Oxfam International

Submission

Oxfam International submission to the Heavily Indebted Poor Country (HIPC) Debt Review

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Executive summary

Three years after its inception, the Heavily Indebted Poor Country (HIPC) initiative has failed to resolve the debt crisis in the world's poorest countries. Early promise has given way to disappointment. Without a concerted international effort to provide earlier and deeper debt relief, and to integrate debt reduction into wider poverty reduction initiatives, the HIPC initiative will join the long line of failed debt relief strategies; and debt will continue to destroy the potential for human development into the next millennium.

This is an important year. The G7, the World Bank, and the IMF may make major decisions to alter the existing debt relief framework, and make it relevant to the needs of the world's poorest countries. World Bank and IMF staff are carrying out a review of the HIPC framework, to be completed in time for the G7 in June. While there is growing international recognition that HIPC is flawed, this has now been coupled with important shifts in the political climate amongst the G7 countries. Germany, the host of the last G7 summit before the end of this millennium, has reversed the position of the previous German Government, and has put forward important proposals in favour of earlier and deeper debt relief. The British Government has taken these proposals even further to actually define increases to the amount of debt relief provided, and to ensure that it is linked to poverty reduction. The French Government has also announced a debt relief proposal to forgive debt service charges for thirty years for eligible countries. The US Government has also announced a debt relief initiative that would provide additional debt relief for "exceptionally performing" countries. Most recently, as this report was going to press, the Canadian Government announced an initiative that could potentially go further than the others announced. The Canadians propose adding to the list of forty one HIPCs and forgiving most bilateral debt. Most significantly, the Canadians call for more generous and deeper debt relief for countries committed to human development. The challenge now will be for supportive governments to work together for agreement on a debt relief proposal to take HIPC further. Global support for debt relief, as evidenced by the Jubilee 2000 movement, has moved indifferent governments, and a momentum for change is being created.

HIPC has been failing

The HIPC framework fails on three accounts:

1. Debt relief too late

Firstly, debt relief is provided too late. This is exacerbated by compliance demands through linking provision of HIPC relief, to performance under the IMF Enhanced Structural Adjustment Facility (ESAF). Inflexible interpretation has meant that even Uganda, one of the best performing HIPCs, after over a decade of strong reforms, received debt relief a year later than necessary, reducing benefits by $190 million and impacting adversely on Uganda's development. Only two out of forty-one countries have actually received debt relief so far, and only three are due this year.

2. Inadequate sustainability thresholds

Secondly, the thresholds that are used to define sustainability are not appropriate to the needs of these low-income economies. This can be seen in the case of Uganda, the first country to pass through the initiative, which has now reverted to an unsustainable debt situation. At the same time these thresholds do little to address the burden of debt servicing on national budgets in poor countries, where on average, debt servicing absorbs up to 40% of national revenue.

3. Insufficient resources

The third problem is that HIPC has been designed to serve the needs of creditors, rather than the needs of the poor. While the HIPC criteria fail on their own account to achieve debt sustainability for poor countries, they also fail to provide sufficient resources to address poverty reduction and human development. This failure further blocks progress on achieving internationally agreed development targets.

A proposal for reform: a Human Development Window

Oxfam International has proposed a simple mechanism to improve this framework: a *human development window* within HIPC. The overarching aim of the *human development window* is to incorporate the HIPC initiative into a global strategy for poverty reduction, geared towards the realisation of the targets set by UN Summits, and adopted by the OECD group of industrialised countries. To achieve these ambitious targets, a range of measures will be required, of which debt relief is one.

This window would operate in a simple fashion. It would provide incentives of earlier and deeper debt relief to countries committed to allocating these resources into a poverty reduction framework. Incentives would include:

- Debt relief within 1-2 years
- Debt relief going beyond modified sustainability thresholds to

    - a debt service ratio of 10-15 per cent
    - a debt-to-export ratio of 100-150 per cent
    - a debt-to-fiscal revenue ceiling of 10-15 per cent

The majority of HIPC countries have, or are developing, national frameworks for poverty reduction, including sectoral investment plans. Resources from debt relief would be channelled into a fund which would allocate finance into a range of sectoral plans, depending on national priorities. Government, donors, UN agencies, and civil society organisations would oversee the fund. This approach would ensure that poor and indebted countries move quickly to achieve debt sustainability; it would ensure that sufficient resources are delivered to enable countries to begin to achieve nationally agreed development targets, and it will ensure that debt relief resources are released in a transparent and accountable framework. This approach would set these countries on the path of achieving the internationally agreed goal of halving world poverty by 2015.

