERTY REDUCTION STRATEGY PAPERS—PROGRESS IN IMPLEMENTATION; INITIATIVE FOR HEAVILY INDEBTED POOR COUNTRIES—STATUS OF IMPLEMENTATION; AND PRGF TRUST AND PRGF-HIPC TRUST—RESERVE ACCOUNT—REVIEW

Documents: Poverty Reduction Strategy Papers—Progress in Implementation (SM/03/279, 8/8/03; and Sup. 1, 8/8/03); Initiative for Heavily Indebted Poor Countries—Status of Implementation (SM/03/294, 8/18/03); Update on the Financing of PRGF and HIPC Operations and the Subsidization of Post-Conflict Emergency Assistance (SM/03/296, 8/19/03); Enhanced Initiative for Heavily Indebted Poor Countries—Considerations Regarding the Calculation of Additional Debt Relief at the Completion Point (SM/03/295, 8/18/03); and Statement by the Staff Representative on the Enhanced HIPC Initiative—Considerations Regarding the Calculation of Additional Debt Relief at the Completion Point (BUFF/03/160, Rev. 2, 9/2/03)

Staff: Mark Allen and Wang, PDR; Lin, FIN

Length: 1 hour, 40 minutes

The Deputy Director of the Policy Development and Review Department (Mr. Allen) submitted the following statement:

The joint Bank-Fund paper on the calculation of completion point topping up for the Initiative for Heavily Indebted Poor Countries (SM/03/295, 8/18/03), which has been circulated for the information of the Executive Directors, was prepared at the request of the Executive Directors. It updates the cost estimates for topping up under the current methodology and also for two alternative methodologies—excluding additional bilateral assistance from the topping-up calculations and excluding new borrowing from such calculations at the decision point.

Directors also requested that the staff prepare estimates of the financing costs associated with the alternative topping-up methodologies. For the Fund, the available resources are estimated to be sufficient to cover the cost of subsidizing PRGF lending through end-2005 and of the Fund's participation in the enhanced HIPC Initiative. Current projections would also indicate that available resources could fully cover the Fund's share of potential topping-up HIPC assistance of about US\$61 million under the

current methodology. The cost associated with Alternative Methodology I is substantially higher, and could not be accommodated without risk to financing of PRGF and HIPC operations within currently available resources. The financing issues are discussed in detail in Update on the Financing of PRGF and HIPC Operations and the Subsidization of Post-Conflict Emergency Assistance (SM/03/296, 8/19/03).”

The staff is not in a position to provide information on the financing implications for the World Bank.

Mr. Padoan and Mr. Lombardi submitted the following statement:

Key Points

Progress continues to be made, though significant challenges remain.

However, governance requirements remain an essential feature for achieving the objectives envisaged through the Initiative.

We welcome the additionality of debt-relief with respect to other forms of external financial assistance.

On the financing aspects, we insist towards the objective of full creditor participation.

Such an objective becomes even more relevant in light of the increasing costs should other countries be entering the Initiative and in relation to the financial implications arising from a possible change in the methodology for topping up.

On this last issue, we look forward to starting a discussion on the costs but also on benefits related to a change in the methodology, though we recognize that it should not be seen as a substitute to a fairer burden-sharing.

Introduction

We strongly welcome the opportunity for reviewing progress with the HIPC Initiative and the PRSP approach and want to thank Staff for producing a set of very informative papers. We shall comment on the following aspects.

The HIPC Initiative

The review delivers the message that progress continues to be made, though significant challenges remain. As pointed out in the main Report, poverty-reducing expenditures in the 27 countries that have reached the decision point are expected to grow at US\$11.9 billion in 2005 from 6.1

billion in 1999. Debt stocks in those same countries are projected to decline by about two-thirds, once they will graduate from the Initiative.

On the other hand, out of the 38 potentially-eligible countries, 11 of them have been still unable to join the Initiative. Of the 19 countries that are in the interim period between the decision and the completion point, only 10 have exhibited a satisfactory performance record in their macroeconomic programs. From September 2002, the time when the latest review took place, only one country has passed the decision point and two more have graduated from the Initiative.

Despite the challenges, we believe that the governance requirements remain an essential feature in the HIPC framework. Attaining macroeconomic stability, strengthening public expenditures management, satisfactorily implementing PRSPs as well as meeting other social and structural completion point triggers remain critical, in our view, for achieving the objectives envisaged through the Initiative. In addition to the already enormous efforts made by Staffs in the implementation of the Initiative, a more proactive approach aimed at further prioritizing technical assistance and at gaining more knowledge on the political economy constraints would help. This could be particularly important for the 11 countries that still strive to reach the decision point. Staff comments would be welcome.

On additionality, we welcome the findings that so far debt-relief provided through the HIPC Initiative has been additional to other forms of external financing assistance—additionality being a key pillar underlying the whole Initiative. However, from the Staff Report we are unable to ascertain whether such additionality might have come at the expense of flows previously channeled to other non-HIPC low-income economies. Staff may wish to comment on this remark.

Financing Issues of the HIPC Initiative

On creditors' participation, we note that some progress has been achieved. In particular, we welcome the decisions by the Libyan authorities to join the Initiative as well as that by the Indian government to write off all the claims to HIPCs. However, our aim is to achieve full creditor participation and, in this regard, actions should be taken against non-compliant creditors along the lines of the discussion we had last March. In this respect, we encourage the Staff to keep exploring all the available options, along the lines already discussed and even bringing the issue of HIPC Initiative participation at the core of bilateral relationship with non-compliant countries.

The objective of full creditor participation is even more important in light of the financing challenges related to a possible change in the methodology for computing topping up and the costs for new countries that

might be entering the Initiative shortly. Regarding the former, we welcome the updated estimates provided by Staffs on the costs related to the change of methodology for computing the topping up (Alternative Methodology I). While we recognize that the concerns raised by Staffs on the financial implications for multilateral creditors are well-grounded, they should not lead, however, to an early dismissal of the discussion. First of all, we should keep in mind that topping up will be granted only under exceptional circumstances. The Staff's exercise assumes instead that all countries with debt above the thresholds will receive the topping up. Furthermore, the Staff's assessment does show increased benefits for the HIPC's in terms of greater poverty-reducing expenditures and sounder debt sustainability. Importantly, on equity grounds, we reiterate our concern that the methodology for computing topping up should not compensate for the aid allocation decisions by the bilateral donors, but should instead remain neutral with respect to those choices. To sum up, we see relevant reasons for discussing the change of methodology, though we recognize that it should not be seen as a substitute to a fairer burden-sharing.

The PRSP Approach

The PRSP approach has gained widespread support and it is providing overall a comprehensive framework for the formulation of country-owned development strategies and for operationalizing the objectives envisaged through the MDGs. In this respect, PRSPs are becoming the encompassing framework for ensuring consistency between—and increasing the effectiveness of—the development of home-grown policies, the actions of the donors and the broader support by the IFIs. In our view, PRSPs are increasingly allowing stakeholders to become familiar with the macroeconomic implications of their own programs and objectives and their inevitable trade-offs. In this regard, however, it is important that the macroeconomic assumptions underpinning PRSPs strike the appropriate balance between realism and ambition.

To strengthen the PRSP framework as the basis for operationalizing the MDGs, further progress needs to be made with respect to integrating the medium-term view embedded in such Papers with the short-term framework of the Budget. Along those lines, it is important to develop a set of intermediate indicators that allow stakeholders to monitor the accomplishment of the objective and—if necessary—to develop alternative strategies.

Mr. Ondo Mañe submitted the following statement:

We thank staff for a comprehensive and informative set of papers. The papers, in particular the one on the PRSP and its supplement contain a wealth of information which raises a wide range of questions. Unfortunately by being part of three other papers, it may not get the attention that it fully deserves. We would, therefore, suggest that we return to the many issues raised in this

paper after the Annual Meetings. The paper describes critical strengths and weaknesses in the PRSP, and a fuller Board discussion on these issues can contribute much to further improvement of the PRSP process.

On the HIPC Initiative, we would like to draw attention to the fact that it is contributing to a significant increase in social expenditure, including the building of social-related expenditures. However, these new schools and hospitals, among others, will give rise to recurrent maintenance expenditure as well as future replacement expenditure, which are not taken into consideration in PRSPs. We think that it is an issue that needs to be adequately analyzed in future documents.

PRSP—Progress in Implementation

Overall, the PRSP process is progressing well. An important outcome of this exercise is that government ownership of the poverty reduction strategy is strengthening. However there is a need to improve that ownership within the government by integrating those departments or units that are still left aside of the process and whose contribution will be helpful.

On the broadening of the participatory process to other groups, while welcoming it as a step towards building consensus, an attempt to elaborate a PRSP satisfying all parties can become cumbersome, as it may lead to an excessive number of proposals. Thus, there is a need to strike a balance. We are of the view that it is the responsibility of the government to design the macroeconomic framework and to ensure that it is consistent with the objectives or the indications contained in the PRSP. On the other hand, Parliament, civil society and NGOs should play their respective roles to ensure that the PRSP is well implemented.

We note a recurring contradiction between on one hand requesting PRSPs to define credible policies to make progress towards the MDGs and on the other hand requesting further realism of macroeconomic projections. The macroeconomic framework contained in the PRSPs generally result from the policies retained to meet the MDGs over time. However, the PRSP implementation experience so far shows that lack of financing lead the national authorities to revise downward the growth projections, endangering the objectives of meeting MDGs by 2015 and hence slowing down the pace of poverty reduction. In such circumstances, how realistic is it to ask for an alignment of PRSPs with MDGs?

We also note the following points which we think deserve more attention in PRSPs: a better assessment of fiscal policy choices in relation to debt sustainability; a better analysis of sources of growth as well as factors that constrain growth; a more thorough and in-depth analysis of trade policy issues which include the risks and costs that the country faces as it proceeds to

liberalize its trade regime, as well as the costs on its economy of other countries' trade policies; a comprehensive analysis of the "taxable base", so that the sources of domestic revenue are well understood, thus helping in the design of fiscal policies; more attention to institution building.

In light of lower than committed external financial assistance, there is a clear need of prioritization; prioritization of objectives, and of policies and reforms needed to meet them. Among priorities, linking the budget processes and MTEFs to, and integrating PEM reforms in, PRSs are essential. We are pleased to note that many HIPC are improving their PEM systems. We think that this will further strengthen predictability and alignment of external financing. On that latter issue, we note that the donors' community is improving their assistance framework in order to harmonize their procedures and review their requirements with the domestically-owned PRS content and budget cycles.

HIPC—Status of Implementation

Progress in the implementation of HIPC Initiative has been slow since our last discussion on the issue, with only one additional country reaching the decision point and two others reaching the completion point—all of them from our constituency.

In the countries yet to reach the decisions point, domestic conflicts and protracted arrears have been the main impediments to move forward to this stage. Nevertheless, in the case of our constituency we should state that appreciable progress towards resolving conflicts has been made with the involvement of the African Union and multilateral intervention. We also welcome donors' efforts to solve the issue of protracted arrears in many HIPCs.

The countries that have already reached the decision point are taking longer than expected to advance to the completion point due to delays in meeting the completion point triggers. We are pleased to note that several countries are taking the necessary measures to address those problems that are related mostly to the achievement of macroeconomic stability and the preparation and implementation of the PRS. The non-achievement of macroeconomic policy as evidenced by the disruption in the implementation of a PRGF-supported program is a matter of concern. In a sense, we think that the initiative is flexible enough to help interim countries that experience delays in the implementation of their PRGF programs to bring the macroeconomic programs back on track. However, we wonder whether the design and the content of the programs could also explain those disruptions and becoming impediments to get the countries back on track. We hope that the forthcoming IEO report on the PRGF arrangements could provide an answer and some recommendations on that issue. Many decision point

countries are also experiencing delays in the preparation of PRSPs due to domestic capacity constraints faced by the authorities.

We think that the emphasis of HIPC Initiative on governance issue through the PRSP process and other conditionality in Bank- and Fund-supported programs is appropriate. The report shows that there is progress in the implementation of good practices, in particular in the public finance management. Given the weak capacity, well-targeted technical assistance will be still needed from the international community to continue sustaining national authorities' efforts.

As already noted in our previous statements, long-term debt sustainability remains a concern, as heavy dependence on primary commodities renders virtually all HIPCs vulnerable to changing prices in the world commodity market as well as to changing in weather conditions. We are of the view that DSA framework should take better account of all exogenous shocks.

We note from staff projections that overall debt indicators for HIPCs will improve after enhanced HIPC relief at the completion point compared with the developing non-HIPCs. So far, debt relief provided has enabled an increase in poverty-related spending in countries that have reached the decision and completion points. However, as we noted above, there is an absence of an estimate of recurrent costs implications for the medium- to long-term which could be a source of fiscal unsustainability.

While we welcome the increasing participation of HIPCs creditors to the initiative, we are concerned by the litigation outcomes. Indeed, in some cases, judgments for creditors have ordered settlements higher than what the debt relief would have been. We would like to reiterate our request for technical legal assistance to help those countries facing litigation. We encourage the Fund and the Bank to continue assisting HIPCs in their discussions with their creditors and help to reach an agreement with them, in order to avoid resorting to the courts. On this issue, could staff comment if any progress has been made in terms of reducing the number of litigations, over the past year?

Enhanced HIPC Initiative – Considerations Regarding the Calculation of Additional Debt Relief at the Completion Point

As regards the issue of the calculation of the topping up in the context of the HIPC Initiative, we welcome the comparison between the current methodology and the proposed alternative methodologies as requested in our previous discussion. We note that, under the current methodology, the present projection of the projected NPV of debt above the HIPC thresholds increased by US\$ 162 million due to changes in the environment of one country. That

number could increase by a further US\$ 587 million to US\$ 1,316 million if the exchange and interest rate parameters remain unchanged at the level of end-June 2003. We note that the additional cost to the Fund could be accommodated with available resources.

The Alternative Methodology I, under which additional bilateral assistance is excluded, will increase the NPV of debt above the HIPC thresholds. Considering the observations of the staff for and against such exclusion of additional bilateral assistance, we remain convinced that donors' additional debt relief beyond their commitment under the HIPC framework should not be included in the calculation of the topping up. Under such a methodology, we ensure that each donor bears its share in the topping up. The unilateral action initiated by one donor, adds uncertainty to the delivery of the additional debt relief, hence reinforcing furthermore the need to switch to the Alternative Methodology I. We think that the best way to ensure that no HIPC faces the risk of withdrawal of commitment of an additional debt relief after the completion point is to adopt the Alternative Methodology I. If this methodology is adopted, it should be applied retrospectively to other countries.

However, we note the potential additional cost some multilateral institutions, including the Fund, may face and, accordingly the financial "instability" the corresponding trusts could experience. Since the HIPC Initiative is not intended to be a permanent facility, we believe that the Fund and other institutions should mobilize more financing, in order to mitigate that risk. Moreover, those cost estimates are based on assumptions that are likely to change "favorably" over the next year. While we note that most of the net benefit will be concentrated on 3 countries, we do not think that funding of additional donors contributions would be diverted from the aid flows to the other low-income countries.

Turning to the second proposal, the Alternative Methodology II, under which new borrowings between the decision and the completion point are excluded, we do think that we should apply the case-by-case approach. Indeed, since the HIPC Initiative is intended to improve debt sustainability and prudent debt management, we do not think that excluding new debt that has been prudently contracted from the calculation of the topping up is warranted. We are of the view that the staff should continue to inform the Board on the appropriateness of the new loans to the country. However, some guidelines on the appropriateness of the inclusion or the exclusion of new loans in the calculation will be helpful. Staff comments are welcome.

Update of the Financing of PRGF and HIPC Operations and
Subsidization of Post-Conflict Emergency Assistance

We are pleased to note that the financial situation of PRGF, HIPC and Post-Conflicts Trusts is adequate and we think that their resources are sufficient to carry out their operations over the next six months. We commend the members for their contributions. However, we note that more resources from the international community will be needed to finance expected increase of operations stemming from future Fund participation in the clearance of protracted arrears and in the provision of debt relief under the HIPC Initiative for some African countries. We urge the staff to keep us regularly informed on that matter. We are also looking forward to staff proposals with respect to financing of PRGF lending beyond 2005.

Mr. Reddy submitted the following statement:

We welcome this well written set of four papers which provides a comprehensive review of the progress achieved in the implementation of the PRSP, the status of implementation of the HIPC initiative as well as the update on the financing of the concessional lending window of the Fund. This discussion also provides a useful background to the forthcoming deliberations in the IMFC on promoting growth in low income countries. As the papers indicate, progress in these challenging initiatives since last year's review, has been steady though uneven. Except for issues relating to financing, there appear to be no new developments which warrant a significant change in policy or approach. The principles of the Monterrey Consensus as well as the PRSP approach continue to be valid. What is now required is consolidation of these initiatives through a stronger and more comprehensive implementation by the concerned member countries, accompanied by a greater involvement in the respective country strategies by the donor countries. These papers bring out well the complexities in implementing the PRSPs aimed at reaching the MDGs in the face of budgetary constraints as well as limitations in donor support. Our views on the issues for discussion for each paper are indicated below.

PRSP—Progress in Implementation

We welcome the progress being made in the implementation of the PRSP approach. It is encouraging that there have been positive developments towards enhancing the participatory process, better articulation of macro economic frameworks and prioritization of expenditures aimed at poverty reduction. The staff papers have appropriately identified the continuing issues and challenges.

We agree that the process of formulation of the PRSP is inherently subject to a number of often opposing forces. The final trajectory of the PRSP will thus follow the resultant of these forces – which will be in a unique direction, but biased in the direction of the strongest of these forces. It is in this context that issues relating to participation need to be examined. While

we accept that participation in PRSP formulation should be as broad and deep as possible, it must be recognized that the views of all the participants cannot be given equal weight in deciding policy. Accountability of the participants should be a key issue, and the views of a democratically elected government accountable to its electorate, as well as the policies it wishes to adopt should be given the greatest weight and should form the basis of the PRSP – even if as mentioned in Para 11, some CSOs feel that they should be given a greater role in policy formulation. It is only through implicit recognition of the ‘weights’ of the views of the different stakeholders, as well as using this to decide the policy trajectory can these tensions be resolved while simultaneously preserving the principle of country ownership. We thus agree with staff that national governments are ultimately responsible for deciding and prioritizing among competing demands in the process of PRSP formulation within the budgetary and political constraints.

We recognize that NGOs may have a role to play as suppliers of information as well as watchdogs in monitoring government’s implementation efforts, in countries where public information systems are not fully developed. In such circumstances, NGOs can play a valuable role in enhancing public awareness of policies underlying PRSPs. The integration of Parliaments into PRSP monitoring must however be approached with caution. The Fund, in its interaction with the authorities of its member countries deals with the agency in the executive branch designated for this purpose. This agency is already responsible to the Parliament for all its actions, through the constitutional framework providing for the executive’s accountability to the legislature. Imposing an additional structure onto this arrangement wherein the Parliament will directly monitor implementation of the PRSP may complicate the monitoring process.

The issue of donor alignment and harmonization remains integral to the successful implementation of the PRSP. The fact that country authorities took the lead in donor coordination in only 3 of the 48 PRSP countries studied is therefore a cause for concern, considering that donor driven rather than national priorities may then have dominated the policy agenda. Is there a systemic reason for such a low participation rate? While capacity constraints as well as systems enhancement can be addressed through targeted technical assistance, the larger issue of unifying as well as simplifying donor procedures and processes to reduce the administrative burden on the member country needs to be substantially addressed.

