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To: Members of the Executive Board

From: The Secretary

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REFORM OF THE POLICY ON PUBLIC DEBT LIMITS IN IMF-SUPPORTED PROGRAMS—SUPPLEMENTARY INFORMATION

EXECUTIVE SUMMARY

This note provides supplemental discussion and analysis of issues raised in the Board Paper on the Review of the Debt Limits Policy (DLP). It is structured as follows:

- ***Section Experience with Implementation of the DLP.*** Provides background on the implementation of the policy.

- ***Section Outreach: Stakeholder Survey and Consultation Results*.** Describes the results of surveys and consultations with stakeholders.

- ***Section Illustrative Guide to Tailoring Conditionality.*** Provides examples of how conditionality can be tailored to address specific debt vulnerabilities.

- ***Section Illustrative Characterization of Countries Relying on Concessional Financing with Significant Access to International Financial Markets.*** Describes criteria that could identify PRGT-eligible countries that have had significant access to international financial markets in recent years, and may thus be eligible for new proposals on conditionality design.

- ***Section Alignment between the IMF's DLP and the World Bank's Sustainable Development Finance Policy (SDFP)*.** Summarizes the SDFP and discusses its relationship with the DLP.

Approved By
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CONTENTS

EXPERIENCE WITH IMPLEMENTATION OF THE DLP

1. The application of the IMF's debt limits policy (DLP) was broadly guided by the DSA risk ratings or signals, as intended (Tables 1–3).

- ***PRGT-eligible countries ("PRGT cases").*** In countries at high risk of (or in) external debt distress, the DLP was applied as intended with debt limits (DLs) taking the form of a zero limit on non-concessional borrowing (NCB). Where debt recording and monitoring capacity was assessed to be adequate, additional limits were applied on concessional borrowing (CB), either in the form of performance criteria (PCs) or indicative targets (ITs), to help contain external debt accumulation. Also, in line with the policy, some of these programs included various exceptions and adjusters on NCB, sometimes added during reviews (e.g., Afghanistan, Cameroon, Ghana, and Mauritania). For countries at moderate risk of external debt distress, however, the policy was applied in a more restrictive way than envisaged. Not all countries featured debt conditionality in the form of present value (PV) limits owing to weak debt recording and monitoring capacity (e.g., Guinea 2017 and Liberia 2019). Among those countries with nominal limits, several were subject to a zero-NCB limit (e.g., Guinea-Bissau 2015, Malawi 2018, and Togo). For low risk cases, the policy was generally applied as intended with no DLs featuring in most programs, except for targeted limits on SOE debt or government guarantees (e.g., Rwanda and Uganda).

- ***Countries not eligible for PRGT ("GRA cases").*** For GRA cases, programs with significant debt vulnerabilities generally featured DLs. Design of these limits varied depending on the nature of the debt vulnerability. Some programs where debt levels were high included ceilings on total public debt (e.g., Barbados, Cyprus, Egypt, Jamaica, and Jordan). Others with high levels of non-resident debt or large external financing requirements included ceilings on external debt (e.g., Equatorial Guinea and Gabon). Many programs also used limits to target vulnerabilities outside the perimeter of fiscal conditionality including guaranteed or SOE debt (e.g., Albania, Armenia, Cyprus, Georgia, Pakistan, Serbia, Sri Lanka, Suriname, and Ukraine). There were also cases where limits were used to capture specific vulnerabilities including short-term (e.g., Bosnia and Herzegovina, and Jordan 2016) or collateralized debt (e.g., Angola). Finally, a few programs with countries that still had access to concessional financing included limits on non-concessional debt or average concessionality (e.g., Armenia and Mongolia). A few GRA cases that did not have debt limits may have benefitted from them. For example, the Seychelles (2017) had significant debt risks flagged in its DSA heat map, including from SOEs which were not covered by fiscal conditionality. Similarly, in Tunisia fiscal risks from SOEs were flagged throughout the program, but fiscal conditionality only covered the central government and there was no complementary debt conditionality to capture these risks. Although Egypt had an IT on the gross debt of the budget sector (which overlapped somewhat with fiscal conditionality), it could have also benefited from a limit on government guarantees given that increased use of calls on state-guaranteed loans to finance infrastructure projects were identified as a potential fiscal risk.

2. Observance of DLs since the implementation of the 2014 DLP has generally been strong, with only a handful of breaches. Debt PCs between July 2015 and April 2020 were breached in 8 programs with at least one review, representing approximately 4 percent of all test dates (Table 4).[1] With the exception of Malawi, the size of the breaches were moderate relative to GDP, but in some cases they were large relative to the debt limits (particularly in Cameroon). Reasons for non-observance of debt limits included weak public financial management and debt monitoring (Cameroon, 2017 (two occasions); Iraq, 2016); reporting slippages (Guinea, 2017; Liberia, 2015; Mozambique, 2015); or technical factors (Malawi, 2018; Mauritania, 2017). Of the four programs that went off-track—Haiti 2015, Mozambique 2015, and Sierra Leone 2017 before the first review, and Kenya 2015 after the second review—one case was due to non-observance of the program debt limit (Mozambique, 2015), while the others were due to exogenous shocks or weak fiscal performance.

3. Accommodation of infrastructure investment or debt management operations through upward revisions of borrowing limits or adjusters has been limited to a small group of countries (Table 5). Upward modifications under IMF-supported programs occurred in Afghanistan, Cameroon, Mauritania, and repeatedly in Ghana. The risk ratings did not deteriorate following the debt-related conditionality modifications (at the same time, improvements have not been observed either). On the debt management side, Côte d'Ivoire and Ghana had multiple modifications to accommodate Eurobond issuances and Togo's program allowed for some NCB to pay down more costly domestic debt. Other modifications have related to changes in projections, capacity or DSA upgrades, technical factors, and missed PCs (Table 6).

[1]Compliance with debt-related ITs has also been strong, with only three instances of missed targets during July 2015-April 2020 (Egypt, Rwanda, and Sri Lanka).

