STRATEGIES FOR FINANCING DEVELOPMENT

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IRWS 4 SETS GOALS FOR PHASE 4

The fourth Inter-Regional Workshop was held from 8-10 May in Addis Ababa, and attended by debt and aid managers from 36 HIPCs. Its main objectives were to:

- ***inform HIPCs about the methods for managing the phase 4 of the HIPC CBP.***
- ***allow HIPCs to set goals for phase 4, including new capacity self-assessments and National Capacity Building Plans.***
- ***exchange experiences in negotiating debt relief and mobilizing new financing***
- ***exchange information on best practices in institutional and legal reforms.***

Capacity Building in Phase 4
The first session presented the phase 4 objectives including: 1) implementing national strategies to assure long term sustainability and avoid future debt crises, 2) building sustainable capacity in HIPCs, 3) defining capacity-building targets for each country, and 4) transferring management responsibilities to Regional Organisations and HIPCs. The resulting discussion showed the need for HIPCs to: 1) formally approve and implement strategies, 2) design capacity building plans to have sustainable debt and aid management capacity, 3) agree realistic capacity-building targets for the end of the phase, and 4) play a greater role in managing the CBP, including co-financing the programme.

The second session allowed HIPCs to analyse the new CBP capacity self-evaluation questionnaire, which was revised to fit the targets for phase 4, and to include more detail on external debt, domestic debt, new financing and capacity building. After discussing the questionnaire in a plenary session, HIPCs defined the baseline scores which describe the present situation in each country. They also analysed the differences between the phase 3 and phase 4 self-assessment scores, mainly reflecting the phase 4 emphasis on whether HIPCs are approving and implementing strategies. It was agreed that final baselines and targets would be validated by national authorities, and be presented to the CBP Steering Committee meeting of November 2006.

The third session provided the opportunity for HIPCs to define national Strategic Plans, including detailed and realistic targets for each country and the activities needed to reach them, risks and mitigation strategies, and possible sources of financial or in-kind contributions at the national level. The resulting Strategic Plans will serve as guide for all PIP activities for Phase 4.

The fourth session focused on the Phase 4 requirement that all HIPCs design National Capacity Building Plans (NCBPs). The objective of these plans is to define capacity building needs for individuals, units and agencies dealing with debt management, to serve as guidelines for PIPs and other capacity building organisations' activities. They will also contribute to programme sustainability and ensure HIPC ownership. A plenary session reviewed the guidelines and format to design the NCBPs. Thereafter, HIPCs and ROs defined the information and reports to be used for compiling NCBPs, the timing of the exercise, and how to coordinate with other organisations training programmes.

Debt Relief, New Financing and Laws/Institutions
The next three sessions of the workshop exchanged information about best practices in negotiating debt relief, mobilising better-quality new financing, and reinforcing the institutional and legal framework for debt management.

The first session dealt with progress in negotiating debt relief. It included the definition of new HIPCs, and the details of the Multilateral Debt Relief Initiative (MDRI) and how it is being implemented in the different HIPCs. In the subsequent discussion, countries shared their experience with lawsuits by creditors and the anti-lawsuit assistance available for HIPCs such as A4ID (see page 16). They also presented their difficulties getting Paris Club and Non-Paris Club creditors to provide relief, with interpreting the impact of MDRI relief on their budgets and net aid flows to their countries, and with extending the MDRI relief to Latin America (via the Caribbean Development Bank and the Inter-American Development Bank).

The second session dealt with recent developments in aid policy and strategy, including the latest developments in implementing the Paris Declaration on aid effectiveness, the lack of progress in establishing systems for mutual accountability between developing countries and donors-lenders, and analysis of countries' best practice in evaluating aid quality and effectiveness, and in designing and implementing aid management strategies. Countries then discussed their experiences of aid falling short of pledges, and their efforts to evaluate aid, and to design and implement aid management strategies. They urged the CBP to integrate aid and debt management analysis to ensure that debt remains sustainable after HIPC, to incorporate Paris Declaration criteria into CBP methodology, and to develop a compendium of donor practices to assist their formulation of strategies. Above all, they stressed that aid effectiveness will improve only if countries develop their own capacities to lead the process, and urged the CBP to play a leading role in this.

The last session provided an opportunity for HIPCs to discuss best institutional and legal practices for debt management. PIPs presented the conclusions of a CBP study on best institutional and legal practices, followed by interventions by Burkina Faso on coordination and Nicaragua on its debt law. The conclusions of this session were that countries needed to have 1) effective coordination structures integrating debt and aid management, macroeconomic policy and MDG spending needs; 2) lead agencies or coordination structures which implement debt and aid management policies; 3) technical teams to conduct supporting "middle-office" analysis and prepare annual government financing policy documents; 4) political procedures to ensure such policies are included in the annual budget; and 5) manuals defining procedures and roles for implementing policies and ensuring adequate exchange of information among different units.

At the end of the workshop, HIPCs expressed their strong support for the CBP, including its continued adaptation of its methodology to their needs. They committed themselves to meeting the capacity-building targets and financial commitments, and to implementing the institutional and legal reforms required of them. They also urged the CBP to focus increasingly in phase 4 on ensuring debt sustainability after HIPC completion point by helping countries to analyse, adopt and implement new external and domestic development financing policies.