While we support the suggestion in principle that governments could lead the dialogue on macro economic principles in the participatory process, such a process must be subject to the legislative procedures in place for discussing the governments macro economic stance and cannot be subordinated to it. The suggestion made by staff in Para 50 that the IMF Resident Representative should be involved early on as part of the

participatory process in interesting, as such participation could usefully address the shortcomings identified in PRSPs, detailed earlier on in the paper. Since the concerns of the Fund will be then consciously be addressed in the PRSP formulation, and if a World Bank representative is also co-opted into this consultative process; perhaps the JSA procedure can then be dispensed with. As staff note, the present JSA procedure tends to undermine country ownership in selecting and implementing policies and removing this procedure may strengthen ownership, while Bank/Fund concerns are addressed upfront in the PRSP formulation. Further, the inclusion of the Fund representative may introduce an additional 'level' in the already challenging PRSP process, which may need to be mitigated in some way.

Initiative for HIPCs—Status of Implementation

We agree that attaining macro economic stability, satisfactorily implementing PRSPs and meeting the completion point triggers are critical to the realization of the objectives of the HIPC initiative. Nevertheless we are concerned that of the 15 countries listed in Table 3, which have recorded delays in the implementation of PRGF programs, 13 have poor macro economic policy implementation listed as a cause for delay. As staff point out, fiscal policy slippages stemming from either revenue shortfalls or expenditure overruns or both have been a common factor. While exogenous factors could have some role in this, apart from poor ownership of the reform agenda and security considerations, could this also reflect excessive optimism on the part of the staff in deciding upon the magnitude of the fiscal adjustment - an issue which was raised by the IEO in the report discussed by the Board last week? While elimination of the debt overhang and putting in place a sustainable debt burden should remain the objective of the HIPC initiative, this should be based upon pragmatic policy implementation.

Staff seem to point out that all the HIPC countries may not be able to reach the decision point by December 2004—when the sunset clause will come into effect. Admittedly security considerations as well as the need to resolve protracted arrears may delay progress in establishing a track record for some countries. In such an event, would yet another extension of the sunset clause be necessary? Staff comments are welcome.

Footnote 30 defines “governance” as the exercise of economic, political and administrative authority to manage a country’s affairs through formal rules and processes while “public sector governance” is defined as including government administration, civil service, decentralization, tax administration, legal and judicial reform, anti corruption and public expenditure management. We support the emphasis given to the establishment of good public sector governance as part of the HIPC initiative, as this remains fundamental for the effective implementation of the PRSP. Naturally, the primary responsibility for providing this rests with the country authorities,

with the international community assisting the country whenever required. We are less sure about the emphasis on good governance, which staff have identified in the issues for discussion. Agreeing on what is good governance on the basis of the above definition for governance may be a difficult task.

Update on the Financing of the PRGF

We support the decision on Page 13 of document SM/03/296.

We also note that the available resources are adequate to cover the Fund's share of potential topping up HIPC assistance under the current methodology. We feel that if any new methodology for calculating the topping up assistance is to be adopted, it should be ensured that the resource position is not undermined.

Mr. Shaalan and Mr. Bakhache submitted the following statement:

We would like to thank the staff for the extensive updating on the status of implementation of the HIPC Initiative as well as the useful accompanying papers on related subjects. In what follows we will focus our comments on some of the issues presented in the staff papers for discussion.

HIPC: Status of Implementation

The progress made in implementing the HIPC Initiative is welcome as important gains have been achieved in countries that have reached the completion point and those that are still in the process of receiving interim relief. Debt indicators for the 27 HIPCs that have reached the decision point are projected to decline significantly, while poverty-reducing expenditures have already risen by close to 40 percent since 1999. Notwithstanding the wide differences across countries, we are pleased to note that external financial assistance (other than debt relief) to countries that have reached the decision point has also increased in recent years. This implies that at least for good performing countries, debt relief is not substituting for other forms of assistance. We hope the donor community can build on this record and further increase official development assistance to levels consistent with the requirements for making credible progress towards the Millennium Development Goals.

Completion Point

A large number of countries in the interim period are facing difficulties reaching the completion point, most notably because of problems in implementing adjustment and reform programs. It is essential that countries achieve a significant degree of stability before they reach the completion point. Debt relief should not be disbursed before assurances are in place that

such relief would be beneficial for improving debt sustainability over the medium term. We believe the existing flexibility in the HIPC Initiative is adequate to ensure that undue delays in reaching the completion point are avoided when countries reverse the slippages that occurred in the implementation of their economic programs. With regard to the implementation of the PRSP, we continue to be of the view that one year of implementation should not be necessary to reach the completion point. The one year mark is an arbitrary period of time, and in principle should not be a binding constraint when performance is broadly satisfactory otherwise. As highlighted in the report on progress in implementing the PRSP, there are inherent problems in the design of the PRSP which we believe complicate its implementation. Assessing the adequacy of implementation has to take account of these difficulties. On the social and structural completion point triggers, we believe a variety of factors can influence the achievement of these triggers. It is therefore necessary to apply the flexibility provided in the HIPC Initiative when judging the progress made toward meeting them.

Decision Point

Domestic difficulties, including conflict, prevailing in a number of HIPC-eligible countries continue to be a hurdle to reaching the decision point. It is important that the Fund remains engaged, to the extent possible, in these countries in order to prepare them to take advantage of the HIPC initiative when circumstances allow. Protracted arrears present another major obstacle to proceeding with the provision of debt relief, particularly for Sudan which has been making serious progress on the policy implementation front. Significant resources, including HIPC and PRGF, are needed to resolve Sudan's high debt and arrear problem and equally important to help in the adjustment process to place the country's debt dynamic on a sustainable path. Similar issues need to be addressed for Liberia and Somalia once the domestic conflicts end.

PRSP: Progress in Implementation

We welcome the candor of the annual progress report on the Poverty Reduction Strategy Paper Process. The report rightly brings out the tensions inherent in the multiplicity of objectives of the PRSP process. Admittedly there are no preset recipes for addressing the tension, for example between increased participation and better prioritization, or between more ambitiousness on the one hand and realism and budget constraints on the other. These issues are best handled by country authorities who can better assess the extent to which participation of parliamentarians, CSOs and other stakeholders, for example, can be enhanced without undermining the optimal choice of priority projects. The Fund and the Bank, and in general the donor community, should give country authorities the discretion to make such

choices and to empower them to implement their vision by providing advice and technical assistance to build institutional capacity.

The apparent inconsistency between the inherent ambitiousness of the PRSP on the one hand and the need for realism to effectively implement policies within the financial resource envelop on the other can be addressed, to some extent, by framing annual policies in the context of the annual budget and by strengthening the link between PRSPs and the macroeconomic framework. Doing so would require a high degree of cooperation between the different stakeholders and country authorities. Country authorities should design their plans in line with donors' commitments. In turn, donors should make a serious effort to ensure that disbursement of financial assistance is consistent with these commitments. There is an important role for the Fund to play in this connection to ensure that targets set under the PRSP are consistent with maintaining fiscal prudence and preventing excessive accumulation of debt. The Fund resident representative can play an important role in this regard as proposed in the staff paper. In doing so, the Fund should exercise a degree of flexibility in setting the balance between promoting prudence in fiscal policy and allowing increases in poverty reducing spending and other government outlays to ensure that growth and poverty reduction indicators can continue to improve

There may be merit in opening up a dialogue on macroeconomic issues in the context of the participatory process. However, it should be recognized that there is a limit to what such an approach can achieve in convincing civil society, labor unions, and other interest groups, of the virtues of fiscal prudence. While these groups may very well be aware of the need to contain spending within the resource envelop, conflicting demands on these resources could result in breaching the aggregate limit on expenditures.

HIPC: Considerations Regarding the Calculation of Additional Debt Relief

We continue to believe that the current methodology for providing additional debt relief at the completion point beyond what is committed at the decision point is appropriate. It should be recognized that a large number of creditors, both multilateral and bilateral, have agreed to participate in the Initiative on the basis of the existing modalities for the provision of relief and topping up. Changing the methodology for topping up will imply a higher cost of relief for many bilateral and multilateral creditors some of whom already are facing constraints in delivering their share of the relief. Even for the Fund, changing the methodology would imply an increase in cost that could risk undermining the PRGF and HIPC operations given the available resources.

PRGF/HIPC Financing Update

Available resources for PRGF and HIPC operations as well as the subsidization of post-conflict emergency assistance are broadly appropriate at least for the foreseeable future, not accounting for Sudan, Liberia, and Somalia. Beyond 2005, lending capacity under the self-sustained PRGF will be significantly reduced to SDR 660 million per year, which is not sufficient to continue the provision of concessional resources at the current rate. While we hope that the financing needs from the Fund of PRGF-eligible countries will diminish over time, it is not likely to decline sufficiently in the next few years to a level consistent with available resources. We therefore welcome the efforts under way to examine ways to enhance the lending capacity of the PRGF facility.

Mr. Portugal and Mr. De Silva submitted the following statement:

We thank the staff for a helpful set of documents that bring to the attention of the Board key second-round issues in the implementation of poverty reduction strategies.

The latest review confirms that the PRSP process has indeed been an instrument of progress in low income countries, although many daunting constraints and obstacles are still to be successfully addressed. The staff reports an encouraging record of improvement in terms of the modalities of the PRSP process itself, and has also noted progress towards achieving the ultimate poverty reduction goals. We welcome the growing indications that the principles of openness and inclusion, so strongly emphasized within the PRSP process, may be taking permanent root in some PRSP countries, and we are also encouraged by the more tangible forms of progress seen in such areas as macroeconomic policy design, service delivery and governance.

On the question of ownership by national governments, the picture seems somewhat ambiguous, as strong signs of progress in some cases are counterbalanced in other cases by seeming reluctance to integrate the PRSP process fully and seamlessly into existing planning frameworks and budgetary processes. However, we do not necessarily see this as a signal that the government may be less than fully committed, as suggested in the paper. We believe that it is better to allow national governments to convince themselves of this point, as to do otherwise could be counterproductive.

The participatory process is a key cornerstone of the PRSP. The staff update notes important gains in this area as, increasingly, trade unions, the private sector and other groups in society are responding to official initiatives and joining the dialogue in many countries. It is important to give rein to this process if the PRSP is to be a legitimate expression of the collective vision of the entire society. This breadth of participation will come at some costs,

including some sacrifice of depth as observed in the report, which also makes the point that technical deficiencies will limit the effective engagement of civil society. The involvement of the Fund should as far as possible be guided by the objective of easing the technical and capacity constraints that hinder effective implementation of the process. We agree that this role should include assistance from the Fund in guiding priorities given the likely difficulties of distilling the multiplicity of options thrown up by widespread consultation.

In the interest of preserving country ownership, the capacity building focus of Fund involvement should be maintained as well in addressing the tensions that inevitably arise as low-income countries seek to accommodate their long-term aspirations to the shorter-term planning and budgetary cycles. It is not surprising that the targets set out in the PRSPs are frequently seen as over-ambitious. In formulating PRSPs in a participatory process, low-income countries are more likely responding to their needs and not necessarily to their capacity constraints. In this regard, the staff paper observes encouragingly that PRSP targets are often in line with the MDGs. Where ambition runs ahead of reality, countries have displayed their capacity to learn and have modified their targets in response to recent performance. The Fund should seek to assist and accelerate this learning process as much as it can, including through the incorporation of public expenditure management reforms into the PRSP process.

Low-income countries have to date not been very successful in establishing a workable fit between assessed macroeconomic policy priorities and longer-term PRSP objectives. It is not surprising, given the understandable desire in these countries to make a quick and decisive impact on poverty, that priority would be given to actions that promise to deliver immediate benefits to the poor, even if these actions are not always linked to the identified obstacles to growth. We support the strengthening of efforts to integrate macroeconomic analysis and policy more closely with PRSP strategies, and welcome the increasing efforts to include trade issues in PRSPs.

Finally, we view efforts to advance donor harmonization and alignment as critical for avoiding an added source of stress on the severely burdened capacities of PRSP countries. There is scope for addressing this issue at both ends as it were, that is to say, by strengthening the coordinating capacity of poor countries at the same time as the donor community and MDBs are moving closer towards harmonization and the establishment of standards of alignment. The initiative by the donor community should aim to rationalize currently uncoordinated donor requirements without intensifying compliance burden. The Fund could also play a key role in the first regard.

Mr. Yagi and Mr. Miyoshi submitted the following statement:

We thank Fund and Bank staff for preparing a comprehensive set of reports on the progress of the PRSP approach, and an informative status report on the HIPC initiative, as well as the financing update of the Fund's operations in low-income countries.

PRSP—Progress of the Approach

Since the Board meeting last year, an additional fourteen countries have completed full PRSPs, and there have also been significant developments in other countries. It is welcome that the PRSP approach remains on track.

At the same time, we see from individual country cases that substantial challenges still remain for the PRSP approach. The issues discussed in this year's staff paper are almost the same as those raised in last year's paper, such as over-optimism in growth projections, poor alignment between the PRSP process and the process for national decision-making, problems in public expenditure management, and the need for greater donor harmonization. That said, it is inevitable that this approach faces difficulties due to capacity constraints of the countries concerned. It is important not to expect quick results in the short term. Rather, the Fund and the Bank should engage in the exercise effectively and flexibly with patience. It is also important for the Fund and the Bank to be more focused on implementing technical assistance to build countries' institutional capacity.

Macroeconomic Framework and Better Alignment with the Budgetary Process

This chair has argued that the implementation of the PRSP should put particular emphasis on the areas of macroeconomic policies and public expenditure management. Like last year's paper, this year's paper refers to the problems in developing macroeconomic scenarios and in the alignment between the PRSP and national budgets. On this point, we would reiterate the comment we made at the Board seminar on the alignment of the PRSP approach and the PRGF. In order to make PRSPs realistic operational plans, it is essential, first and foremost, that their growth projections not be over-optimistic. The starting point should be to formulate a realistic macroeconomic framework and, then, the PRSP's more ambitious framework and poverty reduction targets should be formulated with realistic consideration given to the extent to which donor assistance, including the Fund's PRGF, would contribute to country's economic growth and poverty reduction, in order to establish a strong linkage between the realistic framework and achievable targets.

There is also a need for greater co-ordination of the policy cycles of PRSPs and national budgets. Given countries' substantial capacity constraints, it is also important for the Fund and Bank staff to continue to help countries build capacity in this area.

The PRSP approach and the MDGs

There is a degree of tension between PRSPs, which are compiled under the ownership of countries, and the Millennium Development Goals (MDGs), which are global targets. While moving towards the achievement of the MDGs is an important objective for the international community, it should be recognized that the degree of difficulty in achieving the MDGs differs from one country to another. This chair understands that Fund and Bank staff share this view.

Room should be allowed for each country to establish its own goals that take into account its financial and institutional constraints that it faces, and to make its own decisions on the policies and measures necessary to achieve these goals. It is important to avoid a situation in which over-optimistic and over-ambitious PRSPs become mere wish lists that lack linkage with actual policies and have adverse consequences such as debt accumulation, including through excessive aid inflows. We strongly believe that setting up realistic targets in PRSPs will be beneficial to countries in the long term.

HIPC Initiative—Progress of the Initiative

We welcome the progress made in the HIPC initiative. At the same time, we note the cases of delay in reaching the completion point because of a lack of macroeconomic stability and insufficient implementation of poverty reduction measures. We would reiterate our view that debt relief is only a partial answer to ensuring long-term debt sustainability of HIPC countries. A more important issue to this end is the achievement of sustained growth, which is the foundation for poverty reduction.

In particular, we are concerned that a major impediment to sound macroeconomic policies is fiscal policy slippages. As we have pointed out, strengthening governance and enhancing countries' capacity to absorb aid are essential components of any poverty reduction strategy. The Fund and the Bank should strengthen their co-ordination and effectiveness in this area, while remaining patient and flexible with respect to their involvement in the process. In this connection, we welcome the progress made in the area of public expenditure management, and hope there will be further progress.

Creditor Participation

We welcome the greater participation of non-Paris Club countries in the initiative, as described in the staff paper. Greater creditor participation is consistent with the initiative's principle of fair burden sharing. We encourage Fund and Bank staff to continue their efforts to this end. Further consideration of concrete measures to facilitate creditor participation would also be beneficial.

We believe that the current policies to address the problem of litigation against HIPCs by private creditors, such as monitoring by the Fund and the Bank and publication of the names of creditors that seek recovery through litigation outside the HIPC framework, are appropriate, and we welcome the updated information. Regarding the issue of HIPC-to-HIPC debt relief, we look forward to the staff's further consideration of options for concrete measures, taking into account the basic principle of inter-creditor equity, and expect a feedback to the Boards at an early stage.

Financing Update of PRGF and HIPC Operations

Concerning interest subsidy contributions to the HIPC-PRGF Trust, we urge all countries that have pledged but not yet contributed to finalize the necessary procedures as soon as possible in order to make their contributions effective.

We support the proposed decision since the reserve-coverage ratio of the reserve account of the PRGF Trust for the next six months is judged to be adequate. We believe that it is necessary to at least maintain permanently the current reserve-coverage ratio of around 40 percent, and hope that this can be done in the future.

Topping-up Debt Relief Under the Enhanced HIPC Initiative

We welcome staff's further work on the potential costs of topping-up debt relief assistance under the enhanced HIPC initiative. As this chair has mentioned on several occasions, providing additional debt relief at the completion point should be warranted only to exceptional cases where a country's economic fundamentals have deteriorated significantly because of exogenous factors, and it should be considered on a case-by-case basis. Moreover, it should be reaffirmed that debt relief under the enhanced HIPC initiative is targeted to achieve a debt-to-export ratio of 150 percent.

Taking these factors into consideration, the Alternative Methodology I, which excludes additional bilateral debt relief in the calculation of topping-up assistance, lacks rationality and runs the risk of causing moral hazard in HIPCs. Also, the adoption of this methodology would require additional

financing of more than US\$1 billion, which would fall on the international community. The cost for the Fund would be double that of the current methodology. Given a great need for additional financing, we are skeptical about the feasibility of the Alternative Methodology I.

This chair can support the basic concept of Alternative Methodology II since it comes close to the fundamental rules that should govern the topping-up debt relief assistance, including that such assistance should apply only in exceptional cases where unforeseen exogenous shocks occur, while excluding new borrowing between the decision point and the completion point. While acknowledging the implications of this methodology, namely the significant impact that including new borrowing during the interim period will have on the calculation of financing needs for topping-up assistance, our view is that not all new borrowing is problematic, only borrowing that is made without a serious assessment of the cost involved.

In conclusion, this chair continues to support the current methodology for topping-up assistance, and believe that the HIPC countries need to assess strictly the costs of the new lending in order to avoid rapid lending, while bearing in mind that new lending during the interim period would have a significant impact on the calculation of financing needs for topping-up assistance as Alternative Methodology II clearly shows.

Financing of PRGF Lending Beyond 2005

We are pleased that the necessary operational costs of a self-sustained PRGF, which is expected to start in 2006, are now projected to be fully financed by the Reserve Account of the PRGF Trust, thanks to the amount of projected resources available and the maintenance of a sufficient reserve coverage ratio for claims on the PRGF Trust. At the same time, the staff states that the decline in annual commitments to SDR 666 million under the self-sustained PRGF might be viewed as inadequate, in view of the historical average of annual commitments of SDR 1 billion and the intensified global efforts toward the achievement of the Millennium Development Goals (MDGs). However, as we pointed out at the Board meeting on the Fund's role in low-income countries on August 27, we do not find this argument persuasive because, in our view, the efficiency in the use of Fund resources could be enhanced by greater selectivity, facilitating countries' graduation from the program relationship, and addressing the "seal of approval" problem. Further effort should be made on these fronts, and its effects should be taken into consideration, together with the implications of low-income countries' improved macroeconomic conditions for the need for assistance through the PRGF, when judging the adequacy of PRGF resources. We understand the merit of starting the examination of the various financing options at an early stage, in light of the time-consuming process of bilateral donor contributions. It would not be appropriate, however, if the staff took for granted the need for

an expansion of financial resources for a self-sustained PRGF on vague grounds that the projected commitment level is low compared to the historical average, and that the pressure from the international community on the Fund to make tangible contribution towards the achievement of the MDGs would be intense.