Table 1. Debt Conditionality in PRGT-Supported Programs, July 2015-April 2020[1]

Program	Approval Year	DSA Rating[2]	Debt/GDP (percent)[2]	Capacity to Monitor/Record
Nominal Zero Limit on NC External Debt				
Afghanistan, Islamic Republic of	2016	H	8.0	W
Cabo Verde[3]	2019	H	121.4	W
Cameroon (contracted and disbursed nc external debt)	2017	H	35.7	S
Central African Republic	2016	H	44.3	W
Central African Republic	2019	H	47.1	W
Chad	2014	H	59.7	W
Chad	2017	D	47.6	W
Congo, Rep. of[3]	2019	D	118.0	W
Ethiopia[3]	2019	H	53.4	S
Gambia, The[3]	2020	H	76.8	W
Grenada	2014	D	90.2	W
Guinea	2012	M	44.6	W
Guinea-Bissau	2015	M	49.0	W
Haiti	2015	M	30.2	S
Malawi	2018	M	54.3	W
Mauritania[3]	2017	H	77.3	W
Sao Tome & Principe	2015	H	86.0	W
Sao Tome & Principe	2019	D	94.2	W
Sierra Leone[3]	2018	H	71.5	S
Solomon Islands	2012	M	10.4	S
Somalia[3]	2020	D	74.6	W
Togo	2017	M	79.7	W
Nominal Non-Zero Limit on NC External Debt				
Bangladesh	2012	L	34.0	S
Burkina Faso	2013	M	32.1	W
Cote d'Ivoire	2011	M	45.6	S
Ghana (multiple non-zero limits nc external debt)[3]	2015	H	72.2	S
Guinea	2017	M	42.9	W
Liberia	2019	M	54.1	W
Malawi[4]	2012	M	53.8	W
Niger	2012	M	43.1	W
PV Limit on Total External Debt				
Benin	2017	M	53.4	S
Burkina Faso[5]	2018	M	41.0	S
Cote d'Ivoire	2016	M	47.8	S
Honduras[4]	2014	M	49.1	S
Kyrgyz Republic[4]	2015	M	64.9	S
Liberia[4]	2012	L	29.7	S
Madagascar (nc external debt at varied grant elements)[5]	2016	M	38.7	S
Mali[4]	2013	M	30.0	S (upgraded)
Mali	2019	M	37.4	S
Mozambique	2015	M	88.1	S
Niger[5]	2017	M	51.5	S (upgraded)
Sierra Leone[4]	2013	M	44.5	S
Sierra Leone	2017	M	60.3	S

Table 1. Debt Conditionality in PRGT-Supported Programs, July 2015-April 2020 (concluded)

Program	Approval Year	DSA Rating[2]	Debt/GDP (percent)[2]	Capacity to Monitor/Record
Public Debt QPC (type)				
Kenya[5]	2016	L	52.6	S
Senegal	2020	M	63.7	S
Debt-realted IT (type)				
Rwanda (external SOE debt)[4]	2013	L	37.6	S
Rwanda (external SOE debt)	2016	L	44.5	S
Uganda (guaranteed debt)[4]	2013	L	31.1	S
None				
Honduras	2019	L	41.8	S
Kenya[4]	2015	L	51.6	S
Moldova, Republic of	2016	L	43.2	S
Rwanda	2019	L	55.8	S
Senegal[4]	2015	L	44.5	S
Tanzania[4]	2014	L	40.5	S

[1]Sample includes 54 PRGT-supported programs ongoing between July 2015 and April 2020. FCLs, RCF/RFIs, and SMP are not included in the analysis.
[2]For programs approved after July 2015: DSA ratings and debt levels based on program approval year. For programs approved before July 2015: DSA ratings and levels based on first review after new DLP.
[3]Accompanied by PC/AC (Cabo Verde, Sierra Leone 2018, Somalia) or IT (Ethiopia, Rep. Congo, The Gambia, Ghana, Mauritania, Sao Tome and Principe) on concessional borrowing
[4]Indicates in response to 2014 DLP reform (see Table 5).
[5]Burkina Faso, Madagascar, Niger modified to PV limit in 2018. Kenya (2016) risk rating downgraded to moderate and PC on contracting/guaranteeing of new public debt introduced in 2018.

Table 2. DSA Rating and Nature of Vulnerability in Programs with a Zero NCB Limit[1]

Country	Approval Year	Vulnerability in external DSA	Domestic debt flagged?	Other comments
In debt distress				
Chad	2017	Debt service	Yes	Had external debt arrears
Republic of Congo	2019	Debt level and debt service	Yes	Had external debt arrears
Grenada	2014	Debt Level		Had external debt arrears
Sao Tome & Principe	2019	None	Yes	Had external debt arrears
Somalia	2020	Debt level and debt service	Yes	Had external debt arrears
High risk				
Afghanistan	2016	None		Grant dependent
Cabo Verde	2019	Debt level		
Cameroon	2017	Debt level		
Central African Republic	2016	Debt service	Yes	Domestic payment arrears
Central African Republic	2019	Debt service		
Chad	2014	Debt service and level		
Ethiopia	2019	Debt service and level		
Gambia, The	2020	Other	Yes	High probability of external arrears; large stock of undisbursed semi-concessional debt; SOE exposure
Mauritania	2017	Debt level and debt service		
Sao Tome & Principe	2015	Debt level		
Sierra Leone	2018	Debt level and debt service		
Moderate risk				
Guinea	2012	None		NCB limit breached prior to July 2015
Guinea-Bissau	2015	Debt level	Yes	High overall risk rating
Haiti	2015	Debt level		
Malawi	2018	Debt level	Yes	High overall risk rating
Solomon Islands	2012	None		Only one review post July-2015
Togo	2017	Debt level	Yes	Domestic debt partly unrecorded

[1]For programs approved after July 2015, vulnerabilities based on DSA at program approval. For programs approved before July 2015, vulnerabilities based on DSA at first subsequent review.

Table 3. Debt Conditionality in GRA Cases, July 2015-April 2020[1]

Program	Approval Year	DSA Heatmap Score[2]	Debt/GDP (percent)[2]
External Debt Limit			
Equatorial Guinea	2019	6.5	46.2
Gabon	2017	4.0	66.5
Public debt limit			
Barbados (public debt)	2018	12.0	123.6
Cyprus (public debt; guarantees)	2013	7.5	106.4
Iraq (public debt)	2016	13.5	66.9
Jamaica (public debt)	2013	13.0	124.8
Jamaica (public debt)	2016	7.5	96.9
Other Debt QPC (type)			
Angola (new oil-collateralized debt)	2018	12.5	91.0
Bosnia and Herzegovina (non-concessional st debt)	2016	n.a.	44.7
Georgia (guaranteed debt)	2017	n.a.	41.3
Mongolia (non-concessional external debt; stock of guarantees)	2017	13.5	94.9
Pakistan (guaranteed debt)	2019	12.5	234.0
Serbia (guaranteed debt)	2015	14.0	76.0
Ukraine (guaranteed debt)	2015	14.0	79.3
Ukraine (guaranteed debt)	2018	8.5	64.3
Debt-realted IT (type)			
Albania (guaranteed debt)	2014	12.5	72.2
Armenia (average concessionality contracted debt, guaranteed debt)	2014	5.0	48.2
Armenia (average concessionality contracted debt, guaranteed debt)	2019	2.5	54.6
Egypt (gross debt budget sector)	2016	12.5	113.8
Jordan (central govt debt; st debt)	2016	12.0	95.1
Jordan (public debt)	2020	8.0	99.1
Sri Lanka (outstanding stock guarantees)[3]	2016	12.0	79.3
Suriname (guaranteed debt)	2016	2.5	68.8
None			
Argentina	2018	5.5	64.5
Ecuador	2019	6.5	46.2
Kosovo	2015	n.a.	18.9
Morocco	2014	5.5	64.0
Morocco	2016	1.5	64.7
Morocco	2018	1.5	65.3
Pakistan	2013	8.0	64.0
Serbia	2018	3.0	58.4
Seychelles	2017	12.5	66.9
Tunisia	2016	3.5	56.0

[1]Sample includes 33-GRA supported programs ongoing between July 2015 and April 2020. FCLs, RCF/RFIs, and SMPs are not included in the analysis.
[2]For programs approved after July 2015: Based on DSA heatmap and debt levels based on program approval year. For programs approved before July 2015: Based on DSA heatmap and debt levels at first review after new DLP. Heatmap score from 0-15 based on 1 for each red indicator; 0.5 for yellow, and 0 for green. N.A. indicates low-scrutiny DSA.
[3]Sri Lanka IT on outstanding stock of guarantees introduced at fourth review.

