STRATEGIES FOR FINANCING DEVELOPMENT

The Newsletter of the HIPC CBP and the FPC CBP

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HIPC Debt Analysis & Strategy

Foreign Private Capital Flows

HIPC MINISTERS' VIEWS D

The May-June meetings of the G8 Heads of State in Evian, and Ministers of Finance in Deauville, have for the first time discussed the views of the HIPC Finance Ministers' Network, representing 36 HIPCs. At their eighth meeting, on 28-29 April in Kigali, Rwanda, HIPC Ministers had agreed a reinforced targeted campaign to transmit their ideas to the international community. Donald Kaberuka, Minister of Finance and Economic Planning of Rwanda, began this process by presenting their 'Kigali Declaration' to Chancellor Gordon Brown and International Development Minister Clare Short during visits to the UK at the end of April. Thereafter, in their capacity as NEPAD's founding Head of State, the Presidents of Senegal and Nigeria, Abdoulaye Wade and Olusegun Obasanjo, presented the declaration to the G8 Summiteers, and President Wade also wrote directly to President Jacques Chirac of France. The declaration was also transmitted to other G8 Ministers of Finance, the IMF Managing Director and the World Bank President.

H. E. Paul Kagame, President of the Republic of Rwanda, opening the 8th HIPC Finance Ministers Meeting

The meeting in Kigali was jointly organised by the HIPC CBP implementing partners and the Government of the Republic of Rwanda. It was opened by the President of Rwanda, H.E. Paul Kagame, and chaired by the Minister of Finance and Economic Planning of Rwanda; the Minister of Budget of Senegal; and the Minister of Economy and Finance of Guinea-Bissau. It was attended by 31 HIPCs, 14 of which at Ministerial level. Five further HIPCs sent apologies for non-attendance, due to IMF missions or budget debates in their countries.

In the Kigali Declaration, Ministers reiterated their appreciation for measures by the international community to implement HIPC II, to mobilise additional financing for development, to enable countries to implement poverty reduction strategies, and to enhance HIPC government capacity to manage development financing and poverty reduction programmes. They stressed once more their commitment to designing and implementing poverty reduction strategies, and to doing everything in their power to spend debt relief and new financing productively and transparently on poverty reduction. Nevertheless, they raised important common problems which require urgent attention if HIPC countries are to attain their Millennium Development Goals by 2015.

1. IMPLEMENTING HIPC II

1.1. Assuring Full Participation of Creditors

Ministers welcomed recent progress in convincing some non-participating creditors to participate in HIPC II, as well as the growing acknowledgement by the international community that non-participation of creditors is a severe problem. They urged the international community to:

- Establish as an urgent priority a rapid response legal technical assistance facility to help HIPCs to discourage or deal with creditor litigation. Ministers understood that the Bretton Woods Institutions perceive the management of such a facility as being incompatible with their roles, but insisted that technical assistance could be a key means to avoid litigation, as witnessed in their IDA commercial debt buybacks. An appropriate institution which could manage such a facility must be identified immediately;
- Continue to publish the details of creditors that refuse to provide relief on Paris Club-comparable terms. HIPCs committed themselves to publishing all such details and to working with international organisations and civil society to change such creditors' minds;
- Complete studies on widening the use of the IDA commercial debt reduction facility and agree on its replenishment by the time of the IMF-World Bank Annual Meetings;
- Agree immediately to create a Trust Fund for clearing HIPC debts to other HIPCs, so that all preparatory work can be completed before, and funding mobilised at the IMF-World Bank Annual Meetings.

1.2. Reinforce Long-Term Debt Sustainability

Ministers welcomed the planned BWI staff paper on long-term debt sustainability. They urged that the study and wider international discussions should examine the following issues:

- Including 'likely shocks' such as commodity price volatility, natural disasters and aid shortfalls as the baseline macroeconomic scenarios of BWI programmes;
- Accelerating independently-run capacity-building efforts for HIPCs so that they develop within the next 12-24 months the ability to project multiple macroeconomic scenarios;
- Treating bilateral debt cancellations beyond 90% as 'additional' relief, to reduce HIPC debt burdens below HIPC thresholds and provide a margin to protect against shocks;
- Providing PRGF loans on IDA terms;
- Building into all external funding, especially the IMF, MDBs and EU, floating tranches of contingency finance which can be disbursed immediately to compensate against shocks;
- Accelerating implementation of the recommendations of the World Bank Task Force on Commodity Risk Management;
- Focussing PRSPs on export diversification into higher value-added products, combined with opening markets for such products by OECD countries.

Ministers underlined three recommendations:

- That PRGFs should NOT contain alternative scenarios which do not reach the MDGs. Any baseline scenario should aim to attain the MDGs, and alternative scenarios should show how to attain them in spite of any simulated shocks;
- That debt sustainability after completion point should not be judged rigidly by PV/export

ratios. Higher aid flows should be accommodated even if they lead to PV ratios between 150% and 200%, provided that debt service/budget revenue ratios remain below 10%;
- That all debt sustainability analyses and PRGF documents should examine the total (domestic + external) debt burdens of HIPCs, and that the international community should give enhanced priority to solving domestic debt problems, which are undermining the private sector, growth prospects and therefore the sustainability of external debt.

2. FINANCING FOR DEVELOPMENT

2.1. Financing Needs and Global Initiatives

Ministers welcomed recent initiatives to expand financing for development. In particular, they:
- Endorsed the UK proposal for an International Financing Facility (IFF), while urging that its funding should be fully additional and channelled to grants;
- Endorsed global funds, such as the Education for All Fast Track Initiative, the Global Fund to Fight AIDS, Tuberculosis and Malaria and the Global Environment Facility. However, they stressed that these must be additional and sustainable over the long term;
- Underlined that all new facilities should coordinate resources through PRSPs, and agree streamlined procedures and conditionalities in partnership with developing countries;
- Urged even more emphasis on promoting trade and investment opportunities for HIPCs, to help them achieve more self-sustaining and less aid-dependent development.

Ministers reiterated their view that all BWI Board country papers should present the financing amounts needed for countries to reach the MDGs and national development goals, drawing on UN analyses as appropriate, in order to mobilise the right amounts of additional resources.

2.2. Partnership to Improve Donor and Government Practices

Ministers discussed their difficulties in complying with excessively complex and lengthy donor procedures, and strongly recommended that donors and international institutions:
- Take immediate steps to simplify and harmonise procedures to expedite disbursements;
- Take greater account of national aid management practices and capacities;
- Review the IDA graduation criteria to ensure HIPC countries can continue to have access to highly concessional funds in order to implement their poverty reduction strategies;
- Give preference to budget support;
- Decentralise decision-making and funding to their local embassies and resident offices.

With respect to donor co-ordination, Ministers:
- Supported the Strategic Partnership with Africa (SPA) efforts to review best practices in African countries, but urged greater participation of HIPC country experts in the SPA work and a rapid widening of countries covered (to include non-African HIPCs);
- Cited many other examples of best practice in donor coordination, and of evaluation of donor practices by HIPCs themselves, and urged more initiatives for HIPCs to exchange best donor coordination practices with one another, and continued high-level discussions on aid quality and policy with the OECD DAC members;
- Supported the principles agreed at the Rome High-Level Forum on Harmonisation and recommended their immediate implementation by preparing a detailed plan of action.

Ministers acknowledged that additional funds would require efforts to increase HIPC absorptive capacity. They indicated that large expenditure programmes are currently under-funded and could rapidly absorb additional money. Moreover they stressed that various HIPCs have in recent years successfully implemented programmes such as decentralisation, MTEFs, financial accountability capacity building and procurement reform, which have dramatically increased their absorptive capacity. They suggested a programme to exchange information among HIPCs on best practices.

3. POVERTY REDUCTION STRATEGIES

Ministers again regretted the delay in reaching HIPC decision and completion points. They indicated that failure to streamline conditionalities rather than delay in finalising PRSPs has been the major reason for these delays. While welcoming the reduced the number of conditionalities in BWI programmes, they remained concerned that compliance with conditions is being enforced with insufficient flexibility, that excessive new conditions are being introduced into programmes, and that funders continue to apply separate political conditions. They urged the BWIs to reduce even further the number of structural conditions, by limiting them to those that are essential to growth and poverty reduction, and to eliminate all micro-management of their economies.

Ministers reconfirmed their commitment to macroeconomic stability as a prerequisite for poverty reduction. However, they recommended a much greater degree of flexibility in designing and implementing macroeconomic frameworks, so as to ensure adequate growth to reach the MDGs. While PRSPs have successfully involved civil society in national debates on how to reduce poverty, they have not focussed sufficiently on accelerated economic growth. They also urged that PRSPs be more integrated with wider national development programmes in order to ensure comprehensive and consistent policy formulation and implementation.

To enhance the national PRSP process, Ministers called for an intensive increase in efforts to build their national capacity to design and analyse the potential and actual impact of macroeconomic frameworks and structural policies on poverty reduction, including the provision of analytical tools.

Finally, Ministers suggested a comprehensive annual review of PRSPs, PRGFs and PRSCs, to ensure they are streamlining conditionality and promoting growth and poverty reduction.

4. CONFLICT-AFFECTED COUNTRIES

Ministers made recommendations to overcome specific difficulties of conflict-affected countries:
- More focus on reducing the ratios of debt service/exports and debt service/budget revenue in the early years when designing HIPC debt relief delivery;
- Additional resources to assist countries to clear arrears prior to their entry into HIPC;
- More flexibility of programme conditionalities to allow increased disbursements and more expenditure for reconstruction, reducing insecurity and refugees.

