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Enabling poor rural people
to overcome poverty

IFAD lending terms and conditions – Hardened lending terms

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For: Approval

Recommendation for approval

The Executive Board is invited to approve:

- The creation of a category of lending terms similar to the hardened terms offered by the International Development Association (IDA).
- The application of such terms to IFAD loans for those countries to which IDA provides hardened terms.
- Lending under IFAD hardened terms will be identical to IFAD highly concessional terms except for the maturity period, which will be 20 years instead of 40.
- The category of IFAD hardened terms, as defined in this report, will remain effective for as long as the IDA hardened terms remain in force, as currently defined.
- The revision of section 5.01 (Lending Terms) of IFAD's General Conditions for Agricultural Development Financing to introduce the IFAD hardened terms category as follows:
 - “(b) Hardened Terms: Loans granted on hardened terms shall be free of interest but bear a service charge of three fourths of one per cent (0.75%) per annum payable semi-annually in the Loan Service Payment Currency, and shall have a maturity period of twenty (20) years, including a grace period of ten (10) years starting from the date of approval of the Loan by the Fund's Executive Board.”

The order of the current paragraphs (b) (c) (d) (e) (f) of section 5.01 will be renumbered accordingly.

IFAD lending terms and conditions – Hardened lending terms

I. Background

1. In its resolution 158/XXXIII on the Revision of the Lending Policies and Criteria, the Governing Council decided as follows:
 - “1. Upon the proposal of the President, the Executive Board shall submit to the thirty-fourth session of the Governing Council in 2011 revised Lending Policies and Criteria that shall take into account all developments since the last revision of the Lending Policies and Criteria in 1998 and express concisely and clearly the broad policies and criteria applicable to financing by the Fund.
 2. In the interim period prior to the adoption of the revised Lending Policies and Criteria by the Governing Council, the Executive Board shall have the authority to create a category of lending terms similar to the hardened terms offered by the International Development Association (IDA) and apply such terms to IFAD loans to countries to which IDA provides hardened terms.”
2. The purpose of this report is to seek the Board's approval to create the category of IFAD 'hardened terms', and the modalities of its application to IFAD financing.

II. IDA hardened lending terms

3. The category of hardened lending terms was introduced by IDA starting with the IDA13 period and has been effective since July 2002. Hardened terms are offered to IDA countries with GNI per capita above the operational cut-off for IDA eligibility for more than two consecutive years, but which are not yet creditworthy to borrow from the International Bank for Reconstruction and Development (IBRD).
4. Hardened term credits are provided with a 10-year grace period followed by a 10-year repayment period (i.e. a maturity period of 20 years), a fixed service charge and no interest. The distinction between standard IDA terms and hardened terms is the maturity period, 40 years in the first case, 20 in the latter.

III. Introduction of hardened lending terms in IFAD

Rationale for introduction of IFAD hardened terms

5. In 2009, several countries receiving hardened terms lending from IDA requested similar treatment from IFAD. IFAD management therefore proposed to introduce hardened lending terms similar to those offered by IDA. The proposal was endorsed by the Governing Council in February 2010 (paragraph 1 above). The introduction of this category will allow IFAD to offer terms to its borrowers similar to those available to them through financing with other international financial institutions and will allow the Fund to engage with some developing member states, which would not have been possible otherwise.

IFAD hardened terms – Characteristics

6. The Governing Council has delegated authority to the Executive Board to create a category of lending terms similar to IDA hardened terms, pending the revision of IFAD's Lending Policies and Criteria. In pursuance of this decision, Management proposes that IFAD hardened terms, like IDA's, differ from highly concessional lending with respect to the maturity period only, to be reduced from 40 to 20 years in the case of eligible countries. The table below presents a comparative overview of current IFAD lending terms, including the proposed IFAD hardened terms.

Characteristics of IFAD lending terms, including proposed IFAD hardened terms

<i>Type</i>	<i>Maturity period</i>	<i>Grace period</i>	<i>Interest</i>	<i>Service charge</i>	<i>Concessional (grant element)^f</i>
Highly concessional	40	10	-	0.75%	65%
<i>Hardened terms (proposed)</i>	20	10	-	0.75%	50%
Intermediate	20	5 ^a	50% of IFAD reference interest rate (variable) ^b	-	35% ^d
Ordinary	15-18	3 ^a	IFAD reference interest rate (variable) ^b	-	16% ^d

^a The Executive Board may vary the grace period for the repayment of loans received on intermediate and ordinary terms.

^b As of January 2010, IFAD re-sets its annual reference interest rate each semester – on the first business days of January and July. The IFAD reference rate applicable to loans on ordinary terms is based on a composite SDR LIBOR six-month rate of the four currencies that constitute the SDR basket (United States dollar, Japanese yen, euro, and United Kingdom pound sterling), plus a variable spread. The spread applied by IFAD is a weighted average of the spreads applied by IBRD to its variable rate loans for the same semester.

^c Calculated using the IDA methodology for concessionalities and applying current discount rates.

^d Intermediate and ordinary terms have variable interest rates and the IDA methodology cannot be readily applied for calculating the inherent grant element. To calculate approximate comparative figures, the variable interest rates have been converted to fixed rates by applying market-interest-rate swap premiums as at 1 July 2010 aligned to the maturity profile of the IFAD loans plus the current IFAD spread. The grant element for loans on ordinary terms is based on a 15-year maturity.

Eligible countries

7. The Governing Council decided that, should the Executive Board approve the creation of the hardened-term lending category in IFAD, eligible countries will be the same as those eligible for IDA hardened terms. IFAD hardened terms will therefore be accessible, upon request, to borrowers eligible for IDA hardened terms.

Impact of the creation of hardened lending terms on IFAD's finances and processes

8. The potential financial and other implications of introducing this category for the first year of application of the new facility¹ will be very limited. Based on the projected programme of work for 2010 and the first semester of 2011, only three countries (currently under IFAD ordinary or intermediate terms) are likely to request the application of IFAD hardened terms. The financial impact on IFAD's resources of extending hardened terms to these countries is represented by the difference in the grant element between hardened terms and intermediate terms as shown in the table above.
9. The creation and application of hardened terms in IFAD will be accommodated without any need for changes to IFAD's processes and systems.

¹ Within the framework of the ongoing IDA16 consultation, IDA deputies are discussing phasing out the category of hardened terms as created in 2002. The two existing lending categories of 'hardened terms' and 'blend terms' will be merged into a hybrid category of credit 'blend/hardened terms' available to countries eligible for IDA blend or hardened terms (25-year maturity period, 5-year grace period, 1.25 per cent interest rate). If approved, the change will be included in the IDA 16 resolution and become effective as of 1 July 2011. In the light of the IDA16 decision, the continuation of the category of IFAD hardened terms will be reassessed within the context of the revision of the Lending Policies and Criteria, and appropriate proposals will be brought to the Executive Board for consideration and approval.