RWANDA ADOPTS NEW GOVERNMENT FINANCING STRATEGY

On 10 August Rwanda finalised its new government financing strategy, by adopting the recommendations of an Aid and Debt Strategy Workshop held from 31 July. The workshop, facilitated by DRI and MEFMI, involved 30 government officials, and was funded by MINECOFIN and the HIPC CBP. Its purpose was to identify how to finance Rwanda's development strategy and Long-Term Investment Programme (LTIP), by

1. designing external and domestic debt relief and new borrowing strategies, to feed into the 2007 budget and the 2007-09 MTEF.
2. enhancing implementation of GOR aid policy by analysing donor alignment with this policy and the potential impact of increased alignment
3. producing a compendium of donor policies and procedures, to serve as a guide for mobilizing the best quality resources from the international community; and
4. finalising a capacity-building plan for ensuring that the recommendations of the workshop can be fully implemented, and therefore that the LTIP can be financed.

RESULTS AND POLICY RECOMMENDATIONS

External Debt

The LTIP, which aims to reach US$900 per capita GDP by 2020, could be financed without compromising debt sustainability, as judged using the IMF-World Bank Long-Term Debt Sustainability Framework. Assuming realistic debt relief (ie that not all creditors participate in HIPC), Rwanda would have a peak PV/export ratio of 123% in 2012, compared to its LTDS benchmark of 150%, and all other ratios are sustainable.

The Multilateral Debt Relief Initiative (MDRI) will produce i) a dramatic fall in debt ratios, followed by a switch of AfDF and IDA funding back to loans and ii) a partial offsetting of the debt service reduction provided by MDRI (averaging US$10 million a year for the next three years) by reduction in future AfDF/IDA disbursements.

To maintain debt sustainability, Rwanda will need to keep borrowing down by ensuring that 75-80% of aid continues to be grants, implying a major increase in bilateral grants. It will therefore adopt a borrowing ceiling averaging US$100 million a year for 2007-09 allowing maximum disbursements while keeping debt sustainable. It has also decided to maintain the current minimum grant element of 50% in new borrowing for the next 3 years. This will not reduce Rwanda's access to aid significantly, as virtually all lenders provide this grant element.

New External Financing

Sustainable LTIP financing will also involve increasing aid from US$400 million to US$600 million by 2008, which is compatible with donor pledges to double aid to Africa by 2010. It will also need a dramatic improvement in the effectiveness and absorption of aid, given that Rwanda already has a large pipeline of undisbursed aid due to slow project execution. Donor and creditor alignment with Rwanda's aid policy (as well as their compliance with the Paris Declaration aid effectiveness indicators) varies dramatically. It will be vital to enhance each donor's alignment, focus GOR efforts to increase aid on the most aligned development partners, and diversify its donor base. The workshop also agreed ways in which government can improve its own procurement, financial management and monitoring and evaluation procedures.

At a more macro-economic level, it will be vital to conduct a full analysis of the impact on the economy of scaling up aid flows, and of the balance between investment and recurrent spending, in order to assess any risks of Dutch Disease, and to ensure maximum spending and absorption of the aid without negative impact on macroeconomic stability.

Domestic Debt

The workshop analysed scenarios for restructuring government's debt to the *Caisse sociale du Rwanda* (CSR), and found that the current proposal (issuing bonds with multiple maturity dates) is the best solution for both parties. It also tested various scenarios for future issuance of domestic debt, and recommended that:

- domestic debt should not be used to finance the LTIP, except in the event of temporary liquidity shortfalls (for example in donor aid).
- the primary focus of domestic debt issuance should be to develop financial markets. This will imply issuing small amounts of longer-term securities to promote longer-term savings and investment, moving gradually to 10-year bonds.
- to facilitate financial market development, it will be important to diversify financial institutions vigorously, through leasing, venture capital and micro-financing.

Macro-Economic Policy

Financing the LTIP sustainably will also involve accelerated implementation of policies to increase revenue collection and export earnings, in part through a strategy of private sector promotion. It will be necessary by 2020 to raise the revenue/GDP ratio from 14.5% to 18%, and the export/GDP ratio from 13.4% to 15%. Such increases should be possible if revenue collection rises with higher income and growing formalization of the economy, and if efforts to promote higher value-added in exports are pursued vigorously.

LTIP and Poverty Reduction Spending

The LTIP involves an ambitious scaling up in investment spending. Such expenditures need to be very carefully prioritised according to their impact on the intended results indicators for development and the MDGs, as well as complemented by full analysis of recurrent expenditures necessary to maintain the investments (through the programme budgeting and the MTEF process). Such analysis will need to be disaggregated by district to take account of the decentralization process. These steps will occur during the preparation of the 2007 budget and Statement of Priorities, the 2007-09 MTEF, and the Economic Development and Poverty Reduction Strategy (EDPRS).

CAPACITY-BUILDING NEEDS

The workshop also made a large number of recommendations for reinforcing the institutional and legal framework for debt and aid management, notably:

- creating a Government Financing Policy Implementation Committee to assist government to make the right financing decisions; and
- ensuring that budget debates include discussion of Government Financing progress.
- a wide range of technical training and support needs on debt, aid, macro-economic and anti-poverty spending issues.

Overall, Rwanda could finance its LTIP with a major effort from both government and the international community, without compromising debt sustainability. This will include a major increase in grants, as well as a large budget revenue and export earnings effort, and an improvement in the effectiveness and absorption of aid.

NEW NATIONAL WORKSHOPS ON DEBT STRATEGY AND NEW FINANCING

CEMLA's Work Program for 2006 provides for four National Workshops: Nicaragua (March), Honduras (June), Bolivia (October - co-financed by GTZ) and Guyana (December). These Workshops were designed taking into account countries' Post-HIPC situation after reaching the Completion Point. Therefore, it places a greater emphasis on new financing and poverty reduction as the means to comply with the Millennium Goals, without leaving aside the need for including debt relief as part of the strategy as well.