5. CAPACITY BUILDING REQUIREMENTS

Ministers agreed on a set of recommendations for reinforcing capacity-building efforts, which will be transmitted to the HIPC CBP Steering Committee and other international fora in due course. Finally, they agreed that a further briefing of HIPC Finance Ministers on progress would take place in Dubai at the time of the IMF and World Bank Annual Meetings.

‘SECOND GENERATION’ NATIONAL WORKSHOPS

To date, the Franc Zone national debt strategy workshops focused on analysing debt sustainability in the framework of the HIPC Initiative. The main objective was to help countries to undertake independent analyses of their debt sustainability and to be in a better position to negotiate with the Bretton Woods Institutions regarding their eligibility and the terms they would receive at decision point. It was necessary to refocus the workshops in order to:

- ***assist countries to prepare for negotiations at completion point,***
- ***help countries to maintain their debt sustainability beyond the completion point, and***
- ***consider the region non-HIPCs that face debt sustainability problems (middle income countries).***

Pôle-Dette and DRI have therefore devised a 2nd generation of national workshops to: i) improve the interface between domestic and external debt management, and macroeconomic management and poverty reduction, ii) place public finances and debt sustainability at the centre of national economic policies and iii) set up a mechanism to co-ordinate a sustainable national debt strategy.

1. Innovations of the second generation national workshops

Second-generation national workshops involve the following innovations:

- ***emphasis placed on new financing policy and domestic debt:*** the 1st generation workshops already went well beyond the HIPC Initiative methodology, by emphasising domestic debt. The 2nd generation workshops are focusing on attracting new external financing and formulating domestic debt strategies. New external financing strategies are concerned with mobilising both grants and loans, and deal with issues related to external lenders’ policies, procedures and practices, constraints on using external aid and identifying priority lenders. The enhanced methodology on domestic debt sustainability leads to assess the total sustainability of public debt and review the management of public liquidities and the development of the public securities market.

- ***targeting public debt sustainability and Franc Zone convergence criteria:*** the aim of the 1st generation workshops was to *assess* the country’s debt sustainability at decision and completion points, and to *evaluate* the impact of economic and financial policies and the terms of mobilised new financing on its debt sustainability beyond the completion point. The additional aim of the 2nd generation workshops is to *determine the conditions in which total public debt sustainability could be maintained* beyond the completion point, while enabling the country to comply with the convergence criteria in force in the Franc Zone in the medium and long term.

2. Methodology of the second generation workshops

Second generation workshops are conducted sequentially according to three broad stages:

Stage 1: developing scenarios and preliminary strategies
Participants are divided into two technical groups, each made up of a certain number of sub-groups. The first technical group is responsible for developing three preliminary financial strategies, made up of a basic strategy and two alternative strategies. Each financial strategy involves an existing external debt relief scenario, an existing domestic debt-restructuring scenario, a domestic and external new financing scenario and a residual financing gap-filling scenario.

The second technical group is responsible for designing three preliminary scenarios for the country’s borrowing needs in terms of development and poverty reduction, made up of one basic scenario and two alternative scenarios enabling to measure the impact on both public finances and debt sustainability of a proactive poverty reduction programme or favourable or unfavourable exogenous shocks.

Stage 2: developing reference strategies
The results of technical groups’ tasks in stage 1 are combined to obtain three or more ***reference strategies*** made up of one basic strategy and two alternatives. Each reference strategy is developed by a team consisting of representatives of the various technical groups from stage 1. The reference strategies are simulated in Debt-Pro© to assess their impact on both public finances and public debt sustainability, as well as their overall consistency with poverty reduction objectives.

Stage 3: consensus on debt sustainability and completion of the national strategy paper
At the beginning of this stage, participants debate in order to build the consensus on both debt and public finances sustainability. They determine a certain number of indicators by a given year (X number of years after the completion point). For example, during the first second generation national workshop held in Burkina Faso from 31 March to 12 April 2003, the consensus was built around the indicators shown in the table.

The results of the reference strategies produced in stage 2 are compared with the objectives in order to assess the additional measures required to achieve the objectives. Teams responsible for each strategy then identify the additional measures needed to enable the objectives to be achieved. These are macroeconomic measures (e.g. budget and balance of payments adjustment), measures for restructuring existing debt and new financing policy (reviewing composition, terms and conditions). Each measure is simulated repeatedly until the objectives are achieved by the year set. The strategies that achieve the objectives are called ***final strategies.***

Once these tasks are completed, the country’s authorities have elements enabling them to determine a fiscal policy and a policy to mobilise new resources, which are essential for both sustainable public finances and development.

Table 1 – Consensual indicators for monitoring debt and public finances sustainability in Burkina Faso

INDICATORS	Consensus standard	Timeframe
I – Public debt sustainability		
- NPV external public debt (% exports of goods and services)	150%	2010
- NPV external public debt (% budget revenue)	250%	
- Total public debt stock (% gross domestic product)*	≤70%	2005
- Total public debt service (% budget revenue)	15%	2005
II – Public finances sustainability		
- Basic budget balance, excluding grants (% gross domestic product)*	≥0%	2005
- Average inflation rate *	≤3%	2005
- Wage bill (% tax revenue)**	≤35%	2005
- Public investment financed from own resources (% tax revenue)**	≥20%	2005
- Current external deficit, excluding grants (% gross domestic product)**	≤5%	2005
- Tax ratio ** (tax revenue/gross domestic product)	≥17%	2005

** Primary WAEMU convergence criterion ** Secondary WAEMU convergence criterion*

HONDURAS' PUBLIC DEBT LAW REFORMS

Honduras has for some time been reforming its legislation on the management of public debt. The Constitution of 11 January 1982 mentioned public debt in at least five articles: 205, which establishes the powers of the Congress to approve loans; 245, which authorises the Executive to negotiate and contract loans, subject to approval of Congress; 353, which defines as financial obligations the debts contracted by the State; 356, under which the State guarantees payment of all debt contracted in accordance with the Constitution and other laws; and 357, which orders that all authorisations of external and domestic public debt shall be regulated by a law.

Notwithstanding this constitutional mandate during the 1980's no special law was introduced. The public debt process was governed by regulations resulting from various legal instruments that provided guidance in dealing with specific steps:

- Executive Decree 2, of 30 November 1982, in the throes of the international financial crisis, authorised Central Government to assume external loans guaranteed directly or indirectly by the State, and to process their payment or to negotiate their refinancing.
- Decree 149-88 of December 1988 created a legal framework that permitted operations converting public external debt into domestic debt, establishing annual limits, creating institutions and a procedure, defining a form of payment (Debt Conversion Bonds), discounts on face value and acceptable uses for the resources obtained.

Only on 10 January 1991 was a legal framework for public debt established, with Decree 111-90, the Law on Public Credit. This:

- provides a legal definition for public credit, including debt of the non-financial public sector, and establishes its objectives;
- defines the responsibility for formulating debt policy of the Executive, in the Ministry of Finance, Ministry of Planning (which was later dissolved, passing its powers to Finance) and the Central Bank of Honduras (BCH). The Ministry of Finance, through the Public Credit Directorate General, also implements the debt policy;
- confers powers on Finance including: i) proposing criteria for formulating policies, ii) monitoring the management, negotiation and signing of agreements, iii) managing issuance of the debt instruments, iv) maintaining a debt database, v) exercising financial control over the funds obtained, vi) monitoring the financial execution of projects funded by loans, vii) keeping debt accounts, viii) preparing and implementing a debt servicing budget, ix) keeping a grants register;
- defines the process for negotiating and formalising public debt agreements, which is the responsibility of Finance, with the benefit of advice from BCH and Planning on matters within their competence;
- confirms the constitutional precept that external loans must be approved and ratified by Congress, establishing that a presidential decree needs to be issued for power of signature;
- details the process for issuing domestic debt Treasury bonds and bills, designating BCH as the financial agent of the State for placement of debt instruments and specifying that the Government may issue instruments only up to the amounts authorised annually in the Budget, with any additional issue requiring a special Congressional Decree;
- establishing that guarantees or sureties are subject to the same procedure as any other loan and prohibiting granting them to private sector individuals or legal entities.

Subsequent to the Law, Executive Decrees have regulated specific aspects, including:

- 19-93 (March 1993), creating the National Commission on Public Credit (CNCP) as the organ regulating the formulation and execution of the debt policy, consisting of Finance, Planning and BCH, and establishing a Technical Support Group (TSG) to assist the Commission by analysing and preparing debt strategies;
- 18-96 of (May 1996), which defines debt policy, establishing a minimum grant element of 35% for new debts, and a maximum percentage of 15% of national counterpart funding for external loans. It also requires that debt sustainability studies must exist before arranging each loan.

It is important to point out that when the Law was issued in 1991, Honduras was already severely indebted. By 1989, it was in default to all its bilateral and multilateral creditors and was ineligible for new finance from international financial organisations. In 1990, with the arrival of a new Administration, it commenced negotiations that achieved an IMF Standby Agreement, a Paris Club agreement and clearing arrears to multilateral creditors. This process was simultaneous with the formulation and approval of the Law, as consensus existed within Government for the need to manage debt policy more efficiently.

