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IFAD
INTERNATIONAL FUND FOR AGRICULTURAL DEVELOPMENT
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IFAD'S PARTICIPATION IN THE
DEBT INITIATIVE FOR HEAVILY INDEBTED POOR COUNTRIES
PROGRESS REPORT

I. INTRODUCTION

1. It is the objective of this paper to:
 - (a) seek the Executive Board's approval of a new country case, Burundi, for debt relief under the Initiative; and
 - (b) inform the Executive Board of the status of implementation of the Debt Initiative for Heavily Indebted Poor Countries (HIPC) and IFAD's participation in the Initiative.

II. COUNTRY CASE

2. **Burundi.** In July 2005, the executive boards of the International Monetary Fund (IMF) and the International Development Association (IDA) agreed to support a comprehensive debt-reduction package for Burundi under the enhanced Debt Initiative. Burundi's eligibility for debt relief under the enhanced Initiative framework is evidence of the international community's recognition that, following the implementation of the Arusha Peace Accord of August 2000, Burundi had achieved, through early 2005, demonstrable progress with economic stabilization and reform, and the authorities have remained committed to policies of macroeconomic and financial stability, growth and poverty reduction. Nevertheless, Burundi's heavy debt burden would require strong export growth and external assistance in the form of grants or loans on highly concessional terms.

3. Within a difficult political environment, and starting from dire economic and social conditions, Burundi has made good initial progress in stabilizing the economy, implementing financial and structural reforms, and beginning to restore social services. As more than 90% of Burundi's poor live in rural areas and with the sector contributing nearly 50% of GDP, increasing agricultural productivity and diversification and rural development are among the Government's major priorities to revitalize the economy and reduce poverty. Implementation of the coffee sector reform strategy is expected to raise the income levels of some 800 000 small rural producers of this main cash crop. The Government's

priorities include enactment of new land legislation that would reduce disincentives against on-farm investment; implementation of a matching grant programme designed to provide training and funding support to farmers' groups for the start-up of productive and income-generating activities; a national programme to enhance the supply and quality of training and extension services to small producers, and to provide backstopping support to farmers' organizations; and a national action programme to address the problem of land degradation. Throughout the ten years of the country's conflict until the present, IFAD has continued to finance and otherwise support the implementation of agricultural and rural recovery and development programmes in Burundi. IFAD's interventions are fully compliant with Burundi's interim Poverty Reduction Strategy Paper (PRSP). They are mainly supporting: (i) the empowerment of rural communities to reconstruct social capital and foster reconciliation; (ii) rehabilitation and improvement of the economic and basic infrastructure; and (iii) jump-starting the rural economy, through agricultural rehabilitation, increasing off-farm employment and income, and improving rural purchasing power to support economic activity.

4. In December 2004 (the base year), Burundi's net present value (NPV) of debt (after application of the traditional debt-relief mechanisms) was equivalent to USD 902 million, and its NPV of debt-to-exports ratio was 1 772%. Under the enhanced Initiative, countries are eligible for assistance provided that the NPV of their external debt exceeds 150% of export revenues. To achieve this target, all multilateral creditors are expected to provide a reduction of 91.5% in the NPV of their outstanding claims as of December 2004. Total relief from all of Burundi's creditors would amount to USD 825 million in NPV terms. Based on proportional burden-sharing, bilateral and commercial creditors will provide USD 124 million. Multilateral creditors will provide USD 701 million in debt relief in NPV terms. **IFAD's Executive Board is requested to approve IFAD's contribution to debt relief for Burundi in the amount of SDR 11.7 million (USD 16.7 million) in 2004 NPV terms.** Tentatively, this would amount to SDR 21.4 million in nominal terms, spread over approximately 28 years. The amount of resources freed by HIPC relief would permit a sizeable increase in Burundi's poverty-reducing spending, and is projected to exceed current expenditure on health and education.

5. A sensitivity analysis conducted by the staff of the IMF and World Bank indicates that Burundi's ability to service external debt after HIPC relief is very vulnerable to external shocks, export performance and the composition and terms of external assistance. The analysis underscores the importance of a strong and sustained domestic reform effort, an active programme to develop exportable production (traditional and non-traditional), prudent debt management strategy, and external assistance heavily weighted toward grants.