Mr. Daïri submitted the following statement:

Progress in the implementation of the HIPC Initiative continues to be slow. Since September 2002, only one additional country has reached the decision point, and only two countries have reached the completion point, while eleven countries are yet to reach the decision point. We are encouraged by staff's statement that "a number of countries are well placed to reach their completion points in 2003 or early 2004," that "countries with protracted interruptions in their macroeconomic programs could be back on track within a short period of time," and that "some HIPCs could start establishing a policy performance record by the end of 2004, in order to reach the decision point before the sunset clause of the Initiative takes effect." This, however, requires major efforts from the countries themselves, and from the international community. The well-written staff report identifies a number of key domestic and external factors that impeded progress, including fiscal slippages, limited institutional capacity, weak governance, deteriorating political and security conditions, and adverse exogenous developments, such as the global economic downturn and declines in international commodity prices.

One important finding of the review process is that initial timetable for the preparation of PRSPs turned out to be overly ambitious. We agree with staff that ownership and quality of the PRSP process should not be sacrificed for speed in reaching the completion point. This should not, however, imply too long delays for the country to benefit from the crucially needed and long-awaited debt relief.

We are encouraged by the actual and projected impact of the HIPC Initiative on debt indicators. We reiterate our concerns about long-term debt sustainability. We look forward to the upcoming workshops on these issues, and for the joint paper on policies and operational options to address them.

We reiterate our call that HIPC debt relief should be additional to other forms of external financial assistance. While the staff paper confirms that this has been the case as far as the 27 countries that have reached the decision point, we wonder whether this additionality can be confirmed for low-income countries as a group, or whether resources may have been diverted toward HIPC countries at the expense of other low-income countries. Moreover, it is a matter of concern that the recent increase in aggregate flows to the 27 countries only restores their external official financing to levels of the early 1990s. We have also some problems with the methodology used to analyze

external official assistance. It seems odd, for example, to classify fishing royalties as official assistance in the case of Mauritania. We wonder whether similar classification problems could cloud the interpretation of trends in official development financing.

We appreciate staff attempt to analyze the factors behind program interruptions since the decision point as well as key factors affecting policy performance more generally. Maybe staff could elaborate further on the reasons behind revenue shortfalls, with particular reference to the realism of growth projections on the one hand, and of the country's implementation capacity in tax reform and administration enhancement on the other.

The staff paper highlights conflicts and protracted arrears as key factors behind the delay in bringing several countries to the decision point. As indicated by Mr. Ondo Mañe, we are pleased that appreciable progress has been made in several African countries toward resolving conflicts. We hope that this would help accelerate the pace of implementation of HIPC.

We welcome the increased creditor participation to the HIPC Initiative. In particular, we commend the Libyan authorities for their decision to participate in the initiative, and the Indian authorities for their decision to write off loans to HIPCs. We call on other bilateral creditors to join the initiative, and on staff to continue seeking broader participation through moral suasion. We also call on the Fund and the World Bank to further explore ways of assisting those HIPCs facing litigations from commercial creditors.

The well-focused staff report on progress in implementation of PRSPs highlights areas where progress can be made. In particular, improving the effectiveness of the participatory process could prove instrumental, not only to speed up formulation of PRSPs, but also to facilitate program monitoring and program adjustment during the implementation period. In this regard, like Mr. Ondo Mañe, we are of the view that there is a need to strike a balance between broad participation and effectiveness. The participatory process could be complemented by efforts to disseminate detailed information on the relevant issues. In addition, building on past experience, and given the generally weak domestic capacities, effectiveness of the process could benefit from technical assistance to identified groups to enhance their participation. This could be achieved through, inter alia, organizing targeted workshops, with the assistance of Fund and World Bank staffs. However, this should not undermine the role of the authorities in steering the process. The role of civil society organizations, in particular, should be put under close scrutiny to ensure that their contribution is additional, and not a substitute, to those of other participants in the consultative process.

We also agree on the need to strike the right balance between realism and ambition. Meeting the MDGs requires ambitious growth projections. We

agree with staff that PRSPs need to be ambitious and that it is at the level of budget formulation that the right balance between ambition and realism needs to be stricken. This will help strengthen credibility in the PRSPs, by avoiding potential disappointments and associated adjustments, while maintaining an adequately ambitious incentive structure for identification and implementation of the reform agenda and ensuring its financing. This calls also for enhanced flexibility to ensure that objectives and policies are continuously reviewed and to adjust to changes in circumstances.

We share staff's candid assessment that linkages between PRSPs' discussions of macroeconomic performance, growth prospects, and proposed sectoral and structural policies remain weak. This is an important shortcoming that needs to be overcome through analysis of the sources of growth, including proper assessment of obstacles to growth. We also agree on the need for more specific formulation of the complementary actions to trade policy reform and for its better integration with the overall policy agenda.

Despite recent progress, improvement in public expenditure management will remain an important and long-term challenge. We continue to attach high priority to improving the linkage between PRSPs and the annual budget and MTEFs. The costing of measures in particular could be improved by associating the Ministry of Finance to the PRSP preparations at an early stage. Donor alignment and harmonization is also called for, and we are troubled by the assessment that in some instances priorities are driven by the supply of donor assistance rather than by articulated policy agendas. We support increased technical assistance to PRGF-countries to improve donor coordination.

We support the emphasis put on national governments' responsibility in setting priorities and leading the dialogue on macroeconomic policies in the participatory process. This should help clarify the role of the Fund staff in interacting with participants. The role of the staff should focus on clarifying the authorities' policies and laying down the various trade-offs involved. It is indeed important that such interaction is seen as part of a confidence building exercise and that it does not undermine the authorities' policies.

We thank the staff for the semi-annual update on PRGF/HIPC financing and subsidization of post-conflict assistance. While we take note of staff conclusion that available resources are sufficient, we encourage early consideration of a paper on how to ensure maintenance of PRGF lending at close to historical levels after 2005, and we welcome staff work on alternative financing options to this end. We also urge for early consideration of the financing needs for bringing the remaining HIPC-eligible countries to the decision point, including Sudan, Liberia, and Somalia.

Mr. Zoccali and Mr. Vogel submitted the following statement:

At the outset, we would like to thank the staff for the comprehensive set of reports putting in perspective the progress made under the PRSP and the Enhanced HIPC initiative. While important advances were made, we welcome the focus on the remaining challenges in view of multiplicity of objectives of the PRSP process and its inherent tensions.

The PRSP approach has been shown as facilitating greater openness in policy making. As the staff underline, the private sector has been increasingly active in PRSP formulation, NGOs and trade union participation has been more pronounced, and many governments have attempted to ensure that the voices of marginalized groups are included in the dialogue. We attach utmost importance to the role that consensus plays in the decision-making process. In this regard, a strong backing of support is less subject to reversals due to political considerations and is critical to mitigate the problem of electoral calendars and changes in administration which often have slowed the progress of the design and implementation of poverty reduction strategies.

Staff notes that participation in the PRSP process has tended to be broad rather than deep, citing reservations of some observers about the assumption that maximizing participation will necessarily produce an improved document. Strong government leadership is important to help develop and broaden that participation. In this regard, we share the concerns expressed in Mr. Reddy's preliminary statement about the accountability of the participants and the special weight corresponding to democratically elected governments accountable to their electorates. We note some encouraging progress on the ownership front, even though this is an area where much remains to be done. There is no substitute for leadership and ownership to address tensions, and to reconcile the expectation that the PRSP be comprehensive with the need to identify strategic priorities.

The fact that poverty-reducing spending has increased for the 14 PRSP countries where data is available is a welcome development. Nonetheless, putting in place the mechanisms to allow for better monitoring control and outcomes from such expenditures will require much further efforts. In addition, data constraints constitute a major obstacle for the attachment of these objectives. Consequently while some progress has been made in improving PEM system or in incorporating PEM measures in PRSPs, a recognition by staff that the process is likely to be gradual points to its fragility. In any event, we welcome the new framework for Bank/Fund collaboration in the diagnosis of the PEM system, as well as its design and implementation.

Good governance is critical to improve effectiveness and transparency of expenditure programs and, thus, to mitigate poverty conditions. In this

regard, we welcome the positive steps taken by the Kyrgyz Republic, Cambodia and Ghana. At the same time, we consider that broader participation in the PRSP process by encouraging a more active involvement of civil society, could serve to improve political accountability and reduce incentives for corruption. We welcome the staff finding in SM/03/279, Supplement 1, that increased participation has led to a greater focus on governance, including legal frameworks for civic participation and access to information, in Nicaragua and Honduras. Recognizing the advances made in this area, systematic efforts to encourage good governance would be desirable provided that these do not extend outside the scope of the Fund's core responsibilities. Good governance should generally continue, in our view, to be a strong focus of the instruments and programs of the Fund and staff should continue working to strengthen the reporting on governance issues that normally accompanies HIPC complete point documentation, knowing full well that this is an important but not a sufficient condition, for the success of growth and poverty reduction strategies.

Improving macroeconomic stability has been singled out as the main contributor to a more favorable investment climate in PRSPs. We share this view as well as the need to pay greater attention to the consistency of macroeconomic frameworks than in the past. Despite the progress made on this front, more realistic macroeconomic projections, and stronger links between envisaged policies in the PRSP and the budget are needed. We concur with staff that the government, not the Fund, should lead the discussion on the macroeconomic framework in the public domain and that it become an integral part of the PRSP participatory process. The Fund should support these efforts, among other things, by providing timely assistance to build up countries' administrative, technical and institutional capacity, as well as more research linking macroeconomic stability with poverty reduction.

Regarding trade issues, Box 4 (SM/03/279 Supplement 1) underscores the incomplete nature in several PRSPs of the discussion on the contribution of trade. Staff cite the interesting case of Benin among recent experiences by pointing to its narrow export base and limited market access as trade development constraints. They also note a lack of proposed measures to more effectively address some of these problems. In this regard, however, the costs of trade distorting subsidies in many industrialized countries should be kept in mind as these extend well beyond the international market for cotton which so severely affects countries like Benin, where cotton represents an 80 percent of exports and provides subsistence for 200.000 households. In this case, the process of liberalization of the cotton sector has also been among the most advanced in the region. As we and other Chairs noted in the meeting on the Role of the Fund in Low-Income Member Countries, continued lack of progress on agriculture trade liberalization may not only slow down to reforms but also undermine the effectiveness and even credibility of the Fund as a policy advisor that is working for the benefit of all. We, therefore,

strongly support a sustained engagement by the Fund to advance free trade and open markets in all member countries.

The delays in reaching the completion point may be attributed to the challenge of maintaining macroeconomic stability and preparing and implementing poverty reduction strategies. Moreover, only 10 of the 19 countries in the period between the decision and completion points have had satisfactory macroeconomic performance records. This points to macroeconomic performance as the main cause for the delays. While we consider macroeconomic stability to be critical for reducing poverty, and as such remains a condition for reaching the decision point, the Fund has a clear role to help sustain adjustment efforts by providing adequate interim financing and to allow such countries to deal with external shocks when these occur. Similarly, to help countries meet the requirement of full Poverty Reduction Strategy Papers, technical support should continue to be made available. We agree that ownership and quality should not be sacrificed for speed in reaching the completion point. At the same time we would underscore the importance of timely support to help maintain the reform momentum. In the case of the requirement of satisfying social and structural completion point triggers, we find merit in the suggestion that the Fund's Board grant waivers as necessary, when a particular condition has not been met or has been superceded by events when the thrust of the overall performance is satisfactory.

Finally, we share the reservations of some Chairs regarding the alternative topping-up methodologies. Among others, we note that the majority of HIPC countries see little or no benefit from the proposed change if additional bilateral relief were to be excluded from the topping up calculations. In addition, staff highlight that the cost associated with Alternative Methodology I is substantially higher and, more importantly, that it could not be accommodated without risk for the financing of PRGF and HIPC operations within currently available resources. Similarly, by excluding debt contracted after the decisions point from topping up calculations, there could be important moral hazard considerations. The exclusion of new lending during the interim period could also encourage creditors to finance investment projects without fear that topping up at the completion point would require them to write down the loans.

Mr. Martí and Mr. Siman submitted the following statement:

We would like to thank the staff of the Fund and the World Bank for the well-prepared set of papers that give us an update of the recent developments in the PRSP, HIPC and PRGF/HIPC financing.

We continue to believe that the HIPC initiative and the PRSP process, when prepared with country ownership and broad participation of the stakeholders, serve as the basis for implementing the countries' strategy to

reduce poverty. Therefore, we welcome the staff's report on the steady progress that many countries have made to date, and support the approach in their review of concentrating in those aspects of the PRSP process in which lessons can be learned, and where new challenges to implementation have emerged.

Substantial Improvements in Government Ownership:

We strongly agree with the principle that national governments should 'own' their poverty reduction strategies, being actively engaged at all level, in both, the formulation and implementation stages. It is encouraging to see that the majority of recent PRSPs give evidence of an increased involvement of line ministers in the design and implementation phase.

Nicaragua and Honduras, members of our constituency, are countries where there have been high-level of government ownership which strong involvement and commitment to the process by core and line ministers. The early involvement of the Central Bank president and Ministers of Finance, among others, have shown the countries' commitment to the process and it has greatly contributed to develop institutional arrangements that place the PRSPs in national decision-making processes. In this regard, it is also encouraging to see that there are examples of good practices, such as Nicaragua's PRSP, where authorities have included the matrix of goals and intermediate indicators from the PRSP into the National Development Strategy, consolidating the PRSP into the national decision making process.

Improvements in the Participatory Processes, Both in Formulation and in Monitoring Implementation:

It seems that the majority of PRSPs have included broad consultation processes, demonstrating improvements in opening the discussion to a broad range of stakeholders.

We welcome the staff's comments on the increased private sector participation in the formulation of some PRSPs, both through their involvement in consultations as well as through formal mechanisms such as thematic working groups. However, in many other countries, there is still room to ask for their views more proactively, especially in some cases, where the private sector is requested to react to existing programs more than participate in the discussion of policy options. Another area in which more private sector involvement is appropriate is in the design of actions for the improving the investment climate and increase in productivity.

On the implementation stage, we share the concerns of staff that is not always clear how participatory arrangements could become permanent, translating the involvement by civil society in the consultation phase in other

forms of enduring engagement. It is encouraging to see those PRSPs, as is the case in Honduras, which includes legal frameworks for civic participation and access to information, where stakeholders have played an active role in tracking policy developments.

We agree with the staff's comments on the need to have governments taking the lead in opening up the dialogue on macroeconomic policies in the context of the participatory nature of PRSPs. We concur with the staff's proposal to further support these efforts and build capacity as outlined in the PRSP progress report.

Importance of Setting Strategic Priorities and Strengthening the Budgetary Process:

We welcome the staff's comments on the shift in spending priorities to expenditures targeted towards reducing poverty and the increased efforts to improve public expenditure management.

We acknowledge the tensions that sometimes countries face in deciding between a comprehensive PRSP and the requisite to set their own priorities. Despite its difficulties, prioritization is key in every PRSP and should be reflected in the national budget formulation and execution. We agree that recent PRSPs provide improved guidance for national budget processes but we are concerned on the staff's view that progress in this area is likely to be gradual.

We support the staff recommendation to incorporate PEM reforms into the PRSP processes. However, we are concerned that national budgets in those countries do not provide sufficient basis for achieving the sustained period of higher growth rates necessary to attain the MDGs. As calculated in a recent discussion of the role of the Fund in low-income countries, it would take almost 40 years for those countries to reach the current median level of other developing countries.

As mentioned in a recent statement, we strongly believe that there is a need to work closely with low-income countries for a greater understanding of the necessary elements of the growth process, in order to assist authorities in prioritizing those policy alternatives that may lead to acceleration in economic growth. Despite some evidence of increased attention to sources of growth in some recent PRSPs, the choices of priority public actions are still not derived from the identified growth sources and risks. Staff's comments would be appreciated.

We concur with the staff that in most PRSPs trade issues are formulated in general terms, without clearly specifying the timetable or the need for complementary actions. We encourage staff to include in future

PRSP and PRSP-PRs coverage of trade-related issues. In the case of some small and medium-size countries, the elimination of trade barriers could be a step to jointly achieving the MDGs through the creation of economies of scale or regional markets that could induce private sector investment.

Continued Progress on HIPC, Challenges Remain:

We welcome the continued progress being made under the enhanced HIPC initiative in providing debt relief to more than two thirds of those countries that potentially qualify for assistance. Nevertheless, several challenges remain. Despite progress in implementing PRGFs and PRSPs but countries are taking longer time than envisaged to reach completion point. Full and timely participation of all creditors is crucial to the success of the initiative. We commend those creditors that since the last review have agreed to participate and urge other creditors to provide their required share of debt relief.

Regarding governance, we welcome the importance given under the current HIPC framework, especially in strengthening public financial management. We welcome the workshops on debt sustainability in the context of achieving the MDGs and we look forward to the joint Bank/Fund report on the conclusions reached in these workshops.

On the Financing of PRGF and HIPC Operations:

We take note of the staff's semi-annual update on the financing of the PRGF and HIPC operations and the subsidization of the post conflict emergency assistance. We are pleased to note that, under current projections, PRGF subsidy and HIPC grant resources are estimated to be sufficient to cover the Fund's participation in HIPC and the cost lending through end-2005. However, we are concerned with the projected lending capacity beyond 2005 under the self-sustained PRGF, which shows that the actual trend in annual commitments does not adequately provide for continuing the Fund's role in low-income countries. Given the importance of this topic, we appreciate the staff comments on the other financing options under consideration and look forward to the specific board paper on this issue.

Concluding Words:

Finally, we would like to note that the enhanced HIPC initiative is an important part of a comprehensive strategy to eradicate poverty especially in ensuring debt sustainability. Other issues addressed in the PRSP approach, such as macroeconomic stability, good governance and the strengthening of public finances are also key conditions in attaining the MDGs. However, many countries are still heavily dependent on primary commodities for their export earnings and government revenue, and as a result, they remain

vulnerable to adverse external shocks. In the medium term, these countries would require continued policy reforms aimed at achieving self sustained growth as well as an improved access for their exports to the world markets.

Mr. Usman submitted the following statement:

We thank the staff for their update of these two important and interrelated initiatives; the HIPC Initiative and the PSEA Initiative. We welcome progress made so far in alleviating the debt burden of HIPCs and enhancing the benefits accruing to these countries in terms of increased social spending. We also welcome that the Reserve Account of the PRGF Trust holds enough balances to meet possible obligations in the next six months. We agree with the thrust of Mr. Ondo Mane's preliminary statement and wish to follow-up on a few issues for emphasis.

HIPC Initiative-Status of Implementation

The first concern we have is that the pace of implementation has stalled. After the first wave of decision point cases, 38 countries have reached decision point, yet only eight (8) countries have reached completion point. On the part of eligible countries, conflicts and fiscal slippages have been cited as major causes of delays. Fiscal performance was the subject of last Friday's discussion, during which it was observed that poor performance was not solely to blame for program interruptions, but also possibly faults in program design. We feel that these findings should be taken account of in considering the challenges facing countries in reaching the completion point. We also feel that countries should not be unduly delayed in getting debt relief solely because of concerns about governance. We fully agree that governance remains a key concern in some HIPCs and it is a hindrance to development. However, it should be noted that there are judgmental issues involved in measuring governance, and more importantly, even with the best of commitments from country authorities, strengthening institutional capacity to enforce good governance takes time. We know that perceptions do not change dramatically, just as corruption and other vices could not be eliminated overnight. Besides, governance is a global problem affecting both the public and private sectors in developing and developed countries alike. We urge, therefore, for a more flexible approach to the issue of governance, particularly when it appears to constitute a cog in the wheel of progress towards reaching the completion point.