Clearly, the Law alone did not solve the very complex debt problems, although it did increase continuity and coherence in executing debt policy, which made it possible for Government to exercise centralised direct control over public debt, applying the same policy principles to decentralised borrowers and a common database. For example:

- the CNCP and its TSG have functioned without interruption, constituting a permanent mechanism for coordination of policies;
- the debt conversion programme, operated with the same premises and procedures under three different administrations, reducing the balance of eligible debt by 88%;
- the Public Debt Policy, established by Decree 18-96, remained in force and application;
- Honduras' inclusion in the HIPC initiative was also due to continuous coordination, from preliminary steps in 1997, through to the projected completion point in 2004.
- All actors (national and foreign) have acknowledged the lead role of Finance in this connection, allowing for greater efficiency and order in the process.

Comparing the debt situation in 1990 with that in 2002, having a set of rules for debt management, has also had positive consequences for debt indicators, as shown in Table 1. The fact of having a legal framework for formulating and executing debt policy, has made it easier for Honduras to take advantage of international debt reduction opportunities.

Government is currently revising public debt legislation as part of a consolidated public sector System of Integrated Financial Administration (SIAFI), with the following aims:

- a single coherent legal framework integrating budget, treasury and public debt systems;
- modernising certain aspects of public debt management, especially in the light of the recent guidelines by the IMF and World Bank;
- clarifying certain secondary obscure areas in the current law;
- simplifying processes and procedures to achieve more efficient management.

A draft SIAFI Law has been prepared and presented to Congress. It is still under discussion and review by congressional committees and it is therefore too early to make detailed observations. It is however important to mention that it maintains the fundamental principles established in Decree 111-90, seeking only to improve their execution.

In conclusion, the existence of specific legislation on public debt in Honduras has been highly beneficial for managing a key element of national economic and social development, and has contributed to reducing the national debt burden. However, the problem is still far from resolved and the new SIAFI law will need to be assiduously implemented to consolidate the gains already achieved.

Table 1: Honduras' Debt Indicators

Indicator	1990	1995	2001
External debt stock / GDP	118.3 %	101.0 %	65.2 %
External debt stock / Exports	318.0 %	232.2 %	170.7 %
External debt service / GDP	5.2 %	9.9 %	3.0 %
External debt service / Exports	14.0%	22.5%	7.9 %
Concessional / Total External Debt	46.6 %	55.8 %	76.0 %

FIRST REGIONAL WORKSHOP FOR TRAINING FOR TRAINERS ON DEBT STRATEGY ANALYSIS TOOLS

In line with the capacity building programme (CBP) arrangement, WAIFEM and DRI jointly organised the first regional training for trainers workshop on debt strategy analysis in Accra, Ghana during May 19-30. The workshop was intended as a key step in the transfer of responsibilities for programme execution to the WAIFEM region and its individual member states, by expanding the regional pool of trainers in debt strategy analysis who can help all countries in the region, as well as creating national training teams to conduct training activities in their own countries. It was conducted by seven regional and non-regional experts.

The objective of the workshop was to enhance the knowledge and skills of the participants in the use of debt strategy analysis and to equip them to be in a position to train others in the use of the tools in future. The methodology used during the workshop was based on the HIPC CBP methodology for regional and national debt strategy workshops. However, the participants also used the Debt Strategy Training for Trainers Guide that was developed by the CBP that includes detailed information and instructions for trainers and resource people on how to train participants in workshops.

At the initial stage, the trainees were given a comprehensive presentation of the theoretical foundations underpinning the HIPC CBP methodology; a training session on the key features of Debt-Pro©, the debt strategy analysis tool used by the IMF and the World Bank; and briefing/simulation training on preparing the workshops and organising the opening plenary sessions.

They then worked in six technical groups – External and Domestic Debt Data Specialists, External Debt Strategy Managers, Domestic Debt and New Financing Strategy Managers, External New Financing Strategy Managers, Macroeconomic Forecasting Analysts, and Poverty Reduction Programming Analysts. In each group, the participants were trained and trained one another in the various technical tasks of creating databases and generating alternative debt relief, new financing, macroeconomic and poverty reduction scenarios for 20 years under baseline, optimistic and pessimistic assumptions.

Following the technical groups, the participants were trained in how to make good presentations (and saw an example of a bad presentation to show what not to do!), and gave presentations themselves, on which they received feedback. They then received extensive training on how to enter scenarios into Debt-Pro©, to combine debt relief, new financing, macro and poverty scenarios, to produce and analyse results of scenarios, and to correct scenarios and results for errors. Finally, they were trained in how to analyse country capacity-building needs, how to train others to write a strategy report and to present it to policymakers, and in post-workshop follow-up.

Overall, the training for trainers workshop increased the capacity of a larger number of officials, empowering some of them to act as future trainers in countries of WAIFEM member central banks and beyond. The participants evaluated the workshop positively, with 92% indicating that the training received would be very useful or vital to their jobs in future.

Finally, the workshop made several important suggestions for improving future debt strategy and training for trainers workshops. On technical issues they recommended:
- specifying in more detail the data needed for the new financing analysis;
- increased effort in building capacity for macro economic forecasting and modelling, and on costing poverty reduction expenditures and projecting their impact on poverty indicators, in the constituent countries of WAIFEM; and
- greater sharing between governments and the BWIs of their assumptions underlying debt strategy, macroeconomic forecasts and poverty reduction impacts.

More generally, they recommended issuing manuals and templates to participants 2 weeks before the workshop to give keen participants a chance to prepare data and ideas; and ensuring the nomination of correct participants. They also requested more training in Debt-Pro© in a separate regional workshop.

WAIFEM TfT, May 2003, Accra, Ghana

SECOND SELF-EVALUATION SETS BENCHMARKS FOR HIPC CAPACITY

Following the establishment of a self-evaluation methodology for HIPCs to assess their own debt management capacity, the HIPC CBP partners have conducted two rounds of this process (in October 2002 and April 2003). Both were highly successful in terms of the level, quality and realism of response from countries, showing the high commitment of countries to the CBP.

The second evaluation received responses from all participating countries, and was therefore able to set benchmarks for measuring HIPC capacity and the impact of the CBP. It coincided with the Inter-regional Debt Managers Seminar, at which HIPC representatives wholeheartedly endorsed the tool as a valuable means of assessing their capacity building needs. This allowed 33 countries to analyse their initial responses to questionnaires with the CBP implementing partner organisations, in a face-to-face quality control process that made the assessments highly realistic. Almost all countries also went beyond giving themselves numerical rankings, and explained causes and potential solutions of their problems. Some countries had also prepared evaluations in national missions and workshops.

In future, the country self-evaluation will occur twice a year, once in the first quarter of the year through distribution of questionnaires to the countries and discussion at the annual Inter-regional Debt Managers Seminar; and once in the third quarter of the year as an 'update' to track any new developments. All partners are agreed that the best way to conduct the self-assessments is in a national mission or workshop, taking advantages of face to face dialogue between countries and implementing partners – and are committed to using this tool in all future CBP events.

Results

Overall, it is striking that most countries face very similar problems, due to the absence of a global and integrated vision of debt management, and to a similar negative international environment. Even though some regions and countries have a much higher level of capacity, they face the same institutional and operational weaknesses. Countries were asked to rank themselves from 1 to 5 (5 being high) in 14 categories, and reached the following conclusions:

1) Institutional and Legal Framework. This includes clear institutional and departmental responsibilities, comprehensive and high-quality laws and regulations to provide a sound debt management framework, and solid coordination mechanisms among agencies. The average rating for this category was only 2.59, making it one of the lowest-scoring categories, and reinforcing the need for phase 3 of the CBP to provide institutional and legal support.

2) Human Resources. Most countries showed some worries in this area, reflecting a considerable degree of staff turnover. The average score in this area was 3.11. Most countries mentioned budgetary difficulties and consequent low salary levels as the main cause. However, most also have a very low ratings in 'work units and procedures', 'capacity building plans' and adequacy of working environment which could be used as non-financial ways of motivating and retaining staff.

3) Management, Supervision and Working Environment averaged only 2.90. Most countries mentioned budget difficulties and consequent low salaries as the main cause for low staff motivation. However, most also rated their 'work procedures', 'capacity building plans' and 'adequacy of working environment' low, and strongly suggested that there are non-salary ways of motivating and retaining staff, such as clear definition of work procedures, the design of capacity-building and training plans, and improvement of the working environment.

4) New Financing Policy. This category averaged only 2.92 but, in contrast to some international perception, most HIPCs have clear and centralised procedures for contracting new loans. Instead, they gave the lowest scores to their ability to design and implement policy for streamlining procedures and policies of external financiers. This strongly supports the new orientation of the CBP towards supporting countries in designing such policies and preparing such negotiations.

5) Disbursement is also a back office activity but has received much less support for capacity building from the international community. As a result, its score is considerably lower at 3.19. This again justifies the emphasis which phase 3 of the CBP is placing on building capacity to accelerate disbursements of new PRSP financing.

6) –7) Recording and Servicing. These categories gained the highest scores (3.48 and 3.60 respectively), reflecting the substantial resources invested in these 'back office' areas by the international community, and the pressure placed on countries to have accurate data and make payments on time. However, few countries still lack a solid and reliable debt recording system, or consistently accrue unjustified arrears.

8) Renegotiations. Countries scored themselves relatively highly here, at 3.24. However, they acknowledged that they are still short of international data on the best terms and conditions achieved in renegotiations. As a result, the CBP is conducting a study to disseminate best practices in renegotiation procedures and results (see page 8).

9) Macroeconomic Projections. This area is crucial to medium-term debt sustainability analysis. Though CBP intervention is limited in this area, it has received some attention from donors in assisting countries to build macroeconomic models. However, countries are still crying out for assistance in more practical techniques of forecasting which assess growth prospects, and have therefore scored this area very low at 2.95, underlining the need for many other actors to provide for capacity-building support.