While it is true that the proposals outlined in this paper imply financial costs, earlier and deeper debt relief would cost considerably less than the industrialised countries spend subsidising their agriculture. The benefits would be reflected in increased prosperity and a reduced risk of social collapse. In the longer-term, the costs of continuing with the current HIPC framework will be considerably higher than the cost of removing what is now one of the main barriers to global poverty reduction efforts and increasing the efficiency of aid expenditures.

The real challenge is one of political will. In response to the East Asia crisis, the G7 created a $100 billion loan rescue package within a few months. If the will is there, action is possible to deliver the resources needed. At the same time debtor governments must also demonstrate the required political resolve to allocate finance from debt relief into poverty reduction efforts, and to create transparent mechanisms for ensuring that this finance has an impact. If creditors and debtors work together in this way, with resolve and will, 1999 could become the beginning of the end of the debt crisis.

Introduction

Three years after its inception, the Heavily Indebted Poor Countries (HIPC) initiative has failed to resolve the debt crisis in the world's poorest countries. Early promise has given way to disappointment. Without a concerted international effort to provide earlier and deeper debt relief, and to integrate debt reduction into wider poverty reduction initiatives, the HIPC initiative will join the long line of failed debt relief strategies. If HIPC fails, debt will continue to destroy the potential for human development into the next millennium.

There is, however, cause for hope. The Jubilee 2000 coalition has mobilised unprecedented levels of public support for debt relief. Churches, trade unions, the entertainment industry, development agencies and others have united behind a common demand that poor countries be freed from the yoke of debt. After two decades of studied indifference, the world's governments have been moved by the groundswell of public concern to give debt relief the prominence it demands on the international agenda. Most of the Group of Seven countries now openly acknowledge the failure of the HIPC framework. And in contrast to its predecessor, the new German Government supports the case for urgent international action. It is vital that the IMF-World Bank review of HIPC builds on these developments. If the review develops new and innovative strategies to revitalise international efforts, it may yet prove possible to pronounce 1999 as the year which witnessed the beginning of the end of the debt crisis.

There is, however, a danger that this window of opportunity will close. Bold pronouncements of intent by the world's industrialised countries have yet to be matched by substantive plans of action. The issue of resource mobilisation has been, to a large extent, ducked. So, too, has the critical question of linking debt relief to poverty reduction. Moreover, several key players, including the IMF and Japan, remain resistant to the development of a more ambitious debt relief framework. The United States is proceeding cautiously.

This Briefing reviews progress under the HIPC framework to date. It explains why it has delivered so little, in terms of countries actually receiving debt relief. In addition, it suggests that even the handful of beneficiaries have not been left in a sustainable debt position. In short, HIPC has failed in its central purpose of providing an 'exit' from the debt crisis. The fact that Uganda, the first country to pass through the initiative, has now reverted to an unsustainable debt situation, speaks volumes about the lack of realism at the heart of the HIPC process. Stated bluntly, the framework appears to have been guided less by the needs of debtors, than by considerations of affordability on the part of creditors.

Resolution of the debt crisis will require deeper and earlier debt relief. But the conversion of debt liabilities into human development investments also requires that creditors create an appropriate system of incentives. The Human Development Window proposed by Oxfam, and outlined in this paper, would provide debtor countries willing to transfer savings from debt relief into poverty reduction initiatives, with incentives in the form of earlier and deeper debt relief. Such an approach would enable financing from debt reduction to be integrated into broader financing strategies for achieving the internationally agreed human development goal of halving world poverty by 2015.

The case for debt reduction is rooted above all in moral considerations. It is fundamentally unacceptable for the world to tolerate a situation in which the some of the world's poorest and most vulnerable citizens are left paying for the past mistakes of creditors and debtors. Unfortunately, it is often forgotten that unsustainable debt is about more than foreign exchange losses. It is about the transfer to wealthy countries of resources which should be used for development in poor countries. The human face of debt is represented by children denied an opportunity for education, primary health clinics without drugs, and about destroyed livelihoods.

Debt relief is also a matter of common sense. While it is true that the proposals outlined in this paper imply financial costs, earlier and deeper debt relief would cost considerably less than the industrialised countries spend subsidising their agriculture. And the benefits would be reflected in increased prosperity and a reduced risk of social collapse. In the longer-term, the costs of continuing with the current HIPC framework will be considerably higher than the cost of removing what is now one of the main barriers to global poverty reduction efforts.

