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Statement by Ms. Mannathoko, Mr. Sitima-wina, Mr. Abdullahi, and Mr. Cham on Reform of the Policy on Public Debt Limits in IMF-Supported Programs (Preliminary)
Executive Board Meeting
October 28, 2020

We thank staff for the well-structured report and carefully framed proposals to reform the Debt Limits Policy (DLP). We appreciate the significant effort made to strike an appropriate balance between containing debt vulnerabilities and providing the flexibility needed to finance development needs; this being a critical consideration for most of the countries in our Constituency. We also welcome the supplements to the report that provide insights into what could appear in the Staff Guidance Note (SGN). Nevertheless, where proposals allow staff discretion such as the introduction of additional conditionality and application of judgement in the context of a DSA, we expect that these areas will be carefully addressed in the SGN, in order to promote consistent and evenhanded application of the policy across the membership. We look forward to the circulation of the SGN, and as staff noted in May, Board members may call a meeting to discuss it. We broadly support the reforms and have the following specific comments on the proposals.

Debt Transparency

Enhancing debt data disclosure to staff: We agree with the proposals to introduce an explicit expectation that critical debt data disclosure gaps will be addressed upfront in Fund-supported programs, unless capacity constraints preclude this, in which case (for members committed to transparency) we urge simultaneous TA or CD at the start of the program to address the gaps, rather than the use of prior actions which delay engagement. *Could staff confirm that the Staff Guidance Note will require mission teams to demonstrate that they have consulted with authorities – both to eliminate misunderstandings, and to confirm that there is capacity to fill the debt disclosure gaps, before imposing prior conditions?*

We concur that beyond addressing critical data gaps, additional debt-related information can be obtained during the program. Authorities' efforts to enhance accurate debt data collection, disclosure, and transparency should be supported by technical assistance where appropriate. The proposal for a risk – based approach that identifies "red flags" such as omitted state or local

government, SOE, PPP or SPV debt; or missing information related to large debt holdings is reasonable; however we emphasize that to do this effectively, it will be important for staff to first gain a proper understanding of the country specifics if they are to properly assist the authorities in addressing complexities related to debt monitoring and debt negotiations, without adding unintended frictions.

Enhancing transparency on debt holders' profiles: We support the rationale and see the merit in promoting transparency of debt holders' profiles. Enhanced transparency will facilitate swifter debt operations should a country have to restructure its debt, as the process would start from a widely available information set. It will also strengthen program design, facilitating an accurate assessment of the extent and nature of debt vulnerabilities, including rollover and concentration risks. We appreciate the illustrative debt holders' profile table in Annex I, however we wish to highlight that the expectation that the table be filled in during the early stages of the program and no later than the time of the second review, should be contingent on the adequacy and timeliness of TA or capacity support availed to a country, where such support is needed to enhance debt data disclosure. *Could staff clarify how authorities would be required to report in cases of ongoing negotiations where loan terms are confidential as they are not finalized. We note, furthermore, that some countries face delays when requesting creditor authorization to disclose loan terms to the Fund. Similarly, in some instances with unconventional loan instruments, staff have misinterpreted the terms of the loan. Authorities should not be penalized for these delays. Could staff also update us on the IIF working group's voluntary code on transparent lending and the information sharing platform for private creditors?*

Reforms Covering Countries that Normally Rely on Concessional Financing

We welcome the proposed changes that improve the policy's fit to country-specific circumstances. The categorization also clarifies treatment under different conditions.

B.1. Countries with significant access to international financial markets: For market access countries that are at high or moderate risk of debt distress (i.e. where debt conditionality is applicable), we support the default use of PV- limits derived from the country's public borrowing plan, and informed by the DSA. Regarding the caveat allowing alternative formulations of debt conditionality, we stress that staff guidance should ensure that the authorities are consulted on the alternative format and that country specific circumstances or idiosyncrasies are properly accommodated. *Could staff confirm that comprehensive guidance will be provided in the Staff Guidance Note on the process for any application of judgement?*

Regarding the criteria used to determine that a country has "access to international financial markets on a significant scale" we consider the proposed three-year horizon to be appropriate. However, we wish to guard against the undue exclusion of some small market access countries due to the limited market access definition provided. *We seek staff confirmation that the complete market access definition in IMF policy (SM/20/27, Box 1) will still apply. Namely: "A country would also be deemed to meet the market access criterion if there were convincing evidence that the sovereign could have tapped international markets on a durable and substantial basis, even though the scale or duration of actual public-sector borrowing fell short of the specified thresholds. This would be a case-specific assessment, considering such relevant factors as the volume and terms of recent actual borrowing in international markets and the sovereign credit*

rating". We are of the view that this text should also be added to this report as it is part of the definition. Staff comments are welcome.