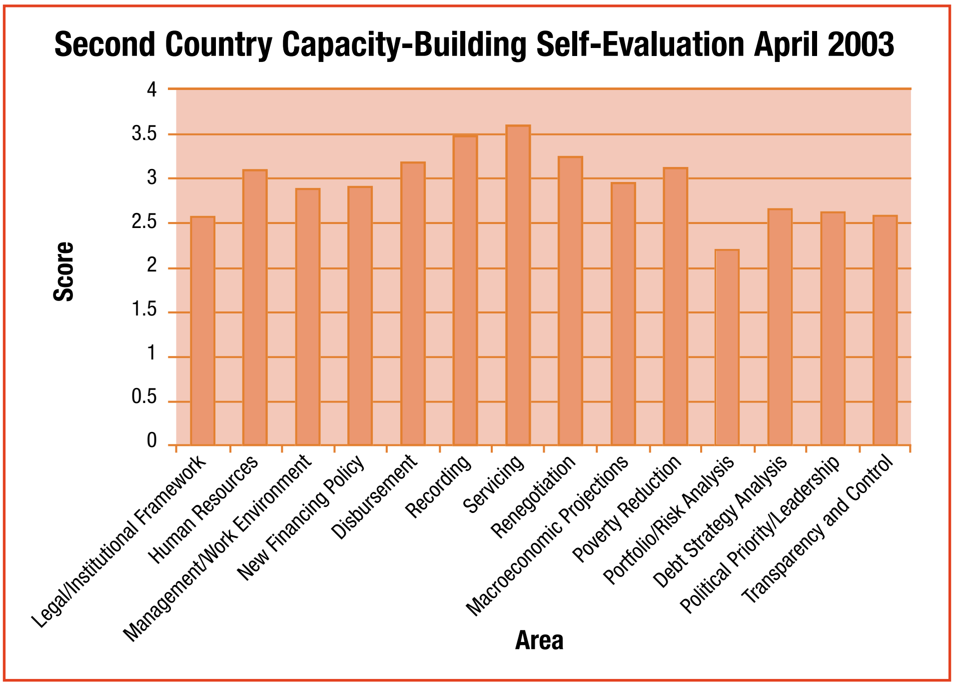
10) Poverty Reduction. The score in this area was 3.13, reflecting some progress in building country capacity as part of the PRSP process. However, while countries indicate a high level of confidence in poverty data, they still need much more support in analysing and forecasting poverty reduction (especially the poverty and social impact of macroeconomic policies, and the costs and impact of poverty reduction spending).

11) Portfolio and Risk Analysis. Countries ranked themselves relatively highly on basic portfolio analysis, but very low on risk analysis, producing an overall score of only 2.19 out of 5. This reflects the limited amount of previous capacity building in this area, but also the limited scope for HIPCs to change their portfolio composition or risk exposure and therefore the countries rated this as a lower priority for action than other areas

12) Debt Strategy Analysis. With an average of 2.66, this category is still below average. This reflects the expansion of the CBP during 2001-03 to a large number of new countries with very low capacity. More longstanding participants in the CBP have made major advances under the CBP, with very high scores for strategy formulation – the primary goal of the CBP in its first two phases - but still need more effort in the area of strategy adoption by government and successful implementation.

13) Political Priority and Leadership. This area received low marks, averaging 2.62, but with wide variations among countries. There was a clear correlation between the level of political commitment and the implementation of all debt strategy-related negotiations capacity-building programmes. As a result, phase 3 is strengthening policymaker sensitisation measures through seminars and executive fora.

14) Transparency, Evaluation and Control. This area scored only 2.59. Most of the countries need to develop more frequent and deeper interaction with civil society and other government institutions (especially Parliaments) in discussing the financing of government programs, and phase 3 is placing more stress on involving these actors.



STUDY ON DEBT RENEGOTIATIONS UNDER HIPC II

The HIPC CBP implementing partners are responding to demands from HIPCs by launching a study on the processes and results of debt renegotiations in the context of HIPC II. It aims to provide countries with as much detailed information as possible on their prospects for reducing external debt (bilateral, commercial and multilateral).

The study will contain chapters on:

- intended and actual structure and implementation of HIPC II;
- prospects for debt relief from Paris Club members;
- prospects for debt relief from non-Paris Club governments;
- possible treatment of commercial debt; and
- prospects for reduction of multilateral debt.

It will not repeat the analysis of the general process of HIPC or the overall framework for debt relief, which has already been published by the BWIs, the Paris Club or the CBP itself (in its studies of the HIPC Initiative, the Paris Club and debt conversions – for more details of these studies see our website on www.dri.org.uk).

Instead, it will focus on the details of the process, terms and conditions that are vital to ensuring that the countries receive the amount of debt reduction to which they are entitled under the HIPC framework.

To assist the study, the CBP has designed a questionnaire to send to the 36 HIPCs that are participating in the CBP. The questionnaire covers the results that countries have achieved in the HIPC context, but also allows flexibility to take into account their own initiatives to reduce their debts and the particularities of each country's debt. In this way, country successes and best practices will be available to all other HIPCs to help prepare and guide them in their negotiations so that they achieve the maximum debt reduction of their debt burdens.

The questionnaire looks in detail at the following points on multilateral and bilateral debt: i) the modalities of debt relief used by each creditor country or institution (especially the refinancing and debt service reduction used by multilateral creditors); ii) the terms (grace and maturity periods, interest and penalty interest rates, applications of conversion clauses); iii) the procedures – especially the degree of initiative taken by debtor and creditor - and duration of the renegotiations; iv) the bilateral treatment of debts outside the Paris Club framework; and v) the design of supplementary relief. On commercial debt, it will focus on the options for discounted debt reduction through buybacks, creditor participation levels, lawsuits and how countries have used strategies to avoid them. The study will also look at the role of the Bretton Woods Institutions and other actors in helping to mobilise relief.

The study will be coordinated by the Pôle-Dette, in cooperation with the other CBP implementing partners, which will make sure that all countries receive questionnaires. Each country will designate a national contact point to respond. The implementing partners will coordinate the collection of responses from their member States and add their own contributions before sending them to Pôle-Dette. Finally, partners and countries will validate the conclusions of the study before publication.

INTER-REGIONAL SEMINAR: EXCELLENT RECOMMENDATIONS FOR PHASE III

Just before the Ministerial Meeting (see article on page 2), the CBP held its first Inter-regional Debt Managers Seminar in Kigali on 24-25 April. The meeting had two main aims:

1. to present to HIPC debt managers the aims and progress of phase III of the CBP; and
2. to get their views on the proposals and their ideas on further priorities for phase III.

1) *Overall Aims and Objectives of Phase III*

The seminar began with a presentation of the overall objectives of phase III, particularly:

- further developing its focus on helping countries to design development financing strategies which go way beyond HIPC Initiative definitions of debt sustainability, particularly looking at post-HIPC new financing strategies and at domestic debt;
- ensuring that countries implement (not just design) strategies by integrating them into their budgetary processes to ensure political leadership.
- It also has as primary objectives to transfer the execution of the programme to the regional partner institutions (BEAC/BCEAO Pôle-Dette, CEMLA, MEFMI and WAIFEM), and to HIPCs themselves.

HIPC representatives agreed with the overall objectives of phase III, in particular with its goal of providing HIPCs with the independent capacity to analyse and implement debt strategies during and beyond the HIPC Initiative. Many countries indicated that they had already developed this capacity with CBP help but that it would need to be maintained after HIPC completion point, and that political commitment and integration into budget processes would be crucial. They therefore especially endorsed the inclusion of post-HIPC financing and domestic debt in the phase III terms of reference. They also stressed the need to continue to support countries which are earlier in their HIPC processes – and which could also benefit from help on domestic debt and new financing as well as the negotiation of HIPC debt relief.

HIPCs also strongly endorsed the objective of decentralisation in phase III, both in reinforcing the regional partner organisations as centres of excellence, and in decentralising to countries by providing them with resources to conduct their own training using national experts. The discussion underlined the view that, although decentralisation would reduce the costs of interventions, capacity building is a continuous process, implying the need for financial support for regional organisations and HIPC countries beyond phase III.

However, HIPCs also expressed strong concern that adequate arrangements should be made to ensure that HIPCs not belonging to a regional organisation should continue to have equal access to the benefits of intensive capacity-building after the end of 2004. About 60% of countries also felt that the timeframe (end 2004) established for the completion of the decentralisation process could prove optimistic, especially with regard to the CBP information products and its governance and advocacy structures.

2) *Information Products*

The second session focussed on the information products produced by the CBP, and the extension of its training methodology into distance learning. Participants completed detailed questionnaires on the existing CBP information products, providing many recommendations for improving them (see box).

HIPCs were also very receptive to the distance learning pilot programme, saying that it would be a key addition to the CBP methodology and much more flexible than workshops, and urging that if successful the pilot be expanded to virtually all other countries as fast as possible. However, they urged that it should complement rather than displace traditional modalities of national and regional workshops, as these had additional advantages of national team-building and national political mobilisation, and of information exchange among countries.

Newsletter

The debt managers urged the CBP to expand its newsletter distribution by 20% because they do not receive enough copies to fulfil local demand. They also suggested that it could be lengthened to give more space to technical questions, reports on the detailed results of CBP activities, analysis of the progress of the HIPC Initiative and other development financing issues, and articles by HIPC country officials.