Table 4. Breaches of Debt QPCs 2015-April 2020

Country	Debt limit type	Review	Size of breach[1] percent of limit/USD	%GDP	Reason for miss	Corrective action
Guinea	Nominal non-zero NCB	R2	1%	0.1	**Investment:** Signed previously undiscussed loan for key infrastructure project.	The authorities did not submit the loan for ratification to the National Assembly, and instead re-opened negotiations to achieve concessional financing terms. Staff modified the QPC to exclude debt that is non-concessional upon signature but later cancelled or renegotiated to become concessional.
Cameroon	Nominal non-zero NCB	R1	64%	0.3	**Investment:** The authorities advanced loan agreement initially included in the borrowing plan for the following year. The loan was related to infrastructure for Africa Cup.	Limit for the following year was lowered by the same amount.
Cameroon	Disbursements of NCB	R2	16%	0.4	**Technical:** Actual disbursements on major development projects were higher than anticipated (Owing to communications problems with a few financial partners).	Measures taken to better anticipate the recording of these disbursements through better planning and monitoring of disbursements
Iraq	Gross public debt	R2	4%	0.3	**Budget/Investment:** Budget deficit higher than programmed and authorities issued guarantees for infrastructure projects	Prior actions to improve fiscal discipline
Liberia	PV Limit	R7R8	8%	0.4	**Reporting:** Reporting slippage (project loan that was ratified by the legislature not included in the total amount).	Debt management unit began monthly reporting on all signed/ratified loans
Malawi	Zero NCB Limit	R1	US$127 million	1.9	**Technical:** Technical oversight in the TMU when nonresident bank purchased domestically denominated Treasury Notes that constituted NCB.	TMU has been modified going forward to exclude domestically denominated Treasury Notes and Bills from the QPC.
Mauritania	Zero NCB Limit (w/exception)	R4	0.02	<0.1%	**Technical:** Actual value of NCB loan exceeded allowed amount by 2 percent when valued at program exchange rates.	None (waiver granted on basis of there being no material impact on the DSA).
Mozambique	PV Limit	R1	n.a.	n.a	**Reporting:** Disclosure of hidden debt by SOEs revealed breach of NCB limit under previous program.	N.A. program went off track.

[1]Size of breach refers to the percent of the debt limit for non-zero limit cases. Breaches of zero NCB limits are given in USD.

Table 5. Modifications of the Debt Limits to Accommodate Financing, 2015-April 2020

Program	Limit Type	Review	Modification
Afghanistan	Zero NCB	R1	**Investment:** Added exclusion for critical infrastructure project.
Cameroon	Non-Zero NCB	R5	**Investment:** Modified from an 2 percent of GDP nominal NCB limit for critical projects to a zero NCB limit with an adjustor of up to 1 percent of GDP for critical projects.
Cote d'Ivoire	PV	R1,R2	**Debt management:** Added adjustor for Eurobond issuance and revised 2017 ceiling upward by 3.2% GDP.
Cote d'Ivoire	PV	R3	**Debt management:** Revised 2017/18 ceiling by 5.8% GDP to accommodate Eurobond issuance.
Ghana	Non-Zero NCB	R1	**Debt management/investment:** 2015 ceiling revised upward by 4% GDP to accommodate larger Eurobond issuance and critical infrastructure projects.
Ghana	Non-Zero NCB	R2	**Debt management/investment:** Established separate debt limits for debt management and critical infrastructure projects to accommodate Eurobond issuance, World Bank loan, and carry over of some priority loans.
Ghana	Non-Zero NCB	R3	**Budget support:** Ceiling revised upwards by 0.4% GDP to accommodate World Bank budget support
Ghana	Non-Zero NCB	R4	**Investment:** Ceiling for project debt revised upwards by 0.7 percent of GDP based on authorities' desire to accelerate development plan.
Ghana	Non-Zero NCB	R5R6	**Debt management:** Debt management limit reset for 2018 for planned Eurobond issuance.
Ghana	Non-Zero NCB	R5R6	**Investment:** Ceiling for project debt revised upward by 3.7% of GDP based on authorities' desire to accelerate development plan.
Mauritania	Zero NCB	R1	**Investment:** Adjustor applied totaling 3.6% of GDP to finance priority projects for which concessional financing not available
Serbia	Guarantees	R6	**Investment:** Ceiling revised upward by 0.5% of GDP to accommodate guarantee of EBRD loan
Togo	Zero NCB	R2	**Debt management:** Added adjustor to allow for some NCB to repay domestic debt.

Table 6. Non-Finance Related Modifications of the Debt Limits 2015-April 2020

Program	Debt Limit	Review	Modification
Modifications in response to changes in macroeconomic or borrowing projections			
Gabon	Total external debt	R1	Ceiling revised downward due to shortfall external financing (1.2% GDP)
Ghana	Non-Zero NCB	R3	Established separate limit for loan for national oil company owing to delays in securing loan
Ghana	Non-Zero NCB	R4	NCB imit for national oil company due to delays in securing loan
Kyrgyz Republic	PV	R2	Ceiling revised downward due to weaker macroeconomic outlook (0.003% GDP)
Kyrgyz Republic	PV	R3	Ceiling revised upward due to improved macroeconomic outlook (0.015 GDP)
Kyrgyz Republic	PV	R4R5	Ceiling revised upward 0.01% of GDP due to improved macroeconomic outlook.
Mali	Non-Zero NCB	R6	Ceiling revised downward 2.8% of GDP due to revised borrowing plan.
Niger	PV	R5	Ceiling revised upward by 2 percent of GDP due to revised disbursement profile.
Modifications due to implementation of new DLP			
Honduras	Non-Zero NCB	R2	Modified to PV Limit
Kenya	Non-Zero NCB	R1	Dropped limit
Kyrgyz Republic	Zero NCB	R1	Modified to PV Limit
Liberia	Non-Zero NCB	R5R6	Modified to PV Limit
Malawi	Zero NCB	R7R8	Modified to non-zero NCB Limit
Mali	Zero NCB	R4	Modified to non-zero NCB Limit
Niger	Zero NCB	R2	Modified to PV Limit
Rwanda	Non-Zero NCB	R4	Modified to IT
Senegal	Non-Zero NCB	R1	Dropped limit
Sierra Leone	Non-Zero NCB	R3R4	Modified to PV Limit
Tanzania	Non-Zero NCB	R3	Dropped limit
Uganda	Non-Zero NCB	R5	Modified to IT on guaranteed debt
Modifications in response to upgrades in risk ratings/debt management capacity			
Mali	Non-Zero NCB	R7	Modified to PV Limit owing to upgrade in debt monitoring capacity.
Benin	PV	R2	Ceiling revised upward due to revised DSA.
Madagascar	Nominal NCB	R1	Modified to PV Limit due to upgrade in debt management capacity.
Burkina Faso	Nominal NCB	R1	Modified to PV Limit due to upgrade in debt monitoring capacity.
Modifications in response to missed PCs			
Cameroon	Disbursements of NCB	R2	Expanded criteria to cover all project loans
Guinea	Non-Zero NCB	R2	Modified the definition of the QPC to exclude debt that is non-concessional upon signature but later cancelled or renegotiated to become concessional
Cameroon	Non-Zero NCB	R1	Ceiling revised downward
Other/Technical modifications			
Gabon	Total external debt	R3	Modified from monitoring on contracting to disbursement basis
Mongolia	Non-Zero NCB	R1R2	Modified ceiling from gross debt basis to net debt
Pakistan	Ceiling on govt guaraunteespaces	R1	Modified defintion to include both issued and executed guarantees (previously limited to issued)
Sao Tome and Principe	Zero NCB	R1	Combined short and long-term debt limits into a single PC