HIPC, one of a long line of failures?

When HIPC was developed in 1996, Oxfam and many other organisations welcomed the initiative.

- *It provided a comprehensive and integrated framework.* For the first time, debt relief was to be provided in a systematic operation by all creditors, bringing to an end the process of negotiation through different creditor clubs.

- *It extended to multilateral creditors.* For the first time the growing problem of multilateral debt was addressed. The Bretton Woods agencies had previously refused to agree to multilateral debt reduction claiming that this would affect their 'preferred creditor' status. In fact, multilateral debt reduction has not affected their status at all.

- *It established the principle that debt relief should be linked to ability to pay, rather than creditor demands.* The stated intention of HIPC is provide a 'robust exit' from unsustainable debt. Criteria were developed to provide appropriate debt relief to bring debt stock or debt servicing to agreed levels, which are described as 'sustainable'. At the same time, in order to avert problems of 'moral hazard', the time frame for compliance with IMF adjustment programmes, was doubled from that required to receive Paris Club debt relief, to six years in total. Some flexibility was agreed for countries demonstrating strong reforms.

While HIPC had some merits, it has failed the poor, and it is this that drives Oxfam's concern over the HIPC initiative. It is no coincidence that some of the world's poorest countries are also some of the most indebted. Of the 41 HIPC countries, over 80% are in the low human development category, according to the 1998 UNDP Human Development report.

- People live 25 years less in HIPC countries, than in industrial countries

- Women are thirty times more likely to die during pregnancy and childbirth, than in industrial countries

- Children are 10 times more likely to reach the age of five in industrial countries, than in HIPC countries.

For many HIPCs, debt servicing exceeds spending on health and education:

- In Nicaragua, debt servicing is two and a half times recurrent expenditure on health and education combined.

- Tanzania spends on debt the equivalent of total spending on health and education; this is four times as much as spending on primary education.

- In Rwanda debt servicing absorbs more than spending on health and education combined, more than ten times the health budget

HIPC, progress so far

Since its approval in 1996, HIPC's progress has been abysmal. The debt relief provided has been too limited, and implementation too slow:

- Only two out of forty-one countries have started to receive debt relief through HIPC, Uganda and Bolivia. Only three countries, Guyana, Mozambique and Mali, will receive debt relief in 1999.

Completion Point - date when debt relief starts	
1998	Uganda, Bolivia
1999	Guyana, Mozambique, Mali
2000	Burkina Faso
2001	Cote d'Ivoire
	Ethiopia, Mauritania
2002	Guinea-Bissau? - delays due to conflict
	Nicaragua, Niger, Tanzania, Togo, Zambia
2003	Madagascar
	Rwanda
	Burundi, Congo Democratic Republic
2004	Myanmar
	Sao Tome and Principe

Even after HIPC, many countries will still remain with unsustainable debt, underlining the inadequacy of the debt relief provided.

- **Uganda:** Following HIPC, debt servicing in 1998/9 fell by \$37m, from \$165m to \$128m, but still accounting for 18% of government revenue, absorbing finance that could be used for implementation of the national poverty eradication plan. Meanwhile over 50% of the population live below the poverty line. Recent falls in coffee prices have meant that even these small HIPC benefits have been lost, and Uganda's debt remains unsustainable.

- **Bolivia:** Debt servicing in 1999 will be reduced by $67m to $228m, however, the government is struggling to increase education sector expenditures, and will probably be forced to undertake further lending from the Inter-America Development Bank (IDB) to assist in this effort. This is in a country where UNICEF estimates 700,000 children are absent from school to support family income.

- **Senegal** is a country judged to have sustainable debt, where in 1999, debt service is expected to be 13% of exports. However this still absorbs 25% of government revenue. This is in a country with numerous development challenges where, for instance, adult literacy at 33%, is half the developing country average.

Too little, too late: why is HIPC failing to meet the needs of poor and indebted countries?

HIPC is failing because of three main problems with the design of the framework. First, the eligibility requirements, and linkage to performance under IMF adjustment programmes have caused long delays. The second problem is that the criteria used to determine whether debt stock and debt servicing are sustainable provide limited debt relief, while at the same time excluding many countries. The IMF and World Bank estimate that only half of the forty-one countries are theoretically eligible to receive debt relief through HIPC. The third problem is that HIPC's links to poverty reduction are too weak.