Publications

HIPCs indicated that they found the publications they receive very useful in their daily work - especially those on Paris Club, Domestic Debt Sustainability and Implementing HIPC II. However, they had not received all the CBP publications, and not in enough copies, restricting their onward distribution within their countries. There was a need to distribute around 30% more publications to HIPCs. They also suggested publications on post-HIPC debt and new financing issues, state enterprise debt, the fiscal impact of HIPC, and of a book pulling together all the different CBP workshops and seminars.

Format of Newsletter and Publications

While around two thirds of the countries present indicated that they would be happy to receive electronic versions by email, all preferred to continue to get paper versions as well, and around a third wanted only paper versions.

Website

The website was also assessed as very useful, especially the technical resource pages for debt managers on the private site, as well as the work programme, newsletters and publications which are available on the site. They indicated that they would like more technical resources and workshop technical output reports to be placed on the site. However, only 36% of the debt managers at the workshop had visited the public site: though all of these had registered as members for the CBP closed site. Half of them indicated that this was because they had no prior knowledge of the existence of the site (although 24% had not done so due to lack of sufficient hardware or internet knowledge), and that they would like to sign up for the site. The CBP partners will therefore prioritise the dissemination of information on the website and the signing up of new members at all events during the remaining eighteen months.

3) HIPC Self-Evaluations of Debt Management Capacity

This session presented the self-evaluation methodology of the CBP, as well as explaining how it is used by the CBP implementing partners and donors to decide on their priorities for future interventions in HIPC debt management (see issue 13 for more details on the content of the methodology).

The self-evaluation methodology met with strong unanimous approval from debt managers as a means for tailoring individual CBP interventions and support at the regional and national level. Countries then used the opportunity of the workshop to finalise their own self-evaluations and to discuss them with implementing partners, improving quality control of evaluations and their usefulness to the CBP (for more details of the results, see article on page 7).

4) Domestic Debt Methodology

The fourth session presented the CBP Domestic Debt methodology, beginning with the overall methodology in the fiscal, monetary and financial sector analysis (see issue 14 for more discussion of this methodology), and then presenting the results and uses of the methodology in the WAIFEM region.

HIPC participants agreed strongly that debt strategy analysis should deepen its analysis of domestic debt, and that the CBP methodology was correct in including analysis of fiscal and monetary constraints, and of financial sector development issues. They urged that the methodology should be adapted to differing country and regional circumstances, especially the existence of common regional central banks and domestic debt markets in the CFA Franc Zone, and the dollarisation of economies in Latin America and elsewhere. Eighteen countries saw the organisation of a national domestic debt workshop as a top priority.

5) Post-HIPC Development Financing Analysis

This session presented the CBP post-HIPC development financing sustainability tools, using which HIPCs can evaluate their donors and creditors, according to a large number of criteria for assessing the quality of aid, and decide which should be the priority sources of funding for their future development programmes (for more details, see article in issue 13). After a general presentation of methodology, Ghana explained why it is so important to evaluate donors and Uganda presented the results of its national workshop (for more details, see article in issue 14).

The methodology for new financing analysis met with enthusiastic approval, as a means to select donor finance with greater concessionality, less conditionality, faster disbursements and stronger alignment with government policy priorities and PRSPs. Countries made several suggestions for refining the methodology which will be taken into account in future workshops. There was very strong demand for assistance through national workshops in this area nineteen countries considered it a top priority and through exchange of policy information at regional and interregional workshops and through publications on practical country experiences.

6) HIPC Debt Renegotiations Study

This session presented the methodology to be used for the study of HIPC debt renegotiation experiences, which is expected to improve HIPC access to information on the best results of negotiations with their creditors (for more details, see article on page 8). HIPCs looked forward impatiently to the negotiations study as a very positive contribution to the updated knowledge of financial conditions relating to debt relief. They indicated that they would be happy to participate in the study and to share details of their negotiations with other HIPCs.

7) Institutional Management Missions

The final session discussed the methodology and results of the recently introduced modality of institutional management missions. Twelve HIPCs have received such missions, with the aim of analysing their institutional structures and recommending improvements to debt management in line with international best practice. They complement earlier and current intensive assistance to 8 HIPCs through a series of missions and on-job training events to improve their institutional structures and basic debt management.

All the HIPCs present saw institutional missions as a very appropriate means to achieve a suitable environment for the Phase III shift in focus from training to permanent capacity building, and to identify intensive assistance needs for countries. They also universally identified better coordination of all government agencies involved in public debt management as a top priority for future action. All welcomed the CBP intention to produce a study on the results of these and future missions, that would be more relevant to HIPC circumstances than international guidelines based largely on experiences of more developed economies.

8) Conclusions

In a concluding session, HIPCs endorsed the above conclusions and recommendations. They indicated that the Inter-Regional Debt Managers Seminar was extremely useful to analyse progress and share experiences in implementing the HIPC CBP, and in country analysis of debt and new financing issues. They also suggested that it should be held annually for such purposes, and that it should be extended to three days in order to allow for more exchange of best practice among participants. The next inter-regional seminar, to be held early in 2004, will also have a major input into the formal review of the CBP phase III and therefore into decisions on debt strategy capacity-building support after phase III.

CBP ACTIVITIES FROM APRIL TO SEPTEMBER 2003

National Debt Strategy Workshops

Burkina Faso Post-HIPC Debt Strategy Workshop

34 Burkinabè officials and two observers from WAEMU attended this workshop, held in Ouagadougou from 31 March to 12 April 2003 and jointly organised by BCEAO/BEAC Pôle-Dette and DRI. Burkina Faso reached its completion point in April 2002, so the workshop aimed at assessing the country's post-HIPC debt sustainability.

The results confirmed that the country's post-HIPC debt would remain unsustainable, due to the shortfall of exports (mainly cotton), the inclusion of large new borrowings, and the effects of the instability in Côte d'Ivoire. The key policy recommendations of the workshop included: ensuring that Burkina Faso would negotiate the best relief terms with non-Paris Club creditors; cautioun with domestic debt, reducing risk by developing a secondary market; giving priority to the most concessional external financing; refining its external new financing strategy and building on the PRSP to streamline further donor procedures and practices.

This was also the first '2nd generation' workshop conceived by Pôle-Dette and DRI with the aim of maintaining the sustainability of public debt and finances in countries that have reached their completion point. Participants agreed that public debt and fiscal sustainability should be monitored through specific sustainability indicators as well as WAEMU's convergence criteria. See page 4 for more details.

Zambia National Debt Strategy Workshop (with MEFMI)

This workshop, held in Livingstone, from 19-29 May 2003, aimed to assist the Government to update Zambia's debt strategy analysis at Completion point, expected later this year. In addition to evaluating debt sustainability, the workshop analysis included the design and simulation of poverty reduction, new financing and domestic debt scenarios.

Following the successful MEFMI regional Training for Trainers workshop in February 2003, 6 Zambian officials took the lead in facilitating the technical groups, with guidance provided by two MEFMI staff and one DRI resource person. There were 35 participants from the Ministry of Finance and National Planning, Bank of Zambia and the key line ministries.

The updated debt strategy produced at the workshop shows that Zambia's debt is expected to be sustainable after receiving maximum relief at its Completion Point. However if Zambia's completion point is delayed beyond end-2003, then the debt service ratio will rise steeply because of substantial payments to the IMF falling due.

Regional Events

1st Inter-regional Debt Managers Seminar

Senior officials from 28 countries attended the first Inter-regional Debt Managers Seminar. See article on page 9.

WAIFEM Regional Training for Trainers (TfT) Workshop

The first TfT workshop for member States of WAIFEM, jointly organised with DRI, took place in Accra, Ghana, from 19 to 30 May 2003. More details can be found on page 6.

8th HIPC Finance Minister Meeting

The Eighth meeting of the HIPC Finance Ministers Network was held from 28-29 April, in Kigali. See page 2 for additional details.

Intensive Assistance to HIPCs

Rwanda: Debt Management Capacity Building and Advisory Project

At the request of the Government of Rwanda, an urgent mission was conducted to Kigali to assist the country in preparing a DSA before the IMF completion point mission. The second mission under the second phase of the capacity building programme for Rwanda took place from 20-27 May. The mission:

- updated and corrected the debt database;
- updated potential debt relief and new borrowing scenarios;
- assessed the potential sustainability of Rwanda's debt at completion point.

The results obtained indicated that Rwanda could expect a cancellation of a further 48% of its remaining debt at completion point. However, in light of difficulties generating macroeconomic forecasts, the mission recommended enhanced co-ordination among all structures involved in debt management to the overall success of the project.

April 2003: lunchtime for the HIPC CBP's youngest recruit!

Guinea: Debt Management Capacity Building and Advisory Project

A joint ComSec/DRI mission was conducted to Conakry from 2-13 June. The main objectives of the mission were to:

- assess the computing equipment recently acquired by the National Directorate for Debt and Public Investments;
- install Oracle and CS-DRMS;
- validate the previous debt database created in Excel and reconciled to end 2001;
- provide basic CS-DRMS training to Guinean officials;
- assist staff to start recording debt data in CS-DRMS;
- install Debt-Pro©, and provide a short introduction to its functions.

Training was provided theoretically as well as through practical exercises in groups, using Guinea's actual loan agreements. Each group then gave a presentation on their tasks, including any difficulties they faced.

