Oxfam
International
Position Paper

Debt relief for Rwanda:

an opportunity for peace-building and reconstruction

March 1999

Debt relief for Rwanda:
an opportunity for peace-building and reconstruction

Executive summary

Background

Rwanda stands at a critical point in its history. The country's people are seeking to rebuild a society shattered by war and a genocide in which one in eight Rwandans - Tutsi and Hutu opponents of the government's extremist policies - was killed, and which further led to the outflow of over one and a half million refugees. Since the 1994 conflict, poverty levels have increased dramatically, the health-care and education systems have collapsed, and the economic infrastructure has been shattered. Conflict in Rwanda continues to have enormous destabilising effects on all the neighbouring countries, including the Democratic Republic of Congo, Burundi, Tanzania, and Uganda. There is an urgent need for peace, security, and poverty reduction.

Despite notable efforts to reconstruct the country, Rwanda remains in need of massive international assistance if it is to enjoy a peaceful and prosperous future. But aid alone is not enough. The present peace is partial and fragile, and there are serious security concerns, largely in the country's north-west. Rwanda has also acknowledged that it is involved in the conflict in neighbouring Democratic Republic of Congo, by providing political and military support to the rebellion against the government of Laurent Kabila. Despite international efforts to secure a cease-fire, the war continues, threatening lives and livelihoods across the entire region. A renewed respect for human rights - economic, social, civil, and political rights - is needed, to break the cycle of violence, and to restore the rule of law. Oxfam believes that international assistance should be provided as part of an integrated strategy aimed at reducing poverty, averting further conflict, and fostering greater respect for human rights.

Fifty years ago, political leaders in Europe and the US embarked on a concerted post-war reconstruction strategy, driven partly by the fear that failure to restore hope, and the opportunity for economic recovery, to a continent devastated by war would create the potential for a return to conflict. Today, Rwanda stands at a similar cross-roads - and it needs a similar sense of political purpose and integrated effort. Failure in the reconstruction project will exacerbate social tensions, increase poverty and insecurity, and raise the likelihood of intensified conflict not only in Rwanda, but across the region. The international community has a moral obligation to use all the means at its disposal to avert such a crisis. But it also has a self-interest in acting decisively now. As Rwanda's recent tragic history has underlined, crisis prevention is far less costly than responding to another humanitarian crisis.

This paper is prompted by a growing concern that an unsustainable debt burden is one of the factors which jeopardise reconstruction efforts in Rwanda, and that debt relief could be a crucial element of a wider strategy of international engagement, aimed at encouraging respect for all human rights and building peace. The paper argues that existing debt relief mechanisms are not being fully utilised. (The dimensions of Rwanda's debt crisis, and the prospects for its relief under the Heavily Indebted Poor Country Initiative (HIPC) are explained in detail in the following pages.) As ever, the question of debt relief is a complex one, involving a wide range of creditors and judgements about Rwanda's future debt-servicing capacity. But the bottom line is that the Government spent approximately US$35m on debt-servicing in 1998. In a country where one in three children is not in school, and where the majority of those who are lack essential educational materials, Rwanda spends more on debt than on basic education. At a time when the level of child mortality is rising - in part as a consequence of the destruction of the water and sanitation infrastructure - debt-servicing dwarfs the amount spent on these basic services. It has been estimated that providing clean water to rural communities could save up to 6000 lives annually. The fact that this could be achieved for less than is currently spent servicing debt speaks volumes about the need for a reordering of priorities, and for a reassessment of current debt relief strategies.

The protection of basic rights

Peace cannot last, and recovery cannot be sustained until the basic human rights of all Rwandans are recognised and respected. Debt directly limits the provision of basic life necessities: thousands of people do not have access to clean water; children die of diarrhoea and other preventable diseases; many people do not have access to affordable health-care. These are violations of human rights. This is not to suggest that debt is the only cause of human rights' violations. The conflict between the Rwandan Patriotic Army (RPA) and insurgent groups in Rwanda's north-west has resulted in the manipulation and abuse of civilian populations. Human-rights groups, including African Rights and Amnesty International, have reported that both the RPA and insurgent groups are responsible for the indiscriminate killing of civilians. Some people are subject to extra-judicial arrest. The failure to address all these human-rights abuses also threatens Rwanda's future. Although the Rwandan government has legitimate security concerns, military expenditure threatens to eclipse social spending. The Government needs to ensure that their own policies do not jeopardise the reconstruction project.

Poverty reduction is urgently needed

The fulfilment of basic rights in Rwanda will require a radical reduction in poverty. Rwanda is one of the world's poorest countries. Seventy per cent of all households live below the meagre poverty line. Not only are more Rwandans living in poverty now than at the start of the decade; those living in poverty have also become poorer. Almost one in five children born this year will die before they reach their fifth birthday. Half of the adult population is unable to read and write. These appalling indicators, and the human suffering that lies behind them, have steadily worsened in the wake of the catastrophic events of 1994. The violent conflict, principally in the north-west, and the return of refugees in late 1996, have placed additional pressures on the country's under-funded social sector and ravaged infrastructure. Poverty reduction in Rwanda is not only an urgent priority in itself, it is also a necessary condition of social and political stability.