1. Time frame and track record

Countries entering HIPC must complete two successive IMF Enhanced Structural Adjustment Facility (ESAF) programmes - up to six years - although this can be reduced for exceptional performers. This eligibility requirement, coupled with inflexible interpretation, leads to serious delays in providing debt relief through HIPC.

The stated intention is to avert 'moral hazard' by ensuring full compliance with economic reforms *prior* to debt relief. In effect, this is a brutal application of 'carrot and stick' to very poor countries. Before HIPC, countries had to comply with three years of IMF reforms before receiving Paris Club debt relief. HIPC added another three years to this. However, there is now growing consensus amongst some creditor countries that three years, rather than six, should also be sufficient for HIPC.

Creditors are recognising that forcing countries to wait for up to six years for debt relief is counter-productive and inequitable. It is counter-productive because debt sustainability is needed to support economic reform; to remove the debt overhang, and to promote economic self-reliance. At the same time, sustained improvements in policy and financing of priority areas, are best achieved when governments can provide resources from their own budgets to achieve these ends. A lengthy time period is inequitable because it subordinates the needs of poor people to the budgetary claims of creditors.

The second aspect of the time frame is the problem of further delays related to compliance with IMF programmes. Oxfam International has argued that compliance with IMF ESAF programmes for HIPC countries is not appropriate, not least because these programmes have failed to generate growth, and have impacted negatively on the poor.

At the same time, compliance requirements can lead to delays in HIPC implementation. A recent external review of ESAF found that only a quarter of thirty-six ESAF programmes reviewed, were completed without significant delays. This has grave implications for the progress of the majority of countries going through

HIPC. Unlike Uganda or Bolivia, most HIPC countries are not seen as model reformers by the IMF and World Bank. Many are 'off-track' with their IMF programmes and could suffer lengthy delays in receiving debt relief.

Even with flexible interpretation of its track-record, after over a decade of strong reforms Uganda was required to go through another year of compliance. This resulted in a Decision Point in April 1997 to a Completion Point in April 1998. The cost of this delay was estimated as $190 million. In effect, Uganda was punished for being the first country to be considered under HIPC. Certain powerful creditors, such as the U.S., did not want too favorable a precedent to be set by Uganda.

The implications of this precedent for other, less well-performing HIPC countries, is that they have almost no chance of progressing rapidly through HIPC. For instance, Nicaragua has been undertaking substantial and deep economic reforms since the early 1990s, covering areas such as inflation, taxation, privatisation, public sector restructuring and retrenchment, and demobilisation. Targets have largely been achieved with relative success, in a difficult political environment. The devastating impact of Hurricane Mitch has meant that creditors have had to take short-term action on Nicaragua and Honduras, and a debt moratorium is now in place. However, while the decision point for Nicaragua is proposed for 1999, at the moment it is unlikely that the IMF will agree to further flexibility in the timeframe, even after the devastation of Hurricane Mitch, and Nicaragua will still have to wait until 2002 to receive limited HIPC debt relief.

- By the end of 2000, four years after the agreement of the initiative, only six countries will have received debt relief through HIPC.

- Countries with dire human needs, such as Tanzania, Zambia, and Nicaragua will have to wait until 2002 and far beyond for debt relief.

2. Sustainability thresholds are not appropriate for poor and indebted countries

The debt sustainability thresholds in HIPC are inappropriate for poor and indebted countries, firstly because the export criteria do not provide for debt sustainability, and secondly because the fiscal criteria do not address the impact of debt servicing on the national budget, while at the same time excluding the majority of these countries. Rather than addressing the debtors problem of ‘ability to pay’ these criteria are more focused on the creditors ‘willingness to afford’. With these criteria, half of HIPC countries will not benefit from the framework at all.

Export criteria

The existing export criteria in HIPC were developed on the basis of experience in the 1980s with middle-income Latin American countries saddled with mostly commercial debt. These criteria are:

- debt stock to exports in the order of 200-250%

- debt service to exports around 20-25%

There are serious questions whether these thresholds are appropriate for HIPC countries. By comparison with middle income countries in Latin America, HIPC countries have poor infrastructure, acute levels of poverty, and appalling social indicators. They also have a far weaker export base, and are especially vulnerable to external shocks, such as falling commodity prices. In this decade, for instance, commodity prices have fallen around 50% from 1990s highs, for commodities such as coffee, cotton, maize, sugar and copper. The impact of the financial crisis in East Asia, Russia, Brazil, and beyond, means that a global recession is driving commodity prices down, where non-energy prices dropped by 13% from end-1997 to end-1998. For a large number of HIPCs, a few commodities make up the majority of exports. For instance Uganda, which relies on coffee for over 50% of its exports, has seen benefits from HIPC wiped out by the fall in coffee prices.