The key recommendations of the mission are to:

- constitute a team to proceed with the immediate recording of all loans;
- nominate a system administrator and a CS-DRMS database administrator;
- finalise data reconciliation with creditors;
- elaborate a procedural manual for debt management; and
- prepare the next mission that will check all recorded agreements and provide additional training on CS-DRMS' advanced functionalities.

CBP Partners' Staff Attachments

WAIFEM's Debt Management Advisor

The Debt Management Advisor at WAIFEM, Sam Omoruyi, went on attachment to DRI in London from April 7–16. The purpose of the attachment was to receive training in how to coordinate regional and national debt strategy workshops, and on all aspects of the workshop methodology, and on that basis to prepare a guide for workshop coordinators as part of the training for trainers manual. During the attachment the Debt Advisor also discussed other aspects of WAIFEM-DRI cooperation under the CBP, and paid a separate visit to the Commonwealth Secretariat during which he was exposed to the modalities for applying CS-DRMS to the analysis of public domestic debt.

CEMLA's Programme Officer
Melissa Quiroz, Programme Officer at CEMLA was attached to DRI from 5-16 May. The attachment aimed to: i) assist in researching information for the CBP study on the fiscal sustainability of debt; and ii) review countries' evaluations and identify needs to improve the debt management capacity of the region's HIPCs.

The results of the attachment were: i) a matrix of historical data on the evolution of HIPCs' domestic debt; and ii) a list of the problems encountered by the region's HIPCs debt management, highlighting: a) the absence of specific laws covering debt management and, b) the shortage of debt management training plans for government officials.

The Distance Learning (DL) Final Preparations

Demand Assessment Missions (DAM) to Bolivia, Cameroon and Ghana
The purpose of the distance learning demand assessment missions was to: 1) identify the training needs of new and existing personnel at ministries of Finance, central banks and other structures involved in the preparation of debt strategies; 2) identify possible mentors and students; and finally 3) review the institutional frameworks and facilities, both computerised and administrative, according to which the programme would be developed.
The joint CEMLA/DRI mission to La Paz, from 5-9 May, interviewed possible candidates and made a provisional selection for the first group of students to be admitted at the start of the programme. Various possible candidates were also identified to co-operate as mentors in the near future. Finally, the mission registered the excellent infrastructure existing at these institutions to serve in a supportive role during the implementation of the programme. The mission extended its recommendation for Bolivia to participate in the pilot phase of the programme.
The Head of BEAC/BCEAO Pôle-Dette conducted the mission to Cameroon from 9 to 19 June. All departments were willing to provide up to 5 hours of staff time per week to allow studies to take place during working hours and to absorb local costs of distance learning, including internet and email access. Access to data and documents and the necessary technological infrastructure appeared to provide no barrier. The mission identified more than 6 potential participants. A further 3 persons would be in a position to act as mentors. One of these, Bruno Iboklene, Director of Debt Operations at the Cameroon Sinking Fund, has agreed, instead, to act as national co-ordinator. The mission recommended that Cameroon be included as the pilot country in the Pôle-Dette region
The joint WAIFEM/DRI DAM to Ghana examined the institutional framework, issues of national coordination, and potential students' access to documents and data, and to communications and computer hardware and software. The programme received a very positive response from the Ghanaian government that agreed to allow each participant six working hours a week for the programme studies. The mission found that there was sufficient demand for strengthening capacity in Ghana to warrant its inclusion in the pilot phase, and identified six potential students from the Ministry of Finance and Economic Planning, and the Bank of Ghana, as well as a national coordinator.

DL Attachments and Mentors Workshop
Mosito Khetisa (Lesotho) and Fred Matyama (Uganda) came to DRI on attachment from 26 May to 30 May, to help finalise the distance learning study materials. Mosito reviewed two data-related modules while Fred focused on the three strategy modules. As each module is designed to take 60 hours to study, the work was intensive in the four days. The materials benefited substantially from the close attention paid.
The Mentors Workshop was held from 2-5 June in Accra. This workshop, conducted simultaneously in three languages, was a new venture for the CBP, with regional experts from Cameroon, Ghana, Lesotho, Mali, Senegal, Nicaragua, Uganda and Zambia. The workshop had two aims: to discuss and agree the role of a mentor in the CBP Distance Learning Programme. The workshop was vital in highlighting the differences between the proposed mentoring role and the usual role of a consultant for the CBP. The most appreciated sessions were those that involved commenting in writing on samples of students' assignments. A further aim was to refine the study materials for the programme. The comments and suggestions are being incorporated, in preparation for the launch of the programme on 4 August.

Future activities
The CBP work programme for the next quarter is summarised below:

- a Demand Assessment Mission to Sudan;
- National Debt Strategy Workshops in Ethiopia, Mali, and Mozambique;
- Institutional Management Missions to Angola, Comoros, DR Congo, Ghana, Honduras, Mauritania and Nicaragua;
- Regional Events: CEMLA/DRI Domestic Debt Sustainability Workshop and the 2nd Pôle-Dette/DRI New Financing Workshop;
- Continuing support by Debt Advisors to Rwanda and Guinea, and a new advisor for Burundi funded by DFID;
- Participation of the HIPC CBP in the BWIs' Annual Meetings in Dubai.

TECHNICAL QUESTIONS

What are the implications of a delayed completion point for HIPC debt relief?

A number of multilateral creditors, notably the World Bank, International Monetary Fund, African Development Bank and Inter-American Development Bank, have set limits on the maximum amount of debt relief, in PV terms, that a country can receive in the interim period between HIPC decision and completion points. If a country achieves its completion point as expected, then the limits on interim relief should not have any impact. However, should a country find that it is going to take longer to reach its completion point than initially expected, then these limits can impinge on the relief a country receives.

Let's consider the example of the country that is receiving the maximum possible interim relief (in PV terms) from one of these creditors and its expected end-2003 completion point is going to be delayed by one year to end-2004. In this case, the country will have already received the maximum possible interim relief by end-2003 and in principle there is no more interim relief available to it even though its interim period has been extended. This would imply that the country might have to service its debt in full in the period between the expected and actual completion points. In practice however it is not clear if the country will have service its debt in full or if interim relief will be extended. The IBWs are currently looking into this issue.

FOREIGN PRIVATE CAPITAL CBP UPDATE

In the second quarter, Ghana completed phase 1, and Zambia neared the end of phase 1. Malawi, Tanzania, Trinidad and Tobago and Tanzania made huge progress in their phase 2 exercises. The Gambia, Kenya and Lesotho are finalising proposals for phase 2, as partners (DFI, CEMLA, MEFMI and WAIFEM) and donors finalise the overall framework.

Countries Finish Phase 1
On 14 May, ***Ghana*** disseminated comprehensive results to stakeholders and the media (see page 13). It is finalising its report, and preparing a proposal to participate in phase 2.

Zambia has obtained 83% response to its survey, overcome earlier data processing problems with help by a DFI/MEFMI mission, and plans results dissemination for September.

Support for Phase 2 Countries Continues
A DFI/MEFMI mission in March helped ***Malawi*** with awareness, training, and the launch of its phase 2 exercise. Due to good organisation and private sector cooperation, responses have already reached 56%, and data quality has improved considerably. A follow-up mission is planned for the third quarter, and Malawi hopes to disseminate results by November.

Tanzania's strong leadership has achieved rapid high response rates of over 90% on the Mainland and (in its first survey) Zanzibar. However, it is still finalising its own Oracle-based software, which has delayed data processing. As a result, the original data finalisation deadline of June has been postponed by several weeks, and DFI/MEFMI are planning a follow up mission to provide more advanced analytical training early in the third quarter, with results dissemination later in that quarter.

Trinidad & Tobago is completing its second quarterly survey of 2003, and financing local implementation costs itself. DFI is providing long-distance advice on implementation, and a DFI/CEMLA refresher-training mission is planned for the second half of 2003.

Uganda has achieved an impressive response rate of 56%, in spite of an unreliable register, thanks to improved fieldwork and media-based awareness campaigns. The team is targeting responses from 75% of companies representing 95% of investment, is pursuing large non-responding companies and checking data, and plans to disseminate results in the third quarter.

Applicants for Phase 2 Finalise Proposals
Kenya is finalising discussions with donors for the exercise to go ahead in the third quarter as an integral part of its multi-donor Statistics Strategic Plan. ***The Gambia*** has submitted a phase 2 proposal to DFI and WAIFEM for comments. This will shortly be shared with donors, allowing the phase 2 project to start in the third quarter. ***Lesotho*** is drafting a proposal to donors in consultation with DFI and MEFMI.

DFI Meets Deadlines to Broaden Methodology
In phase 2, donors have set tough deadlines to widen the capacity-building methodology to new areas, and to refine existing techniques. As a result, DFI has written new guidelines on techniques for improving company registers, for calculating Book and Market Value of PFC, and for rating up data to overcome non-response, all based on best OECD practice. It has also expanded its methodology to take more account of non-survey techniques for data collection, and to provide assistance with basic questions on sustainability of investment and corporate responsibility of investors. In addition, it has refined software to produce detailed analysis of industrial classification. All guidelines and versions of software are available on the website.

Information Products and Evaluations Move Forward
The FPC pages of the DRI/DFI ***website*** (www.dri.org.uk) are being substantially updated to include enhanced information on programme contacts, and web links on international codes and standards for monitoring foreign assets and liabilities. The draft ***Country Capacity Evaluation*** methodology (see page 15) is being commented on by countries and implementing partners.