STAKEHOLDER SURVEY AND CONSULTATION RESULTS

A. Roundtable Discussions

4. Staff held over the course of 2019 several roundtable discussions with stakeholders to discuss preliminary findings from the review and ideas for reform over the course of 2019:

- **Department for International Development (DFID) Hosted Roundtable Discussion.** The IMF and the World Bank held a joint discussion with borrowing country authorities, MDBs, CSOs, and development experts, hosted by DFID. The main messages included the following:
  - Participants expressed broader concerns about inadequate concessional resources, pointing to the need to explain staff's ultimate proposals against this backdrop.
  - They welcomed the idea of enhancing debt data transparency and a broader use of PV limits, and advocated for taking on more risk in moderate-risk countries to promote investment and encourage growth.
  - At the same time, some participants noted that in high-risk countries with access to concessional financing, zero NCB limits would probably continue being appropriate given the rising debt levels.
  - Participants acknowledged that NCB exceptions can be important in some high-risk countries (e.g., there might be an urgent need for NCB to rebuild infrastructure). In that context, they suggested to focus on strengthening countries' capacity for selecting and implementing projects (e.g., through developing PIMA-like frameworks).
  - Participants also provided broad support for staff's proposals to better tailor debt limits to country vulnerabilities.
- **Annual Meetings Roundtable with Country Authorities.** Feedback from borrowing country authorities on the DLP was generally positive.[2] Several delegates emphasized that the DLP helped to prioritize investments, led to a more careful review of borrowing plans, increased the focus on maximizing favorable borrowing terms, and improved central government control over debt contracting by SOEs. At the same time, delegates emphasized the importance of fiscal targets, sound financial management institutions, and strong governance in controlling debt. In addition, they noted the key role of debt management and transparency in helping to safeguard debt sustainability. Moving ahead, delegates underscored the need to better understand country-specific challenges and for more flexibility in setting and modifying debt limits.

[2]Attendees included representatives from Angola, Barbados, Cote d'Ivoire, Egypt, Ghana, Sri Lanka, Tunisia, Ukraine, and the Center for Global Development.

- **Annual Meetings Roundtable with Multilateral Development Banks.** A roundtable discussion jointly organized with the World Bank was held with Multilateral Development Banks (MDBs).[3] Several MDBs noted that rising debt vulnerabilities presented challenges to their operations. In this regard, they noted the limitations of evaluating public investment on a project-by-project basis, particularly due to political considerations that can undermine a project's ability to realize expected revenues (e.g., setting and collecting appropriate tariffs, tolls, etc.). Some emphasized the need for more flexibility in DLs, including for profitable non-concessionally financed projects, especially in countries with relatively limited access to concessional financing. At the same time, it was noted that more flexibility could result in fewer incentives to provide concessional financing, potentially further reducing the availability of concessional resources in the future.

B. Survey Results

5. A survey of mission chiefs (MCs) with programs that started after January 2015 was conducted in December 2018, broadly indicating the DLP has been effective. The survey received 33 responses. Most respondents considered that the DLP had been effective or somewhat effective in containing debt vulnerabilities, including by: (i) limiting NCB; (ii) limiting borrowing in general; and (iii) pushing back line ministries (See Figure 1 Qa). Most respondents also considered that the DLP complemented fiscal conditionality by capturing: (i) contracting of debt; (ii) guarantees; and (iii) specific borrowing terms (e.g., short-term debt, non-concessional debt, collateralized debt) (see Figure 1 Qb). MCs that responded that the DLP was not effective indicated that it: (i) was overdetermined and fiscal conditionality would have sufficed; and (ii) did not prevent the authorities from concealing debt.

6. MCs also identified issues that suggested the need for further refinements of the DLP (See Figure 1 Qc)**.** Key among them were that the policy: (i) constrains investment (including by limiting semi-concessional loans); (ii) leads to incentives to avoid requesting a program (and borrow from non-concessional external and domestic sources); and (iii) leads to nontransparent practices to circumvent conditionality. Several MCs indicated that circumvention of DLs was an issue, citing concerns with PPPs and collateralized borrowing. Implementation challenges pointed to the need for further guidance, issues relating to government practices, as well as policy design issues (See Figure 1 Qd and Qe). Finally, less than 10 percent of MCs indicated that the DLP was effective in encouraging progress in strengthening debt recording and monitoring capacity, while 45 percent indicated it was somewhat effective. Reasons cited for the DLP not being effective included (i) the existence of other priorities and/or that the needed capacity building takes time as the most relevant factors; and (ii) the fact that the IMF does not provide TA in this area.

