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Statement by Mr. Moreno and Mr. Lopez on Reform of the Policy on Public Debt Limits in IMF-Supported Programs (Preliminary) Executive Board Meeting October 28, 2020

The current approach to debt limits is still valid but additional enhancements are warranted and timely. We thank staff for their comprehensive set of papers and for their efforts to present proposals to encompass the challenges of countries with debt vulnerabilities, while preserving sustainability, ensuring even-handedness and allowing for flexibility. The 2014 reform introduced significant improvements to the DLP that should be preserved, although some gaps remain and other challenges have emerged, especially in a context of increasingly high levels of public debt, changing landscape in the creditor and debtor structure, and extended episodes of debt distress in LICs. The COVID-19 crisis has exacerbated some of these pre-existing vulnerabilities. In this regard, the G20–Paris Club Debt Service Suspension Initiative has been instrumental to support the poorest countries through the pandemic by creating much needed fiscal space to support health spending and counteract its economic consequences.

We are reassured by staff´s findings that the DLP has served countries with IMF-programs well, anchoring fiscal policy in program design and containing debt vulnerabilities. DLP implementation has been ample, although—according to the Stakeholder Survey results—more flexibility would be needed to ensure DLP principles are more linked to country-specific circumstances. *Nevertheless, based on the analysis provided by staff, it is not clear if the 2014 reform has improved the former framework in terms of program success. Staff´s report presents a comparison between countries with and without programs, but it does not evaluate diff-in-diff outcomes of pre- and post-reform developments in IMF-programs. Staff´s comments are welcomed.*

Staff´s report appropriately identifies some gaps and challenges affecting the different phases of the debt limits process, as illustrated in Fig. 11. The lack of transparency and disclosure of debt data is a recurrent issue in policy discussions and international initiatives. We also share the concern on the rising debt vulnerabilities that can emerge from State-Owned Enterprises (SOEs), Public-Private Partnerships (PPPs) and collateralized debt. We must insist on the importance of urgently addressing this problem, which is essential not only to detect and identify debt vulnerabilities, but also to design well-fitted programs and to swiftly deal with restructuring processes. Nevertheless, some flexibility, based on a case-by-case approach, may be needed in countries with limited capacity.

Technical assistance on debt management, monitoring and reporting should continue to play a complementary role in the DLP.

We support the introduction of an explicit expectation that critical debt data disclosure gaps should be addressed upfront in IMF-supported programs, including creditor/debtor composition, debt structure, borrowing terms or other debt-instrument characteristics. If data gaps should lead to conditionality, it is important to recognize that these gaps are not only critical for program implementation, but also for the rightful pricing of risks by creditors. Furthermore, introducing a table providing a profile of debt holders in program documents may proof to be useful. In the current situation, where many debtor countries have large and increasing exposures to non-Paris Club creditors, using conditionality to broaden the creditor base could reduce debtor´s vulnerabilities. However, this conditionality should be managed carefully in order to avoid a discretionary behavior. *We would appreciate further clarification by staff on how this tool could be implemented.*

Regarding the conditionality design of the DLP, rules should ensure flexibility and consistency in reducing debt vulnerabilities, while preserving access to non-concessional financing in certain circumstances. We have some comments depending on the specific-country situation:

- **Countries that rely on concessional financing**. We welcome the amendments introduced in the DLP for countries that usually rely on concessional financing, making a specific distinction between countries with and without significant access to international financial markets, since their challenges may be different. We also support the aim to extend the use of PCs or ITs in present value terms in the case of countries at high and medium risk of debt distress. We believe that the use of PV limits better reflects debt burdens, which at the same time facilitates comparability between debt categories and incentivizes concessional financing.

- **Besides, for countries with significant access to international financial markets, a more tailored approach is warranted**, including alternative formulations of conditionality on debt limits. These conditions would depend on country-specific circumstances and should be fully explained and justified by staff.

- **However, we have several concerns on the proposals in the case of countries with significant market access**. First, the use of PV limits differs from the use of nominal term limits by the WB in the SFDP, which could generate confusion. Second, the use of PV limits derived from a public borrowing plan could create some additional borrowing space. In the current context of large debt accumulation, this flexibility could be cumbersome. *Staff´s comments are welcomed. Additionally, could staff clarify what are the options in case the country does not have adequate capacity to record or monitor debt?* Finally, regarding the eligibility criteria for countries with significant access to markets, conditions stated in the document have a qualitative nature and do not seem to establish quantitative targets in order to reach the minimum bar. *It would be useful to clarify how staff is planning to implement it.*

- **For countries without significant access to international financial markets and at medium risk of debt distress, we see the need to retain the flexibility** introduced in the 2014 reform in cases of limited debt management capacity, conditioned to a well-justified assessment by staff. Well-designed borrowing plans, including buffers, and strict monitoring will also facilitate debt stability and risk management. *However, there is no information on the report on how these buffers would work or would be designed. Staff´s comments are welcomed.*

- **Regarding countries without significant access to international markets and at high risk of debt distress, we support retaining the zero NCB rule**. Besides, a clearer guidance on exceptions to this rule is welcome, with the aim to ensure that exceptions serve to improve the profile and the present value of debt. In the case of exceptions related to the NCB financing of investment projects, the signal-based approach proposed by staff could be a useful tool to identify core projects aligned with national development plans. However, if badly calibrated, signals could be excessively loose, which could lead to further debt accumulation. *We would appreciate staff´s clarifications on how the internal process to approve and review these exceptions would be implemented.*

Finally, we welcome the clarification on the definition of concessionality. We support the revised definition of concessional debt in specific cases, such as the inclusion of grants in kind, due to the difficulty in assessing its value, and of debt collateral unrelated to the transaction, which could create new vulnerabilities and increase the cost of uncollateralized debt. Moreover, we back the simplification of the definition of concessional debt taking solely into consideration the standard 35 percent threshold.