Yet despite this bleak picture of rising poverty and continued conflict in parts of the country, there is also cause for hope. Rwandans, with the support of the international community, have begun the painstaking reconstruction of their society and economy. The Rwandan Government has already made budget commitments to poverty reduction, in particular by increasing its social-sector spending for 1999. But while donors have given substantial assistance to develop a framework for poverty reduction, their response to Rwanda's great and urgent needs has often been too slow, insufficient, and incoherent. Rwanda continues to spend scarce resources on debt-servicing, at a time when the pace of the reconstruction programme appears to be slowing. Once the limits of recovery-based growth are reached, rapid and broad-based growth will depend on further resources being released for priority social investment.

The cost of indebtedness

The facts of Rwanda's debt tell their own story. Debt stock has doubled over the past five years to US$1bn stock, over five times the value of Rwanda's exports. Repayments are absorbing almost one third of foreign exchange earnings and one quarter of government revenues. Using the debt-sustainability criteria adopted under the IMF-World Bank Highly Indebted Poor Countries (HIPC) initiative, Rwanda's debt is unsustainable. It will remain so until well into the next decade - Rwanda will not qualify for comprehensive debt relief under the HIPC framework until 2003, or later. Although bilateral creditors have reduced their claims, the impact has been limited, because multilateral debt accounts for over 80% of Rwanda's debt stock.

Rwanda's parlous position underlines the shortcomings of the HIPC framework, which has provided too little debt relief, too late. This delay results from the requirement that eligible countries must adhere to two consecutive IMF programmes over a six year period. The limited benefits which have resulted for those countries which have been eligible reflect the fact that the debt-sustainability targets have been set at levels which are too high for heavily indebted poor countries. For a country such as Rwanda, which faces a combination of unsustainable debt and extreme reconstruction needs, the HIPC framework is grossly inadequate.

In the interests of stability and improved self-reliance, an immediate ceiling must be set on repayment levels, at no more than 10% of public spending levels; and the debt reduction framework must be accelerated. Early implementation of HIPC debt relief in 1999 could make available an extra US$31.8m for the Government budget, enough to finance an immediate phasing-out of user fees in health-care and education, as well as provide funds for training and better materials for schools and health centres. If a 'poverty window' were created which provided incentives for the Rwandan Government to invest savings in priority social sectors and basic infrastructure, such early treatment under the HIPC initiative could act as a catalyst for economic recovery and human development gains.

The need for engagement

As conflict continues in north-west Rwanda, with reports of serious human rights abuses by all sides, and as many of Rwanda's people slip deeper into poverty, it is essential that the international community uses fast and deep debt relief as part of a wider strategy of reducing poverty, averting further conflict and fostering greater respect for human rights and international humanitarian law. This requires action on many fronts - by the Rwandan government, donors, NGOs - and a form of contractual agreement about these actors' respective roles and responsibilities. At the heart of this approach is a strengthened dialogue between the international community and the people and Government of Rwanda.

Oxfam believes that such a strategy will only be effective if, as a result of strengthened and sustained dialogue, all parties make commitments which they are prepared to be held accountable to. All parties should agree to a clear and costed poverty-reduction plan with explicit benchmarks and targets, as well as mechanisms to monitor performance. The plan should focus on outcomes, not just outputs. This plan should be accompanied by agreement on the timing and volume of resources that will be disbursed as part of the plan and on the measures required to ensure that debt relief is given in such a way as to contribute directly to poverty reduction. Benchmarks and targets should also be agreed for a further range of issues, such as strategies to strengthen Rwandan judicial and human rights institutions, and ensuring greater participation by Rwanda's people in the decisions that affect their lives.

Rwanda's involvement in the DRC conflict threatens to scupper the possibilities for such dialogue, or at least to postpone it, as donors' articulate concerns about the diversion of scarce funds to the war effort. Oxfam's argument is that Rwanda's people cannot afford such delays or diversion of resources. An end to the war in DRC and the speedy disbursal of aid are both critical for the country. So long as Rwanda is involved in DRC's conflict, there is likely to be little political will among donors to provide Rwanda with the exceptional help it needs. The Rwandan Government will have to convince donors that deeper, swifter debt relief will be effectively used for fighting poverty, not fomenting conflict. Rwandan signatures on a cease-fire agreement in DRC will contribute to this. Donors on their part must be able to show Rwanda that assistance is a realistic prospect.

Among the multilaterally agreed commitments which Oxfam calls for, as an outcome of dialogue, Oxfam calls for the following action.

Oxfam urges the creditor community to ensure that:

- **HIPC debt relief is provided this year or during 1999-2000.**
- **A fiscal cap of 10 % is placed on debt-service claims.**
- **Increased funds are provided to reduce the burden of multilateral debt during the interim period.**
- **Donors make clear commitments to provide substantial human and financial resources for a poverty-reduction plan with clear targets on the increase of poor people's access to economic opportunities and basic social services. Disbursal should be calibrated with progress towards the benchmarks and targets agreed with the Rwandan government.**
- **All UN members co-operate more fully with UN Security Council resolution 978, which requires international action to arrest and extradite those suspected of genocide in Rwanda.**
- **Resources are directed at the continued rebuilding and strengthening of Rwanda's judicial system, and the establishment of an independent and impartial National Human Rights commission.**

Oxfam urges the Rwandan Government to fulfil its stated commitments to reduce poverty, avert further conflict, and respect human rights by:

- **Allocating resources from debt relief to a clear and costed poverty-reduction plan which has clear targets on increasing poor people's access to economic opportunities, education, and health-care.**
- **Ensuring that the overall policy and expenditure framework is coherent with the aims of poverty reduction and reconstruction. This requires that scarce Government resources are not diverted from health-care and education into military expenditure, and that all possible measures are taken to reduce military expenditure.**
- **Establishing full budget transparency, in order to demonstrate the use of debt relief for poverty reduction. The Government should fulfil its commitment under the 1998 Budget Law to consolidate all revenues and expenditure in the budget, and to prohibit extra-budgetary expenditure.**
- **Fulfilling commitments to involve non-government actors, such as civil society, in the scrutiny of expenditure and the assessment of expenditure against priorities.**

- **Establishing mechanisms for joint monitoring of the use of finance by the Government, donors, and Rwandan civil-society groups.**

- **Expediting the process of decentralisation to include civil society in decision-making, and to equip and entrust local government with the management of local development budgets, rooting out corruption.**

- **Denouncing, investigating, and punishing all war crimes, extra-judicial killings, and violations of humanitarian law, regardless of the identity of the perpetrator.**

Inevitably, there will be financial costs associated with this strategy. But these costs must be set against the potential for achieving human development gains and increased self-reliance. They must also be considered in the light of the threats posed to the entire reconstruction process by unsustainable debt.

This paper is organised as follows. The Introduction sets out the broad context in which reconstruction is taking place, and summarises Oxfam's view. Section 1 outlines the financial aspects of Rwanda's debt problem. Section 2 looks at the human cost of debt, and Section 3 discusses the prospects for reform under the HIPC initiative.

Debt relief for Rwanda: an opportunity for peace-building and reconstruction

Introduction

Four years after a genocide which killed 800,000 people - Tutsi and Hutu opponents of the governing regime's extremist policies - Rwanda continues to struggle to rebuild itself. The challenges are huge: to recover from the civil war that preceded the genocide; to heal the wounds caused by genocide's grim aftermath of loss, trauma, and fear; and to accommodate 3.8 million people, whether internally displaced people (IDPs), or refugees returning, either from the vast refugee camps on Rwanda's borders or from decades-long exile. Many refugees and displaced persons who have returned to their homes now compete with others for land they had previously occupied. Thousands of ex-combatants are swelling the ranks of urban unemployed. Over one hundred thousand children are described as 'unaccompanied' - orphaned by conflict and HIV-AIDS, or simply abandoned. The war and massacres have left behind a large number of female-headed households, who are often at a social, legal and economic disadvantage, and who constitute one of the poorest and most vulnerable groups in Rwandan society. The integration into society of the vulnerable, traumatised, disenfranchised, and impoverished is critical to long-term stability and development in Rwanda, and across the Great Lakes region. All these groups, indeed every Rwandan, must be given a stake in a peaceful future.

There are numerous potential obstacles to peace and development, which require imaginative responses from government and civil-society groups, in conjunction with donors, regional organisations, and Northern NGOs. Large-scale financial and technical assistance will be needed. Rapid population growth is placing pressures on an under-resourced social sector, and is increasing competition over land and water in densely populated rural areas. The social sector, cruelly targeted during the genocide, urgently needs new investment. Training of teachers, health workers, and administrators is crucial. The Government also faces serious security concerns, largely in the north-west. In addition, Rwanda's involvement in the conflict in the neighbouring Democratic Republic of Congo endangers poverty-reduction efforts. Despite international efforts to secure a cease-fire, the war continues, threatening lives and livelihoods across the entire region. A renewed respect for human rights and the rule of law are urgently needed to break the cycle of violence and end impunity.

In October 1997, Oxfam International called on the OAU and the UN, the Bretton Woods Institutions, the EU, and bilateral donors to engage with the Rwandan Government. While recognising the complexities and difficulties of pursuing an effective reconstruction strategy, Oxfam International argued that the costs of failing to address both the causes and effects of conflict were too great to contemplate. It emphasised that aid is not enough, and outlined an integrated programme. This aimed at:

- **reducing poverty**;
- **averting further conflict; and**
- **fostering respect for human rights and the rule of law.**

Because of the past failures of the international community in Rwanda, not least in reinforcing the conditions that gave rise to the 1994 genocide, Oxfam International called on the actors concerned to recognise their extraordinary responsibility to promote recovery and development.

While Rwanda continues to receive substantial aid flows, these are insufficient to fulfil the basic rights of Rwanda's children, women and men to health-care, education, and security. Not only is external assistance insufficient, it is also unpredictable, and ultimately unsustainable. While in the medium term, Rwanda will remain heavily dependent on aid even with debt relief, reducing the country's debt would lay an important foundation for greater fiscal autonomy, as well as releasing further finance for reconstruction.

Rwanda's debt problems pose a formidable barrier to reconstruction. The diversion of resources to external creditors, equivalent to one quarter of public expenditure, seriously undermines the Government's ability to fill the financial resource gap and achieve greater fiscal independence. This debt burden has immediate human, as well as financial costs. The US$35.8m in debt-service repayments falling due in 1997 was equivalent to:

- more than one and a half times the operational budget for education;
- more than ten times the operational health-sector budget.