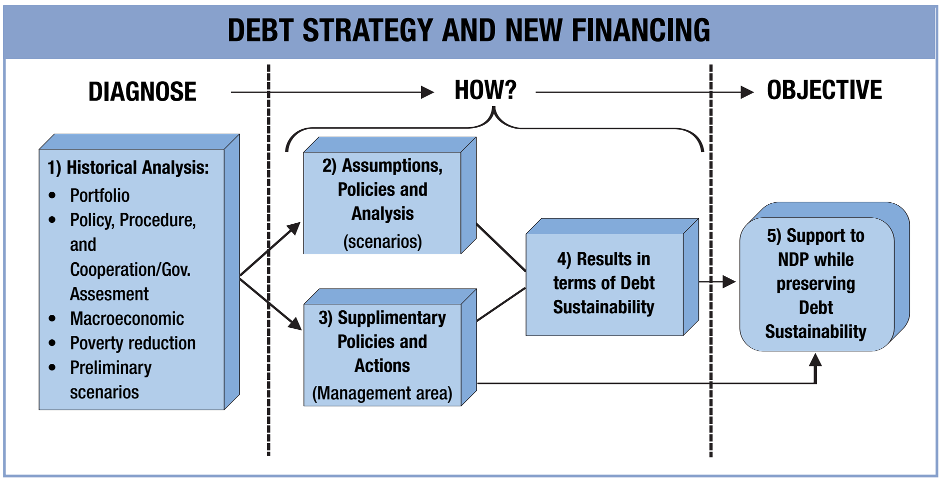
In accordance with the new context and thanks to the flexibility of the PFC methodology, CEMLA has redefined in general terms this type of events so as to provide for elements supporting the implementation of more effective policies, without disregarding capacity development. Thus, it will be ensured that, for example, debt strategies and new financing will serve to reach the specific goals of national development plans (NDPs) or poverty reduction strategies as designed by the countries themselves. Consequently, the Program explicitly includes one of the design guidelines of its work plan that relates to the level of commitment, ownership and leadership that member countries expect to achieve by reducing their dependence from external technical assistance.

The countries in the region have made significant progress towards the design of new NDPs, not only to address the social sector but also the production sector through the promotion of economic growth. Nevertheless, such efforts need to be better supplemented by reviewing financing requirements, identifying what areas could be possibly financed, or the actions that should be implemented to obtain the necessary additional financing for attaining the goals provided for in the plans, which not only involve quantitative issues but, above all, the form (quality) of financing.

The development of the above mentioned events may be graphically expressed in the chart below:

Box 1 shows the need for counting on every available and recent information from all working groups (External and Domestic Debt, New Financing, Macroeconomic issues and Poverty Reduction), as well as on the relevant historical analysis (e.g. Financing Portfolio, Macroeconomic Situation, etc.) A key aspect in the preparatory stage is the assessment of policies and procedures implemented by both donors and creditors, and the government; these, together with financing amounts, are the foundations for designing a new strategy and future financing policies.

Box 2 refers to assumptions, treatment, and policies underlying the various scenarios of each group, while Box 3 reflects supplementary actions to be taken for NDP implementation (e.g. measures aimed to increasing project implementation capability and improving the legal framework and financing coordination.)



Box 4 shows the need for counting on a combined scenario which, besides including NDP and financing strategy requirements (amounts and quality), should also provide for public debt sustainability. Thus, financing strategy becomes an instrument supporting the Plan implementation (Box 5).

The above makes it clear that Debt Sustainability Analysis is not an end in itself but a tool that helps to define the best possible financing combination which, besides meeting NDP requirements, may also reflect into a sustainable debt. Consequently, this exercise starts with NDP pricing or the attainment of the Millennium Goals and the analysis focuses on the financing strategy.

Methodological Characteristics of National Workshops

The new outline of National Workshops requires an accurate definition of previous preparatory works, their contents, and policy messages to be included in the reports. These events will develop as per the following stages:

- The preparation stage is most important to reach the objectives provided for and mainly involve the review of available information for strategy design, database checking, and the design of possible scenarios. Additionally, the costs to be afforded by the country for NDP implementation should be established with a long-term approach.
- The workshop development consists of the presentation of government perspectives for the purpose of conveying to the participants their approach and expected results, the review and analysis of the scenarios proposed during the preparation stage, and the outcome analysis and report drafting. The workshop should achieve a financing strategy consistent with NDPs, the restrictions of international cooperation, and long-term debt sustainability.
- The final report will be revised by a small group responsible for refining this document prior to its submission to government officials. One important aspect consists of adjusting the document according to its purpose, e.g. using the applicable terminology in compliance with the country legal framework or with the presentation of financing requests to donors/creditors.

REFERENCE FRAMEWORK FOR PUBLIC DEBT POLICY

PÔLE-DETTE

In April 2006, the Regional Debt Management Training Unit for Central Africa and Western Africa (Pôle-Dette) undertook preparation of a reference framework for public debt policies in the franc area countries. This initiative is one of the major recommendations of the institutional support missions that DRI and Pôle-Dette have organised since 2002 in virtually all countries of the region, to encourage adoption of laws on public debt policy that meet international standards. The initiative undertaken by Pôle-Dette targets a legal community text (règlement) to serve as a reference framework for preparation of national texts. We must answer two questions in order to understand this initiative.

