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Statement by Mr. Itam on Debt Limits in Fund-Supported Programs--Proposed New Guidelines; Review of Some Aspects of the Low-Income Country Debt Sustainability Framework
(Preliminary)
Executive Board Meeting 09/91
August 31, 2009

1. We wish to thank staff for the set of papers intended to guide the Board discussion on the proposed new guidelines on debt limits in Fund-supported programs and a review of the debt sustainability framework. The opportunity for the Board to consider the proposed draft guidelines is critical not only for the debt limits in the Fund-supported programs but also in all other areas of the Fund's work that entail the use of guidelines by staff. We would recommend that this practice be a norm going forward.

2. Over the last six to eight months the Fund has made considerable progress in reforming its rules of engagement with its member countries. Among these were the modernization of conditionality, the review of access levels, and the establishment of new financing instruments in particular the new financing architecture for the LICs and the FCL. Having made such commendable progress, it would be regrettable that the review of the debt limits in Fund-supported programs and the debt sustainability framework would amount to backtracking from the stated goal of strengthening engagement with these countries. We would like the proposed guidelines and the review of the DSF to be seen also in that light.

3. Fundamentally, it should be recalled that the LICs, together with other members, on several occasions, both at global fora and country-level policy formulation, have expressed strong and explicit commitment of not reverting back to unsustainable high indebtedness of the pre-HIPC and pre-MDRI era. The experience in the post-HIPC and post-MDRI in observing such commitments, as indicated in the staff papers, should provide us with clear guiding principles when considering the proposed guidelines and the review of the DSF.

4. In this regard, and of critical importance, the LICs have repeatedly demanded that the DSF thresholds and related conditionalities on external debt limits be revised with the view of providing them with space to expand the financing of high-growth yielding public investments, especially those in infrastructure with high employment intensity that relieve

specific constraints and facilitate exploitation of economic potential in mining, agriculture and manufacturing sectors. In the current economic conditions, such investments would help restore and raise the countries' growth potential and, in the post-crisis period, sustain high growth trajectory and raise employment potential as well as crowd-in private investment. Such opportunities were clearly recognized by the G20 at their London summit of April 2009, and hence, their demand for the urgent review of the DSF. The IMFC's April 2009 statement on this was unequivocal as per paragraph 10 of its communiqué.

5. That said, we wish to register our disappointment that the three sets of documents do not go far enough to meet the expectations of the LICs nor respond adequately to the calls of the G20 and the IMFC. We would also like to recall that the decision on these critical issues will carry important signaling and operational effects to the LICs and their development partners. While we welcome and encourage staff to expand their analysis of debt management and public investment-growth nexus, we will limit our observations to the broad issues of contention in these papers and the proposed decision.

LIC Debt Sustainability Framework

6 We concur with the purpose of the DSF as conceived, in particular the objectives of (a) helping countries monitor their debt burden and take early preventive action, and (b) providing guidance to creditors in ensuring their lending decisions are consistent with countries' development goals. In this regard, and as staff correctly notes the Nouakchott declaration that emanated from discussions between African Governors and traditional and non-traditional financiers including all IFIs, and further restated at the Africa-IMF conference of March 2009, the review should have at best responded to the demand for a review of DSF thresholds (box 1 and table 1 of the staff paper).

7. The analytical underpinnings of the DSF policy-dependent indicative thresholds notwithstanding, lack of proposals on the possible adjustments in these thresholds defeats the purpose of the intended review. While we would agree with the proposal for streamlining the DSAs and incorporation of remittances in the DSAs and risk ratings for countries where remittances are large, we caution that their value in helping both the LICs and financiers respond to the twin objectives stated in para 6 above is very limited. We, therefore, urge staff to revisit the DSF thresholds and propose alternative indicators that are current. As per the expectations of the IMFC and G20, this review should be ready by the 2009 Annual Meetings.

Debt Limits in Fund-Supported Programs

8. We welcome staff analysis and proposals for a menu of options that closely reflects the diversity of situations in LICs as per the four broad categories (table 1). We concur with staff analysis that such categorization constitutes a sound basis for determining flexibilities in the debt limits and concessionality levels. While we see value in injecting capacity analysis in the new framework, we would have liked to see linkage with actions to address capacity constraints for countries with lower indicators and even those with high indicators.

9. We also welcome staff effort to deepen their analysis on this subject. However, we strongly caution that the multiplicity of indicators, for instance, five under the World Bank's Country Policy and Institutional Assessment (CPIA) and twenty-eight under the Public Expenditure and Financial Accountability (PEFA), and others under DeMPA, HIPC/CBP, ROSCs, WGI, and PPA (table 2 of staff paper), negates or falls short of the intended value of the review effort. For instance, to the extent that LICs' risk of debt distress depends on their vulnerability to exogenous shocks, rather than performance under the proposed multiple indicators, the framework introduces an allocation bias against those countries with the greatest need of liquidity to counter the immediate effects from such shocks. *We, therefore, wished to have seen greater rationalization of these indicators in line with the spirit of modernizing conditionality and operational procedures. Staff comments are welcome.*

10. Like the review of the DSF, the review of debt limits in Fund supported programs was intended to respond to the financing needs of the LICs and, therefore, inject sufficient flexibility to all countries (the four categories). Like Messrs. Rutayisire, Fayolle, Talbot and Ward, we regret to note that the review has disadvantaged the LICs with lower capacities and higher vulnerabilities. For these categories we also see the introduction of new sets of conditionalities – new target indicators – that negates the purpose of the exercise and the Fund's work on modernizing its conditionalities. *Staff comments on the value of the new set of conditionalities are welcome.*

Proposed New Guidelines – Proposed decision

11. In light of the above, we would not support the inclusion of the following paragraphs in the new guidelines: 8 (b), (f); and (g – i, ii, iii, iv, and v). We look forward to see the revised guidelines that takes into account these serious concerns. Like the review of the DSF, we urge staff and management to complete this review by the 2009 Annual Meetings.