Progress in implementing PRSPs and social and structural triggers seem impressive. These notwithstanding, however, they do not appear to translate into marked reduction in poverty. A number of studies seem to suggest that absolute poverty in some regions, particularly in sub-Saharan Africa, is actually increasing. There is need, therefore, to synchronize completion point triggers and PRSPs implementation, with the goals under the

MDGs. Even staff acknowledge that HIPCs, in particular, are having difficulty in maintaining macroeconomic stability and debt sustainability. This therefore points to the urgent need to accelerate the harmonization of the areas of PRGFs and PRSPs, particularly in cushioning countries from the impact of exogenous shocks, broadening the sources of growth and expanding export market opportunities for HIPCs.

Creditor Participation and Creditor Litigation

We welcome the increasing number of creditors that are committing themselves to deliver debt relief on HIPC terms. We welcome the decisions made by Libya to provide debt relief and by India to write-off all the claims all the claims to HIPCs. We urge the remaining creditors to do the same. Threats of litigation remain a serious concern for many HIPCs and we are amazed that the staff seem to suggest that nothing could be done in this connection, other than moral suasion.

Financing of the PRGF and HIPC Operations

As noted in the staff paper, there has been a prolonged slowdown in export market growth for HIPCs, with global interests rates at historic lows and HIPCs' GDP growth being adversely affected by high oil prices. These factors would tend to push up the costs of the HIPC Initiative and would thus warrant a significant increase in resources to implement the initiative. There has so far been no such dramatic increase. Staff may wish to clarify further.

It is important that the Fund maintains adequate resources for topping-up debt relief at completion point for those cases that have experienced fundamental changes in their debt sustainability outlook. The volatility in oil prices, and the depressed prices for most HIPCs' exports, as well as the impact of natural calamities, especially adverse the weather in the case of sub-Saharan Africa could increase the requirements for topping-up and we would therefore like to see staff base their estimates on higher topping-up requirements.

Regarding the PRGF, we are concerned about the inadequacy of resources for the self-sustaining PRGF. It is projected that beyond 2005, lending capacity under the self-sustained PRGF will be SDR 660 million, way below the current level of SDR 1.1 billion per year, and could be further reduced by the risks mentioned in paragraph 10 of the financing paper.

We welcome staff's beginning to examine other financing options that would enable sustaining current levels of PRGF lending beyond 2005. We look forward to discussing these options. In that context, we urge the Fund to explore the use of its own resources, including GRA resources.

Resources Needed for Protracted Arrears Cases

We have always urged the staff to include countries in protracted arrears in the costing of the HIPC Initiative. We welcome the staff's giving timely consideration of this issue. Concerns about data limitations are valid for Liberia and Somalia, however, the situation in Liberia is rapidly changing and we urge the staff to begin working on a possible Fund arrangement with the country, including modalities for clearing the arrears as well as HIPC costings. We particularly welcome staff's urging for urgent efforts to mobilize the necessary financing to resolve Sudan's arrears situation and for PRGF arrangement and the HIPC Initiative. We feel that since Sudan has been under staff-monitored programs since 1997, the quality of data is such that tentative costings are feasible and the staff have indeed provided an estimate. We wish to reiterate that the Sudanese authorities stay committed to prudent economic policies and are working tirelessly to conclude the most complicated peace negotiations the UN has ever experienced thus far. Adequate resources after the peace agreement would be critical to sustaining peace and to enabling Sudan to progress rapidly in social and economic development.

Subsidization of Post-Conflict Emergency Assistance

Finally, while some regions have been afflicted by conflicts, efforts to achieve peace are gathering momentum, particularly in sub-Saharan Africa. The implication being that a number of post-conflict cases will come on stream in the period ahead. We note that contributions for subsidization of post-conflict emergency assistance (PCEA) are adequate only through end-2004. Could the staff clarify what this implies for those post-conflict cases that could be considered later. Another concern we have raised are the repurchase terms for PCEA which are more stringent than under the PRGF. Could the staff clarify the implications of current terms or possible softening thereon, for countries that move to PRGF and HIPC Initiative.

Mr. Ge and Mr. Yu submitted the following statement:

We thank staff for the well-written papers. Since its commencement, the HIPC Initiative has made important progress in alleviating debt burdens and improving macroeconomic stability in the eligible poor countries. So far, more than two thirds of them have reached decision point, with eight countries reaching the completion point. These countries have begun to benefit from the debt relief. As indicated in staff's reports, the debt dynamics have improved dramatically. Debt stocks are projected to decline by about two thirds and debt service indicators also improved significantly. As a concrete benefit, the savings from debt relief have resulted in the considerable rise in poverty-reduction expenditures. Notwithstanding these encouraging developments, continuous efforts are indispensable to secure the progress made and ensure

sustainable debt dynamics in these countries over the medium term. In this area, challenges remain.

Among the 38 eligible countries, 11 of them have yet to reach the decision point to benefit from debt relief. The pace of these countries to move toward decision point seems to be relatively slow due mainly to domestic conflicts and protracted external arrears, as pointed out in staff report. In this respect, we share the view that continued Fund engagement is essential for these countries to benefit from HIPC initiative. For the 19 countries with interim HIPC Initiatives, 9 of them have either experienced problems in program implementation recently or do not have a Fund-supported program due to protracted delays in establishing a satisfactory track record. Extended program interruption is primarily due to fiscal policy slippages which have been caused by various factors. While some of the causes are beyond the authorities' capacity, we encourage them, with assistances from IFIs, to adopt fiscal consolidation urgently and strengthen institutional framework as circumstances allow. We believe that the built-in flexibility of the HIPC Initiative provides sufficient room for these countries to correct policy slippages in time.

We share the view that good governance is of great importance in achieving pro-poor growth in HIPCs. However, given the constraints they face, the advancements require persistent efforts on both their part and that of the international community. The PRSP framework serves well the objective of improving governance. We are pleased to note that public expenditure management (PEM) reforms are increasingly being addressed in PRSPs, although some of them need a certain degree of upgrading. Meanwhile, good governance has also been promoted by PRGF programs and World Bank arrangements.

The HIPCs need to strike a balance between mobilizing financing to help achieve the MDGs and maintaining long-term debt sustainability. We appreciate staff's work in developing a framework for the assessment of debt sustainability and development financing which will provide important guidance for HIPCs in determining a sustainable path towards MDGs without a fallback to debt overhang.

The PRSP approach has been broadly applied and gained significant progress in formulating a coherent home-owned development strategy, improving institutional capacity and governance, and establishing broad-based consensus. To further enhance the role of the PRSP, efforts should be concentrated on improving realism, strengthening PEM, sharpening the focus and, perhaps most urgently, improving donor alignment and harmonization around national strategies. In applying the PRSP approach, we share the view of Mr. Shaalan that flexibility is necessary and the one-year requirement

should not be made a strict binding condition when performance is broadly satisfactory.

Finally, on the financing of the HIPC Initiatives and the PRGF, the calculation is generally appropriate and we appreciate staff's estimate on the potential needs arising from the possible topping up. While it is agreed that the Fund is not in a position to provide long-term development financing, its ability in low-income countries is essential at the current stage. A sudden and substantial drop in PRGF access may not be consistent with the Fund's mandate and policy objectives. We join some other Directors in advocating probing the possibility of enhancing the PRGF lending capacity.

Mr. Zurbrügg and Mr. Inderbinen submitted the following statement:

We welcome the progress under the HIPC initiative since last fall. We are aware that the process of reaching the completion point has been slower than envisaged in certain cases. However, the fact that the pace of implementation has slowed down is primarily due to the difficulty of a number of countries that have passed their decision points to maintain macroeconomic stability, and in particular fiscal prudence. It is important that the authorities of the countries concerned take measures to address these imbalances. In our view, slower than envisaged progress should not lead to a relaxing of the criteria of the current framework.

On decision point eligibility, we acknowledge the substantial challenges faced by the countries that have yet to build their policy track records. Besides performance on macro-policy, a proven track record on governance and justified expectations of continued efforts in this area, particularly in public expenditure management, should be key to gaining eligibility. In any case, we would not support a rush for the countries in question to become eligible before end-2004. If necessary, we would be prepared to consider postponing the sunset clause next year.

On the issue of topping up assistance, we take Mr. Padoan's point that both the benefits and the costs of a change in methodology should be considered. However, we see the latter clearly outweighing the former. There are several arguments against changing the current methodology. The exclusion of additional bilateral relief would lead to a considerable increase in debt relief costs under the HIPC framework. This could come at the cost of resource flows to non-HIPC low-income countries. The cost increase of the initiative could also come at the expense of a fair burden sharing among all creditors, given that several multilateral institutions would not be able to participate if their costs rose to the point of compromising their financial integrity. We also reject Methodology II. In order to mitigate the risk that countries borrow in the expectation of receiving additional relief at completion point, we would like to reiterate that topping up should only be

granted as an exceptional measure if exogenous shocks lead to fundamental changes in the long-term debt dynamics.

Regarding the self-sustained PRGF, we welcome staff's intention to prepare a financing paper by year-end. However, we should discuss all options, including the option of PRGF lending capacity below historical levels. This option will become more prominent if countries are able to graduate from the Fund's concessional assistance. With the situation in Sudan improving, we note that at some point there will be a need to secure resources for arrears clearance, HIPC assistance and a successor financial arrangement. However, it is important that the cost to the Fund be financed through a fair burden sharing mechanism. Finally, we gladly take note that the financing of PRGF and HIPC operations through end-2005 is secured. We endorse the proposed decision on resource accumulation in the Reserve Account of the PRGF Trust. However, we should continue to monitor the reserve coverage closely as its balance went up only marginally due to low investment returns and Zimbabwe's arrears.

We are looking forward to the upcoming paper on how to assess long-term debt sustainability in low-income countries. We hope the paper will also provide some concrete information on the status of debt management capacity in HIPC countries and on the Fund and the Bank's strategy to address weaknesses in this area. Here, co-operation should be sought with existing mechanisms, such as the Debt Relief Capacity Building Program of bilateral donors. We welcome the staff's intention to analyze how grants and other financing mechanisms could potentially be made more countercyclical, more predictable and better coordinated to address volatility. It would, in general, be valuable if IFIs participate in the discussions with bilateral donors in the context of joint donor budget support programs. An improved dialogue will be even more important when countries begin to graduate from financial assistance and move to a surveillance-based relationship with the Fund. Finally, it will be critical that the IFIs and bilateral donors alike carefully consider the impact of all new lending on the debt sustainability of HIPCs.

Overall, we agree that emphasis on governance under the HIPC Initiative is appropriate. We also encourage staff to continue their work to strengthen reporting on governance of HIPCs at the completion point. We believe that governance issues need to be addressed as concretely as possible in order to avoid any vagueness.

We are pleased to note that PRSP approach has gained widespread support and that there is some evidence of improvement and progress. The key concepts that mark the difference to former approaches are clearly ownership and participation. Ensuring fully participatory processes has been more time consuming than initially thought, and preparation of full PRSPs has on average taken longer than expected. Staff also notes that most HIPCs are

not constrained in reaching the completion point by the one-year satisfactory PRSP implementation requirement. This requirement should, therefore, be maintained.

In promoting broad ownership, we believe governments should do more to encourage parliaments and civil society to participate not only in the elaboration of PRSPs, but also in monitoring and assessing implementation. The ‘delineation’ of roles should take place in a policy dialogue rather than by being defined by the government, since this would increase transparency and accountability. So as to guarantee the quality of PRS processes, donors and the IFIs should support countries in reinforcing the necessary institutional capacities.

Staff mentions the tension between comprehensiveness and prioritization inherent to the PRSP process. In our view, the key to attenuate this tension is to put more weight on the costing of planned actions. On the other hand, tensions are necessary to foster debates on tradeoffs. There are also possible tensions due to conflicting frameworks for poverty reduction and other governmental strategies. It is noteworthy in this regard that in some cases the development of strategic frameworks parallel to PRSPs seems to be a reaction to a perceived concentration of the PRSP process on social issues and a neglect of questions relating to the sources of economic growth, and of the role of private sector. We thus agree with staff that more attention should be paid to growth in the PRSP process.

On donor alignment and harmonization, we welcome the increased cooperation among the Bank and the Fund and donors. However, this seems to follow an uneven pattern and depends on local authorities and the disposition of local representatives. Namely, donor alignment is particularly challenging when the country plays a weak leading role. In order to ensure a more systematic approach, the inclusion of guidelines in the terms of reference for resident representatives regarding responsibilities for relations with donors could be helpful.

Ms. Indrawati submitted the following statement:

The set of papers prepared by staff provide a rich account of progress in the implementation of HIPC Initiative and poverty-reduction strategies as well as their key issues that need to be addressed moving forward.

The HIPC Initiative: Status of Implementation

In essence, as the papers indicate, the progress made in the implementation of the HIPC Initiative and poverty-reduction strategies since the last review has been mixed. We note that only one additional country, i.e. Democratic Republic of Congo, has reached the completion point in 2003 and

during the same period, only two countries, i.e. Mali and Benin, have reached the completion point. This unsatisfactory development is a major concern as we set our minds towards achieving the Millennium Development Goals (MDGs) which is rapidly approaching. The opportunity cost of these delays are significant to the HIPCs in terms of forgone real GDP growth, investment, employment and poverty reduction.

While we can understand that non-economic factors have slowed down the progress of some HIPCs in securing debt relief under the HIPC Initiative, it is disappointing to note that recurring problems continue to prevent these countries from proceeding further in the debt relief process. We also note that to reach completion point requires longer time—this delay is understandable and justified as long as the countries continue to make progress on macroeconomic stability, PRSP implementation and attainment of social and structural triggers. In this regard, we urge concerned donors to make additional efforts in resolving the issue of protracted arrears with many HIPCs. We call on the Fund, the World Bank and other donors to continue and intensify their involvement in providing technical assistance to overcome capacity constraints that have thwarted many HIPCs from making substantial progress in their overall adjustment efforts. Enhanced institutional capacity is crucial for effective policy implementation and minimizes program interruptions. Thus the Fund/Bank should help these countries from facing chicken-and-egg problem of lack of institutional capacity that leads to poverty.

On the other hand, for countries that have reached the decision point, we recognize that there has been an encouraging development in that spending for social and poverty-alleviation purposes has increased which is made possible by the release of resources under the debt relief. However, as Mr. Ondo Mañe has indicated in his preliminary statement, it is important to consider the question of how to ensure that social spending can be sustained to benefit these countries. Increase in social and poverty-reduction spending has been productively targeted at improving education, health as well as related social areas. With the construction of the necessary infrastructure for social requirements, there needs to be adequate provision for maintenance costs of these infrastructures. It is therefore essential and appropriate that these costs be considered in the formulation of PRSPs.

On the importance of good governance as part of the HIPC process, we believe this is not just appropriate but essential in helping ensure success in the overall reform efforts. To achieve good governance requires not only sole efforts and strong ownership of the countries concerned, but the support of the international community particularly in the provision of adequate technical assistance. In this instance, it is important to recognize that achieving good governance may take considerable time and efforts, and the role of international communities to strengthen the demand of good

governance as well as the ability of the country to respond appropriately and consistently.

The PRSP: Progress in Implementation

We generally welcome the progress in the implementation of the PRSP process as it provides an avenue for building consensus on the overall reform efforts. What is, however, worrying is the ambitiousness of the approach in trying to satisfy a multitude of objectives, many of which result in tensions. Therefore it is crucial to address these tensions to arrive at operationally relevant strategies that can be executed in practice. We believe that more efforts are needed to strike a right balance among conflicting objectives and provide ample room for countries to explore and present their own alternative policy scenarios and timetables. It is also important for international communities (especially Fund and Bank) to provide clear signal and incentives for a country to be able to adopt a realistic target and well-focused PRSP.

To make the PRSP more effective, it is critically important to design a more realistic PSRP that is properly-costed and harmonize PRSP objectives within the national budget framework. Greater efforts at improving data will certainly be helpful in this regard. In addition, we see merits in the trend towards deepening the participatory process and the idea of having the authorities at the highest possible level to get engaged with various representations of the society in the articulation and discussion on macroeconomic policy in the context of PRSP participatory process. On the latter, undoubtedly it requires the authorities to have a deeper understanding of the issues involved as well as the ability to coordinate various program in order to be able to highlight the importance of synchronizing macroeconomic as well as socio-political objectives. Again, capacity building, quality of leadership and coordination continue to be prominent in the efforts to make the PRSP process remaining relevant and acceptable to all its stakeholders. It is important for Fund to provide technical assistance as well as supporting information and documents in an easy-to-digest format to facilitate this process.

Fund and Bank's role as a confidential policy advisor should provide a candid and frank judgment through the JSA in order to improve the PRSP implementation. Without sacrificing the quality of judgments and advises, the communication strategy should be adjusted to the political and cultural realm. We also agree that strengthening budgetary process is key to successful PRSP implementation. Fund and Bank can assist countries to integrate sectoral programs and expenditure plans more fully into PRSP by providing not only technical assistance but also by providing understanding the important linkage between poverty alleviation with the choice of sectoral and expenditure

policies. Fund and Bank can also facilitate outreach activities by government in this area by providing resource person and materials for discussion.

Enhanced HIPC: Considerations Regarding the Calculation of additional Debt Relief at the Completion Point

We concur with Mr. Shaalan that modifying the current methodology for providing additional relief at the completion point beyond what is committed at the decision point could result in increased costs for many creditors and risk the effectiveness of the HIPC and PRGF initiatives.

PRGF/HIPC Financing Update:

We note that existing level of resources is appropriate to enable HIPC and PRGF initiatives be carried out in the near-term. This is a welcome development and donors are to be commended for their forthcoming contributions and assistance. We particularly commend the Libyan authorities for their decision to participate in the HIPC Initiative and the Indian authorities for agreeing to write off all the claims to the HIPCs.

Mr. Duquesne and Mr. Scholar submitted the following joint statement:

We are grateful to staff for the comprehensive progress reports and the paper on the costs, and benefits, of changing the topping up methodology.

PRSP—Progress in Implementation

We welcome the papers which provide a comprehensive overview of the main issues. We agree with much of the analysis and generally support the conclusions. The main purpose of these annual reviews should be to focus on the actions of the Bretton Woods institutions, to help strengthen accountability and improve performance. There is a lot of valuable material in the background papers, but there is an inevitable risk of the summary report becoming too general. For future reports, we would suggest a more explicit focus on Fund and Bank activity, highlighting strengths and weaknesses in their work in support of PRSPs (for example, in areas such as alignment of lending instruments, capacity building work and management of the PRS Trust Fund). In particular we would like to see more on the IMF's contribution to the PRSP process, particularly on PRGF alignment and the use of PSIA in program design.

On Issues Raised in the Paper:

Annual reports on PRSP implementation are an important opportunity to learn lessons on how to strengthen the role of the PRSP and further embed

it in national policy-making processes. To achieve this national governments must remain in full control of the review process.

We support deeper links between the PRSP and budget processes in-country, and think the Bank and Fund should continue to strengthen this link through capacity building efforts, and PER processes.

Reinforcement of public expenditure management will be critical to the success of the PRSP process. We would welcome a greater role for Staff in outlining action plans in order to bolster public expenditure management and accountability, in which each bilateral or multilateral agency could expand its assistance.

We strongly support donor cooperation, coordination and alignment around these processes, to improve coherence and reduce transaction costs. The Fund and Bank should lead by example in their own practices. Apart from the reference to the SPA and program selectivity, the papers are thin on the Fund and Bank's commitment to working with other donors in support of the PRSP, and future reports should say more.

In a number of areas which are governments' responsibilities (such as participatory processes, and tensions between comprehensiveness and prioritization) the Fund and Bank have an important role to play in identifying and focusing on good practice.

We agree on the importance of PSIA, including as a new opportunity for participation. We agree that PSIA can add to the debate, even where the data is poor: a basic analysis can help identify potential poverty impacts. There is scope for the Fund and Bank, under the leadership of the government, to do much more here.