In Oxfam International's view, these indicators must be adjusted to take into account the true position of HIPC countries, and should be lowered to at least 150% for net present value debt to exports, and 15% debt service to exports. More appropriate ratios such as these would allow higher numbers of countries to benefit from the framework, while at the same time, ensuring a complete exit from unsustainable debt.

Fiscal criteria

Because debt distress is measured under HIPC primarily on the basis of export criteria, the fiscal burden placed on government budgets from debt servicing is not sufficiently addressed. The fiscal criteria developed for HIPC also fail in this respect, and not least because they exclude an overwhelming majority of HIPC countries.

The existing fiscal criteria apply if net present value debt stock to revenue is greater than 280%. However there are two eligibility conditions. First, countries must meet revenue collection levels of over 20% of GDP. The second condition is that exports must be greater than 40% of GDP. The fiscal criteria were a later addition to the HIPC framework. The French Government was especially keen to add this particular set of fiscal criteria to ensure that Côte d'Ivoire, which would not have qualified for HIPC on debt to export criteria alone, could enter the initiative.

Only *four* HIPCs meet the fiscal criteria: Côte d'Ivoire, Guyana, and, possibly Congo Democratic Republic and Mauritania. Although the majority of HIPCs have debt stock to revenue above 280%, most have revenue collection under 20% of GDP, and few have exports over 40% of GDP.

While there are concerns that countries make best efforts to raise revenues, the revenue collection criteria under HIPC are unrealistic. The majority of HIPCs start from a very low revenue base, since incomes are so low. In Uganda, for instance, which has over a decade of successful reforms under IMF and World Bank programmes and is seen as one of the best performers in Africa, revenue as a percentage of GDP was just over 11% in 1997/1998.

However, even with modification, these fiscal criteria may not be the most appropriate approach, since they do not fully reflect the burden that is placed on the budget by debt servicing. In HIPCs, average debt service to government revenue stood at 40% in 1996. This can be seen in a range of HIPC countries:

- Nicaragua's debt servicing absorbed two thirds of the budget in 1997;

- In 1997, Niger and Ethiopia used almost half of the government budget on debt servicing;

- In 1996, debt servicing absorbed 44% of the Zambia budget, and 35% in Malawi.

Even when countries pass through HIPC, they remain with a heavy burden of debt on the national budget:

- **Mozambique** will receive HIPC benefits in the middle of 1999, of a reduction in nominal debt stock of $2.9 billion, yet the immediate effect is only an 11% reduction in debt servicing, from $108 million to $96 million. In one of the poorest countries in the world, recovering from decades of conflict, debt servicing will remain more than government health and education spending combined.

- **Mali** will receive HIPC debt relief in 2000, with a proposed reduction in debt service from $99m to $87m, some $12m. This is a reduction equal to 10% of the education budget, where after HIPC, debt service will remain more than the basic education budget in a country where almost 70% of adults are illiterate.

An alternative fiscal indicator would recognise the burden that debt servicing places on this national budget, and thus on human development. Oxfam International has proposed that a 10-15% ceiling be placed on the portion of government revenue that is allocated to debt servicing. This approach would ensure that debt servicing was constrained to reasonable limits. However, a more radical approach to debt relief is required, one that that is driven by human development concerns, rather than by the needs of creditors.

3. HIPC does not take into account human development concerns

The major problem with HIPC as it stands, is that it has little impact on poverty reduction. While the debt overhang is partly reduced, with consequent benefits in future investment growth, governments see little immediate impact on reducing domestic resources allocated to debt servicing. Oxfam International, along with some governments, and many other agencies, have argued that debt relief should be linked more closely to poverty reduction.

The IMF and World Bank have attempted to do this to some extent within HIPC. At the moment, increases in social sector spending form part of the wide range of conditionalities that debtor governments must comply with *before* receiving debt relief through HIPC. Conditionalities have included, for instance, targets for increases in education and health spending, where countries have to meet these targets before being allowed to go through HIPC. This is a flawed approach.

Firstly, HIPC countries are among the poorest in the world. If attempts are made to address poverty through HIPC, it requires a more integrated approach than simply tacking-on conditionality near the end of a process. The process of bolting-on social sector provision to flawed macro-economic approaches has already been discredited by the World Bank itself. Poverty reduction should be built into the debt relief process from the start, in the same way as it should be built into macro-economic policies. Thus poverty reduction concerns should properly influence the development of appropriate debt sustainability thresholds.