Such skewed resource allocation ought to be regarded as intolerable in a country where over forty thousand children die each year from easily preventable diseases, and where education typically means classes without desks and books, and teachers without training. Not only is the prioritisation of creditors' claims over children's lives a human-rights violation; it is also inconsistent with donor programmes aimed at promoting peace and development. If donors are to develop a coherent and co-ordinated approach to Rwandan reconstruction, then substantial and quick debt relief, based on human-development needs rather than narrow financial criteria, must be a pivotal element.

The protection of human rights

This is not to suggest that debt is the only cause of the problems facing Rwanda. Debt has a direct bearing on some rights such as access to clean water and affordable health-care. There are other rights violations which require action by the Rwandan Government. Indefinite numbers of civilians are the victims of indiscriminate killing, whether by armed groups or the Rwandan Patriotic Army (RPA). Some people are subject to extra-judicial arrest. Oxfam International urges the Rwandan Government to denounce, investigate, and punish all those responsible for extra-judicial killings, regardless of their political affiliation.

Military spending has fallen substantially in the last year but remains unacceptably high. Its level must be reduced further if the human-development needs of Rwandan children, women, and men are to be met. While recognising that the Rwandan government has legitimate security concerns in its western prefectures and border areas, and that military spending for defence is not discretionary, current spending levels threaten to eclipse social spending. At present, there are 55,000 men under arms in the RPA, absorbing 40% of the Government's budget. Meanwhile, health-care and education continue to receive only 25% of Government spending. This situation must be reversed, with the government making a commitment to reduce military spending over the next three years. Uganda, which has almost halved the proportion of public spending going to the military in recent years while confronting violent conflict in the north and the west of the country, provides an important precedent. Donor governments have a responsibility, in the context of broader dialogue with the Rwandan Government, to create incentives for this reduction to be achieved.

Poverty is central to the debt issue

Seventy per cent of Rwandans live below the poverty line, and are in desperate need of equitable, broad-based economic growth. Yet economic recovery remains incomplete. Today, GDP is only 85% of its 1990 levels, and underemployment is threatening social stability in urban areas. Devising strategies for economic growth which provide viable opportunities for the poor to earn a livelihood is a priority. Export diversification will also be crucial to a convincing economic recovery. Yet the options are limited. Over 90% of Rwanda's population work in agriculture, typically on small plots of deteriorating quality. Rwanda is overwhelmingly dependent on two primary commodities, tea and coffee, for its small foreign exchange earnings. International prices for both are highly volatile.

Section 1

A profile of Rwanda's debt

Like other HIPCs, Rwanda's heavy indebtedness is the result both of domestic policy failings, and of external events beyond Government control. In common with other African countries, Rwanda borrowed heavily in the late 1970s and early 1980s. While some of this borrowing was wasted, much of it was invested prudently in physical infrastructure and clean water systems. But the total stock of external debt rose rapidly after 1985, as regional recession and a collapse in world coffee prices hit the Government's earnings.

After 1990, Government revenue-raising capacity was further constrained by escalating conflict in the north of the country. Between 1990 and 1995, Government revenue as a percentage of GDP fell from 10% to 7%, one of the lowest ratios in sub-Saharan Africa.[i] At the same time, society became increasingly militarised as communal tensions and violence increased. Public spending on arms rose sharply, crowding out social sector budgets. Poverty levels rose, and investment fell. Against this backdrop, the Government soon found it was unable to meet the demands of creditors. Arrears rapidly accumulated, and the debt stock became increasingly unsustainable. Between 1985 and 1997, the stock of external debt more than doubled, from US$400m to over US$1bn.[ii] Rwanda also built up a large public domestic debt, reaching the equivalent of US$220m in mid-1997.

In common with other African HIPCs, the share of the multilateral creditors in Rwanda's external debt has steadily risen, as the debt crisis has progressed. Today, over 80% of Rwanda's debt is owed to multilateral creditors, the highest proportion of multilateral debt owed among the HIPCs. The HIPC initiative was designed to resolve the multilateral debt problem, by requiring for the first time that multilateral creditors reduce their claims in conjunction with bilateral and commercial creditors.

Table 1. **Rwanda's external debt indicator**

Net present value of GDP	65%
Net present value/exports	557%
Debt service/exports	32%
Debt service/government revenues	23%

WB 1998

Debt stock

At the end of 1997, Rwanda's external debt stood at US$1164m including arrears. This debt is large even by the standards of other HIPCs, and equivalent to 65% of Rwandan GDP. US$947m is owed to multilateral creditors; 48% of the total external debt - US$558m - is highly concessional debt owed to the International Development Association (IDA), the World Bank's 'soft loan' arm. A further US$203m (17% of the total external debt) is owed to the African Development Bank (ADB). Only 16% of the total external debt was owed to bilateral creditors at the end of 1997, and 6% owed to the Paris Club. In descending order, the principal bilateral creditors at the end of 1995 were: France (US$54m), Saudi Arabia (US$27m), Kuwait (US$18m), China (US$14m) and Japan (US$14m). Private debt amounted to only US$18m, less than 2% of the total. Figure 1 illustrates the distribution of Rwandan debt at the end of 1997.