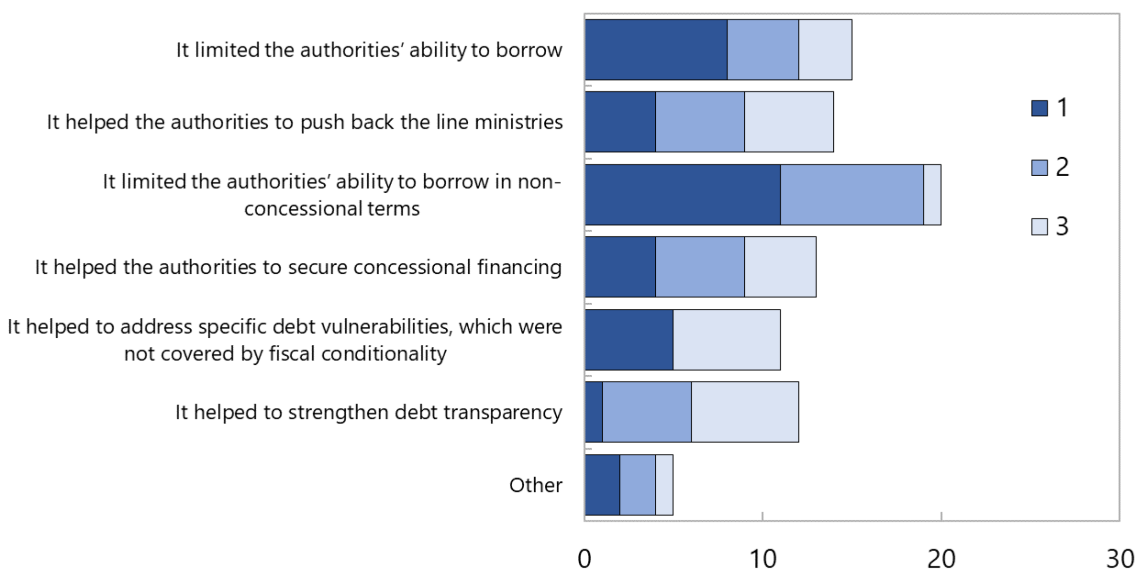
7. Surveys of country authorities and creditors were also conducted but received limited responses. Only two respondents replied to the country authority survey. A survey of 53 creditors

[3]Attendees included representatives from the African Development Bank, the Asian Development Bank, Inter-American Development Bank, Islamic Development Bank, European Bank for Reconstruction and Development, International Fund for Agricultural Development, and the Asian Infrastructure Investment Bank.

was conducted, but only 7 with significant lending activities responded.[4] Most respondents (71 percent) indicated that they had a strong understanding of how the DLP applies to their operations, the role of the authorities, and how to contact the IMF/WB for clarification. Views on the effectiveness of the DLP in containing debt vulnerabilities were mixed. Assessments ranged from effective (33 percent) to somewhat effective (50 percent) and not effective (17 percent). Meanwhile, indications of respondents adapting the financing they offer to comply with the DLP were limited. Creditors also pointed to information gaps presenting a key challenge for compliance with the DLP. Most (71 percent) indicated that they did not have enough information to check compliance with the debt limits conditionality agreed between the authorities and the IMF in their lending operations.

Figure 1. DLP Mission Chief Survey Results
(Number of respondents, 1= most relevant)

Qa. Three key reasons DLP helped contain debt vulnerabilities



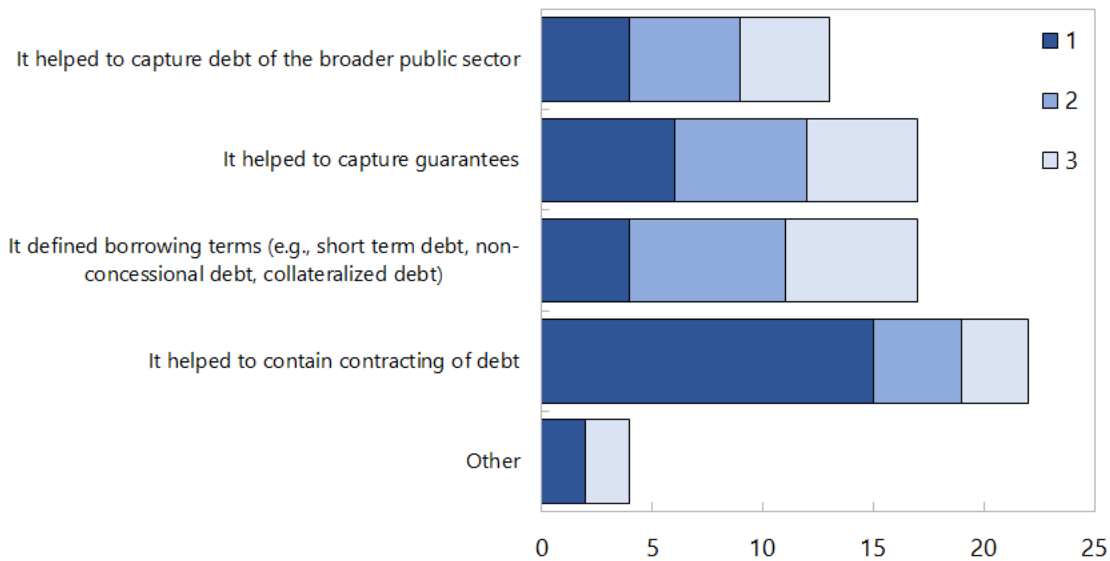
Source: December 2018 Survey of Mission Chiefs in IMF-Supported Program Countries.

[4]These included the Czech Export Credit Agency; The Export-Import Bank of Korea; UK Export Finance; EKF (Denmark Export Credit Agency); Norwegian Guarantee Institute for Export Credits; EXIMBANKA SR (Slovak Republic); Credendo (Belgium Export Credit) An additional respondent, Swiss Export Risk Insurance (SERV), did not answer most questions owing to lack of experience with lending.

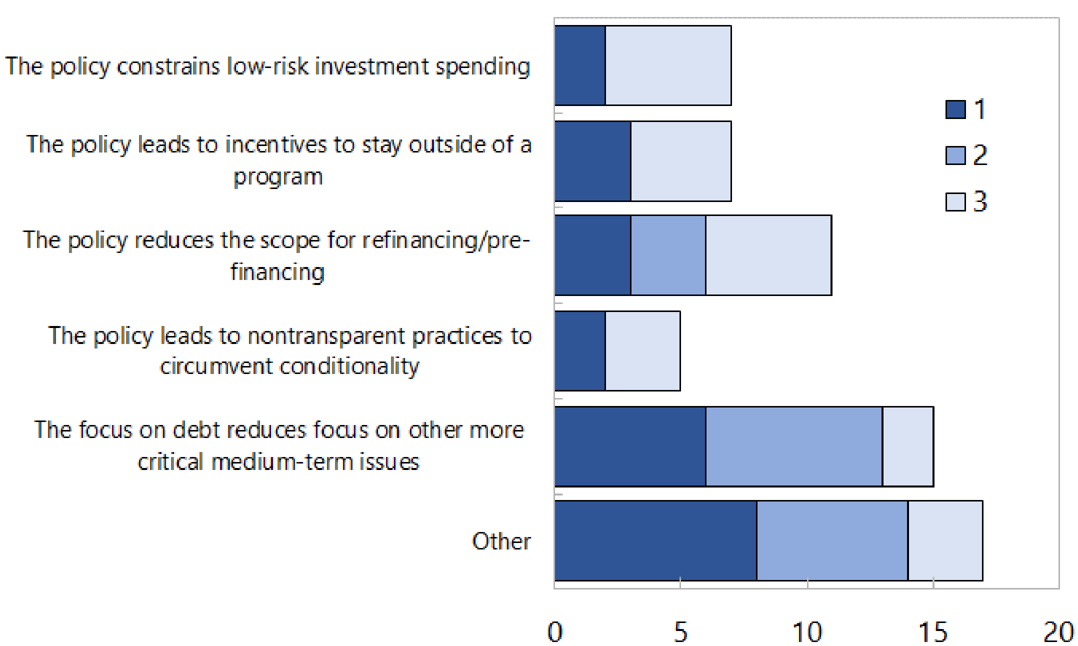
Figure 1. DLP Mission Chief Survey Results (continued)