Secondly, as long as governmental budgets are heavily constrained by debt servicing, they are in a weak position to make major commitments to increased social sector spending. Reallocations can take place between military and social sector expenditure; reduction of parastatal subsidies, or within sectors, for example, from tertiary to basic education. However, when HIPC countries on average use 40% of their national budgets on debt servicing this seems to be a somewhat backward approach.

We strongly contend that external debt servicing diverts finance away from social sector spending but the IMF's standard response is that this is a misleading argument, partly because HIPC countries are net recipients of external finance. They receive more in grants and loans than they allocate in external debt servicing. While net external flows may be positive, the IMF appears to ignore the fact that the majority of these countries have extremely high levels of poverty and human suffering. They will not meet, according to current trends, internationally agreed human development targets into the next millennium. Aid alone, while of vital importance, has not, and will not, provide enough resources for sustainable improvements in development in HIPC countries. Debt relief will also be required.

If the IMF and World Bank are committed to seeing the world's poorest and indebted countries make progress in reducing poverty, they need to ensure that debt relief is provided earlier on, and deep enough, so that investments in poverty reduction, in health and in education, in rural roads and in the productive capacity of the poor, can be made. That is why Oxfam International proposes that an incentive approach be developed through creating a *human development window* in HIPC.

Improving HIPC: A Human Development Approach

The overarching aim of the *human development window* is to incorporate the HIPC initiative into a global strategy for poverty reduction geared towards the realisation of the targets set by UN Summits, and adopted by the OECD group of industrialised countries. To achieve these ambitious targets, a range of measures will be required, of which debt relief is one. High levels of pro-poor growth will be necessary. For sub-Saharan Africa it is estimated that levels would need to be around 3% higher than that during the 90s. Such growth will require stable and appropriate policy environments, particularly for equitable growth to be achieved. At the same time, improved international terms of trade will be important. Both aid and debt relief will be required to support improvements in national policies, and ultimately in budget allocations aimed at poverty reduction.

How would the Human Development Window convert HIPC into a mechanism to deliver on poverty reduction targets? Principally by offering governments incentives to convert debt liabilities into human development investments. Converting debt into development is nothing new. Debt-for-development swaps have helped to finance a large number of projects over the last decade. However, improving HIPC in this simple way would have far greater impact than any mere debt swap, since it addresses the entirety of debt stock in one operation, and would go beyond project based approaches. The incentives would take the form of earlier and deeper debt relief than that offered under the reformed HIPC framework outlined above, and would include:

- Debt relief within 1-2 years
- Debt relief going beyond modified sustainability thresholds to
  - a debt service ratio of 10-15 per cent
  - a debt-to-export ratio of 100-150 per cent
  - a debt-to-fiscal revenue ceiling of 10-15 per cent

Eligibility for the Human Development Window would be based on three conditions:

- **Debtor government commitments**

Firstly, debtor governments would commit themselves in advance of the HIPC debt relief process to allocating 70-100 per cent of budgetary savings on debt over a five year period to poverty reduction initiatives.

- **Poverty Action Framework**

Secondly, debtors would be required to develop a Poverty Action Framework (PAF) summarising existing poverty reduction and social sector investment strategies and plans. These could include a range of initiatives to reduce poverty, for instance: sectoral investments in basic education; in rural feeder roads to access remote and poor rural areas, or assistance to poor farmers to improve agricultural production. The PAF would also set out the major human development goals agreed with donors, multilateral institutions, UN agencies and civil society. This would include detailed financing requirements for accelerating the attainment of the human development targets. Critically, the PAF would set out in detail how resources released through debt relief would be allocated between different sectors, along with broad overviews of allocations between recurrent and development budgets.

- **National Poverty Fund**

Finally debtor governments would establish a national poverty fund, into which the savings from debt relief would be transferred. They would be required to make clear commitments to transparency and accountability, including the independent auditing of accounts and public reporting on expenditure. Provisions for regular consultation with civil society would be required in evaluating progress towards to poverty reduction goals set under the PAF, monitoring allocations, the impact of investments, identifying problems, and re-defining new priorities.

Oxfam has previously shown that, for instance in Tanzania, application of this proposal would enable the Tanzanian government to set itself on the path of achieving universal primary education. If debt servicing were limited to a 10% ceiling on revenue, and if 60% of resources thus released were allocated to primary education, Tanzania could raise the gross enrolment rate from the 85 per cent envisaged for 2002 under the Basic Education Master Plan, to 95 per cent. This would create a platform for achieving high quality universal primary education by 2005.