Debt service

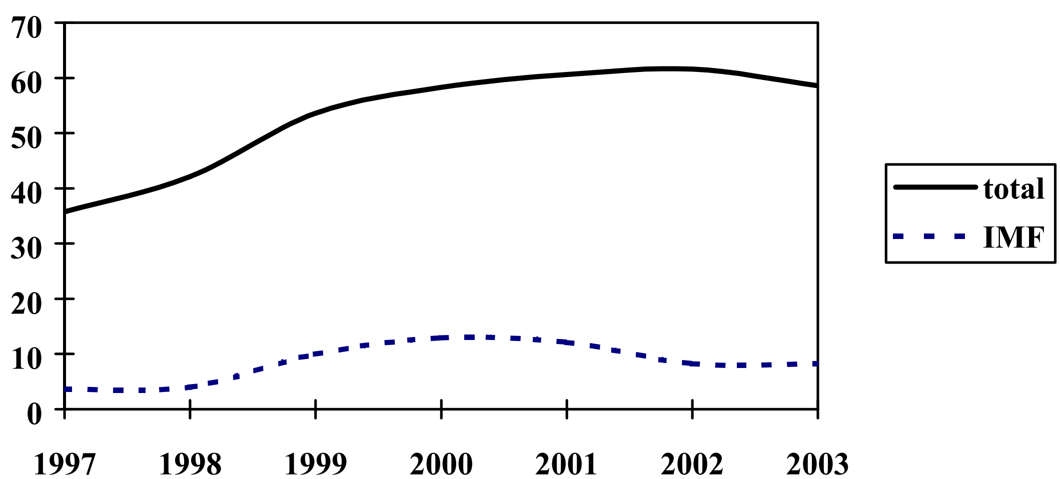
Debt-service repayments due in 1997 totalled US$35.78m, equivalent to 32% of Rwanda's export earnings. This represents more than the operational health-care and education sector expenditures *combined*.[iii] On 23 July 1998, 67% of Rwanda's Paris Club debts were rescheduled according to the Naples terms. This is a welcome measure, but it will have limited impact because of the small size of bilateral debt. While the application of Naples terms will reduce Government debt repayments to bilaterals by US$76m in 1998 - US$63m of it arrears - and by about US$15m in 1999 and 2000, scheduled debt-servicing is nonetheless set to rise steeply over the next three years.

In 2001, total scheduled debt service is set to reach US$60.6m, and it is projected to fall only slightly in 2003. More than a third of this increase is accounted for by IMF debt. This represents only 4% of debt stock, but one fifth of debt-servicing, because the Fund's lending terms are less concessional than those of other multilateral creditors. Working even with the most optimistic economic growth projections, Rwanda's crippling debt will not fall until well into the next decade, compromising reconstruction efforts. On the basis of the optimistic export growth projections of the IMF and World Bank, conventional debt rescheduling will leave Rwanda with a debt to export ratio of 360% in 2003.

Multilateral Trust Fund

Creditors have recognised that Rwanda will continue to carry a heavy debt burden before a sustained debt-relief strategy is in place, and that conventional treatment would be inadequate. Therefore a proposal has been made for a World Bank-managed Multilateral Debt Trust Fund (MDTF), which will aim to cover about one third of servicing on multilateral IDA and ADB debts over the next three years. The fund will support Rwanda's balance of payments and could help avoid a build-up of arrears with bilateral creditors and delay in the Government's reform programme. It will also make available significant funds in the recurrent budget, which can be directed to priority sectors. But the US$17m a year on offer under the MDTF remains an inadequate sum compared to the amount of total external debt-servicing - US$197m payable through to 2001.

Figure 2. Rwanda's total debt service (US$m)



World Bank 1998

Section 2

The human face of indebtedness

Behind the figures and flow charts used to summarise debt problems, there are human faces. In Rwanda's case, they are the faces of children who are denied the opportunity to learn, because their Government is expected to prioritise debt repayment over education. They are the faces of the fifty thousand infants born this year who will die before their first birthday, most of them from diseases which could be easily prevented by the transfer of only a fraction of debt-service repayments to clean water and primary health-care provision.

Debt-servicing at current levels carries high social costs, especially in a country like Rwanda. As Table 2 shows, child mortality, literacy, and nutritional indicators are extremely poor, and have deteriorated significantly since 1992. The health of Rwandans has suffered dramatically. Maternal mortality has almost quadrupled since 1990, and severe wasting of children has increased more than sevenfold. The genocide in 1994 and its devastating aftermath eroded the Government's revenue base and its capacity to deliver basic services. Last year, the UNDP ranked Rwanda 174th out of 175 countries, using a composite of welfare indicators in its human-development index. Prior to the genocide, Rwanda's human-development indicators were better than the regional average**.**

With a predominantly rural population engaged in smallholder farming, and a tiny export base, the scope for raising additional revenues remains limited. In 1995, a year after the genocide**,** government revenues were only 7% of GDP, among the lowest in sub-Saharan Africa. While economic recovery has been rapid, it remains incomplete. Real GDP in 1997 reached only 85% of its 1990 levels. Per capita GDP amounts to only US$200.[iv]

Table 2. Rwanda's deteriorating human development - 1992 and 1996

Indicator	1992	1996
GNP per capita (US$)	**250**	**209**
Infant mortality rate*	**85**	**125**
Child mortality rate*	**141**	**185**
Illiteracy - aged 10+ (%)	**56**	**60**
Severe wasting - under-fives (%)	**0.7**	**5.3**