(Number of respondents, 1= most relevant/important)

Qb. Three key reasons DLP complemented fiscal conditionality



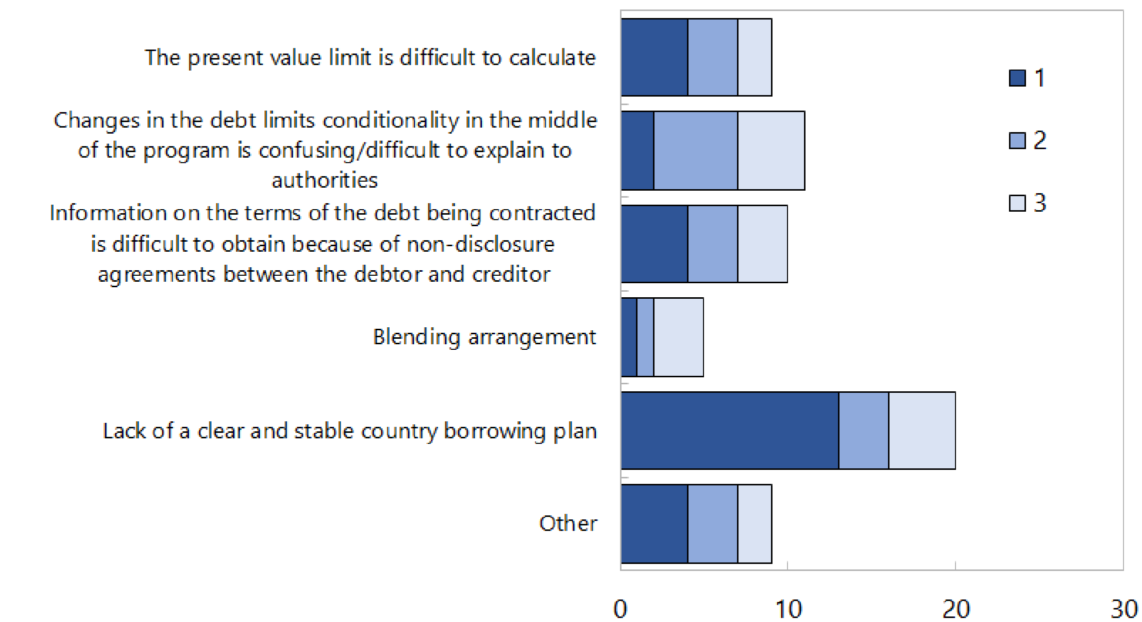
Qc. Other issues suggesting need for policy refinements



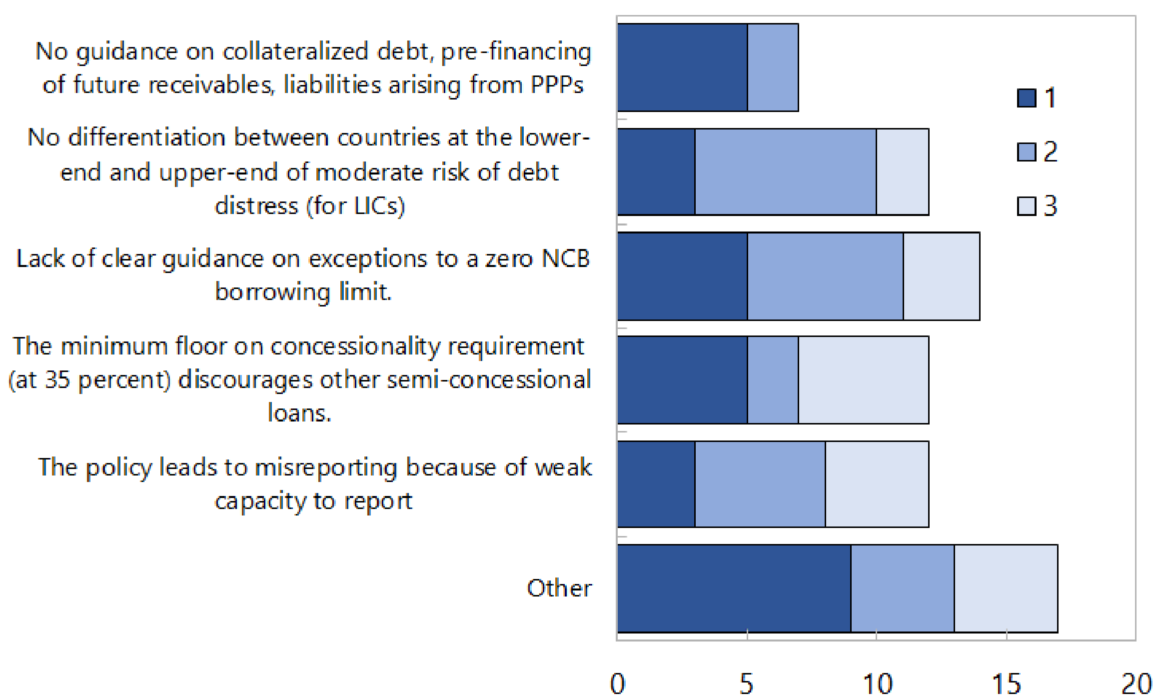
Source: December 2018 Survey of Mission Chiefs in IMF-Supported Program Countries.

Figure 1. DLP Mission Chief Survey Results (concluded)
(Number of respondents, 1= most relevant/important)

Qd. Three key DLP implementation challenges



Qe. Three most important gaps in the DLP framework



Source: December 2018 Survey of Mission Chiefs in IMF-Supported Program Countries.

ILLUSTRATIVE GUIDE TO TAILORING CONDITIONALITY

8. **There are several circumstances where tailored debt conditionality could be invoked in the revised DLP.** These include: (i) as the standard approach for countries that do not normally rely on concessional financing; (ii) as a potential approach for countries that normally rely on concessional financing but regularly tap international financial markets; and (iii) as an optional approach to target specific debt vulnerabilities (not addressed through standard debt or other program conditionality) for countries that normally rely on concessional financing.

9. **Tailoring is a case-by-case process, but it is underpinned by analysis of debt-related risks.** Broadly speaking, DSAs distinguish between three types of risks: (i) risks stemming from elevated debt levels; (ii) risks related to gross financing needs (GFNs) (high interest and/or amortization payments); and (iii) risks originating from debt structure (maturity, debt guarantees and related contingent liabilities, currency composition, and/or debt collateralization). Each risk can be concentrated in domestic or external debt. Both the MAC-DSA and LIC-DSF produce indicators which are informative on the extent of vulnerabilities along each of the aforementioned dimensions.