Various objections have been raised to this proposal. Some debtors fear that it would create another layer of conditionality, thereby undermining their prospects for debt relief. In fact, the incentives would provide *additional* benefits for governments with a commitment to poverty reduction. **It would not exclude governments lacking such a commitment, from access to HIPC on less preferential terms.**

On the creditor side, various fears have been raised. One concern is that governments might renege on their commitments by failing to allocate debt service savings to the areas identified. Where this occurs as a consequence of policy failure (as distinct from unavoidable fiscal problems associated with drought, floods or a collapse in export prices, for example), strict conditionality would have to be applied. One approach would be to penalise any shortfall in actual spending on a dollar-for-dollar basis in the form of reduced aid commitments. At the moment the IMF and World Bank would rather see social conditionalities imposed *before* providing debt relief, this new approach provides an incentive of early and substantial debt relief, but with penalties for default, *after* providing debt relief.

Other creditors - such as the IMF - claim that the arrangement would be too complex and cumbersome to administer. In fact, it would be considerably less complex and cumbersome than existing IMF conditionalities, under which governments are expected to comply with several dozens of targets on a quarterly basis. While there is some heartening discussion around improving IMF programming through the inclusion of 'social principles' to promote a pro-poor policy environment, such changes may take many years to achieve. The *human development window* approach allows debt relief resources to be released immediately into a pro-poor framework, and is a mechanism which can be rapidly agreed, simply implemented, and properly monitored.

The *human development window* proposal also builds on growing evidence in the World Bank and elsewhere that increased government ownership increases the success and sustainability of national programming. Where this programming is developed with civil society participation, a broader ownership and political consensus can evolve, further enhancing progress. Recent World Bank approaches, such as 'Comprehensive Development Framework' proposal, recognise the need to balance macro-economic issues with human development concerns. This approach supports the notion of improving a cold financial debt relief framework, into a mechanism which can also address human development concerns.

Uganda, implementing a human development approach to HIPC

An example of what could be achieved through a compact between creditors and debtors has been provided by Uganda, the first country to receive HIPC debt relief. All of the budget savings from debt, amounting to just under $40 million a year, have been allocated to a Poverty Action Fund. This fund allocates resources to priority areas defined in the national Poverty Eradication Action Plan; a plan that was developed in a consultative fashion, and with broad national consensus, over a period of two years. The fund allocates finance to rural feeder roads, agricultural extension, water supply, primary health care and primary education.

Transfers to this fund are helping to finance implementation of the ambitious universal primary education programme, which has more than doubled primary school enrolment to 5.3 million children since its introduction in 1997. Apart from the direct benefits, the Poverty Action Fund is helping to improve government accountability and transparency. All financial flows are reported on a quarterly basis, an independent audit is to be published annually, and civil society is involved in the steering committee which oversees use of the Fund.

At a wider level, Uganda has also implemented laws which ensure that Parliament scrutinises new lending to ensure it is undertaken within a prudent lending strategy, and meets national development priorities. In fact, new lending must be on IDA terms or better, and there is a strict annual cap of $10 million on non-concessional lending in exceptional circumstances. Opening up debt management to civil society and parliament, coupled to a prudent strategy, builds the foundation for improved lending and use of lending into the future. Uganda shows what is possible, even in difficult circumstances, when there is sufficient political will.

Reforming HIPC, eradicating poverty: Political will

This initiative is a breakthrough… It deals with debt in a comprehensive way to give countries the possibility of exiting from unsustainable debt. It is very good news for the poor of the world.

James D. Wolfensohn, President, World Bank, 1996, on the HIPC agreement

Three years on, HIPC has not been good news for the poor of this world. It has failed because the framework has been implemented with a view to minimising the costs to creditors, rather to deal once and for all with the problems of debtors.

One of the requirements for more effective debt relief is additional finance. IMF gold stocks represent a potential source. These amount to around 100 million ounces, and at today's prices the total value is approximately $30 billion. There are a number of reasons as to why gold sales are an appropriate tool to support HIPC. Firstly, they are a poor investment. Gold prices have been falling, and may continue to do so. Secondly, a sale of reserves will not undermine the IMF's position or ability to provide resources to developing countries in the future. If half of the gold was sold, some $15 billion, and finance from sales were appropriately invested in financial securities, interest payments could provide substantial support to an improved HIPC.