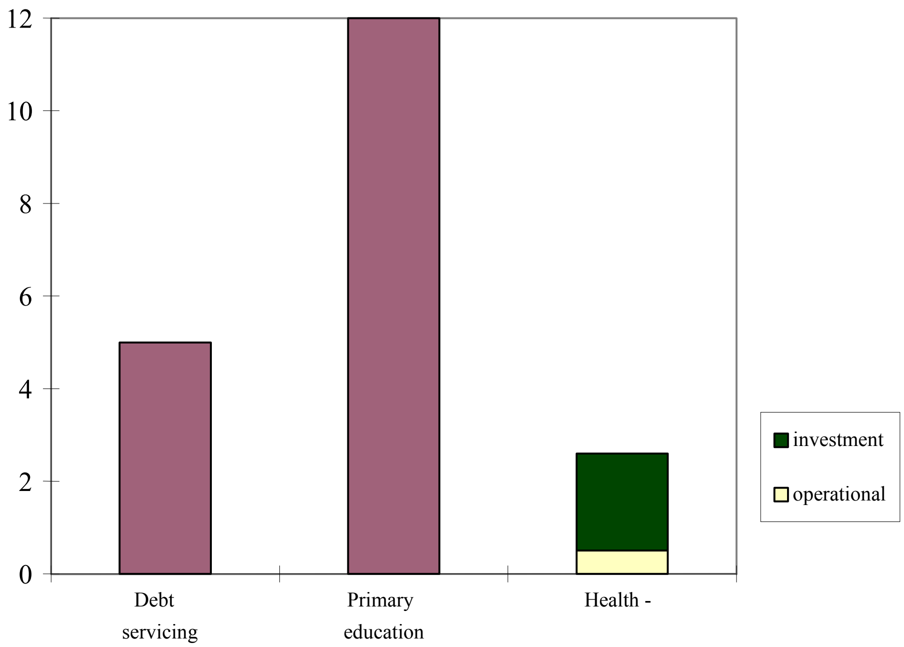
* (per 10,000 live births)

UNICEF 1998, UNDP 1995

Health and education

There is an urgent need for public investment in health-care and education, in water-provision and livelihoods projects, and in demobilisation programmes. Yet debt-service repayments continue to crowd out social-sector spending. Last year, for every Rwandan child, woman, and man US$5 were spent on servicing the external debt, but only 50 cents were spent for each Rwandan on the operational health budget, and US$2 per capita on capital investments (see Figure 3). While the spending situation in education does not seem quite so dire as in health-care, Rwanda massively under-invests in its children, even in comparison with other sub-Saharan African countries. Rwanda allocates approximately US$12 to recurrent spending on primary education for each primary-age child, whereas the regional average is US$49. In this context, it is important to remember that per capita debt-servicing is set to almost double over the next three years.

Figure 3. Rwanda - per capita spending 1997



UNICEF 1998, World Bank staff estimates 1998
(Education spending is per primary-age child)

Budget constraints

In effect, external debt problems are eroding the Rwandan government's capacity to direct domestic resources to where they are most needed. Last year, servicing the external debt absorbed US$35m, one quarter of the entire budget. This is equivalent to more than the health-care and education operational budgets combined.

Although social-sector expenditure is projected to rise by 30% this year, proportionately the burden of debt service repayments will remain heavy, since total debt service is rising. For ordinary Rwandans the costs of this resource diversion are high.

- 30% of children are never enrolled in school.
- Children who are in school often learn little, because almost half of all teachers have no training, and basic materials such as books, pencils, and school furniture are often lacking.
- 55% of primary health centres are in urgent need of physical rehabilitation.
- 120,000 unaccompanied children - most of them traumatised by violence - are in need of support services and appropriate education.
- Water supplies need rapid new investments. One third of all installations were damaged in 1994, and a quarter of people in rural areas are without access to potable water. Clean water for all would prevent over 6,000 child

deaths annually from diarrhoea, as well as improving the health of the wider population.

Aid dependence

The Government's *Programme d'Investissements Publics*, (PIP), is seeking to address these reconstruction needs. The programme is running for 1996-1998, and one third of its budget is allocated to human resources and social development. But, while the US$52m earmarked for reintegration of refugees and displaced people, health-care and population planning, and for primary and secondary education, is a valuable contribution to Rwanda's short- and medium-term needs, the PIP is almost entirely dependent on outside donors. Unsustainable debt is therefore creating a dependence on aid.

This dependence on external assistance for the social sectors raises serious doubts about the sustainability of interventions under the PIP. In education and in health-care, many of the social and economic benefits come through only in the longer term. The integration and reconciliation process the PIP is intended to contribute to will require substantial resources for at least a decade, if poverty reduction and political stability are to become realities. But donor funding is unreliable, and it cannot be assumed that current levels of external assistance will be maintained beyond the next few years.

Substantial and quick debt relief would provide a far more sustainable financial basis for reconstruction than ongoing donor support. With commitments from government to use budget savings from debt relief to meet reconstruction targets, debt relief could provide a sustainable foundation for Rwanda's recovery into the next century. Imaginative incentives, rather than further conditionalities, must be created which provide the Rwandan government with opportunities to meet their poverty eradication targets.