On macroeconomic policy, we agree on the need for a broader treatment of growth, shocks and macro frameworks in PRSPs. We agree that this will often require support and capacity-building and a more open dialogue on macro policy options, but strongly support Government leadership in this area, with the Fund playing a supporting role. We agree on the need for contingency plans to deal with shocks and for greater realism in growth projections. We would like to see more work on macroeconomic frameworks which encourage and accommodate higher volumes of aid.

Judgments in the JSA, which are clearly internal IFI documents, should not undermine country ownership but should focus on general issues relating to the overall effectiveness of the PRSP and its ability to deliver intended outcomes. They should better reflect the concerns of donors and national stakeholders.

HIPC Progress Report

We welcome the progress that has been made, and look forward to more countries moving to Decision and Completion Points in the near future. We however regret that during FY03 only two additional countries were able to reach the completion point and only one additional country reached the decision point.

The paper suggests that five more countries - Guyana, Niger, Rwanda, Sao Tome and Principe and Senegal - could reach Completion Point this year, with a further eleven in 2004. This is encouraging but one also has to acknowledge that this type of forecast has often been contradicted in the recent past. We welcome the staff's analysis on delays in reaching Decision and Completion Points. The reasons explaining the delay incurred are generally well known, but Staff realized a useful study by highlighting the main obstacles faced in a country-by-country analysis.

We hope the countries concerned will be able to increase their efforts, and urge the Bank and Fund to work intensively in their support. We are reassured that the requirement to implement successfully a PRSP for 1 year is not expected to be a problem for most HIPCs in the interim phase.

We note that the Sunset clause lapses at the end of 2004. We will need to look at this further, without excluding any options ex ante so that countries moving towards HIPC, though not yet within it, are not penalized.

We stress the importance of improving governance and public expenditure and financial management and urge Fund and Bank staff to continue to support countries in this.

On creditor participation, we welcome steps by Libya and India, though regret that others have failed to move in a similar direction. We welcome the information on creditor litigation, but regret that this shows that a number of HIPCs face actions for over \$400m face-value debt. We welcome the work of the IDA-buyback facility in extinguishing commercial debt. We would like to see more active IFI support for countries facing creditor litigation, and we continue to urge staff to explore all the options, including technical assistance, to promote fair and equitable settlement and to prevent damaging litigation. One interesting avenue would be to systematically include a paragraph on participation in the HIPC initiative in Article IV reports and present the reasons given by the concerned country to justify its non participation.

On the issues for discussion, we agree with the points raised by staff.

HIPC: Topping-Up Methodology

We strongly support a change in the methodology for calculating topping-up (by disregarding the additional voluntary debt relief (100 percent) provided by some creditors). This would bring it into line with a key principle of the HIPC Initiative – additionality. When France and the UK, and other governments, agreed to provide 100 percent relief to HIPCs it was intended to be additional to the debt relief already provided under the HIPC framework, and to benefit the HIPC countries, not other creditors. But the current methodology directly undermines this principle.

So we welcome the staff paper. The evidence on the likely impact on debt sustainability underlines the compelling case for a change in the rules. We strongly support option 1. We note that the costs falling to the HIPC Trust Fund are manageable and that any costs to IDA can be addressed in the agreed, back-to-back meetings within the IDA-14 replenishment process.

We hope that there will be sufficient support in the near future to move forward on this issue. However, we note that opinion remains divided and would like to suggest a possible avenue for compromise. Recent experience demonstrates that the probability of a country facing a debt distress situation can be increased when the country has suffered first, from external shocks and, second, is affected by poor institutions and bad governance. Our current topping-up methodology addresses only the first of these items. Would a solution addressing also the second element provide a wider basis for support? Although we are aware that it raises several issues, we would encourage Staff to examine the pros and cons of such a proposal and report to the Board for our next discussion on the HIPC Initiative.

We note the recent steps taken by individual creditors to ensure that their additional bilateral relief goes to the full benefit of the HIPCs involved.

We do not support option 2 and do not find the moral hazard argument persuasive.

Mr. Bischofberger and Mr. Fabig submitted the following statement:

Key Points

We welcome the progress made in implementing PRSPs. We note, however, that macroeconomic projections in the PRSPs continue to be unrealistic in many cases. Furthermore, we are disappointed with the extent to which PRSPs provide guidance for national budget processes. Well-targeted technical assistance could be provided to address this weakness. We would like to stress that it is the responsibility of recipient countries to harmonize aid and to prioritize expenditure.

While we are pleased with the number of successes that have been achieved under the HIPC Initiative, we regret the slow progress of many HIPCs in reaching the decision and completion point. But still, going forward, we would emphasize that quality is more important than quantity. There should be no change in conditionality. We urge countries that have not yet reached the decision point to step up their reform efforts in order to reach decision point eligibility before the sunset clause applies.

We support the proposed decision on the Financing Update. The planned self-financing of the PRGF Trust by 2006 should not be questioned. We are concerned by the new cost estimates for the HIPC Initiative topping up. We note that the cost of Alternative Methodology I is even substantially higher. Obviously, the amounts involved cannot be borne by the IFIs themselves, but would have to be provided by member countries. A final decision on the methodology should be made as soon as possible. But before any decision is made on a change in methodology, the financing of the cost of such a change as well as of the cost of debt reduction for potential decision point countries has to be clarified. We continue to support the current topping up methodology. Creditor participation should be as broad-based as possible.

We thank Staff for a set of very informative papers that provide a comprehensive update on progress in the implementation of PRSPs, on the status of implementation of the HIPC Initiative and on the Financing of PRGF and HIPC operations. We would like to offer the following comments.

Poverty Reduction Strategy Papers – Progress in Implementation

We welcome both the short report on progress in implementation of PRSPs that gives a good overview and the comprehensive supplement paper which provides more detailed information. We share the thrust of staff's analysis and have only a few specific points.

We welcome the progress made in implementing PRSPs. We note, however, that macroeconomic projections in the PRSPs continue to be unrealistic in many cases. The wide-spread overestimation of actual economic growth calls for a more critical assessment by the Fund and the Bank with regard to these projections.

While we welcome the average increase of poverty-related expenditures, we think that this could be the result of some countries performing very well while others stagnate. Therefore, we would be interested in disaggregated data. Staff's comments are welcome.

We continue to be disappointed with the extent to which PRSPs provide guidance for national budget processes. More efforts should be made in this respect. Well-targeted technical assistance could be provided to address this weakness.

On the question of aid and donor alignment and harmonization, we would like to stress that it is the responsibility of recipient countries to harmonize aid and to prioritize its expenditure. Only if carrying out these tasks is severely impaired by weak institutional capacity do we see a role for IFIs and other international bodies which would consist of helping these countries to improve this capacity.

Initiative for Heavily Indebted Poor Countries – Status of Implementation

We very much appreciate the comprehensive HIPC Initiative progress report. While we are pleased with the number of successes that have been achieved under this initiative, we regret the slow progress of many HIPCs in reaching the decision point and, in particular, the completion point. We do hope that the countries mentioned in the report can indeed reach their decision or completion points as envisaged by the end of 2003 or in early 2004. At the same time, this chair continues to emphasize that quality is more important than quantity.

We believe that there should be no change in conditionality with respect to attaining macroeconomic stability, satisfactorily implementing PRSPs and meeting other social and structural completion point triggers, including good governance, even if this results in some delay for countries to reach the completion point. Also, if a PRGF-supported program of a country in the interim period goes off track and does not get back on track, it should remain an option to finally conclude that the completion point was not reached.

On the issue of decision point eligibility, we would like to point out that it is primarily the responsibility of the countries themselves to qualify for the HIPC Initiative. We urge all countries that have not yet reached the decision point to step up their reform efforts and thereby to establish the preconditions for decision point eligibility before the sunset clause applies.

Update on the Financing of PRGF and HIPC Operations and the Subsidization of Post-Conflict Emergency Assistance

We welcome this update. We notice that the financing of the PRGF and the HIPC Initiative is sufficient under the current assumptions, and we support the proposed decision.

Going forward, we reiterate our view expressed in last week's discussion on the Fund's role in low-income countries that the planned self-financing of the PRGF Trust by 2006 should not be questioned. The halving of financial resources associated therewith should be mitigated by the fact that the HIPC Initiative will be quite advanced by that time, thereby reducing financing needs. A progressively lower access PRGF for pre-emerging market

countries, as discussed on the same occasion, should also serve to ease financing pressures for the PRGF Trust.

We are concerned by the new cost estimates for HIPC topping up, in particular when exchange rates and discount rates of June 30, 2003 are applied. The cost of Alternative Methodology I is even substantially higher. It is obvious that the amounts involved cannot be borne by the IFIs themselves, but would have to be provided by member countries—as staff admits. Consequently, we would be interested to learn from staff how much financing could be provided by the IFIs and how much would have to come from member countries if a change in methodology took place. We urge the Bank and the Fund to monitor closely the new borrowings of the HIPCs, also in the context of a possible topping up decision at the completion point, in order to avoid an unsustainable build-up of new debt at an early stage.

We deem it very important that a final decision about the methodology on the calculation of debt sustainability is made as soon as possible. But before any decision is made on a change in methodology, the financing of the cost of such a change as well as of the cost of debt reduction for potential decision point countries has to be clarified. We note that these cost dimensions are surrounded by high uncertainty. In our view, it is very important that a possible inclusion of Sudan, Liberia, Somalia and Laos is taken into consideration, given the cost increase of an estimated 25 percent associated with such an inclusion.

Since we are not aware of any pledges to finance a change in methodology, we continue to support the current topping up methodology. Moreover, we think that the topping up, independent of its calculation, should be granted only in exceptional cases where the underlying cause for the deterioration of the debt situation is an external shock beyond the control of the authorities. Finally, we would like to underline that it is of utmost importance for the effectiveness of the HIPC Initiative that creditor participation is as broad-based as possible. We therefore support all measures that are conducive to including as many creditors as possible and to ensuring a debt relief quota as high as possible.

Ms. Jacklin and Mr. Dohlman submitted the following statement:

PRGF Financing

We thank the staff for the useful documents prepared for today's Board discussion. One of the key issues before us is the adequacy of Fund resources in helping achieve our goals in low income countries (LICs). Some argue that the resources we are devoting to encourage growth and poverty reduction in low income countries are insufficient, especially as additional demands on HIPC and PRGF resources are made by eligible countries

emerging from protracted conflict, such as Liberia. At some point the donors are going to need to engage to conclude the HIPC program for those countries that were never tabulated in the original HIPC cost estimates. This may or may not involve the PRGF, and in fact the entire timing and sequencing of reengagement with such countries remains unclear at this time.

What is clear, however, is that the Board should consider the case of PRGF resources need as a separate question from the potential needs related to reengagement with large arrears cases. On the former, we believe that the most valuable contribution that the IMF can make to macroeconomic stability and growth has little to do with the actual resources that could be lent from the IMF. Rather, we should put more of our energy (including in the proposed staff paper on financing options) into exploring how best to package and leverage the staff's unique ability to deliver high quality technical assistance and policy advice to LICs, and to practice greater selectivity in our PRGF lending. In the competition for scarce donor resources, we would rather not have the IMF competing for resources against alternative uses, such as grants. We would certainly not be supportive of efforts to tap GRA resources to increase the size of available PRGF resources, which would raise a host of difficult policy problems.

Additional Debt Relief ("Topping Up")

We have always supported the agreement that additional debt relief can be provided on a case-by-case basis when exceptional exogenous shocks have caused a fundamental change in a country's economic circumstances. In its information paper to the Board, the staff estimates that the potential overall costs of "topping up" would more than double from \$567 million to \$1.3 billion under the most recent exchange rate and interest rate assumptions. This is quite worrisome.

This points to the need for extreme caution in considering any adjustments in our policies, such as the suggestion that we exclude additional bilateral debt reduction when debt ratios at the Completion Point are calculated ("Alternative Methodology I"). We do not support this approach for a number of reasons. First, it would misrepresent the actual debt of the country and would support the wrong incentives by keeping the focus on more debt relief, when a broader development focus on good policies and the provision of new assistance on appropriate terms is needed. Other problems with this approach are that it could divert resources from the core HIPC program, as well as non-HIPC low-income countries, which we note seem to have—on average—higher debt burdens than do the HIPCs after they received HIPC debt relief. The projected potential overall costs of this "alternative" would exceed \$3 billion based on the most recent exchange rate and interest rate assumptions (of which the Fund's share would be \$350 million). Moreover, the forgiveness of recent loans that could occur under this

methodology is a tremendous moral hazard, a questionable input for monitorable results-based outcomes, and a very expensive competitor for scarce donor resources.

The fact that an alternative topping up methodology which excludes new borrowing results in virtually no topping up costs is quite enlightening. It underscores the importance of recognizing the exceptional nature of possible topping up and the importance of tying it to shocks, which are outside the control of countries, rather than to actions more directly under the control of countries, such as new borrowing.

In a broader context, we caution against drawing a misleading causal link between debt reduction and debt sustainability. Debt relief alone cannot guarantee debt sustainability, much less fiscal sustainability without the need for long-term dependence on foreign assistance flows. We must give greater attention to the broader development agenda that lies beyond debt relief. This is the best thing we could do to ensure the success of the Initiative and help LICs reach our common goals. We encourage the staff to move quickly in its related work on debt sustainability in LICs.

HIPC Initiative Effectiveness

We share the views expressed yesterday by the U.S. Executive Director at the World Bank at that institution's Board discussion of the joint HIPC status report. We will not repeat those more lengthy remarks, but in summary, the report would benefit from inclusion of the findings of the OED review, including: (1) highlighting the risk of promising outcomes that the HIPC Initiative cannot—due to its multiple objectives—deliver by itself; and (2) that it is vitally important to maintain standards for HIPCs' policy performance and for achieving completion points, in order to achieve and maintain the HIPC Initiative's objectives. We agree with Mr. Zoccali and Mr. Vogel that we should not sacrifice ownership and quality for speed.

Other

We thank the staff for its ongoing work in encouraging greater HIPC creditor participation. Like others, we welcome evidence suggesting that HIPC savings are broadly associated with substantial increases in poverty-reducing expenditures. We join others in urging stronger efforts to ensure realistic projections, and to better align PRSPs and PRGFs, in line with the views expressed at last April's Board discussion.

Poverty Reduction Strategy Papers: Progress in Implementation and Detailed Analysis of Progress in Implementation

Our more detailed views on the PRSP process were outlined yesterday by the U.S. Executive Director at the World Bank meeting on this joint paper. We briefly mention some of the key points. We acknowledge the progress that has been made on PRSPs since the last discussion. We particularly welcome the increasingly active role of the private sector in the PRSP process and encourage even more on this front. Other improvements in the overall quality of these documents should also be made. In particular, PRSPs should do a better job of identifying and prioritizing sources of growth, setting and achieving measurable objectives, addressing governance and corruption issues in coordination with the World Bank, and strengthening public expenditure management. It might be useful for IMF Resident Representatives to engage in some limited form of feedback early in the PRSP process on the realism of assumptions and the implications of PRSP plans for macro stability. But we should ultimately hold countries accountable for their strategies. We agree on the importance of PSIAs. Finally, we share sentiment expressed by Mr. Daïri and others that we should guard against the PRSP process becoming so extensive and involved that it overloads the implementation capacity of officials.

Mr. Duquesne said that he wanted to clarify the proposal that he and Mr. Scholar had made in their joint statement. Empirical analysis had demonstrated that the probability of a country facing a debt distress situation increased when the country was affected by an external shock, but also when it suffered from poor policy performance related to institutional weaknesses and poor governance. The current topping up methodology addressed only the consequences of exogenous shocks. To reduce the probability of a country suffering from unsustainable debt, the second aspect—governance—should also be dealt with. From that perspective, his and Mr. Scholar's proposal was to link the benefits of an exclusion of additional bilateral debt relief in the calculation of the debt ratio at completion point (methodology 1 in the staff report) to the existence of a good track record in terms of governance. Thus, the new methodology for calculation of topping up could become a good incentive for countries not only to address the issue of governance in their PRSPs, but also to effectively implement their programs. It should be noted that the proposal would impose new conditionality, since all HIPC countries suffering from exogenous shock would continue to benefit from the current topping up methodology. The point was that, to benefit from the new and more generous methodology, HIPC countries would have to demonstrate some achievement in terms of governance. That proposal might break the stalemate on the new methodology for topping up, by closing the bridge between those countries that favored the change, and those countries—including France and the U.K.—who opposed it. Of course, it was a preliminary proposal that would need to be studied by the staff, refined, and discussed further.

Mr. Ondo Mañe thanked the donor community for the assistance provided to countries participating in the PRSP and the HIPC processes. He welcomed the statements issued for that day's discussion, in particular the joint statement by Messrs. Duquesne and Scholar. The authorities of low-income countries were aware of the daunting challenges that they were facing, and were hopeful that they would continue to rely on the donor community's policy advice, technical assistance, and financial support. However, while progress was being made toward the improvement of ownership of programs, the success of the PRSP and HIPC operations would also depend on donor cooperation and coordination of assistance.

Mr. Daïri said that he supported the interest expressed by several Directors, including Messrs. Duquesne and Scholar, in ensuring broad participation of all creditors in the HIPC Initiative. However, he did not support going as far as asking potential donor countries to explain, in the context of Article IV consultations, why they were not participating in the HIPC Initiative. That would be the same as asking countries to justify why they did not raise their official development assistance to the level proposed by the U.N., or why they did not contribute to PRGF financing. It should be remembered that participation in the HIPC Initiative was a voluntary endeavor and that the Fund should not be overly intrusive in countries' sovereignty.

Mr. Bischofberger remarked that, while he did not yet have a firm view on the proposal made by Messrs. Duquesne and Scholar, it certainly deserved to be elaborated and discussed further.

Mr. Lombardi noted that he also found the preliminary proposal put forward by Messrs. Duquesne and Scholar interesting, and deserving of further exploration ahead of the next Board meeting on the HIPC Initiative. To stimulate further debate on this proposal, the staff should explore, in particular, its consistency with the overall Initiative in terms of equity, and how it might be implemented from an operational perspective.

Mr. Miyoshi said that he wanted to comment on the issue of macroeconomic dialogue and Fund engagement in the participatory process. Since the PRSP was a country-oriented initiative, he shared the staff view that governments, and not the Fund, should take the lead in the macroeconomic discussion that should take place during the participatory process of the PRSP. At the same time, however, because macroeconomic discussions required substantial expertise, it could be a significant challenge for the authorities to provide a forum for such dialogue. Given their limited capacity to do so, the Fund staff should be willing to help the authorities in that regard.

The Deputy Director of the Policy Development and Review Department (Mr. Allen) made the following statement in response to questions and comments from Executive Directors:

The intention following this meeting will be to revise the two PRSP papers and the HIPC paper in the light of remarks made by Directors, both here and at the Bank Board, and to issue these papers to the IMFC and to the

Development Committee. They will also be published on the web at the same time. The paper on HIPC-PRGF financing will be published on the web in the normal course of events. The staff does not recommend at this time to publish the paper on topping up.

Directors at the Bank Board had a couple of suggestions, which received quite strong support, on things that they would like to see changed in the papers. First, a number of Directors called for inclusion of alternative macroeconomic scenarios in PRSPs. As I understand the results of the discussion in earlier Board meetings here in the Fund, there is no objection to having more than one scenario in a PRSP. However, the Fund Board has underscored that such scenarios need to be rooted in a realistic assessment of resource availability, and that multiple scenarios should not just be used to avoid having to make tough decisions on how to use limited resources. Subject to Directors' views today, we will be making some changes in the paper along these lines.

Second, a number of Bank Directors felt that the paper on the HIPC Initiative should make reference to the results of a study on the Initiative recently conducted by the Bank's evaluation department (OED). That report was also circulated to the Fund Directors for information. It made a number of recommendations about the HIPC process, and those would be reflected in the revised version of this progress report that will go to the IMFC and to the Development Committee.