I - WHY A COMMUNITY LEGAL TEXT?

This approach is explained primarily by the many factors the franc area countries have in common. They are members of two monetary unions (the Central African Economic and Monetary Community-CEMAC and the West African Economic and Monetary Union-WAEMU), which, since the 1990s, have undertaken to strengthen their economic, monetary, and financial integration. This situation has led to more uniform legislation in the monetary and financial areas. This convergence, attributable primarily to the fact that the franc area countries have a common currency (the CFA franc-CFAF) issued by the Central Bank of West African States (BCEAO) and the Bank of Central African States (BEAC) has promoted integration of national monetary, banking, and financial systems. It has also led to the existence of uniform legislation in the areas of banking, the financial system, foreign exchange, government paper issues, and certain aspects of fiscal management.

Accordingly, the adoption of a community legal text in the area of public debt is consistent with the aim of strengthening economic and financial integration in the franc area. Further, the adoption of a community text has the advantages of being expeditious and avoiding discrepancies between the national texts.

II - HOW WILL THE COMMUNITY FRAME OF REFERENCE AND THE NATIONAL LEGISLATION BE LINKED?

A community *Règlement* will be adopted for each of the two monetary unions, one for the CEMAC and another for the WAEMU. The content of these two *Règlements* will be identical and will not rule out the adoption of specific texts for each member country. The national texts, however, must in all cases be consistent with the provisions of the community text. It is also provided that the national texts (laws, decrees, and other regulations) will give top priority to the community reference framework in their preamble.

In this connection, the community *Règlement* will primarily aim to allow the internalization of international public debt management standards through:

- The uniform definition of the scope of public debt policy, that will apply to domestic and foreign borrowing arranged directly by the state or by decentralized units of the state, or guaranteed by the state or its decentralized units;

- The obligation to establish national public debt policies: each member country will be required to implement a public debt policy establishing the general guidelines in the area of public borrowing and public debt management. These guidelines will determine a strategy to ensure that the level and rate of growth in debt will be sustainable, that public debt service will be paid on a regular basis, and that the state's cost and risk objectives will be attained. In addition, national public debt strategies will be enshrined in a document appended to the budget law, and will comprise minimum indications such as the justification of borrowing, debt and guarantee ceilings, portfolio structure and indicative terms for new borrowing, as well as the public debt sustainability profile for the next 15 years;

- The obligation for states to define and observe the competence of administrations and agencies involved in the formulation, implementation, and monitoring of public debt policy to avoid overlapping of tasks and conflicts of authority; and to implement a manual of procedures covering public debt management functions and activities;

- The obligation for states to take the necessary steps to guarantee transparency in the public debt process, and to ensure availability, accessibility, quality, and safeguarding of data and information involving public debt, and to subject the agencies responsible for public debt management or for the use of resources deriving from public borrowing to independent audits;

- The obligation for states to implement a structure to coordinate public debt policy with monetary and fiscal policies, under conditions (terms of reference and composition) provided by the community text *(Règlement)*;

- The obligation for member countries to designate a single authority competent to conduct negotiations and to sign borrowing conventions and any other agreements related to state debt and guarantee conventions issued by the state to its decentralized units or to third parties. The *Règlement* will also require states to abstain from guaranteeing loans at conditions more onerous than their own borrowing.

The national legislation will aim primarily to establish these obligations in each member country, primarily through internalization of the provisions of the community *Règlement*, while specifying in each country the modalities to define the competence and responsibilities in the debt chain, and specific provisions regarding transparency in the process and public debt reporting. The national texts will also organize the structure for coordination, designate the single authority competent in the area of public borrowing and state guarantees, as well as the conditions under which the agencies responsible for debt management and the use of resources deriving from public borrowing will be subject to independent audits.

HIPC CBP DOMESTIC DEBT WORKSHOP FINDINGS

In the MEFMI region, the necessity to include domestic public debt in overall debt strategy analysis cannot be over emphasized. This is for three reasons:

1) The standard debt sustainability analyses that have been conducted under the HIPC Initiative do not take into account the overall budget financing constraint, and the effects of fiscal and monetary adjustments on domestic debt issuance needs.
2) The switch from foreign to domestic borrowing experienced in a number of HIPCs, especially as they graduate from the HIPC Initiative, could undermine overall debt sustainability and limit the benefits countries get from external debt relief programmes. Mounting domestic indebtedness in MEFMI member countries is becoming a great concern. It results from shortfalls in external aid, IMF programme restrictions preventing borrowing externally on commercial terms, and prohibitions on financing deficits by monetary means - pushing them to rely more on domestic borrowing.
3) Most MEFMI HIPC member states need to design a domestic debt issuance strategy which ensures long-term financial sector development and enhanced domestic savings and investment.

Moreover, past evaluations have indicated lack of capacity in the MEFMI HIPCs to design domestic debt strategies. Against this background, MEFMI organized a regional workshop targeting policy analysts in the Ministries of Finance and Central Banks of HIPC member countries. The workshop was designed to provide comprehensive training to participating officials in the analysis of domestic debt strategy, and to establish sustainable Government teams capable of updating domestic and total debt strategy analysis regularly, for the foreseeable future, and with minimal external assistance.

Policy Issues Arising from the Workshop.
Experience from the field indicates that there exist tensions and challenges in managing public domestic debt in the context of broader macroeconomic management, including fiscal and monetary policy operations. The most important are:

- to achieve fiscal stabilisation, what would be the level of fiscal deficit that can be financed sustainably, with the aim of spending sufficient amounts to reach the MDGs, without foreign financing, and what should be the level of reliance on domestic debt ?
- how can countries reconcile the objective of eliminating excess liquidity to lower inflation, with the objective of financial sector development and development which requires increase in M2/GDP and NCE/GDP ratios ?