Future Work Programme
In the next six months:

- The phase 2 framework and documentation will be finalised and circulated.
- Malawi, Tanzania, Trinidad and Tobago, and Uganda will finish their first annual phase 2 exercises, with support from follow-up missions and closing workshops.
- Three to four other countries will start phase 2 with demand assessment missions and / or opening workshops.
- Methodology on sampling, grossing up data, and sustainability analysis will be further developed.
- A software users manual will be produced.
- DFI will produce three publications on technical and institutional issues in monitoring and analysing private foreign capital, as well as analytical lessons of phase 1.
- The first country self-evaluation will take place.

GHANA: INVESTMENT PROSPECTS RECOVER AFTER 2000 FALL

Ghana has completed the first stage of its effort to build structures to monitor and analyse private foreign assets and liabilities, and foreign and local investors' perceptions of government policies, in order to improve the stability and sustainability of these flows. A National Taskforce led by the Bank of Ghana, Ghana Statistical Service, Ghana Investment Promotion Centre, and Ministry of Finance presented the results to stakeholders in Accra on 14 May, supported by DFI and WAIFEM.

The exercise has dramatically improved on previous data, which were based on investment approvals rather than actual figures. Many Government agencies, donors and international organisations are already using the findings to inform their policy formulation.

Due to political and institutional factors, the survey took almost 3 years. As a result, the FAL data refer to the years 1999-2000, which saw peculiar negative circumstances (pre-election uncertainties, deteriorating terms of trade and GDP growth, sharply rising inflation and devaluation, shortfalls in aid flows and divestiture receipts, and a collapse in foreign exchange reserves due to the hedging activities of Ashanti Goldfields). So the data show the negative effects of these factors on private flows. As the table shows, outflows (payments) substantially exceeded inflows (receipts), and the overall stock of foreign assets fell even further due to exchange rate depreciation.

Overall patterns

Private foreign investment is much more significant than previously estimated: as a share of GDP, stocks averaged 32%, compared to IMF estimates of 13.5%.

Investors favour equity finance over debt. Nevertheless, equity accounted for only 59.6% of private capital stocks at the end of 1999. Low equity stocks and flows reflect the negative factors described above, which offset very high estimated returns on investment by sector. Though equity rose to 60.6% of stock in 2000, this reflected large repayments of private sector debt by one company, which created a net outflow of private capital during 2000, and exceeded the impact of devaluation on equity stocks.

While private sector debt is only 9% of Ghana's total external debt, it represents about 33% of total debt service. This is because major sub-sectors such as mining and quarrying, communications, transport and storage, have very high debt/equity ratios.

Foreign Direct Equity Investment

FDI equity is mainly from the OECD (UK, USA, and France), with surprisingly little from non-OECD and African sources. UK investors are sectorally the most diverse. Manufacturing is the largest recipient of foreign direct equity (33%), followed by electricity, gas and water (20%), retail (14%), and finance (11%). There is a heavy regional bias, with around two thirds of FDI equity in and around the capital city.

Profits and remittances were very high, especially for finance and manufacturing. Sectors earning very high rates of return on their investment (calculated as the ratio of net profits during 2000 to the average total equity for 1999 and 2000) included construction (73%), finance (38%), agriculture (35%), and agro-industry (31%). Mining and communications incurred heavy losses, with negative returns on investment (-70% and -38% respectively). All sectors combined saw a return on investment of 15%. Very encouragingly, profitable companies reinvested 43% of their profits in Ghana (especially in utilities and retail), which was 2.5 times the amount they remitted to non-residents. Two thirds of remittances were to the largest source countries (US and UK).

Foreign Portfolio Equity Investment

Stock declined in US$ terms due to devaluation, but increased in local currency terms. Eighty per cent was from unidentified source countries, invested anonymously through fund managers, highlighting the need to conduct fund manager surveys. The UK (11%) and Libya (4%) were the main identified source countries. Investment is concentrated in mining, and hence in the Ashanti region.

Debt Finance

Ghana is highly exposed to private sector debt, mostly to sources unrelated to the borrower. Debt from related companies is mainly long-term and highly concessional, with low implicit interest rates of 3.1%, making it a very attractive source of finance in difficult times. The stronger financial positions of OECD investors and the most profitable sectors (mining, light manufacturing, machinery, and communication) allowed them to expand this type of financing in 2000, and to account for over 90% of stocks.

However, debt to unrelated companies was mainly owed by one company. This company had very high foreign exchange earnings collateral and a good international credit record until 2000 – resulting in a relatively low implicit interest rate of 8.7%. However, this company's poor financial position in 2000 led to large short-term debt repayments, reducing Ghana's exposure but also impacting negatively on the balance of payments.

Investor Perception

Data on investor perceptions were captured for 2000-2002. Since 2000, Government has promoted an enabling environment for investors, allowing free flow of profits and dividends, with comprehensive incentives, and presidential and ministerial initiatives. In addition, Ghana has benefited from a large reduction of its debt burden, as a result of qualifying for the HIPC Initiative in 2000. However, the new government has only recently begun to improve the macroeconomic environment. As a result, perceptions on macro variables were negative, but those on the general investment climate were positive, leading to very encouraging conclusions on company investment intentions.

The vast majority of domestic and foreign respondents indicated their intent to expand or maintain their investment in the next 3-4 years. Most cited a stable political and economic climate, investment and tax incentives, and the availability of educated and skilled staff as the key reasons. They also indicated an overwhelming desire to receive more information and analysis from Government to assist with their decision-making.

Conclusions

In spite of major implementation problems and delays, the survey resulted in a major improvement in historical data accuracy on private foreign capital in Ghana. It also produced findings on investor perceptions that are immediately valuable to policy formulation, notably raising the need to diversify investors' sectoral and regional focus, and to target African and Asian source countries for investment promotion.

However, future CBP activity in Ghana faces several challenges. The key factor in success will be greater ownership, coordination and financial contributions by Ghanaian institutions, emulating those of other countries participating in the CBP. Ghana will also need to improve data coverage (in the current survey only 30% of investors responded, though they account for around 85% of investment) and the timeliness of data collection (to reach GDDS standards of dissemination 6 months after the reference period). Given the high debt ratios identified above, Ghana also needs to enhance its monitoring and analysis of private external debt. Finally, given the volatility of private foreign capital in 2000, analysis of volatility and sustainability will be crucial to Ghana's development and poverty reduction strategy.

Foreign Liabilities (US$ millions)*	STOCK End-1999	TRANSACTIONS (Balance of Payments) Receipts	Payments	Valuation / Other Changes***	STOCK End-2000
Foreign Direct Investment	1,054.1	93.4	2.0	-262.8	882.7
Equity Capital	947.4	5.2	0.0	-212.7	739.9
Reinvested Earnings	23.4	24.6	0.0	-24.6	23.4
Short-term Intercompany Loans	5.4	62.0	1.4	-61.6	4.4
Long-term Intercompany Loans	77.9	1.7	0.6	36.0	115.0
Portfolio Equity Securities**	79.1	0.0	0.0	-31.1	48.0
Other Investments	630.5	63.6	219.6	-65.9	408.6
Short-term	167.4	11.3	152.0	-3.7	23.0
Long-term	463.1	52.3	67.6	-62.2	385.6
TOTAL	1,763.7	157.1	221.6	-360.0	1,339.2

*Notes: * Equity stocks are presented as market values. These generally exceeded book values, except for portfolio.*
*** Portfolio debt securities were not captured in the survey.*
**** Including effect of major exchange rate depreciation.*

ASSESSING CAPACITY TO MANAGE FOREIGN PRIVATE CAPITAL

In April 2003 DFI, regional partner organisations and donors introduced a methodology for countries to assess their management of foreign private capital (FPC). This will also help countries, regional organisations (ROs) and donors to make a comprehensive evaluation of national FPC management capacity and capacity-building needs. The methodology draws on that of the HIPC CBP (see Issue 14), and incorporates suggestions from regional organisations and donors.

1. Advantages and Risks of Self-Evaluation

Self-evaluation has the major advantage of allowing countries to make their own assessment of capacity, and then submit this to regional partner organisations and DFI, promoting country ownership. However, this raises obvious risks that countries might overestimate or underestimate their capacity. To overcome these, the evaluation system uses clearly defined, objective and measurable criteria. This is vital, as an optimistic self-assessment may mean that the international community sees no need to provide further support, and a pessimistic assessment may discourage the international community from further intervention, if past efforts have produced no improvement.

Objectively measurable criteria also facilitate consistent evaluation by different parties, ensuring that the application of the methodology by different stakeholders over the same period and for the same country should result in the same conclusions. The criteria are also consistent across countries, enabling cross-country comparisons over time.

2. Evaluation System

2.1 Evaluation Areas

The methodology assesses 12 areas to give a comprehensive picture of FPC management, going beyond the areas of FPC CBP intervention. It also acknowledges that statistical efforts in developing countries encompasses wider issues, and therefore takes account of institutional cooperation, integrated surveys and avoidance of overlap, to ensure cost-effectiveness in using scarce resources, and reduce private sector survey fatigue.