Section 3

Debt relief prospects under the HIPC initiative

Because of the structure of Rwanda's debt, the country urgently needs multilateral debt reduction. Even after the country has received bilateral debt reduction on the Naples terms, it will continue to spend close to one third of export earnings on debt-service in 2001. Unfortunately, under existing rules, Rwanda is unlikely to qualify for multilateral debt reduction for at least six years. Even then, it is far from certain whether it will receive a level of debt reduction commensurate with its needs.

The failure on the part of the creditor community to establish a closer link between debt relief and poverty reduction is one of the HIPC initiative's major shortcomings. At present, access to HIPC is determined partly by the debtor country's success in meeting conditions set under IMF programmes, and partly by estimates of debt sustainability. These criteria for access to HIPC will probably result in Rwanda receiving too little debt relief, too late.

Time frame

Part of the problem facing Rwanda derives from the eligibility criteria for entry to the HIPC initiative. Broadly, all candidates are required to complete two consecutive IMF programmes over a six-year period. This arrangement is intended to avert problems of moral hazard, although an element of flexibility has been

introduced, whereby a country's past track record of compliance with IMF programmes can be taken into account. Oxfam International believes that, in requiring Rwanda to wait for six years, insufficient weight is being attached to the country's track record.

The new Rwandan Government began a reform programme in 1995, one year after the genocide, which was closely monitored by the IMF. The early stages concentrated on trade and fiscal areas, and, even though the new Government was faced with many pressures**,** the IMF and World Bank have judged their performance to be 'satisfactory'. In June 1998 the government signed up to a three-year Enhanced Structural Adjustment Facility (ESAF), which was soon followed by a flow rescheduling on Naples terms. The ESAF is a detailed reform programme, enforced by loan conditionality, which is designed to improve both resource mobilisation and human development, while also accelerating public-sector restructuring. Privatisation, improved social-sector performance, and further investment in the reconciliation process are being supported.

According to the IMF and the wider donor community, Rwanda's track record begins in 1998, with the new ESAF programme. Oxfam International takes the view that three years of track record have been established since 1995, and that the advent of the new Government, rather than 1998, should mark the start of this period of track-record accumulation. If this view is adopted, and if the creditor community recognises the country's special needs, a decision on debt relief can be made this year.

Debt sustainability

Debt sustainability under the HIPC initiative is decided on a case-by-case basis, within a band of 200-250% for the debt to exports ratio (NPV/XGS), and a band of 20-25% for the debt service to exports ratio (TDS/XGS).

There is little doubt that, even with the maximum amount of bilateral debt relief, Rwanda will qualify for HIPC on these two export criteria. Between 1997 and 2004, the ratio of net present value debt (NPV) to exports is projected by the World Bank to fall only slightly from 393% to 358%. Moreover, this is a best-case scenario, arrived at by using the IMF's optimistic export projections (see Table 3), which understate the extent of debt relief required. According to the Fund's projections, Rwanda's exports will grow by 65% in only seven years, from US$101m in 1997 to US$168m in 2004. As a small, landlocked, overwhelmingly rural and low-skill economy, dependent on tea and coffee for an average of 80% of foreign exchange earnings, Rwanda will have to achieve rapid diversification into higher value-added manufacturing and services industries if these targets are going to be met. The IMF's projections also ignore the potential for continued low-level conflict and instability in the country, which will make growth precarious for some time to come. The IMF has projected that manufacturing's share of export earnings will increase from 14% in 1997 to 34% in 2004. So far, there are few signs of this happening, and foreign direct investment has been disappointing since the reform programme began.

Past export-growth rates suggest more modest rates of export growth, with volatile prices and volumes for coffee and tea leading to marked fluctuations year on year. While the IMF has a 'downward projection' to account for the possibility of external shocks, their estimate remains extremely high, projecting a 57% increase in export earnings over 1997-2004. In contrast, using a sample seven-year period from 1986-1993 gives a dramatically different picture of where Rwanda might be in 2004, especially with the debt-service ratio almost doubling (see Table 3). From the IMF's point of view, there are good reasons for systematically underestimating a country's debt burden, and minimising the costs to itself of HIPC debt relief. Yet without unprecedented export growth, Rwanda's debt-service ratio will rapidly become unsustainable, and further arrears will accumulate. **Far deeper and faster relief than is currently provided for under the HIPC initiative is needed to avoid this outcome**.

Table 3. The debt-service ratio under IMF export projections, and less optimistic projections (US$m)

	total exports	debt service	TDS/XGS
1997	101.0	35.8	35.4%
2003/4			
IMF upward projections	168.0	58.6	34.0%
IMF downward projections	159.0	58.6	36.8%
past record projected*	106.5	58.6	63.4%

IMF 1998, WB 1995 * export growth from 1986 - 1993

The case for early action

Although Rwanda is highly likely to become eligible for special relief under HIPC on the export criteria, the track record conditions threaten to jeopardise the reconstruction process. The track record of two uninterrupted ESAF programmes is designed to guard against 'moral hazard', reasoning that unless the preconditions of debt relief are onerous, there is little incentive for countries to borrow responsibly in the future. Oxfam International agrees that there is a need for some form of track record. However, the process is unduly protracted, and linking eligibility to compliance with IMF programmes has in practice slowed down the process further.