Participating countries concluded that these issues were essential components of their future national development and that domestic debt strategy analysis would be crucial to pursue in the MEFMI region.

Capacity-Building Issues
The major successes of the workshop were:

- training on domestic debt data recording for strategy purposes and its transfer from Excel to Debt-Pro format, as well as training on producing and interpreting overall total debt sustainability results.
- in addition, the technical working groups during the workshop enabled participants to rigorously go through the practical challenges to conduct domestic debt strategy analysis in their respective countries.
- The working groups and plenary sessions also provided an effective opportunity for the exchange of practical experiences and useful lessons for the participants.
- The capacity-building sessions allowed each country to assess its capacity to do a total debt DSA by examining the prerequisites, and to develop a capacity building plan.

On the other hand, the workshop faced three main challenges:

- The working groups tasked to do technical analysis of the fiscal, financial and monetary forecasting, did not perform to expectations reflecting weaknesses in the understanding of the linkages among these sectors. This calls for targeted training of the relevant staff so as to empower them with the appropriate skills and knowledge.
- the failure of member states to nominate participants with sufficient technical skills to meet the required criteria for constituting national technical teams after the workshop. This implies that countries may not be able to undertake their own Domestic Debt Strategy Analyses, or to provide regional experts to assist other countries in this area.
- the data used for the case study exercises during the workshop had some inconsistencies, which meant that participants had to spend considerable time improving data quality during the workshop.

Next Steps
Participating countries and implementing partners came up with a number of recommendations to ensure that they adopt sustainable domestic debt strategies:

- HIPC governments need to ensure the appropriate participants are nominated to attend training events.
- domestic debt sustainability analysis needs to be included in national workshops so as to ensure that capacity is transferred to the maximum number of qualified staff
- all participating countries need to enhance skills to handle specific technical areas, especially the fiscal, monetary, and financial sectors.
- the Debt Pro analytical tool needs to be installed in a wider range of offices, and staff made aware of its usefulness, by improving information flow and coordination
- after training workshops, participants need to be incorporated into national teams to implement the debt strategy methodologies transmitted by the CBP. This calls for follow-ups by implementing partners to ensure that the capacity to manage public domestic debt built during workshops is sustained thereafter.
- after training, staff should train their colleagues in house so as to spread the skills. This would help in facilitating implementation of best practices in the respective countries.
- governments need to maximize staff retention and remuneration packages to ensure that retention of experts is maintained at sustained levels. Participants decried civil service practices of transferring staff without considering the contributions they make in specific areas, which greatly undermines the capacity building efforts.

MEFMI and DRI will be focussing their future capacity-building efforts in these areas in order to ensure that domestic debt not only remains sustainable but makes the maximum contribution to national development in the HIPC member states.

GHANA NEW FINANCING STRATEGY ANALYSIS WORKSHOP

Following Ghana's achievement in reaching the HIPC completion point, and receiving relief under the multilateral debt relief initiative (MDRI), WAIFEM and DRI organized a National New Financing Strategy Workshop from July 3-14 in Accra. Six national experts and three regional and international consultants facilitated the workshop. Participants comprised officials from the Ministry of Finance and Planning, Bank of Ghana, Controller and Accountant General's Department, National Development Planning Commission, Ministries of Education, Health, Transport, Energy, Local Government, Rural Development and Environment, and other MDAs.

The workshop provided comprehensive training to the Ghanaian officials in analysing new financing strategy issues, and identified a technical team of officials which could update the strategy for Ghana regularly in future, with minimal external assistance. The workshop also assisted Ghana to consolidate debt sustainability beyond the HIPC Initiative by defining and implementing national policies for mobilizing new financing.

The workshop covered the following broad themes:

- reviewing the aid Ghana has received in recent years, broken down by loans/grants, by types (programme, project, other), by donor/creditor and by conditions for acceptance of financing, mobilization and repayment;
- reviewing the commitment and disbursement profiles by each donor/creditor and elaborating a country-specific disbursement profile for loans and grants;
- analyzing the procedures and practices used by donors/creditors and the government and their impact on the mobilization of grants and loans, and identifying the country's priority donors/creditors for scaling up future aid flows;
- designing new external financing and gap-filling scenarios to meet the financing needs of an accelerated poverty reduction programme for Ghana;
- projecting alternative macroeconomic scenarios for twenty years, on budget, balance of payments and GDP; and
- projecting anti-poverty spending needs for twenty years.

Methodology

The workshop used the HIPC CBP National Debt and New Financing Strategy Workshop methodology, dividing participants into five technical groups - Debt Data and Portfolio Specialists, Domestic Debt Strategy Analysts, New Financing Strategy Analysts, Macro Analysts and Poverty Reduction Analysts. In each group, participants completed relevant technical tasks, complemented by lectures, hands-on exercises and plenary presentations.

The workshop designed two macro-economic scenarios, two for domestic debt and three for external financing.