6. Burundi will reach its completion point under the enhanced Initiative when the following measures have been completed: (a) the standard general triggers pertaining to (i) the preparation of a full PRSP through a participatory process and one year of implementation; (ii) maintenance of macroeconomic stability; and (iii) utilization of enhanced HIPC Initiative budgetary savings in line with the priorities identified at the decision point and in the PRSP and approved by the Parliament; and (b) specific and monitorable policy measures on public expenditure management, governance, demobilization, structural reforms, key social sectors (health and education), and debt management. These triggers are considered essential to the success of the enhanced HIPC Initiative in Burundi.

7. At completion point, Burundi will, under the terms of the Multilateral Debt Relief Initiative (MDRI), be eligible for further debt relief from IDA, IMF and the African Development Bank only. Such further relief as may be determined will be made **after** any debt service relief available under the enhanced HIPC Initiative.

III. STATUS OF IMPLEMENTATION OF THE DEBT INITIATIVE

8. **Status of implementation.** Eighteen countries have now reached the completion point, while ten are in the interim period between the decision and completion point (Table 1). The pace at which countries in the interim period reached their completion points accelerated over the last two years as countries made progress in implementing their macroeconomic programmes and their poverty reduction strategies. Since September 2004, Honduras, Madagascar, Rwanda and Zambia reached their completion points; Chad and Malawi could reach their completion points during 2006. Of the remaining HIPC's in the interim period, six are advancing with the implementation of their Fund-supported and IDA-supported programmes. Seven HIPC's in the interim period have completed a full PRSP.

Table 1: Heavily Indebted Poor Countries

Completion Point Countries	Decision Point Countries	Pre-decision Point Countries
Benin	Burundi	Central African Republic
Bolivia	Cameroon	Comoros
Burkina Faso	Chad	Congo
Ethiopia	Democratic Republic of the Congo	Côte d'Ivoire
Ghana	Gambia	Lao People's Democratic Republic
Guyana	Guinea	Liberia
Honduras	Guinea-Bissau	Myanmar ^a
Mali	Malawi	Somalia
Madagascar	Sao Tome and Principe	Sudan
Mauritania	Sierra Leone	Togo
Mozambique		
Nicaragua		
Niger		
Rwanda		
Senegal		
Uganda		
United Republic of Tanzania		
Zambia		
18	10	10

^a No IFAD exposure.

9. **Costs and creditor participation.** The total cost of the HIPC Initiative to all creditors for the 28 decision point HIPC's is estimated at USD 38.2 billion in 2004 NPV terms, somewhat above the 2003 estimate of USD 35.7 billion.¹ IFAD is the seventh largest contributor to the HIPC Initiative (out of 23 multilateral creditors) and the fifth largest creditor in Africa after the IMF, World Bank, African Development Bank and European Union.

10. **Total HIPC Debt Initiative cost to IFAD.** The total NPV cost of IFAD's participation in the full HIPC Debt Initiative, at December 2005, is estimated at SDR 269.5 million (USD 384.4 million), which corresponds to an approximate nominal cost of **SDR 422.2 million (USD 602.2 million)**.² The current cost estimates are likely to increase due to countries' delays in reaching decision and completion points, worsening economic conditions leading to the need for completion point top-ups, and continuing low discount rates. IFAD has thus far provided USD 92.0 million of debt relief to all completion point countries. For 2006 it is estimated that IFAD will have a nominal requirement of approximately USD 47.9 million.

11. **IFAD commitments to date.** To date IFAD has committed the required debt relief to all 27 HIPC's that have reached their decision point. IFAD's total commitments so far amount to

¹ HIPC Initiative: Status of Implementation, IMF/World Bank Development Committee 13 September 2005.

² December 2005 base estimates at exchange rates prevailing at 31 December 2005.

SDR 194.4 million (USD 277.3 million) in NPV terms, which amounts to **SDR 296.7 million (USD 423.2 million)** of debt service relief in nominal terms.