B.2. Countries without significant access to international financial markets: For non-market access countries at moderate risk of debt distress, we welcome the expanded use of PV limits in cases where debt monitoring and reporting capacity is assessed as adequate; however the Staff Guidance Note will need to provide clear direction on what aspects of debt management and TA reports can be applied to this assessment, to ensure consistent treatment across countries. It will also be important that staff ensure that the authorities understand and are satisfied with the basis for the staff assessment. *Could staff elaborate on what they have in mind for staff guidance on this issue?*

We note that higher scrutiny of borrowing plans is needed for countries at moderate risk of debt distress but with limited space to absorb shocks, so they do not regress into high risk of debt distress; and we agree that having a buffer in the form of adequate flexibility in project execution, is desirable, as is having suitable state-contingent features in sovereign debt. In this regard, we urge staff to advise authorities on the use of state contingent debt instruments as they incur new debt or restructure existing debt.

For non-market access countries at high risk of debt distress, we note the proposal to retain the presumption of a zero limit on NCB. Exceptions would be allowed to finance key projects or debt management operations. In this regard, we welcome the proposed signal approach for NCB project exceptions, noting that staff also allow for the expansion of the indicative set of core options. Nevertheless, the option staff have to block the financing of a valid or critical project because it is in a national development plan (NDP) that a stakeholder considers to be of "poor quality or not credible" because it has some vanity projects, remains a concern for us. It is worth noting that the stakeholders cited in Box 5 all participate in the NDP process leading up to national validation of the NDP. *More importantly, however, to the extent that the specific projects being considered for financing are not vanity projects and are clearly beneficial for the country (e.g. SDG-related projects) the rationale for withholding financing remains unclear, since the financing would not go to the vanity projects. Could staff reconsider the framing of this requirement and confirm that the staff guidance note will ensure critical projects are not blocked due to criticism of unrelated projects in an NDP?* With respect to concerns over the repeated use of NCB exceptions, it would be important for authorities to be informed at the time of the first use of NCBs for debt management operations, that repeated use could trigger an assessment at some point.

B.2.4. Adjusting the definition of concessionality: We appreciate why staff prefer that blended financing arrangements that include a financially significant amount of grants in kind, be classified as non-concessional in the absence of international competitive bidding (that helps determine the fair value of such in kind assets); and given the challenge of obtaining neutral and fair evaluations from third-party technical consultants. However, we would also urge that the SGN requires staff to first ensure (in consultation with authorities), that a fair assessment of the assets is not available, before discounting an in-kind grant, as this could prevent critical project financing. With respect to collateralization, we agree that financing involving collateral that is unrelated to a project or transaction should be treated as non-concessional. We also welcome the elimination of the high-concessionality tool that required a grant element in excess of 35 percent for selective cases.

Debt Management Considerations

We concur with staff that the proposed DLP structure retains incentives to improve debt management capacity, since access to flexible PV limits would require adequate capacity to record and monitor debt. Furthermore, countries with significant access to international financial markets will also be incentivized to adopt a MTDS and an active annual borrowing plan in order to access the more flexible tailored conditionality regime. However, for countries that are found to have significant debt recording and monitoring weaknesses, while we agree that programs will need to address these deficiencies, we urge staff to facilitate capacity building in a manner that still enables timely financing, as the implications of delayed financing for critical poverty-related spending in these countries can be significant.

Staff will also need to ensure that the authorities understand the rationale for the determination of weak capacity and are satisfied with the assessment, given the possibility of shortcomings in some of the assessment tools proposed. *We would expect the staff report to provide a full explanation for the determination, including the viewpoint of authorities.* We wish to avoid situations where developing countries perceive that they are being punished for weak capacity, rather than being supported to overcome it. We encourage staff to see capacity weaknesses as an opportunity to introduce an enhanced CD agenda on debt management into a program, and to align the CD delivery to strengthening debt management and reporting, in the program. Beyond this, we also note that countries with adequate debt recording and monitoring capacity may nevertheless need CD in new areas relating to access to international capital markets and the management of more complex debt instruments. We therefore encourage a supportive, productive approach to debt-related capacity issues in general.