The World Bank and IMF has made tentative estimates of various costs for reforming HIPC. The most expensive would cost around $45 billion in net present value terms.

Tentative costings for illustrative changes in the HIPC framework	
Total Debt stock of HIPC countries (1996)	$167 billion
Debt stock after receiving full Naples Terms	$100 billion
Cost of HIPC relief following Naples Terms: with 3 year eligibility, debt/exports 100%, debt/revenue 150%, no fiscal thresholds	$45 billion
Source: IMF, 1999; excludes Nigeria, Sudan, Somalia, Liberia; does not include the cost of additional countries which would enter the initiative due to reduced thresholds	

The Oxfam human development window proposal would seek to shorten the timeframe to 1-2 years for those countries willing to adopt this approach, and would also utilise a fiscal cap which would raise the costs of HIPC further. These approaches would also ensure that countries presently excluded from HIPC are included. Clearly, delivery of debt relief of this magnitude will be expensive, although the debt relief itself is provided over many years. Given the expense, it will be of utmost importance to ensure that such finance is well used, when resources are so scarce. The human development window proposed by Oxfam ensures that this can happen.

The real question is one of priority. If these figures are put in context, $45 billion is equivalent to what the European Union provides in subsidies to their farming community. It is less than 6% of global military spending. Nonetheless, it is possible to mobilise these levels of resources, after all, in response to the East Asia crisis, the G7 created a $100 billion loan rescue package within a few months.

The real problem is not resources, but political will. As we reach the end of this millennium, what is required is the political resolve to make debt relief work for the world's poor. There is a major opportunity now, as G7 leaders and finance ministers are developing their positions in the run-up to the G7 summit in Cologne. Already there are proposals on the table to reduce the time frame by three years; to lower the sustainability thresholds; to increase Paris Club debt relief beyond Lyon terms; to eliminate ODA debt; to sell IMF gold, to establish a strong connection with human development and to deliver agreements on $50 billion of debt relief before the end of the year 2000. If world leaders worked together, and delivered the political effort and will that their public demand, then progress can be made. It is important that they work together. It benefits no one to see improvements to HIPC lost in competing proposals. What is necessary is a unified purpose in making HIPC work for the poor. Resolve will be required to address this broader goal, and resolve will be required to deliver the resources necessary to put an end to the debt crisis. Millions of people in Africa, in Latin America, in Europe and in North America will be demanding an achievement worthy of a millennium celebration.

Appendix: HIPC Progress

Countries going through HIPC	**Completion point (date when debt relief starts)**	Decision point (date when assessment of debt is made)	HIPC relief (NPV) $million	HIPC relief (nominal terms) $million
Uganda	April 1998	April 1997	347	650
Bolivia	September 1998	September 1997	448	760
Guyana	Spring 1999	December 1997	253	500
Mozambique	mid-1999	March 1998	1,442	2,900
Mali	December 1999	End 1998	128	250
Burkina Faso	April 2000	September 1997	115	200
Côte d'Ivoire	March 2001	March 1998	345	800
Ethiopia	Spring 2002	Spring 99	636	1,300
Mauritania	Spring 2002	Spring 1999	271	550
Guinea-Bissau	Delay - Conflict	Delay - Conflict	300	600
		Total debt relief agreed so far	**4,285**	**8,510**
Nicaragua, Niger, Tanzania, Togo, Zambia	2002	1999	**-**	**-**
Madagascar, Rwanda	2003	2000	**-**	**-**
Burundi, Congo Democratic Republic, Myanmar, Sao Tome and Principe	2004	2001	**-**	**-**
21 countries				

Countries unlikely to receive debt relief through HIPC			
Benin	June 1997	0	0
Senegal	March 1998	0	0
Chad, Guinea, Sierra Leone, Vietnam, Yemen	1999	0	0
Cameroon, Republic of Congo	2000	0	0
Angola, Central African Republic, Guinea, Honduras	2001	0	0
13 countries			
Not determined			
Ghana, Kenya, Lao-PDR, Liberia, Malawi, Somalia, Sudan (Nigeria has recently been excluded)			

Oxfam International is a network of eleven aid agencies that work in 120 countries throughout the developing world: Oxfam America, Oxfam in Belgium, Oxfam Canada, Community Aid Abroad (Australia), Oxfam Great Britain, Oxfam Hong Kong, Intermon (Spain), Oxfam Ireland, Netherlands Organisation for International Development Cooperation (NOVIB), Oxfam New Zealand, and Oxfam Quebec. Please call or write to any of the agencies for further information.

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