On the PRSP paper, Mr. Ondo Mañe asked how realistic it was to align PRSPs with the MDGs, given the current financing uncertainties. Our view is that this is realistic. What is important is that PRSPs be based on existing capacity and financial constraints, but set out credible plans, policies, and financing that would alleviate those constraints and lead to more ambitious outcomes—including, where possible, the achievement of the MDGs. It will be important to keep plans ambitious yet realistic. We hope the PRSP can be used as a vehicle to allow countries to mobilize the financing for achieving the MDGs, by identifying clearly the obstacles that need to be overcome to do so.

Mr. Marti and Mr. Siman asked the staff to comment on why, despite some evidence of increased attention in PRSPs to identifying sources of growth, the choices of priority actions are not often derived from those identified growth sources. It is important to keep in mind that we are at the start of a process, and that progress will necessary be incremental. It is very encouraging that PRSPs are showing increased attention to identifying sources of growth. However, we also have to recognize that PRSPs are the result of a consultative and participatory process, and thus do not always relate perfectly to identified constraints to the growth process. Nevertheless, we hope that, as

time goes on, the priorities of the authorities will become more and more closely aligned with measures needed to foster higher growth.

Mr. Reddy wondered why there was a poor track record of country authorities taking the lead in donor coordination. There are problems on both sides here, I suspect. On one hand, there is a wide variety of donor requirements, which creates difficult coordination problems for countries. On the other hand, the countries themselves often have fairly poor institutional capacities for dealing with the complexity of these requirements. We are working together with the DAC and others on the issue of the harmonization of donor requirements, to try to improve coordination from the donor side. We are also trying to do what we can to improve capacity inside the countries. We hope that, over time, we can see countries taking more of a lead in the process of coordinating donor assistance. That is certainly the objective.

Mr. Bischofberger and Mr. Fabig requested disaggregated data on poverty-reducing spending. Table 5 of the HIPC background paper contains some data, but it does not cover all PRGF countries, and in some cases the data is only a subset of data for poverty-reduction spending. The Fiscal Affairs Department has been working on identifying spending patterns, and we will be passing on your request to them so that in the future we can provide better data.

On the HIPC paper, the sunset clause of the HIPC Initiative stipulates that the Initiative will expire at the end of 2004. That clause was established to prevent the Initiative from becoming a permanent facility, and to encourage heavily indebted poor countries to adopt adjustment and reform programs as rapidly as possible. It is not a deadline for countries to reach decision point. It is a deadline for countries to start showing that they are establishing a track record of policies, under post-conflict or PRGF-supported programs, which will allow them to utilize the facility. Those countries that have started establishing a track record by the sunset date could still reach the decision point, and then the completion point, following the sunset. We plan to come back to the Board in plenty of time before the date of the sunset to review the options at that point for any heavily indebted poor countries which have not yet qualified for the Initiative.

The staff representative from the Policy Development and Review Department (Mr. Wang) made the following additional remarks:

There were four main questions from Directors, which I will attempt to answer.

First, on whether additional HIPC Initiative relief comes at the expense of resource flows to other non-HIPC low-income countries, preliminary data from the OECD indicates that gross and net resource flows to

developing countries—including to the HIPC—declined in the second half of the 1990s, but recovered somewhat in 2002. In the HIPC paper, we show that net resource flows to the 27 HIPC countries that have reached decision point certainly increased after their decision points. Therefore, it is possible that those HIPCs committed to reform and poverty reduction are benefiting from an increasing share of aid flow. This is also consistent with the fact that many donor countries are applying increased selectivity to their official development assistance allocations, and are increasingly rewarding countries for good performance and good governance.

Second, on whether optimistic projections on exports, growth, and revenue in PRGF-supported programs explain the difficulties faced by some countries in keeping their programs on track, one should note that, typically, in Fund-supported programs, there is a built-in adjustment mechanism to respond to potential exogenous shocks. Moreover, performance criteria are usually set for the next program review and not for a very long period. It is also useful to note that many of the fiscal slippages that we have reported occurred on the expenditure side, or in countries that experienced difficulty in tax collection, rather than because of shocks. Having said that, more efforts are certainly needed to improve projections in low-income countries, including HIPCs, and work is under way in that regard.

Third, on whether progress has been made in terms of reducing creditor litigation against HIPCs, the 25 cases reported in this paper are the same that were reported in the 2002 paper. Of those, four have been resolved, and one case has resorted to an out-of-court settlement. Therefore, it appears that there is some progress.

Finally, on why the cost estimates of the HIPC Initiative have not shown a greater increase despite low world interest rates and low export growth in HIPCs, there are two factors: First, the HIPC Initiative cost estimates are based on debt relief commitments made at the decision point, based on the DSA at that time. They do not include topping up costs, unless those costs are identified. So far, Burkina Faso is the only case where topping up—amounting to U.S. \$139 million dollars—was identified. Second, the impact of changing world interest rates, exchange rates, and low growth shocks to HIPCs would be taken into account in the DSA at the completion point, based on actual information available at that time. If more topping up cases are identified, then, of course, the total cost of the Initiative will increase.

Mr. Daïri said that he had asked whether additional HIPC relief was at the expense of resource flows to non-HIPC low-income countries because he felt that, in that case, it was not appropriate. Some non-HIPC low-income countries embarking on adjustment and growth programs were also in need of resources, and they should not be penalized for having lower levels of debt. Moreover, there seemed to be a problem of definition for official development

assistance. For example, fishing royalties for Mauritania were considered as official development assistance, rather than payment for a service or for exploitation of resources. That was an issue that needed to be looked into and resolved to ensure equitable treatment for all low-income countries.

The staff representative from the Finance Department (Mr. Lin) made the following remarks:

I am pleased to report that, since our paper on PRGF-HIPC financing was issued, Fiji and Tonga have made their contributions to the PRGF-HIPC Trust effective. We will ensure that these contributions will be reflected in the paper for publication.

On the availability of resources for post-conflict emergency assistance, the staff estimates that subsidy requirements could amount to about 5 to 6 million SDRs through end-2004. This estimate already assumes that some countries might come forward requesting such assistance during this period. The current resources available amount to about 10 million SDRs, which are roughly twice the estimated need. Of course, should the need exceed the resources available, it will be necessary to mobilize additional resources.

The issue of repurchase terms for post-conflict emergency assistance was discussed intensively by the Board in 1999, when the post-conflict emergency assistance policy was reviewed. On that occasion, Directors were of the view that providing subsidies to reduce the rate of charge to 0.5 percent per annum, and resources through the PRGF above the normal access to allow countries to make early repurchases, would be effective ways to provide assistance to post-conflict countries. And indeed, since 2001, the lending rate to all seven post-conflict countries has been subsidized. Moreover, two cases were provided with higher-than-usual PRGF access, to allow them to make early repurchases; and five countries were able to move to PRGF arrangements within about a year.

Mr. Andersen made the following statement:

I thank the staff for an interesting and well-written set of papers for today's discussion. My intervention will cover three areas; financing issues, status of HIPC implementation, and lastly progress in PRSP implementation.

On financing issues, I agree with staff that the resources available in the PRGF and PRGF-HIPC Trusts are at the moment sufficient for financing PRGF and HIPC operations, including topping-up under the current methodology. I also support the proposed decision on the adequacy of balances in the Reserve Account of the PRGF Trust. However, a number of pending financing issues are looming. First, the envisaged annual commitment capacity under the self-sustained PRGF is much lower than the historical

average of the PRGF lending capacity. Second, the possible entry of protracted arrears cases into the HIPC framework would require a considerable amount of new resources. The third pending financing issue, one on which I hope the international community will soon come to a new conclusion, is the question of methodology used to calculate topping-up assistance. Here, I would like to thank staff for providing us with the paper on the calculation of completion point topping-up we have requested earlier. Even though the topping-up paper is not formally on the agenda today, I would like to touch upon a few issues raised in the paper. I still believe that additional bilateral debt relief beyond HIPC relief should be excluded when calculating topping-up assistance in order to avoid that some creditors subsidize others and to provide an extra cushion for eligible countries. Thus, my preferred option would be to change the current methodology for calculating debt sustainability at the completion point. Of course, one way to address these concerns is by “unilateral action”, as staff have labeled an option where a country informs IDA and the Fund that it will decide about additional relief only after the completion point. This option has the same effect as the Alternative Methodology I, but it is, of course, inferior to a concerted effort to address the shortcomings of the current methodology. In our constituency, Norway has taken this so-called “unilateral action” and is now excluded from the topping-up calculations at our Norwegian authorities’ request.

On creditor participation, I agree with Mr. Padoan and Mr. Lombardi that our aim is to achieve full creditor participation and that we should keep exploring all available options to get all creditors on board. While I think Mr. Daïri has a point when he cautions against overloading the Article IV consultations, I hope that the upcoming meetings in Dubai provide opportunities to follow up on creditor participation issues.

Let me now turn to the HIPC issues. I welcome the steady implementation of the HIPC Initiative, even though the progress has been slower than anticipated. It is worrying that only half of the countries currently in the interim period have a satisfactory performance record under their respective PRGF programs. On a more positive side, the countries that have reached the decision point have already seen an improvement in their debt indicators. I find it encouraging that all the twenty-seven countries, which have reached the decision point, are now spending considerably more on poverty-reducing measures than on debt-service payments. For decision point countries, the ratio of poverty-reducing expenditure to GDP is at the moment around 9 percent. Looking also at other aggregate indicators, one gets quite a positive picture of the progress made.

I would, however, caution not to make very general and far-reaching conclusions based on the so-called “average” performance alone, as it masks a somewhat uneven progress. For example, the 9 percent average of the ratio of

poverty-reducing expenditure to GDP, which I just mentioned, hides the fact that there are considerable differences at the country level. In 2003, the ratios of poverty-reducing expenditure to GDP range from 0.7 percent in the Democratic Republic of Congo to 26.6 percent in Sao Tome and Principe. In addition, definitions of poverty-reducing expenditures vary across countries complicating the comparisons even more. Here, I would like to thank staff, who have done a good job on various tables and annexes in trying to highlight the differences at the country level.

With regard to the sunset clause of the HIPC Initiative, I believe that it would be advisable to establish transparent criteria for exceptions to the sunset clause when the time is ripe, rather than to rush these countries through the decision point.

Finally, on the PRSP papers, I think it is promising to note that almost all interim period HIPCs have prepared full PRSPs and are now implementing them. There is, however, significant room for improvement in several areas before we can say that the PRSP process is a fully effective and integral part of HIPCs' policymaking. I would like to draw attention to a few areas, which I think are among the most important ones.

First, PRSPs tend to have too optimistic growth projections. I believe that it is important to be both ambitious and realistic in order to set the bar high enough but at the same time be mindful of not creating expectations that cannot be fulfilled. Also, it seems that unrealistic targets can lead to weak prioritization, a point emphasized by staff. Mr. Ondo Mañe refers to a contradiction between having realistic projections and making progress towards the Millennium Development Goals. Obviously, we should not bridge the gap between realistic PRSP targets and the Millennium Development Goals by making the targets overambitious and unrealistic, but I agree with staff that presenting those gaps gives an opportunity for various stakeholders to discuss actions needed to meet the long-term objectives.

I would also argue that it is important to make sure that the macroeconomic framework is fully embedded in the PRSP. I agree with staff that PRSPs should take better into account macroeconomic trade-offs and how such choices relate to the country's broader goals. In this regard, increased attention to sources of growth is welcome.

Second, in country discussions this chair normally takes up the importance of public expenditure management, and I want to reiterate once again that adequate public expenditure management is a key in ensuring that the HIPC Initiative resources are properly spent. The staff assessments of public expenditure management systems in HIPCs show that the quality of public expenditure management remains a serious concern, as out of 24 countries 15 countries require substantial upgrading of public expenditure

management systems. So this is an area where the room for improvement is quite significant.

This brings me to a related issue, namely improving governance in HIPC's. Good governance is imperative for achieving macroeconomic stability and fundamental to progress both in the public and private sectors. The importance of good governance and anti-corruption measures cannot be emphasized enough. These are key elements in any strategy for achieving pro-poor growth.

Finally, I would like to mention that the Nordic countries have made their own review of the PRSP process in some of the HIPC countries. The review has also been made available to staff. One of the objectives of the review was to strengthen donor coordination and support to the PRSP process at the country level. Concerning donor coordination, the review found out that the existence of the PRSP seems to promote an impetus for enhancing donor coordination by creating a framework for donor coordination systems and activities. However, like in other areas, there is still room for improvement, and I agree that donor alignment and harmonization around PRSPs must be improved. I also share Mr. Duquesne and Mr. Scholar's view that the staff reports are thin on the Fund and Bank's commitment to working with other donors in support of the PRSP, and I agree that future staff reports should say more on this.

Mr. Nijssse made the following statement:

I welcome the report on PRGF financing, and I agree to the proposed decision that there are adequate balances in the reserve account of the PRGF trust to meet all obligations to the lenders to the loan account in the upcoming six months. I would, however, like to make one remark about the financing of PRGF lending. The staff document notes that staff has begun to examine other financing options that would allow the PRGF lending capacity to reach close to historical levels after 2005. We recently had a discussion on the role of the Fund in low-income countries where it became clear that there is quite a number of Directors who are not convinced that there is a long-term financing role for the Fund in those countries. We should first discuss the Fund's role—including the possibility of longer-term economic programs without large Fund financing, such as under precautionary arrangements or low access PRGF-support—before trying to assess how much money will be necessary to finance the PRGF after 2005. Discussing options while assuming that the capacity should remain at the current level is not realistic.

On topping up under the HIPC Initiative, I welcome very much the additional calculations done by staff to show the cost of the different topping up methodologies, something we have asked for several times in the past. Our chair would be prepared to consider adopting alternative methodology 1,

which excludes additional bilateral debt provided from the topping up calculations, if two preconditions are fulfilled: first, there needs to be an appropriate burden sharing of the extra cost of the topping up; and second, the financing of the cost of this option for the IFIs should be secured ex ante. The IFIs should not end up with an open-ended bill. As to whether the application of this alternative should be linked to a track record on improved governance, that is an interesting option which we should consider.

With regard to alternative 2, we can see from the calculations done by the staff that, for many countries, taking up new IFI loans after the decision point has contributed greatly to a lack of debt sustainability at the completion point. The lesson is that many HIPC countries should only receive grants, particularly if financing is required to address economic shocks in the interim period. This also brings me back to our recent discussion on the role of the Fund in low-income countries. After an initial stabilization phase, the Fund's role should not always be a financial one. The Fund should not automatically fill gaps that donors leave open with relatively expensive short-term credits.

On the PRSP, I have three points: First, the progress report gives a very good description of the dilemma between the ambition of reaching the MDGs and the usefulness of making an economic program that can be financed. Second, I agree with the staff that we should have realistic expectations about the pace and scope of PSIAs, though this should not be a reason for restraining from further work in this area. The IMF continues to have a role to play in assisting countries in the implementation of PSIAs in the macroeconomic area, especially regarding fiscal policy matters. Finally, more outreach with civil society partners might sometimes be necessary to achieve a meaningful link between the PRSP process and the PRGF program framework. While Fund missions have limited capacity, more work could perhaps be done in that regard.

Ms. Gust made the following statement:

We thank the staff for its report on the status of implementation of the HIPC Initiative. The paper clearly demonstrates that the Initiative is making a significant contribution to debt relief for the poorest countries. Like other Directors, we particularly welcome the information that HIPC debt relief has indeed been additional to other forms of financing assistance. We also underscore the importance of governance and ownership and reiterate the need for full creditor participation in the Initiative.

I would particularly like to associate myself with the statement of Mr. Ondo Mañe, Ms. Indrawati, and Mr. Andersen's emphasis on the importance of good governance; the call by Messrs. Padoan and Lombardi for the staff to continue to gain more knowledge on political economy issues; Mr. Duquesne and Mr. Scholar's useful suggestions on how the annual reports

can be more focused; and Ms. Jacklin and Mr. Dohlman's point that the report would have benefited from the inclusion of the findings of the recent OED point. On this last report, I thank Mr. Allen for noting that the OED findings will be included in the revised version of the staff report.

Let me turn to the substantive issue of topping up. It should come as no surprise that Canada continues to support changing the topping up methodology to exclude additional bilateral debt relief in order to provide the most generous relief for all countries, and not subsidize other creditors as was originally intended. Eligibility for topping up should continue to be determined on a case-by-case basis, including with due regard to performance in the area of governance. The cost of topping up would need to be addressed, including within the context of IDA 14 discussions. However, given the sensitivity of the total cost to exchange and discount rates, and that it is subject to revision when countries reach completion points, it is clear that the issue of additional cost cannot be fully dealt with at the current time. Nonetheless, the objective of ensuring a lasting exit from unsustainable debt would be facilitated by this change in the methodology. Given the mixed support for topping up, this issue will clearly be around for some time and I want to make three brief comments on moving forward.

First, it would be helpful to once again take a close look at the debt sustainability of post-completion point countries. I suspect that significant changes in interest rates, the value of the dollar, and economic prospects would have some important impact on debt ratios and could give us further clues on the extent to which topping up—and what specific type of topping up—would be most appropriate to ensure a lasting exit from unsustainable debt.

Second, very much in the same vein, previous reports have provided updates on efforts to enhance HIPC's capacity for external debt management, an important element in achieving and maintaining lasting debt sustainability. The upcoming workshops and the joint Fund/Bank report to be presented in December of this year on policy and operational options for long-term debt sustainability in low-income countries can help to fill this void. In this respect, I wonder whether staff could comment on whether they envision that the outcome of this December's report is likely to bring any changes to the HIPC Initiative, or on how it could influence the debate on topping up.

Third, Mr. Duquesne and Mr. Scholar proposed that we explore ways of requiring improvements in governance in return for granting more generous topping up by disregarding the additional voluntary relief provided by some creditors. To the extent that this avenue broadens support for the more generous topping up methodology, we support more work on this front.

The second topping up option presented in the staff paper—alternative methodology 2—provides interesting empirical evidence on how large new borrowing is for some countries between the decision point and the estimated completion point. We do not support the idea of excluding all borrowing in determining the amount of topping up. That seems like a far too crude methodology, and may not create the right incentives in terms of discouraging excessive borrowing. We are particularly concerned about borrowing outside the IFI framework, especially on nonconcessional terms. To the extent a country does undertake nonconcessional borrowing outside of the framework agreed to by the IMF and World Bank, this should certainly be taken into account in considering if, and to what extent, topping up is warranted. In this respect, the analysis provided in the paper would have been more interesting if a breakdown was provided on which creditors loan to the countries, and on what terms. To the extent that significant borrowing from IFIs worsens the debt ratios, this underscores the need for IFIs to continue the work discussed this spring on aggregate borrowing limits, and try to move to the greatest extent possible from debt to grant financing.

On the sunset clause, we are glad to hear from Mr. Allen that we will be reviewing the sunset clause later this year or possibly next year.

On the PRSP papers, I thank staff for both the summary and the more detailed progress report on the implementation of the PRSP approach. The papers clearly show that overall progress on PRSPs has been considerable, within a relatively short period of time, but they also rightly identify a number of important issues that still require attention. We have already issued a detailed written statement for yesterday's meeting at the World Bank which I will submit for the record, and pass on to staff. I will not repeat the points made there. Instead, I propose that three issues be examined in greater detail for the next report: First, the tension between the desire of donors and IFIs to have a detailed PRSP, versus the desirability of producing a simple document accessible to the general public, and that can help build an understanding of policies, and ultimately, ownership. As it stands, the balance has been clearly tilted in favor of satisfying the demands of the donor community, with little hope that ordinary citizens will understand or relate to these intimidating documents. Since donors are unlikely to be satisfied with anything less, what the Bank and Fund can do is to identify best practices in how to supplement the I-PRSPs, PRSPs and PRSP progress reports, with documents and other forms of communication to explain the policies detailed therein. That should be done not only through translating the documents and posting them on the Internet, but also by supplementing these cumbersome documents with greatly simplified booklets and verbal presentations, given at various levels of sophistication. These could be disseminated early in the consultation process and continued to be adapted as the PRSP is implemented and as progress reports are made. Staff have already broached this issue in past reports, but it needs to be pursued in a much more systematic way in future reports. The

PRSP process will be ongoing for many years and for many countries, and we need to continue to examine ways to improve it.