- macroeconomic scenarios. The baseline was consistent with PRGF projections and the macroeconomic framework of the 2006 budget. The optimistic scenario assumed 8 percent real GDP growth.
- domestic debt scenarios. The baseline scenario incorporated current policy, to reduce the domestic debt burden by lowering borrowing costs. The optimistic scenario accelerated the lengthening of the domestic debt maturity profile by introducing 5, 7 and 10 year bonds, to reduce borrowing cost of government.
- new financing scenarios. Scenario 1 included current expectations from Development Partners as agreed at a recent Consultative Group meeting. Scenario 2 assumed accelerated financing to meet the MDGs, included a slight increase in loan financing after 2015, and Scenario 3 assumed accelerated commercial borrowing from 2007 to meet the MDG-related infrastructure spending needs for self-financing projects.

Findings and recommendations

In 2004, external debt reduced drastically to US$6,447.9 million, reflecting the cancellation of US$1,624.9 million under HIPC. In 2006, it fell to around US$2 billion, as a result of MDRI relief, freeing additional resources to achieve the Millennium Development Goals (MDGs).

On the other hand, Ghana's domestic debt increased by 4.1% between 2004 and 2005 (though falling as a percentage of GDP), due largely to new issues of Revaluation Stock to the Bank of Ghana. Nevertheless, the domestic debt profile shifted towards the longer end of the market, which represented 31% in 2005.

The workshop demonstrated that Ghana's external debt was sustainable in the baseline scenario in terms of solvency compared to exports, budget revenue and GDP. This was mainly due to the significant reduction in the external debt stock following the delivery of the Enhanced HIPC debt relief and MDRI, which reduced the PV/XGS indicator below 50% in 2006. However, if Ghana borrowed non-concessionally, its debt would become unsustainable compared to exports from 2018. However, due to considerable assumed increases in budget revenue, Ghana's PV/budget revenue ratios remained sustainable.

The workshop results also indicated that Ghana has high risks of domestic debt unsustainability, in terms of both solvency and liquidity ratios compared to budget revenue. In spite of government determination to restructure the debt by lengthening maturity profile, increased domestic borrowing for investment and market development could cause unsustainability.

Finally, Ghana's aid dependency is expected to increase significantly in the short- to medium-term, as a result of increased borrowing and faster disbursement to fund the MDGs. The aid dependency syndrome would, however, reduce in the medium to long-term, as the export base of the economy widens and revenue collection improves.

DEBT RELIEF INITIATIVES AND PRSP PROGRESS: OCTOBER 2006

Countries	HIPC II Dates		PRSP Dates		HIPC Initiative
	Decision	Completion	Interim	Final	Creditor Participation
Angola	no current timetable		2005	…	NA
Benin	7/00	3/03	7/00	3/03	99%
Bolivia	2/00	6/01	2/00	6/01	95%
Burkina Faso	7/00	4/02	5/00	7/00	76%
Burundi	8/05	mid-2007	1/04	4Q2006	84%
Cameroon	10/00	05/06	10/00	7/03	98%
Central African Rep.	4Q2006	…	1/01	4Q2006	NA
Chad	5/01	end-2007	7/00	7/03	93%
Comoros	mid-2007	…	05/06	2007	NA
Congo, Dem. Rep. of	7/03	2nd half 2007	6/02	7/06	93%
Congo, Rep. of	03/06	end-2009	12/04	4Q2006	60%
Côte d'Ivoire	mid-2007	…	3/02	…	NA
Ethiopia	11/01	4/04	3/01	9/02	92%
Gambia	12/00	end-2007	12/00	7/02	81%
Ghana	2/02	7/04	8/00	4/03	90%
Guinea	12/00	mid-2007	12/00	7/02	85%
Guinea-Bissau	12/00	2009	12/00	2006	81%
Guyana	11/00	12/03	11/00	9/02	81%
Honduras	7/00	4/05	7/00	10/01	93%
Kenya	DSA Nov. 2003		8/00	2/04	NA
Laos	no current timetable		4/01	12/04	NA
Liberia	mid-2007	…	Q4/2006	end-2007	NA
Madagascar	12/00	10/04	12/00	11/03	91%
Malawi	12/00	09/06	12/00	8/02	97%
Mali	9/00	3/03	9/00	3/03	85%
Mauritania	2/00	6/02	NA	1/01	90%
Mozambique	4/00	9/01	4/00	9/01	88%
Myanmar	no current timetable		no PRSP process		NA
Nicaragua	12/00	1/04	12/00	9/01	87%
Niger	12/00	4/04	12/00	2/02	86%
Rwanda	12/00	4/05	12/00	8/02	95%
São Tomé & Principe	12/00	Dec-06	4/00	8/05	85%
Senegal	6/00	4/04	6/00	12/02	81%
Sierra Leone	3/02	Nov-06	9/01	7/05	87%
Somalia	no current timetable		no PRSP process		NA
Sudan	no current timetable		Q3 2006	…	NA
Tanzania	4/00	11/01	3/00	12/00	90%
Togo	end-2007	…	…	…	NA
Uganda	2/00	5/00	NA	5/00	96%
Vietnam	DSA 2002		4/01	6/02	NA
Yemen	6/00	…	2/01	8/02	NA
Zambia	12/00	4/05	7/00	5/02	97%
Eritrea	no current timetable				NA
Haiti	Oct 2006	Q3 2008	Oct 2006	end-2007	NA
Kyrgyzstan	end-2006			02/03	NA
Nepal	no current timetable			11/03	NA

Sources: HIPC Governments, IMF & World Bank

Dates for HIPC decision and completion points and PRSPs are those of final BWI Boards' approval. Most governments have published PRSPs several months before BWI approval.

Malawi reached its completion point and qualified for MDRI in September 2006, while Haiti has become eligible for HIPC relief, on the basis of its preliminary DSA in September 2006. Haiti is scheduled to reach decision point in October 2006.