The 12 areas are:

I. Legal and institutional framework
II. Human resources
III. Management, supervision and working environment
IV. Conduct of surveys
V. Non-survey reporting mechanisms
VI. Recording and compilation
VII. Capacity to comply with international codes and standards
VIII. Basic FPC analysis
IX. Advanced FPC and corporate social responsibility analysis
X. Design of development financing strategy
XI. Political priority and leadership
XII. Transparency, evaluation and control

2.2 Evaluation Criteria

In each area of assessment, five criteria are established. These are the key attributes, which affect effectiveness and capacity. Changes in these criteria are therefore expected to reflect improved capacity. The fifth criterion, relates to outcomes. For example, the main criteria for *VIII – Basic FPC Analysis* are:

- Effectiveness of political and technical coordinating bodies/groups/task forces in generating FPC analysis
- Quality of basic analysis of broad categories – FPC (Balance of Payments, Private Sector External Debt & International Investment Position), Perceptions & Corporate Social Responsibility
- Quality of analytical linkages to and effects on other macroeconomic variables/sectors
- Quality of linking results to policy recommendations
- Outcome: Macro economic and investment promotion/facilitation policy changes

2.3. The Ranking System

For each criterion, a five-level ranking system is defined, from 1 to 5, with 5 being the highest, reaching ideal international standards. For example, for the criterion *Quality of analytical linkages to and effects on other macroeconomic variables/sectors* under the area Basic FPC Analysis, the following ranking system is defined:

1 = Very poor – only data are reported
2 = Poor – analysis covers a few linkages and effects (e.g. with the real sector)
3 = Adequate – analysis covers most major linkages/effects (e.g. real, fiscal, monetary)
4 = Good – analysis covers all major linkages and effects
5 = Excellent – analysis focuses on all applicable national priorities

An average is then made of the scores for the five criteria for each area to determine the rank for each area. The closer to 5, the closer the country is to ideal international standard. For example, the ranks for the criteria in area VIII might be as follows:

VIII – Basic FPC Analysis	3.2
Effectiveness of political/technical coordinating bodies in generating FPC Analysis	4
Quality of basic analysis of broad categories – FPC (BoP, PSED & IIP), Perceptions & CSR	4
Quality of analytical linkages to and effects on other macroeconomic variables/sectors	3
Quality of linking results to policy recommendations	2
Outcome: Macro economic and investment promotion & facilitation policy changes	3

Once individual scores are established for each area, an average of the scores in the 12 areas is calculated to assess the country's overall capacity to manage FPC.

3. Other Features of the Evaluation

- It focuses on impacts and outcomes, not activities or outputs: for example the ability to generate more comprehensive and consistent BoP statistics on a timelier basis.
- All areas are evaluated net of external technical assistance. For example, the ability of the country to establish a comprehensive sampling framework should be assessed before external consultants recommend additional sample sources.
- The evaluation asks countries to assign a priority for each criterion and each area ranging from low to high, depending on the scale of FPC management problems in this area and the benefits expected from acting to improve capacity.
- It also asks countries to define gaps in capacity, causes of these gaps and recommended solutions.

4. Applying the Methodology

Various institutions and departments are involved in FPC management. For example, the Statistics Bureau may be responsible for data gathering and compilation, the Central Bank and Finance Ministry for analysis, and the Investment Board for investment promotion. It is thus impossible for one unit or department to complete the evaluation and we recommend that a country team be responsible. For the countries included in the FPC CBP, the National Task Force would be the logical body to do this work.

Results should be submitted to a senior policymaker from one key institution for approval, before sending to the FPC CBP implementing partners for quality control, compilation and presentation to donors. Overall scores for each country, and an overall analysis of the results will be presented at the FPC CBP Steering Committee meetings in May and November each year (more detailed aspects will not be disseminated to avoid potential input into conditionalities by the Bretton Woods Institutions). These will be used to evaluate progress, provide input and to mobilize political, technical and financial support for capacity-building actions in phase II countries.

5. Next Steps

After incorporating country comments, the first round of evaluations will be completed for presentation to the November 2003 Steering Committee meeting.

FOREIGN PRIVATE CAPITAL: FREQUENTLY ASKED QUESTIONS

HOW TO ESTIMATE MARKET VALUES OF EQUITY CAPITAL?

In Newsletter 15, we concluded that book value (BV) is a starting point in estimating the value of an enterprise – but that it has limited analytical use, as it reflects historical values. Better methods are needed to assess the value of equity in an economy. This article covers the concept and importance of market value (MV), and experiences and best practices in its estimation relevant for developing countries. An expanded version will be made available on the DFI website and in all FPC CBP events.

Definition and Analytical Uses

The IMF Balance of Payments Manual 5th Edition defines a market price as the amount that a willing buyer pays to buy something from a willing seller, based on commercial considerations. The UN *System of National Accounts* also recommends MV as the most relevant way to measure value of resources, especially for developing countries experiencing inflation, which widens the gap between MV and BV.

Worldwide, governments, companies, lenders, risk analysts and credit rating agencies use MV for economy-wide and sectoral analyses, including balance sheet and wealth studies. MV allows an objective comparison of non-financial with financial liabilities, liabilities with assets, yields on investments with those of other investors; and risk exposure or net international investment positions. MV also provides a measurement of globalisation, assisting analysis for trade & investment negotiations and strategic business planning.

Practical Difficulties

However, MV can be extremely difficult to calculate. It assumes that stocks are regularly revalued in enterprise balance sheets due to national accounting standards. But this is not the case in most countries, because the data needed to establish a market price may be absent, requiring the use of proxies.

Recognizing some of the above difficulties, the IMF and OECD surveyed their member countries in 1997, to determine current practices. The results showed that only 30% of countries used MV as the basis for their statistical reporting. For this reason, the IMF, OECD and DFI recommend that where (frequently) MV is derived indirectly and differs from BV, both should be reported.

Country Best Practices

In this context, how should countries estimate MV?

The US and Australia are examples of best OECD practice. The US Bureau for Economic Analysis (BEA) is one of the leading institutions in valuation methodology, but its methodology is highly complex and at the same time very aggregated. It uses 3 methods to measure FDI, based on historical cost (i.e. BV); current cost (revaluing balance sheets tangible assets objectively using complex formulas); and market value (revaluing all balance sheet liabilities).

The Australian Bureau of Statistics (ABS) experience in valuing FDI stocks is more practical and workable for most developing countries. However, it is important to note that they have managed to use MV largely because accounting standards have required enterprises to revalue balance sheets at least annually to current costs.

- **For incorporated enterprises which are listed on stock exchanges,** the market value of equity should be reported using a *recent transaction share price*. If unavailable, respondents should use the midpoint of the quoted buy and sell prices of the shares on their main *stock exchange* at the reference date, multiplied by the number of issued shares held by foreign direct investors.
- **For unlisted incorporated enterprises**, survey respondents are requested (in order of preference) to value their shares using *a recent equity transactions price*; or *director's valuations*; or the *net asset value* (the value of an enterprise's total assets including intangibles less non-equity liabilities and less the paid up value of non-voting shares) at current cost.
- **For unincorporated enterprises** (branches), the ABS requires *NAV*, but encourages respondents to value underlying assets at current market values.

African country experience may be even more relevant:

- the Bank of Namibia (BoN) has been estimating MV since 1991. It uses the 1st method above for listed companies, and the 3rd for branches, but relies on *auditor's estimates* to estimate MV for respondents of unlisted companies, because company auditors have intimate knowledge of the enterprises and the financial estimation techniques necessary (e.g. replacement cost, discounted models of earnings) to calculate MV. Some very large companies also undertook special internal current cost revaluation studies for the BoN.
- FPC CBP phase I country teams have found that many companies simply equate MV to BV, requiring intensive follow-ups by enumerators to get more accurate MV data. They have therefore used pragmatic IMF/ABS/BoN methods to revalue company responses, especially stock exchange prices and NAVs. Unfortunately, accounting standards in most low-income countries are weak, and therefore auditor's MV calculations are too expensive and thus impractical. In addition, stock exchanges are very small and have few recent transactions. Given major disputes over the accuracy of even the US BEA method of balance sheet revaluations, countries generally did not use this technique. Furthermore, *valuation by analogy* – comparing with a trade for a similar sized company sharing the same characteristics – was tried successfully to a limited extent, constrained by available information on competitors. However, there is potential for further application for this proxy, using publicly available financial statements and other sources
- However, for management purposes in medium-to-large enterprises, balance sheets are often internally available on a current cost accounting basis, enabling managing directors or financial managers to provide MVs. Where this was not the case, respondents preferred to ask accountants to give NAVs.

MV/BV Ratios

It is not possible to use standardised MV/BV ratios to calculate MV, because the factors influencing such ratios are so volatile (due to volatile profitability of different sectors and stock exchanges). The US BEA MV/BV ratio for inwards FDI peaked at 2.9 in 1999, before the correction in world stock markets lowered the ratio to 1.9. Research in the United Kingdom (which currently uses NAV) estimated MV/BV at 2.1. The ratios for FPC CBP phase 1 countries ranged from 1.4 in Uganda to 1.8 in The Gambia and Malawi. In stark contrast, BON finds a ratio of 5.6, due to very large and profitable mining and wholesale & retail enterprises.

Conclusions

The country estimates in phase 1 of the FPC CBP are already a major step towards the 'true value' of investments. They use current best international practices to make pragmatic MV estimations as follows:

- **For listed incorporated enterprises:**
  - a *recent equity transaction price*, or if unavailable
  - the *listed price* as quoted on the stock exchange.
- **For unlisted incorporated enterprises:**
  - value shares at MV if available, otherwise
  - a *recent equity transactions price;*
  - *auditor's valuation,*
  - *managing/other director, financial manager or accountant's valuation,*
  - *valuation by analogy,* or
  - *NAV at current cost.*
- **For unincorporated enterprises (branches):**
  - Value the equivalent of shares at MV or NAV at current cost.

Newsletter 17 will continue this theme, by describing the methods countries in the FPC CBP have adopted to improve the quality of MV data supplied by the private sector.

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