The second suggestion I would like to make is the role of the resident representatives be enhanced. They should take on a special role in helping to build ownership by educating the public on the macroeconomic issues that need to be confronted in designing a poverty reduction strategy. I have heard through anecdotal reports that in some countries resident representatives plays a tremendously useful role in helping people understand these macroeconomic issues. For example, I have heard that some resident representatives regularly lead seminars at universities or provide informational web sites. In contrast, I have also heard that in other countries resident representatives tend to focus more efforts on building their golfing skills. Resident representatives have an important role to play, and probably one that is a little more proactive than suggested by paragraphs 49 through 51 of the summary document.

My third and final suggestion of what could be examined in more detail in future reports is donor alignment and harmonization. The paper suggests that considerable progress has been made on this front. However, I have heard some argue that much of this progress has been “window dressing” and that, in fact, the PRSP process has not led to much harmonization. I wonder whether staff could identify more objective measures to determine the extent to what extent donor alignment and harmonization has occurred. For example, staff could produce data on the extent of PRSC cofinancing. Objective measures such as this could help increase peer pressure for further donor alignment and harmonization.

Here is my statement at the World Bank:

“We appreciate the cogent analysis and focused approach that has gone into both the summary and more detailed report by World Bank and IMF staff as to progress made in the implementation of Poverty Reduction Strategy Papers (PRSPs). While the reports identify a number of important issues that still require attention, overall progress on PRSPs has been considerable within the relatively short period of time since their introduction. Moreover, we agree that the PRSP continues to evolve in several important and fundamental ways and that it must be seen not as a static document but as part of an ongoing process. In particular, paragraph 43 reminds us that PRSPs have shifted from being narrowly focused on how spending could increase in light of debt relief, to being much more comprehensive documents based on stronger country ownership. This evolution in the process, increasingly based on CDF principles and the Monterrey Consensus, has created a number of the tensions identified in the paper before us. And there is no one formulae for resolving such tensions as countries continue to adapt the PRSP process to their own context. We note with some concern the questions raised about the relevance of the PRSP Progress Reports for governments in the absence of specific

imperatives such as new PRSCs and PRGFs and will appreciate future assessments of how to maintain the momentum on PRSP implementation. This in fact underscores the importance of ensuring that PRSPs are seen as country-owned and driven; are integrated within existing structures and processes, and are seen to play a central role in government decision-making.

The Bank and IMF will need to continue to play important support roles through its ESW and local capacity building efforts to strengthen the PRSP process and through the sharing of "best practices" gained from its international experience. Given issues raised in the report, a particular emphasis by World Bank and IMF staff seems warranted in helping countries to balance comprehensiveness with the need to prioritize; to identify expected outcomes and results and related indicators against which progress can be assessed and to strengthen the linkages between the PRSP and the annual budget and MTEP processes. We welcome as well the attention given by the World Bank in its lead role in assisting countries in the distributional analysis of reforms to inform PRSP design and the work being done to assess the pro-poor growth dimensions of the PRSP process. The papers would have perhaps benefited from a treatment of the "external" implications for the Bank and Fund work with other development partners under the PRSP framework, such as the UN agencies and regional development banks.

Specific Comments:

Participatory Process and Ownership

There is concern that the role of Parliament is being undermined in the participatory process. As the sole representative body with a legal mandate to hold the government accountable for poverty reduction strategy (PRS) implementation, parliamentary structures should sit at the apex of PRS monitoring structures.

Macroeconomic Policies and Growth

Governments should lead discussions on macroeconomic policies. PRSPs will increasingly need to deepen their attention to sources of growth and better integrate issues related to the impact of trade liberalization. Staff efforts to build capacity in these domains are appropriate, with courses, workshops, and regional technical assistance centers structured in a way that supports the national budget and the PRSP consultative processes.

Realism in growth projections is needed. Many PRSPs contain projections that exceed the country's average growth over the previous 5 years. Overoptimistic growth projections may harm growth prospects by instilling complacency about the adequacy of existing policies and institutions.

While PRSPs should be anchored directly to a realistic macroeconomic framework, we would find it useful for PRSPs to include alternative scenarios, based on a sensitivity analysis, thereby building in more flexibility to changing circumstances. Is there scope for staffs to provide assistance, by way of technical assistance or capacity building, in order to facilitate the inclusion of alternative scenarios?

Budget Process and Public Expenditure Management

We fully agree with staffs that improvements in public expenditure management (PEM) are critical and will take time. The document notes that there are several cases where Ministries of Finance have not been fully engaged in the PRSP process. We feel that this seriously jeopardizes the principle that national governments own their poverty reduction strategies. In this context, we agree with the observation in paragraph 14 that the annual budget is where the appropriate balance between optimism and realism has to be struck as the PRSP is operationalized.

Donor assistance to strengthen budgetary and PEM systems tends to be fragmented with multiple small projects. Consequently, systems tend to lack integration with only limited performance improvements being made. This situation could be significantly improved if Bank officials were to take the lead in encouraging both recipient governments and donors to take a more programmatic, less project-oriented approach to strengthen the capacities of Ministries of Finance.

Progress and Harmonization

Acceleration of the PRSP process that comes at the expense of decreased country ownership and donor coordination/harmonization is clearly undesirable.

Coordination of donor assistance can be enhanced through (a) better coordination at both the institutional and policy level; (b) gathering and sharing data; (c) strengthening monitoring of donor conditionalities and their implementation; (d) regular report cards on aid portfolios; and, (e) sensitizing development partners to the need to move away from project-aid to more liquid forms of aid. We would support Bank and Fund staff taking a more active role in building country capacity to coordinate assistance of development partners.”

Mr. Callaghan made the following statement:

The progress report on the PRSP is comprehensive. It illustrates that progress continues to be made, and raises some important challenges in the implementation of PRSPs. One of the most telling comments in the report is the statement that the PRSP is an instrument being charged with multiple

objectives, many of which imply tensions. I think that tension is a theme that comes through in this report, and it is a point that Ms. Gust has already commented on, and one I would like to pursue. Some of the tensions identified are long-term ambition versus budget constraint or realism, comprehensiveness versus focus or prioritization, meeting international community expectations versus country ownership, and broad versus deep participation in the preparation of PRSPs. What is not really covered in the report is how to balance these various tensions within the PRSP, a point raised by some other Directors.

Perhaps in order to do so there needs to be a clearer idea as to what a PRSP is attempting to achieve—a clearer idea of its basic purpose. Experience shows that, in order to address tensions when they arise, it is always good to have a basic framework or a fundamental objective to fall back on. The IEO issues paper for the forthcoming evaluation of the PRSP notes that, while stating that the ultimate goal of the approach to low-income countries is poverty reduction and the achievement of international development goals, the policy framework does not spell out the objectives of PRSPs. As the IEO notes, what is outlined when describing PRSPs are process requirements. The process requirements are that the PRSP should be country driven, results-oriented, have a long-term perspective, and include a partnership with all stakeholders. In all respects, the staff's progress reports focus on these process requirements or intermediate objectives rather than how the PRSP is measuring up in helping to achieve some fundamental objectives. Hence, as noted, to help address the many tensions that have been identified, perhaps we have to have a clearer understanding as to what is the basic objective of the PRSP. For example, if we are looking for a detailed planning document which fully articulates the proposed road map to development, provides itemization of resource requirements, fully articulates the challenges confronted with alternative approaches should events turn out differently, then a detailed lengthy document is required. In many respects, it is a technocrat's document. But if the objective is to involve as many people as possible and explain the key policy steps necessary to reduce poverty, to help set the scene for developing the necessary consensus to support some fundamental changes rather than detailing all those changes, then the focus is likely to be more on clarity, participation, and communication, and perhaps less on detail, prioritization, costing, distributional analysis and alternative strategies. It would be more a people's document rather than a technocrats document.

What should the basic objective of a PRSP be? Or in other words, where should the emphasis go in handling the various tensions in the PRSP instrument? Some Directors have indicated where they think the emphasis should lie, and Ms. Gust has already made a suggestion on the question of trying to turn a technocrat's document into a more of a people's document. But the most fundamental criteria should be that the PRSP be as useful as possible for the country concerned. One of the key concerns is that the PRSP

may be predominantly seen as a hoop through which the international community makes low-income countries jump. The process requirements for this hoop are specified in Washington. You sometimes wonder when you see a 200-plus page PRSP if the document is really useful for the country. It might be a very comprehensive document, prioritized, costed and containing well-articulated alternative strategies. However, for all its polish, if it was prepared by a self-contained PRSP unit with the help of consultants and Fund/Bank staff, and not really owned by the government and seen as truly forming part of the country's decision-making process, it is unlikely to be particularly useful.

Such concerns increase when you read in the staff paper that the lag in preparing PRSP progress reports in a number of countries raises questions about the relevance of the PRSP for the government. That is the most fundamental question to be addressed. Is the PRSP relevant? A simple, more strategic document that is truly country owned, that has captured the interest of the population and increased understanding of the policy process may be more useful, even though it has many shortcomings in terms of details. As noted, the key consideration is how to make the PRSP as useful as possible for each country. Where the emphasis may lie in terms of balancing the various tensions that have been identified so as to make the PRSP as useful as possible is likely to vary between countries.

This is recognized in the key statement in paragraph 119 of the background staff paper, which states that "importantly, country ownership implies that countries should choose the nature and extent of details in their own PRSP." Unfortunately, the statement was not repeated anywhere else, and it immediately follows a claim by the staff that it would be inappropriate to streamline the PRSP into a summary strategic document because that would be inconsistent with the basic tenet of the PRSP approach. The staff argue that a summary statement would lack the value of a more detailed document in providing specificity with respect to underlying diagnostics, corresponding policy and program commitments, budget implementation, goals, indicators, proposed implementation monitoring arrangements, and so on. The staff does not seem to allow much scope for a country to choose the nature and extent of the detail in its PRSP, to make it as useful as possible for the country circumstances, capacity and so on.

There are quite a few instances in the staff report which come across as being somewhat prescriptive when it comes to saying what should be in a PRSP. For example, while the MDGs are important goals, the concern raised that PRSPs may not be consistent with the attainment of the MDGs seems to be inconsistent with the idea that PRSPs are meant to be allowing governments to identify their own development goals. As many have said in the past, the PRSP has to be less of a Washington product.

To summarize, perhaps we need a clearer idea of the basic objective of the PRSP in order to accommodate the various tensions identified. The basic objective of the PRSP, and in turn where the emphasis will be placed in handling the many tensions identified, will depend on the circumstances facing each country. To pay full regard to the critical aspect of country ownership we need to more clearly recognize that it is for each country to determine the level of detail included in their PRSP.

The fundamental consideration is how to make the PRSP as useful as possible for each country. This should also be the focus of implementation reports. Finally, we are very much looking forward to the IEO evaluation of the PRSP, because this is an area where we think we would benefit from a fresh perspective.

Turning to the implementation of the HIPC Initiative, progress in reaching completion points is taking longer than earlier envisaged. Policy performance standards cannot be relaxed solely to speed up the reaching of completion points. The quality of progress cannot be compromised for speed.

On the financing of the PRGF in HIPC operations, the consideration of various financing options that would allow a PRGF-lending capacity at close to historical levels would be very important. Last week, when we discussed the role of the Fund in low-income countries, Mr. Kiekens highlighted the tension between the fact that lending under the self-financing PRGF will fall by nearly half in 2006, and the fact that the international community is talking about the need to increase resources going to low-income countries in order to meet the MDGs. But as we discussed in that meeting, the PRGF should not be seen as a source of long-term development financing.

As to the alternative methodologies for calculating additional relief at the completion point, we do not support alternative methodology 1, for the reasons cited in the paper. Furthermore, given the costs involved and the difficulty faced in securing financing for the HIPC Trust fund, it seems an unrealistic option. As for alternative methodology 2, there are merits in excluding new lending after the decision point in determining topping up. Nevertheless, decisions on topping up will have to be considered on a case-by-case basis. The provision of topping up should only be considered where a fundamental change in the country's economic circumstances is clearly due to exogenous factors.

Mr. Alazzaz made the following statement:

I thank the staff for a comprehensive and informative set of papers.

The evidence is clear that the progress has been considerable under both the HIPC Initiative and the PRGF. For the HIPC Initiative, reaching the

Decision Point for over two-thirds of the eligible countries and some 85 percent of the total envisaged debt relief is certainly a considerable achievement. Progress is evident also on pursuing the PRGF goals. Further, it is reassuring that the debt relief has been supplemental to other forms of development assistance to the countries making policy progress. Additional progress along these lines is crucial in view of the Millennium Development Goals.

That said, the difficulties are also evident from the problems in getting to the Decision Point and the shortfalls in reaching the PRGF goals for many countries. The limited progress is indeed partly reflective of the domestic conflicts situations and protracted arrears. Here, the Fund should remain vigilant to help countries move to the Decision Point when their circumstances improve. For better PRGF results, it is necessary to be also watchful of any room for improving the policy design and implementation. In that connection, it is important for the staff to be mindful that the expectations regarding a detailed articulation of a full PRSP should reflect the countries' capacity limitations.

On the participatory process, it is to be expected that progress will continue to vary with the country circumstances. In that connection, I also share the concern that Mr. Ondo Mañe has raised over dangers of creating excessively cumbersome processes. Engaging the stakeholders in the process is ultimately a matter for the local authorities. In addition, the Fund should be mindful of the limits of its own core expertise and mandate.

Regarding the budgetary process, the Fund is on firmer ground. This also underscores the importance of continuing to provide the appropriate technical assistance within the usual efficiency safeguards. Indeed, the Fund is particularly well-placed to help harmonize the longer-term PRSP goals within the shorter-term horizon of the budget process.

Regarding the financing aspects, I support the decision proposed regarding the adequacy of balances in the Reserve Account of the PRGF Trust.

On the methodology for calculating additional debt relief, I can associate myself with the argument by Mr. Shaalan and Mr. Bakhache for continuation of the current practices. As the staff shows, this would raise costs to creditors, including the Fund. Given the resource constraints on creditors, a change could raise new challenges to the financing of the PRGF and HIPC operations.

On program design and implementation, a close attention to the countries' specific circumstances and local ownership are critical. Here, like other Directors, I have doubts regarding the usefulness of the arbitrary

criterion of a one-year track record for reaching the completion point. The staff should also make use of the available scope for a flexible assessment of the progress in meeting the social and structural completion point triggers.

It is important to underscore that the HIPC Initiative and the PRGF goals cannot be pursued independently of the progress in enhancing access for the exports of these countries in world markets. As more countries near the Completion Point, questions regarding continued debt sustainability will be important, especially in view of the Millennium Development Goals. The next staff paper on the issues should, therefore, take due note that the success in realizing the HIPC Initiative and PRGF goals is contingent on faster dismantling of the existing trade barriers for exports from these countries..

Before I conclude, let me note that the HIPC Initiative paper includes two contradictory references to Saudi Arabia. On P.47, the staff notes that Saudi Arabia had not indicated a willingness to provide HIPC relief to Guinea. However, on p. 99, Saudi Arabia has \$22 million shown as relief “directly delivered” to Guinea. Staff’s comment will be welcome. Also the paper contains references that Saudi Arabia had not indicated willingness to provide HIPC relief for other countries. As we have stated in the past, we work with all HIPC countries on a case-by-case basis.

Mr. Josz made the following statement:

I will address, in turn, the PRSP Progress Report, the status of HIPC Initiative implementation, and finally the financing updates for the PRGF and the HIPC Initiative. But first, let me second Mr. Ondo Mane’s request to allocate more Board time in the future to dealing with the many important issues that the staff has flagged for Board discussion, which are too numerous to be dealt with in a single Board session.

PRSP Progress Report

The leadership of the staffs of the IMF and the World Bank, and the willing acceptance of low-income countries' authorities have made the Poverty Reduction Strategy Papers a major means of involving all stakeholders in the design and implementation of policies for increasing growth and reducing poverty. The staffs of the World Bank and the Fund rightly point out that implementing such ambitious policy tools sometimes results tensions arising from conflicting imperatives, a situation on which I will offer my first comments.

The first is the tension between the comprehensive scope of poverty-reducing measures designed with the participation of a wide variety of stakeholders, which may conflict with the strict prioritization required for efficient allocation of scarce budgetary resources. The way to get past these

problems is to strengthen the linkage between the PRSP and the budget process, which has generally been weak (according to paragraph 32 of SM/03/279). Finance ministries, which hold the keys to the Treasury, should be explicitly designated partners in the PRSP process, to avoid a troublesome and persistent disconnect between policy design and policy implementation.

Second is the tension between the time it takes to produce a poverty reduction strategy using a fully participatory process, and the time pressure on the authorities created by the amount of aid provided to support the completion and implementation of a PRSP. Here, one solution would be to base the financial support first on a country's interim PRSPs, and then on its more elaborate PRSPs and PRSP progress reports. The latter should include increasingly thorough Poverty and Social Impact Analyses (PSIAs) and better consultation on the strategy's macroeconomic design, in parallel with the development of new and better tools in these difficult areas.

I continue to insist that the poorest people should have a say in the poverty reduction strategy, because they know better than anybody else what could make a real difference in their lives. Trade unions and business organizations should also see their role in the participatory process increased, to obtain the important benefits of the role they could play in promoting private sector led growth. I also support the staff's suggestion that Fund resident representatives actively assist the authorities in recruiting more participants in the macroeconomic policy debate, and increasing the attention given to the opinions of the poorest citizens, the trade unions, and business leaders. PSIAs should not shy away from analyzing the impact on poverty of difficult but necessary measures like closing redundant state owned enterprises, liberalizing food or energy prices, or introducing the VAT.

Third, there may be tension between rate of change needed to reach the Millennium Development Goals (MDGs) in 2015, and the budget constraints which the design of PRSPs must respect. Here it is the Fund which is responsible for ensuring that the programs it supports are fully financed, and also shares responsibility with the World Bank of warning the international community when the objectives of the PRSPs risk falling short of the MDGs, whether due to policy slippages or for lack of aid. I note with interest that up to now, the targets of PRSPs have been broadly in line with the MDGs (see paragraphs 33 to 35 of SM/03/279 Supplement 1), but I am concerned that for some key goals such as reducing child and maternal mortality, the majority of PRSPs are falling short of the MDG targets. This calls for special monitoring by the World Bank.

And fourth is the tension between the speed with which low-income countries would like to see the many conditions attached to bilateral aid replaced by the joint conditionality attached to the PRSP, and the time it takes to develop Public Expenditure Management Systems sufficiently reliable to

satisfy bilateral donors' need to account for the taxpayers' money that they channel to low-income countries. The only way to relieve this tension is for low-income country authorities to install reliable Public Expenditure Management Systems as quickly as possible.

Implementation Status of the Enhanced HIPC Initiative

With two thirds of the heavily-indebted poor countries beyond their decision points, and one fourth beyond their completion points, the HIPC Initiative is well underway. The eleven countries that have not yet reached their decision points should get their acts together and seize this opportunity, which will not last forever, to normalize their financial relations with the international community.

I welcome the recent deliveries, by Libya and India, of their shares of HIPC debt relief. I urge the 24 countries listed on the last page of the staff paper (SM/03/294) to finally follow the examples of Libya and India and all other bilateral creditors, who now have fulfilled the commitments to participate in the HIPC Initiative made on their behalf by their representatives in the Boards of the IMF and World Bank. I fully support the proposal of Mr. Duquesne and Mr. Scholar to ask countries, in the course of their Article IV consultations, why they have not yet delivered their shares of HIPC debt relief, and to include the answers in the staff report on the consultation.