Key Debt Relief and New Financing Issues	Key Macroeconomic and Poverty Reduction Issues
HIPC CBP DSA shows ratios under HIPC thresholds	Discussions for a new staff-monitored programme (SMP) on-going
Most creditors provide relief, unsustainable due to new borrowing. MDRI	1st review of new PRGF expected. PRSP II due soon
Sustainable external debt/exports. But unsustainable total debt on fiscal criteria when domestic debt is included. MDRI	Stand-by agreement ended in March 2006.
Kuwait and Saudi Arabia offer non-comparable reschedulings. MDRI	6th PRGF review underway. PRSP on-track
Decision point reached in August 2005	Final PRSP expected 4Q2006. PRGF remains on-track.
Reached CP in May; MDRI approved. Still facing lawsuits	PRGF and PRSP on-track. 2nd PRGF review in Q4 2006.
Significant arrears accumulated	Emergency post-conflict assistance programme (EPCA) approved in 2004. Preparation of PRSP has resumed
IsDB and BADEA providing interim assistance	Agreement with IDA reached on petroleum revenue issues. Updated PRSP to be completed in 2007.
DP could be mid-2007 if PRGF concluded by end-2006. High arrears.	PRGF to be negotiated. PRSP expected in 2007.
USA only PC creditor yet to finalise relief. Agreements with 13 commercial creditors signed.	Full PRSP adopted in July 2006. SMP for April-December 2006.
DP agreed March 2006; CP Cologne terms. IMF interim relief pending negotiations with London Club. Lawsuits continue	PRGF expected to remain on-track. PRSP expected end-2006.
DP delayed because of civil conflict. Potentially qualify with PV/revenue=361%	New I-PRSP expected in 2007. EPCA discussions on-going.
Still to conclude with some non-Paris Club creditors. MDRI	No PRGF currently intended. New PRSP prepared.
Interim IMF relief suspended, IDA and AfDF interim relief limit reached	New PRGF to be negotiated.
Signed agreements with almost all creditors. MDRI	Current PRGF ends October 2006. Updated PRSP approved
IMF, AfDB, PC interim relief suspended. Egypt, Kuwait, Saudi and Morocco willing to provide relief	New government confirmed commitment to have IMF programme.
Only IDA and AfDB providing interim relief	EPCA projected for 4Q2006
Lawsuit relating to government bonds ongoing. MDRI	Satisfactory progress on PRGF
PC Cologne stock terms agreed in May 2005; with additional topping up. MDRI	PRSP and PRGF on-track
DSA shows ratios under HIPC thresholds. PC Houston terms relief	2nd PRGF review still under discussion
Despite eligibility, government does not wish to participate in HIPC	PRGF expired in April 2005, no new developments
Debt stock estimated $3bn (600% of GDP), nearly all in arrears	SMP agreed through Sept. 2006. PRSP process has begun
Well advanced with PC relief, contacting all non-PC creditors. MDRI	New PRGF agreed in July 2006.
CP plus topping up reached in September ; MDRI approved.	PRGF on-track. New PRSP to be approved
Difficulties with non-PC creditors. MDRI	4th PRGF review completed.
Unsustainable due to lack of relief from Arab creditors. MDRI	SMP satisfactory review, PRGF in pipeline.
Agreements with China, Kuwait and South Africa. MDRI	4th PRGF review completed satisfactorily. New PRSP being finalised.
No WB lending since 1987. Probably unsustainable	No IMF programme since 1981-82
Strong debt strategy and borrowing ceiling. New non-PC relief but lawsuits continuing. MDRI	PRGF extended to Dec 2006. PRSP on-track, but less successful in health
No agreement with non-Paris Club creditors. Taiwan won lawsuit. MDRI	PRGF on-track, modest growth in 2006. New PRSP being prepared.
Ceiling on new borrowings. Received topping up at CP. MDRI	On-track with new PRGF signed in June 2006. PRSP-II expected mid-2007.
To receive retro-active PC relief following new PRGF	PRGF satsifactory. First PRSP progress report submitted to BWI
Benefited from non-PC creditors relief. MDRI	PRGF expired April 2006, PSI under discussion. On track with PRSP.
Lawsuits for US$35m. AfDB interim relief resumed July 2005, IFAD and BADEA provide arrears clearance	PRGF and PRSP on-track
Accumulating large arrears to creditors. World Bank engaged under LICUS	No IMF programme since 1987, no PRSP process.
IMF urge to minimise non-concessional borrowings. Need to clear arrears.	SMP extended through 2006. I-PRSP being prepared
Benefited from non-PC (Bulgaria, China and Kuwait) relief. MDRI	4th PRGF review completed. New PRSP published in 2005
Potentially qualify with PV/revenue of 394%	SMP discussions on-going. Government approved I-PRSP in Nov 2004
Ceiling on new borrowings, seeking more grants as debt is unsustainable. MDRI	PSI approved in Jan 2006. Revised PRSP in August 2005
Board report on HIPC eligibility due	No current PRGF
Ratios under HIPC thresholds so Paris Club Naples stock treatment	No current PRGF
Lawsuits pending. MDRI	PRGF on-track. Revised PRSP expected soon.

Potentially qualify with PV/exports of 362%	Draft I-PRSP completed but further work has halted. SMP under discussion.
Possible HIPC relief of US$ 139m in PV terms.	PRGF to be approved, along with DP, in Oct 2006. I-PRSP being prepared
Potentially qualify with PV/revenue of 345%	New PRSP expected. PRGF on-track.
Potentially qualify with PV/exports of 201%. Authorities undecided about HIPC participation.	PRGF expires in Nov 2006, could move to SMP with macro deterioration.