12. **Financing of IFAD's debt relief.** IFAD is funding its participation in the HIPC Debt Initiative through its internal HIPC Debt Initiative account, from external contributions (paid either directly to IFAD or transferred through the World Bank-administered HIPC Debt Initiative Trust Fund) as well as from its own resources. External contributions (paid or pledged) amount to about USD 83.7 million (57% of the total). IFAD's own resource contributions amount to about USD 59.7 million (40%) through three separate Executive Board-approved transfers in 1998, 1999 and 2002, the last totalling USD 41.0 million. Investment income in the IFAD HIPC Debt Initiative account amounts to USD 4.0 million (3%). Table 2 shows the external contributions received (and those pledged). All funds actually received, together with IFAD's own funds, are utilized as the nominal cost of debt relief to IFAD falls due; on current estimates, these funds will be used up by early 2007.

**Table 2: Total HIPC Debt Initiative Contributions (Including Pledges)
as at 31 December 2005**

	Currency	Local Currency	USD '000
IFAD	USD	59.7	59.7
Netherlands	EUR	12.1	12.4
Germany	EUR	7.7	7.0
Belgium	EUR	3.0	2.7
Switzerland	USD	3.3	3.3
Italy	EUR	3.7	4.6
Sweden ^a	USD	17.0	17.0
Norway	NOK	40.0	5.9
European Commission	USD	1.00	1.0
	EUR	7.50	9.5
Luxembourg	EUR	0.90	1.0
Iceland	USD	0.3	0.3
Finland	EUR	2.00	2.5
	USD	2.7	2.7
Canada ^b	CAD	16.10	13.8
Total external contributions			83.7
Investment income			4.0
TOTAL			147.4

^a Includes USD 7 million pledged not yet received.

^b Full amount pledged but not yet received.

13. In order to mitigate the impact of debt relief on IFAD's resources available for commitment to new loans and grants, IFAD's management pursues two avenues for mobilizing more such additional external resources, encouraging IFAD's Member States to:

- (a) directly provide IFAD with additional resources to help finance its participation in the Initiative; and/or
- (b) provide IFAD with access to the core resources of the World Bank-administered HIPC Debt Initiative Trust Fund. This is the approach taken by several Member States and, as a next step, IFAD has been requested to present a technical paper detailing its HIPC Debt Initiative exposure to the next HIPC Trust Fund technical pledging session with a view to IFAD

accessing, for the first time, the core resources of the Trust Fund. This will also ensure that the extent of IFAD's financial involvement in the HIPC Debt Initiative is reviewed in the context of the overall analysis of the Trust Fund's requirements.

14. **Possible future increases in IFAD HIPC Debt Initiative costs.** In September 2004 the IDA executive directors extended the "sunset clause" until December 2006 to allow pre-decision point countries to secure their involvement in the HIPC Initiative. The sunset clause stems from the 1996 Programme of Action, which established a time limit in order to prevent the HIPC Initiative from becoming a permanent facility and to encourage HIPCs to adopt adjustment programmes that could be supported by the IMF and IDA. It was also agreed to allow **further** countries over and above the existing 38 countries to join, subject to indebtedness criteria. The World Bank is currently assessing the potential extent of debt relief to be provided and is expected to present a paper to its board in April 2006 identifying the countries and the extent of the debt relief required. The Executive Board of IFAD will be kept informed accordingly.

IV. RECOMMENDATIONS

15. It is recommended that the Executive Board:

- (i) approve the proposed contribution to the reduction of **Burundi's** debt to IFAD as of 31 December 2004, in the amount of SDR 11.7 million in 2004 NPV terms. This relief will be provided in accordance with the terms of the following resolution:

"RESOLVED: that the Fund, upon declaration at completion point by the International Monetary Fund and the World Bank that Burundi has satisfied the conditions for debt relief under the Debt Initiative for Heavily Indebted Poor Countries, shall reduce the value of Burundi's debt to IFAD through the reduction by up to 100% of its respective semi-annual debt-service obligations to IFAD (principal and service-charge/interest payments), as these fall due after the respective completion point, and up to the aggregate NPV amount of SDR 11.7 million in 2004 NPV terms";

- (ii) take note of the status of implementation of the HIPC Debt Initiative and IFAD's participation therein.