10. **Table 7 provides illustrative examples of how different types of debt conditionality can be used to address a variety of identified vulnerabilities.** These are not meant to be exhaustive, and in all instances the full details of the case would need to be accounted for. In order to keep conditionality parsimonious, tailored debt-related conditionality should only be invoked if it is aimed at addressing a macro-critical vulnerability that cannot be addressed through other forms of conditionality like fiscal conditionality.

Table 7. Illustrative Forms of Debt Conditionality in Response to Different Vulnerabilities

Area of vulnerability	High debt level	High GFN
Domestic	*(Most naturally addressed through fiscal conditionality)*	- Limit on domestic borrowing, aiming to substitute with external borrowing and/or encourage refinancing at longer maturities
External	- Limit on external borrowing, aiming to substitute with domestic borrowing	- Limit on external borrowing, aiming to substitute with domestic borrowing and/or encourage refinancing at longer maturities
Domestic + external	- Fiscal conditionality augmented with a limit on external borrowing	- Encourage refinancing at longer maturities
Area of vulnerability	**Debt structure**	
Maturity	- Limit on short-term borrowing - Limit on issuing debt maturing in specific years (to avoid bunching of maturities in years characterized by high financing needs) - Target for future average maturity of debt stock	
Contingent liabilities	- Limit on government guarantees - Limit on borrowing by vulnerable SOEs that can issue debt directly - Limit on the size of PPP programs - Broadening fiscal indicator coverage, to encompass the source of the vulnerability	
Currency composition	- Limit on foreign-currency denominated borrowing	
Collateralized debt	- Disclosure requirements - Limit or prohibit new issuances of collateralized debt - Set target to reduce the existing stock of collateralized debt	

ILLUSTRATIVE CHARACTERIZATION OF COUNTRIES RELYING ON CONCESSIONAL FINANCING WITH SIGNIFICANT ACCESS TO INTERNATIONAL FINANCIAL MARKETS

11. The following describes the criteria that are proposed for use in identifying countries eligible for the proposed tailoring approach. This eligibility is not meant to be fixed, but would vary depending on recent developments and the financing strategy underlying a program.

12. The proposed criteria draw on principles similar to those used for determining market access for PRGT blending and graduation purposes.[5] This approach would ensure broad consistency with both the IMF's access policies as well as the World Bank's criteria for IDA eligibility. "Significant access to international financial markets" would entail:

1. Drawing on measures used for determining market access for PRGT blending and graduation purposes, "significant access to international financial markets" would entail cumulative borrowing of at least 50 percent of quota in at least two of the preceding three years.[6]

Or

2. This access definition would also be met if access to these markets is an integral component of the member's borrowing plan or of the baseline projections of the Medium-Term Debt Strategy (MTDS), provided that the program envisages financing on international financial markets in the amount of at least 100 percent of quota over the course of the program period. This threshold would apply only in cases where the country does not meet the criterion of 50 percent of quota in prior borrowing.

13. For illustrative purposes, of the 70 PRGT-eligible countries there are 14 that currently meet the proposed significant market access definition based on past data (Table 8). Based on 2016–18 data, NCB had an average share of 37 percent of total new borrowing in these countries.[7]

[5]See *Eligibility to Use the Fund's Facilities for Concessional Financing, 2020*.

[6]See Eligibility to Use the Fund's Facilities for Concessional Financing, 2020. The proposed DLP test for regularly taping international financial markets does not include an income criterion and has a shorter horizon (three years) than the criteria for PRGT blending (five years) given the need for debt conditionality to reflect a country's more recent financing circumstances. The cumulative borrowing of at least 50 percent of quota threshold is similar to the PRGT blending threshold for countries at high risk of debt distress.

[7]In line with the practices to determine market access for PRGT-blending and graduation purposes, this analysis uses the World Bank's International Debt Statistics (IDS) database as the default, which typically has a ten-month lag. Allowing the definition to be reached if market access is an inherent element of the authorities' borrowing plan under the program would also capture more recent developments.

Most of the identified countries are also presumed or potential PRGT blenders except for Benin and Ethiopia which do not meet the additional income criteria.[8]

Table 8. Illustrative List of Countries Normally Relying on Concessional Financing and Meeting the Proposed Definition of Market Access[1]

Country (Current DSA rating)	Cumulative Eligible Financing 2016-18[2]			NCB/New Borrowing
	Quota (percent)	GDP (percent)	USD millions	Share of Total (percent)
Benin (M)	535	6.6	939	53.3
Cabo Verde (H)	86	1.5	29	12.4
Cameroon (H)	82	0.8	321	7.4
Côte d'Ivoire (M)	475	10.2	4376	60.8
Ethiopia (H)	552	2.9	2353	22.4
Ghana (H)	375	6.0	3914	72.5
Honduras (L)	200	3.0	708	36.5
Kenya (M)	484	4.2	3720	26.7
Lao P.D.R. (H)	672	5.6	1007	30.1
Maldives (H)	1486	8.4	446	25.6
Papua New Guinea (M)	278	4.5	1036	47.9
Senegal (L)	732	14.3	3352	51.3
Tanzania (L)	92	0.9	516	14.9
Zambia (H)	145	7.5	2002	50.2

Source: World Bank IDS.
1/ Cumulative market borrowing of at least 50 percent of quota in at least two of the three proceeding years (2016–18).
2/ Includes issuance of bonds or disbursement of commercial loans in international markets and covers public and publicly guaranteed debt.

THE DLP AND THE WORLD BANK'S SDFP

A. Overview of the World Bank's Sustainable Development Finance Policy

14. **In June 2020, the World Bank approved transitioning from the Non-Concessional Borrowing Policy (NCBP) to the Sustainable Development Finance Policy (SDFP).**[9] The objective of the SDFP is to incentivize countries to move toward transparent, sustainable financing and to promote coordination between IDA and other creditors in support of countries' efforts. The SDFP will help to achieve this objective by: (i) supporting IDA clients to strengthen policies, institutions,

[8]For countries at low to moderate risk of debt distress: GNI per capita higher than 80 percent of the IDA cutoff (currently US$1,175); for countries at higher risk of debt distress GNI per capita higher than 100 percent of the IDA cutoff.

[9]Sustainable Development Finance Policy of the International Development Association (IDA, 2020)

and practices for transparent and sustainable financing of development goals; (ii) enhancing coordination among borrowers, creditors and other development partners; and (iii) introducing a more robust monitoring and accountability framework. Country coverage has also been expanded from post-MDRI and IDA grant recipients to cover all IDA-eligible countries. The policy centers around two pillars detailed below: the Debt Sustainability Enhancement Program (DSEP) and the Program of Creditor Outreach (PCO).

15. The DSEP pillar focuses on incentives for IDA-eligible countries to move toward continued sustainable and transparent borrowing practices. Under this pillar, performance and policy actions (PPAs) aimed at strengthening debt transparency, fiscal sustainability, and debt management will be defined annually for all IDA countries at moderate or high risk of debt distress in close consultation with country authorities.[10] In the near term, with assessment of PPAs concluded at the end of FY2021 and set asides kicking off at the beginning of FY2022, the focus will be mostly on improving debt data transparency and debt management, given the post-COVID-19 environment. The PPAs will be calibrated to countries' specific debt vulnerabilities and government capacity constraints. If progress in implementing the PPAs is unsatisfactory after the first year, a portion of the IDA allocation will be set aside.[11] If there is satisfactory implementation progress on PPAs after the second year, the allocation set aside during the first year will be released.