Put simply, Rwandans cannot afford to wait for debt relief from HIPC while creditors concern themselves with insuring against what they perceive as a 'moral hazard'. Even with additional transitional measures such as the Multilateral Debt Trust Fund, Rwandans cannot afford to wait. Without debt relief that goes beyond HIPC mechanisms, the reconstruction process will be slowed, and the risk of a descent into further poverty and violence will inevitably increase. Delay will incur a heavy cost in terms of human lives, as well as in terms of recurrent emergency interventions. Rwanda's experience points to the inadequacies of the existing HIPC framework for countries emerging from conflict in three respects. First, any country which has experienced a widespread conflict, violent change of government, and the economic and social upheaval associated with sudden political change, is unlikely to have an uninterrupted track record of reform under IMF programmes. Second, conflict leaves challenges of reconstruction which go beyond the normal challenges associated with debt in poor countries. Finally, excessive debt makes it more likely that post-conflict countries will fail to implement successful adjustment programmes, and jeopardise their access to aid and debt relief in the process.

Converting debt into development

In the case of Rwanda, early implementation of HIPC - especially if debt sustainability were defined at the lower end of the export criteria - could generate significant budget savings (see Table 4). In 1999 alone, projected debt-servicing would be reduced by 60%. The US$31.8m of funds thus released could finance an immediate phasing-out of user fees in health-care and education, as well as contribute to complementary qualitative interventions. This would help raise private demand for basic social provision, and extend access to the poorest households, for whom user fees are a major deterrent to medical care and school enrolment. If a 'poverty window' were created which provided incentives for the Rwandan Government to invest savings in priority social sectors and basic infrastructure, such early treatment under the HIPC initiative could act as a catalyst for economic recovery and human development gains.

Table 4. Implementing HIPC in 1999 (US$m unless otherwise stated)

NPV	TDS	XGS	NPV/XGS	TDS/XGS
1999 projections	**724.1**	**53.6**	**109.0**	**664.3%49.2%**
after HIPC*	**218.0**	**21.8**	**109.0**	**200.0%20.0%**
reduction	**506.1**	**31.8**	**- -**	**464.3%29.2%**

IMF 1998 * at NPV/XGS of 200%, and TDS/XGS of 20%

Inevitably, each country emerging from conflict must be considered on its merits. But as a broad principle, Oxfam International believes that post-conflict countries should be provided with debt-relief arrangements which limit repayments to 10% of public revenue for the duration of the reform and reconstruction programme. As Table 5 shows, a fiscal cap set at this level would free substantial funds. These could be allocated to government sectoral plans of action. Placing a ceiling on debt-servicing would result in substantial accumulation of arrears, which would need to be sterilised with the agreement of creditors through a debt work out, on the condition that the government remained on track with its commitments on poverty and human rights.

Table 5. Projected savings from a fiscal cap of 10% of total revenues (US$m)

	1998	**1999**	**2000**	**2001**
revenue projections	**227**	**270**	**320**	**382**
debt service projections	**42**	**54**	**58**	**61**
debt service at 10% of revenue	**23**	**27**	**32**	**38**
Budget savings	**19**	**27**	**26**	**23**

IMF 1998

Conclusion

Oxfam International urges both multilateral and bilateral creditors to take bold steps to alleviate Rwanda's debt burden, and to build on the existing hope for peace and the possibility of development. People are striving to rebuild their lives in the wake of the genocide. Economic recovery is underway, and there is a commitment on the part of Rwandans to succeed in the transition from recovery to development. If the opportunity for peace is not to be wasted, this willingness must be matched by coherent co-operation from the international community.

Debt is not the only problem facing Rwanda, whose peace is partial and fragile. Resolving conflict in the north-west, reducing the diversion of scarce resources into military expenditure, and developing coherent policies for poverty reduction are among the necessary measures. This requires action on many fronts - by the Rwandan government, donors, NGOs, and civil society. But the debt problem, left unresolved, will contribute to wider pressures endangering Rwanda's development prospects. Rwanda's debt burden is a fundamental obstacle to the reconstruction and rehabilitation efforts of the Rwandan Government and members of the international community. It is diverting scarce resources away from priority social sectors and the infrastructure, and hampering economic recovery. The HIPC framework has proven inadequate in tackling the problems of unsustainable debt in a country emerging from conflict. The creditor community must develop more flexible mechanisms for substantial, and fast, debt relief as a matter of priority. Without a new debt agenda which focuses on basic rights, an opportunity for reconstruction and development will be squandered.

The cost of the HIPC initiative would rise if the proposals outlined in this briefing were implemented. Yet Oxfam International believes that failure to achieve a swift resolution to the crisis of unsustainable debt in Rwanda will incur far higher costs, by diverting resources from the reconstruction programme and jeopardising peace efforts. The costs of a failure by the creditor community to act immediately, and decisively, will be counted in lives, as well as dollars.

END

[i] David Woodward The IMF, the World Bank and Economic Policy in Rwanda: Economic, Social and Political Implications September 1996

[ii] World Bank Rwanda: Debt Sustainability in the Transition to Growth with Equity Rwanda's Donor's Meeting June 2-3 1998

[iii] UNICEF Children and Women of Rwanda: a situation analysis of social sectors 1998

[iv] WB The Transition to Long-Term Economic Development: an overview of external financing needs June 1998

Published by Oxfam International March 1999
Published by Oxfam GB for Oxfam International under ISBN 978-1-84814-304-3