I also welcome the updated list of private creditors, who, contrary to the spirit of the HIPC Initiative, are litigating against HIPC countries to recoup the full share of their claims. Short of an SDRM, we can do little beyond moral suasion, and remembering their uncooperative behavior when there is business to be done with the international community, to convince these creditors to stop free riding on our efforts to reduce the debt of the poorest countries.

I also welcome the finding that HIPC debt relief seems to have been additional to, and not a substitute for, aid to the heavily-indebted poor countries (see Figure 4, p. 12 of SM/03/294). In the next progress report on the HIPC Initiative, it would be worthwhile to include aid flows to non HIPC countries, so that we can assess the additionality of HIPC debt relief to total bilateral aid.

Financing PRGF and HIPC Operations

Thanks to a complex but effective financing structure, the Fund has gathered enough resources to finance both its share in the HIPC Initiative, excluding Liberia, Somalia, and Sudan, and its shrinking yet perpetual concessional window to low-income countries, which will be about half its present size from 2006 onwards.

Although satisfactory at first glance, this financial position glosses over substantial potential financing needs that must be analyzed sooner rather than later.

First, as Mr. Kiekens proposed last week, the staff should assess the amount of resources needed to keep the access to the PRGF constant in real terms until 2015 and enable the Fund to make a visible contribution to the achievement of the Millennium Development Goals. Calculation on the back of the envelope leads me to think that additional subsidy resources of about \$40 million a year for ten years would be needed (SDR 650 million x 4.5 percent x 1.3742 = \$40 million). This represents a mere 0.7 percent of the total official development assistance of about \$55 billion supplied each year by donor countries to developing countries, and would be a worthwhile investment which would help instill the financial and macroeconomic discipline without which any amount of aid cannot be effective.

Second, the Fund will need additional subsidy and grant resources of about SDR 1.5 billion (\$2 billion) when Liberia, Somalia, and Sudan will be ready for arrears clearance, new PRGF loans, and HIPC debt relief. In view of the prospect for an imminent end to civil conflict in Sudan, the Board should consider soon how the Fund can cover the financing needs arising from Sudan's participation in the HIPC Initiative.

At the request of several key shareholders, the staff has once more assessed alternative methodologies for topping up HIPC assistance at the completion point. I am not prepared to consider an alternative methodology involving additional costs for the Fund and other multilateral creditors without simultaneously considering the solutions proposed for covering the financing gaps. I have noted with interest that my suggestion to exclude new concessional credit contracted after the decision point from additional debt relief, in conformity with standard bankruptcy rules and as envisaged under the SDRM, would eliminate the need for additional debt relief at the completion point.

Finally, I cannot conclude my comments on PRGF and HIPC financing without urging Zimbabwe to clear its arrears to the PRGF Trust, and without encouraging the few countries that have not yet paid the bilateral contributions to the PRGF HIPC Trust that they pledged in September 1999, to do so promptly.

Mr. Mozhin made the following statement:

I support the proposal made by Mr. Ondo Mañe to come back to some of these issues after the Annual Meetings. As noted by Mr. Josz, there are simply too many issues for one session of the Board.

On the PRSP process, we welcome a number of important advances, including the growing attention paid to the sources of growth and establishing an appropriate macroeconomic framework, as well as the greater orientation of expenditures to poverty reduction. At the same time, key challenges still remain, especially regarding fully integrating the PRSP process into member countries' decision-making process. We agree with the staff that the Fund has an important role to play in assisting developing countries to improve the macroeconomic framework of PRSPs. There is clearly a need to place great emphasis on aligning PRSP goals with the macroeconomic framework and the PRGF objectives.

The issue of developing a strong macroeconomic framework for the PRSP process is closely related to the pressing need to regularize the inclusion of vulnerability assessments, alternative scenarios, as well as contingency measures with respect to the variety of possible risks to the baseline growth outlook. In the end, the ability of the country to develop these important tools will determine the degree to which the PRSP is aligned with the respective PRGF.

Last but not least, PRSPs play a key intermediary role between short-term fiscal priorities and the long-term MDGs. In this respect, the greater the comprehensiveness of the macroeconomic framework in PRSPs, the smoother will be the transition from short term to longer-term objectives.

Turning to the financing paper and the HIPC paper, let me only say that we are not prepared at this stage to support any modifications to the current methodology for determining additional debt relief at the completion point, for the reasons mentioned by the staff, as well as a number of previous speakers.

The Deputy Director of the Policy Development and Review Department (Mr. Allen) noted, in response to a question by Ms. Gust, that the current work being done by the Fund and the Bank on debt sustainability in low-income countries was not expected to lead to a revision of the HIPC Initiative. That work focused more how to maintain debt sustainability, rather than on how to reduce the debt stock, something which the HIPC Initiative was meant to address. Therefore, the staff was working on analyzing borrowing flows, the impact of the accumulation of new debt, and the policies needed to build debt-servicing capacity.

The staff representative from the Policy Development and Review Department (Mr. Wang) said that the staff would correct a mistake in one of the Appendix tables of the HIPC paper, referring to the debt relief delivery by Saudi Arabia. The paper would also be revised to correct the amount of additional bilateral debt relief being granted by Finland.

Mr. Ondo Mañe asked the staff to comment on his request for a further discussion of the papers after the Annual Meetings.

The Deputy Director of the Policy Development and Review Department (Mr. Allen) replied that a further discussion had not been planned, so the staff would have to consider Mr. Ondo Mañe's request. There would be an opportunity to discuss PRSP and PRGF issues when the IEO produced its report on the PRGF and PRSP, fairly early in the first quarter of 2004.

The Acting Chair (Ms. Krueger) added that the Board would be discussing the work program shortly after the Annual Meetings, and that would be the appropriate time to discuss the possibility of adding a further discussion to the agenda.

The Acting Chair (Ms. Krueger) made the following concluding remarks:

Poverty Reduction Strategy Papers—Progress in Implementation

Executive Directors welcomed the continuing strong momentum of the Poverty Reduction Strategy Paper (PRSP) approach. They noted that there is evidence of progress across a wide range of fronts as the approach begins to mature, but that the progress is uneven across countries. They indicated that the imperative now is to address the emerging challenges in implementation in individual countries.

Directors underscored the importance of government ownership of poverty reduction strategies, including during their implementation. They emphasized the need for greater cohesion between PRSPs and other planning documents and for better integration between teams responsible for PRSP preparation and other units of government. They welcomed the increasing engagement of Parliaments in the PRSP process and the greater openness of policy-making processes which the PRSP approach is facilitating. Directors encouraged dialogue with civil society, including the private sector and non-governmental organizations.

Consistent with country ownership of PRSPs, Directors emphasized that the government, and not the Fund, should lead the discussion of the macroeconomic framework in the public domain and ensure that it is integral to the participatory process. Directors saw an important role for the Fund in informing this dialogue, through continued outreach efforts to the authorities, civil society, and donors. They called on governments to provide an explicit forum for macroeconomic dialogue in the context of the PRSP process where Fund Resident Representatives could participate. Noting that deepening and widening of skills is a prerequisite to strengthening the government's ownership of the macroeconomic framework, Directors emphasized that the Fund would need to continue to support countries' capacity building efforts.

Directors emphasized the need to align the PRSP approach with the national budgetary process. This requires the formulation of concrete plans and policies that can feasibly be implemented in the context of annual budgets

and within given resource constraints. To this end, Directors considered improvements in public expenditure management to be critical. They noted that the linkage between PRSPs and the annual budget and medium term expenditure frameworks generally remains weak, with PRSPs continuing to include numerous uncostered measures. Stressing that problems in costing stem from weaknesses in fiscal data, capacity constraints, and institutional arrangements, Directors called on the Fund and the Bank to continue to provide technical assistance to tackle these deficiencies and help improve public expenditure management and accountability.

Directors generally stressed the importance of designing realistic macroeconomic frameworks, taking into account financial and institutional constraints. Particularly important is the need to avoid over-optimistic economic growth projections. Directors welcomed the broader discussion of macroeconomic assumptions in recent PRSPs. However, they agreed that the linkages between sectoral and structural policies and the discussion of macroeconomic performance and growth prospects could be strengthened. Several Directors called for more attention to the sources of and constraints on economic growth, noting that better growth performance is essential to attaining the Millennium Development Goals. Directors also urged more discussion of the impact of shocks, and that macroeconomic frameworks should be designed so that higher volumes of aid could be accommodated. In this regard, Directors encouraged countries to devise strategies that can respond flexibly to changing circumstances, and saw significant scope for PRSPs to flesh out contingency plans to address unexpected developments.

In general, Directors considered that it would be too early, given the initial stages of implementation, to form judgments about whether PRSP policies are delivering on their stated objectives. Noting the identification by a number of PRSPs of weak governance and corruption as significant constraints, they considered the implementation of measures to address these issues as key to improving growth prospects. Directors welcomed the focus being placed in PRSPs on measures to foster private sector development and improve the investment climate. They noted that poverty-reducing spending has increased in the PRSP countries where data are available, and were encouraged by the tentative signs of improved access of the poor to some basic services. They encouraged greater use of poverty and social impact analysis to help monitor the impact of PRSPs and to inform policy design and choices. A few Directors called for the development of intermediate indicators to allow stakeholders to monitor the attainment of PRSP objectives.

Directors supported donor coordination and alignment around a common development framework, and welcomed the broad endorsement by both donors and partner countries of the principles of good practice and standards of alignment and harmonization developed by the OECD-DAC in conjunction with various multilateral development banks. They noted that the

implementation challenges in these areas remain significant, in part due to tensions between the priorities of external partners, including the Fund and the Bank, and country ownership and capacity. Directors stressed that many countries will need to strengthen their aid management systems to enable them to take the lead in donor alignment, and considered coordinated donor technical assistance to be crucial in this respect. Directors also urged greater efforts from donors, including the Fund and the Bank, to rationalize their requirements and to align their support around PRSPs. A number of Directors urged greater integration of trade policy issues in PRSPs and the overall policy agenda, to factor in the impact of other countries' trading practices as well as of PRSP countries' own potential complementary action on trade reform.

Directors noted that insufficient prioritization often resulted in inadequate focus in PRSPs. They supported efforts being made to address this weakness. They believed that external partners, including the Fund and the Bank, have a crucial role in helping countries improve prioritization over time by providing support in capacity building, respecting country priorities, and sequencing their own advice and assistance.

Directors saw Joint Staff Assessments as important means for providing constructive and candid feedback to governments about their PRSPs. They underscored the importance for such feedback to highlight the factors that are expected to be critical to the overall strategy, including capacity building needs. Directors, however, also emphasized that the JSA and the Board's consideration of the PRSP should not undermine country ownership.

Directors concluded that the broad principles of the Comprehensive Development Framework expressed in the PRSP approach remain fully valid and that with progress in addressing the emerging challenges in implementation, the PRSP approach should be able to make a significant contribution to improving economic outcomes and reducing poverty in low-income countries.

Directors agreed that the next progress report on the implementation of the PRSP approach should be prepared jointly by Fund and Bank staff in 12 months time. Some Directors noted, however, that the issues raised in the present PRSP progress report warrant a fuller, stand-alone discussion; and they asked the staff to consider holding a follow-up discussion after the Annual Meetings.

HIPC Initiative—Status of Implementation; and Update on the Financing of PRGF and HIPC Operations and Subsidization of Post-Conflict Emergency Assistance

Executive Directors welcomed the progress made under the enhanced HIPC Initiative in providing debt relief to the world's poorest countries. They noted that together with associated debt forgiveness, debt relief committed under the HIPC Initiative to the 27 countries that are already past their decision points would lower the outstanding stock of external debt of these countries by about two-thirds and lower debt-service payments for most HIPCs to less than 10 percent of exports over the medium term.

Nevertheless, Directors reiterated that, in addition to debt relief, fiscal discipline and sustained economic growth are critical for achieving debt sustainability. In this context, they regretted that many countries in the interim period are taking longer than envisaged to reach the completion point, due mainly to the difficulties in implementing their macroeconomic programs. They emphasized that attaining macroeconomic stability, satisfactorily implementing PRSPs, and meeting other social and structural completion point triggers are critical to realizing the objectives of the HIPC Initiative. They encouraged HIPCs to stay on track with their economic reform and poverty reduction programs, especially the fiscal component of these programs, in order to reach their floating completion points without further delay. Directors underscored the importance of providing technical assistance, where possible, to alleviate constraints in PRSP design and implementation, particularly concerning the macroeconomic framework and public resource management.

Directors also recognized that while several members could adopt programs of adjustment and reform supported by the Fund and IDA before the sunset clause takes effect at the end of 2004, bringing the remaining countries to the decision point would be challenging, as most of these countries are affected by conflict, and a number of them have substantial arrears to official creditors. They urged the staff to continue to work with these countries and their development partners, wherever possible, to develop strategies to move ahead quickly. Some Directors were of the view that the sunset clause would need to be re-examined to ensure that countries moving toward HIPC debt relief, but not yet eligible for it, are not penalized, and to avoid a rush for countries to participate before 2004 at the expense of solid progress in key areas. In this regard, they welcomed the staff's indication that a review of the sunset clause would be discussed at the appropriate time in 2004.

Directors considered the emphasis on governance under the HIPC Initiative to be appropriate, observing that good governance practices require the concerted and continued efforts of both country authorities and the international community. They called on the staff to continue to strengthen the reporting on governance of HIPCs at their completion points.

Directors noted the challenges faced by HIPCs in mobilizing the financing to support reforms for achieving the Millennium Development

Goals while ensuring long-term debt sustainability. They welcomed initiatives by the staff, in cooperation with other members of the international community, in developing a framework for assessing debt sustainability and its policy implications for HIPCs and their external creditors and donors.

Directors welcomed the increased participation of non-Paris Club creditors in the HIPC Initiative, and reiterated their call to the creditors that have not yet done so to contribute their share to reducing HIPCs' external debt to sustainable levels. They asked the staff to take all possible measures, within the existing legal and institutional constraints, to help increase creditor participation in the Initiative, including publicly identifying those creditors not participating in the Initiative. Directors regretted that a number of HIPCs face creditor litigation. Some Directors encouraged the staff to further reflect on ways and instruments to help HIPCs facing litigation initiated by creditors. Directors also looked forward to the staff's further consideration of options for resolving the issue of HIPC-to-HIPC debt relief, taking into account the basic principle of inter-creditor equity.

Directors welcomed the finding that, under the current framework, available PRGF loan, subsidy, and HIPC grant resources are estimated to be sufficient to cover the projected costs of PRGF lending through 2005 and the Fund's share of the HIPC Initiative assistance, including the currently projected amount of topping up of HIPC assistance at the completion point. Directors reaffirmed, however, that topping up should be used only in exceptional cases where a country's economic fundamentals have deteriorated significantly because of exogenous factors. Many Directors stressed that, in light of the uncertainties associated with projections and the lack of any pledges of extra financing by creditors, adopting a more costly approach to calculating topping-up assistance would be inappropriate and could endanger the financing of PRGF and HIPC operations. A number of other Directors, however, supported a change in the methodology for calculating topping up to exclude voluntary debt relief provided by some bilateral creditors, stressing that such bilateral debt relief was intended to be additional to the debt relief provided under the HIPC Initiative. There was some interest in a compromise proposal that would exclude voluntary bilateral debt relief in calculating topping up for countries that are not only suffering from exceptional exogenous shocks and but also have a good track record in terms of governance. In addition, a few Directors noted that they would support this alternative approach to calculating topping up assistance only if financing for the additional costs were secured ex ante. Directors urged that pending bilateral subsidy contributions to the PRGF-HIPC Trust be made effective as soon as possible. Directors expressed satisfaction that subsidy resources for post-conflict emergency assistance were estimated to be sufficient through end-2004.

Looking ahead, many Directors underscored that addressing the arrears and debt problems of Liberia, Somalia, and Sudan would require mobilization of substantial additional loan and subsidy resources and that this task would become urgent when a peace agreement is reached in Sudan. A few Directors, however, stressed that the financing of countries emerging from protracted arrears should be discussed separately. A number of Directors also expressed concern that, beyond 2005, the lending capacity under the so-called self-sustained PRGF framework would fall sharply and would not be adequate to provide for a suitable level of Fund financing for its low-income member countries. Some other Directors stressed that the planned self-sustained PRGF should not be questioned, noting that pressures on PRGF resources should be eased by the advance of the HIPC Initiative, the progressively lower financial needs of some low-income countries, and the consideration of alternative instruments that do not involve Fund financing to serve as signaling devices. Directors looked forward to the forthcoming staff paper on options for financing the continuation of the Fund's involvement in low-income member countries.

The Executive Board took the following decision:

PRGF Trust and PRGF-HIPC Trust—Reserve Account—Review

Pursuant to Decision No. 10286-(93/23) ESAF, adopted on February 22, 1993, as amended, the Fund has reviewed the adequacy of balances in the Reserve Account of the PRGF Trust, and determines that they are sufficient to meet all obligations that could give rise to payments from the Account to lenders to the Loan Account of the PRGF Trust in the six months from October 1, 2003 to March 31, 2004 (SM/03/296, 8/19/03)

Decision No. 13089-(03/84), adopted
September 3, 2003

4. INTER-AMERICAN DEVELOPMENT BANK—INVITATION TO ATTEND EXECUTIVE BOARD MEETING

The Executive Directors agreed to invite a representative from the InterAmerican Development Bank to attend the Executive Board Meeting on Guyana.

Length: 5 minutes

DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Board without meeting in the period between EBM/03/83 (8/29/03) and EBM/03/84 (9/3/03).

5. LIBERIA—OVERDUE FINANCIAL OBLIGATIONS—SUSPENSION OF VOTING AND RELATED RIGHTS—POSTPONEMENT

Paragraph 4 of the Decision No. 12955-(03/19) adopted on March 5, 2003 shall be amended by replacing “within six months of March 5, 2003” with “no later than March 5, 2003. (EBS/03/121, 8/19/03)

Decision No. 13090-(03/84), adopted
September 2, 2003

6. UGANDA—POVERTY REDUCTION STRATEGY PAPER ANNUAL PROGRESS REPORT—JOINT STAFF ASSESSMENT

The Fund has reviewed the PRSP annual progress report submitted by the Republic of Uganda and concludes that it continues to provide a sound basis for Fund concessional assistance. (EBD/03/71, 8/18/03)

Decision No. 13091-(03/84), adopted
September 2, 2003

7. SDR DEPARTMENT—DESIGNATION PLAN FOR SEPTEMBER-NOVEMBER 2003

The Executive Board approves the SDR designation plan for the quarterly period September-November 2003 as set out in EBS/03/119 (8/18/03).

Decision No. 13092-(03/84) S, adopted
August 29, 2003

8. FINANCIAL TRANSACTIONS PLAN FOR SEPTEMBER-NOVEMBER 2003

The Executive Board approves the list of members considered sufficiently strong and the financial transactions plan for the period September-November 2003 as set out in EBS/03/120 (8/18/03).

Decision No. 13093-(03/84), adopted
August 29, 2003

9. ADVISORS TO EXECUTIVE DIRECTORS—REMUNERATION

The Executive Board approves, with one abstention from Ms. Jacklin (UA) and one objection from Mr. Scholar (UK), the recommendation to increase the remuneration of Advisors to Executive Directors as set forth in EBAM/03/113 (8/25/03).

Adopted August 29, 2003

10. APPROVAL OF MINUTES

The minutes of Executive Board Meeting 03/31 are approved.

11. EXECUTIVE BOARD TRAVEL

Travel by Executive Directors, by Advisors to Executive Directors, and by Assistants to Executive Directors as set forth in EBAM/03/116 (8/29/03) is approved.

APPROVAL: February 6, 2004

SHAIENDRA J. ANJARIA
Secretary