16. The PCO pillar focuses on promoting stronger collective action among borrowers, creditors, and international development partners. The goal is to promote stronger creditor coordination (in particular among MDBs), and facilitate information sharing and dialogue, to help mitigate debt-related risks. IDA initiatives would build on the experience and the platforms built after the HIPC/MDRI initiatives where individual country efforts toward sustainable financing will also be promoted by other creditors. Specific actions under this pillar include: the promotion of "Core Principles of Sustainable Financing" across MDBs and IFIs; expanding the boundaries of MDB outreach; strengthening outreach and communication with bilateral creditors on the SDFP; promoting dialogue on sustainable financing and debt transparency with Paris Club, non-Paris Club and private creditors; strengthening dialogue and coordination around debt-related TA; and enhancing use of the Lending to LICs platform.

17. Debt limits under the SDFP would primarily take the form of nominal limits on non-concessional external PPG for countries at moderate or high risk of debt distress. PV limits on external borrowing could also be considered if circumstances warrant it. Low risk countries

[10]Countries normally excluded from the PPA and set aside system would include: low risk of debt distress under the LIC-DSF or countries under the MAC DSA for which World Bank Management determines that debt vulnerabilities are limited; those without regular IDA programs due to loans/credits in non-accrual status; and countries that are eligible for IDA's Remaining Engaged in Conflict Allocation.

[11]For moderate and high-risk countries the set aside would be 10 and 20 percent of IDA allocations, respectively. For blend and gap countries under the MAC DSA there will be a set aside of 10 percent unless WB management determines that the country's debt vulnerabilities are limited.

would normally not be subject to a ceiling. However, the setting of a ceiling could be triggered under certain circumstances (e.g., a rapid debt build-up).[12]

18. Ex-ante exceptions to the SDFP framework for setting borrowing ceilings maybe granted where borrowing is linked to projects with high economic and social returns. Such exceptions would be made on a case-by-case basis and require the borrower to share comprehensive information on financing and the impact of the project (volume, financing terms, disbursement schedule, use of proceeds and available project analysis). In principle, ex-post exceptions would not be granted, unless the financing was in response to an exogenous shock, or if the authorities could provide evidence that the project met the criteria for an ex-ante exception and provided a clear rationale for why it was not discussed ex-ante.

B. Complementarity Between WB and IMF Debt Policies

19. The two policies would continue to be closely aligned (Table 9):

- Staff from both institutions would coordinate to ensure close alignment between the debt policy commitments in an IMF-supported program and those specified in the SDFP. When initiating a new IMF-supported program, program design would take account of borrowing limits set under the SDFP together with an updated assessment of debt vulnerabilities. The SDFP would maintain the approach of aligning, in principle, borrowing limits with the DLP when there is an IMF-supported program. When an IMF-supported program expires, the SDFP would take account of borrowing limits set under the DLP together with an updated assessment of debt vulnerabilities.

- Exceptions for NCB would also be broadly aligned. Both the DLP and SDFP would only allow for NCB exceptions related to the general framework for setting borrowing ceilings under these policies when related to critical projects where concessional financing is not available, and/or related to debt management operations.

- The policies would complement each other in promoting improved debt transparency, fiscal sustainability, debt management, and governance. IMF-supported programs are well-positioned to obtain relevant information on debt more systematically (particularly at the outset). World Bank operations are often better positioned to address the underlying legal and institutional problems that give rise to inadequate transparency and other capacity shortfalls, particularly where there are multiple competing priorities in an IMF-supported program.

- The calibration of limits for countries normally relaying on concessional financing under both policies would be underpinned by the joint LIC-DSF.[13]

[12]Annex 3 of IDA (2020) presents a framework for setting borrowing ceilings under the SDFP.

[13]For countries that do not normally rely on concessional financing, the calibration of limits, if any, would be supported by the IMF's MAC DSA for the purposes of the DLP, and the World Bank's analysis of debt vulnerabilities for the purposes of the SDFP.

Table 9. Comparison of WB SDFP and IMF DLP Under Reform Proposals

	SDFP	IMF DLP w/Proposed Reforms
Duration	Applies continuously	Applies exclusively under IMF-supported program
Context of Setting Limits	Debt sustainability and macro dialogue; IDA's fiduciary responsibility to its contributors; prudent management of scarce concessional IDA resources	Within programmatic macro approach, limits are set in the form of performance criteria and indicative targets, and are part of wider range of parameters.
Country Coverage	All countries eligible for IDA resources (74 countries during IDA19)	IMF membership (189 countries)
Available Instruments	Set-aside portion of IDA-allocation to incentivize completion of performance policy actions (PPAs), which include debt limits (consistent with IMF DLP). Hardening of terms may apply in cases of severe or repeated breaches of PPAs such as the NCB ceiling.	Under IMF program: performance criterion on non-concessional borrowing or present value of debt.
Framework for debt ceilings:		
LIC-DSF low risk of debt distress	Normally not subject to ceiling unless circumstances warranted (e.g. significant debt build-up).	Ceiling not required (option for targeted if needed)
LIC-DSF moderate risk of debt distress	Normally nominal NCB ceiling to avoid risk of external debt distress downgrade.	PC on PV limit of external borrowing (in most cases) calibrated to avoid external debt distress downgrade
LIC-DSF High risk of debt distress (sustainable outlook)	A zero ceiling on NCB borrowing will apply in principle. NCB would be allowed only under exceptional circumstances (e.g. for debt management operations).	Zero NCB for countries w/o significant access to international financial markets (w/ NCB exceptions allowed under limited circumstances). PV on external borrowing for countries w/ significant access to international financial markets (or alternative if better targeted)
LIC-DSF In debt distress or at high risk of debt distress (unsustainable outlook)	A zero ceiling on NCB applies. A non-zero ceiling could be considered, for example, for arrears clearance operations only.	N.A. (IMF lending prohibited)
MAC DSA	Normally not subject to ceiling unless circumstances warranted (e.g. significant debt build up)	Tailored limits if there are significant debt vulnerabilities
NCB Exceptions	Ex-ante exceptions for projects with high economic and social returns when concessional financing is not available and if the operation is needed for debt management operations that do not lead to a worsening of the debt profile, and is consistent with the MTDS and MTFP (if exists). Ex-post exceptions only if in response to exogenous shock or if project meets ex-ante criteria and rationale for not being discussed exante.	Exceptions for projects integral to the authorities' development program where concessional financing is not available (assessed using a signals-based approach) or debt management operations that result in the overall improvement of the debt profile.
Institutional Process	Management-driven given nature of continuous application (Board regularly informed to promote oversight)	Board-driven as debt limits are an integral part of IMF programs.

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