Regional Workshops/Seminars

The 4th Interregional Debt Managers Seminar took place in Addis in May (see page 2).

MEFMI's 1st Regional Domestic Debt Strategy Workshop took place in Zambia, in July (see page 6).

Pôle-Dette's Regional Seminar on Institutional and Legal Best Practices. Immediately after the inter-regional workshop, Pôle-Dette and DRI organised on 11 May a seminar on international best practices in debt management, aimed at debt and new financing managers of African francophone HIPCs. The seminar lasted only one day, because it was intended to complement the inter-regional workshop, by encouraging francophone HIPCs to reinforce their legal and institutional arrangements for managing government financing. As a result, the seminar allowed participants to make detailed recommendations on:

- A generic legal framework for public debt management in the Franc Zone, building on Burkina Faso's national experience in elaborating a national law;
- Reinforcing coordination of debt management with macro-economic policy, through national debt and financing committees, such as Benin's National Debt Commission;
- Best practices in monitoring and analysing aid, including designing and implementing national aid strategies, and compiling compendia of donor policies and practices
- Improving management techniques and information flows within government, by designing a procedures manual for managing public debt and government financing.

Pôle-Dette 2nd Regional Domestic Debt Sustainability Analysis Workshop. Pôle-Dette and DRI organised this seminar in Dakar, Senegal from 22 May to 1 June, training 41 domestic debt managers from 9 francophone African countries in a new deeper methodology for analysing domestic debt sustainability and formulating strategies for restructuring domestic debt and issuing new domestic debt instruments. After a day of introductory presentations, the remainder of the first week was allocated to technical group work in order to: construct domestic debt databases and write portfolio reviews; determine the need for debt issuance to finance fiscal and monetary policy; and analyse potential demand for public debt in the financial markets. The second week combined the work of these groups into three government financing strategies, and simulated their results for future domestic debt sustainability, fiscal and monetary policy and the development of financial markets. The workshop used a case study of Cameroon to practice the methodology. However, every country prepared its own national domestic debt database and portfolio review, as well as reviewing its domestic debt capacity-building needs and how domestic debt sustainability analysis could be deepened in future national workshops.

National Workshops

Bolivia: CEMLA has mobilised cofinancing for the CBP, through the German development cooperation agency GTZ, to help Bolivia to design a National Strategy to finance the MDGs. The CBP Coordinator in CEMLA undertook a coordination mission from 24 to 29 July, to finalise technical, financial and logistical arrangements. From 21 to 25 August, a Preparation Mission worked with a National Technical Working Group to review information available to prepare the National Strategy, and agreed with Government on the focus and results expected from the workshop. The mission worked closely with officials of the Ministry of Development Planning, Ministry of Finance, Central Bank of Bolivia, Jubilee Foundation Bolivia and the GTZ. The mission allowed the Technical Group to plan the tasks to be completed to ensure a successful national workshop, due in mid-October.

Congo. The national workshop was organised from 19 June to 1 July, training 32 technicians from all agencies involved in debt management, and poverty reduction spending ministries. The workshop simulated four financial strategies, and decided that the strategy most likely to maintain long-term debt sustainability, while providing sufficient financing for poverty reduction, was one combining HIPC debt relief, with an optimistic macro-economic scenario based on current high oil prices. Its results were:

- external debt will become sustainable again before completion point, because of the high proportion of debt owed to bilateral creditors;
- public finances will become gradually sustainable: the debt service to budget revenue ratio will be 12.2% in 2006 but fall sharply to 5.4% in 2020;
- the CEMAC economic convergence criteria related to debt will be respected from 2007, with a dramatic reduction in debt/GDP and no further accumulation of arrears.

However, implementing this strategy will depend on keeping government's new financing concessional, meeting the conditionalities set for reaching completion point at the end of 2007, and using current petroleum revenues to diversify the economy away from oil.

Ghana. The National New Financing Strategy Analysis Workshop was held in July in Accra (see page 7).

Honduras. The National Debt and New Financing Strategy Workshop took place in Tegucigalpa, from 19 to 24 June. It aimed to update the Strategy, by conducting a comprehensive analysis of debt and development financing policy based on international best practice, and to reinforce staff capacities to analyse and negotiate debt relief and new financing. The event allowed a national team to present a complete report to policymakers, who strongly endorsed the team's work. The key conclusions and recommendations were:

1) Honduras' external public debt is sustainable throughout the projection period, unless there is an increase in non-concessional borrowing
2) Honduras has additional space for new borrowing compared to that included in the current IMF programme, especially due to the effects of the MDRI, even before any possible relief by the Inter-American Development Bank.
3) However, IADB debt relief, especially if it provides additional liquidity, could make a crucial contribution to debt sustainability and the financing of the MDGs.
4) Given the possibility of combining debt sustainability with higher levels of external financing, Honduras should try to reach the MDGs more rapidly and comprehensively.

Nigeria Sensitisation Seminar. WAIFEM and DRI organised with the Nigerian DMO a seminar on debt development financing strategies at the state level for 95 participants from the thirty-six (36) states of the Federation of Nigeria from June 14 - 15 in Abuja, under a project financed by DFID Nigeria outside the HIPC CBP. The seminar concluded that it was essential for state governments to:

- set up debt management offices and build capacity for debt management in order to enhance prospects of maintaining debt sustainability;
- secure improved quality new financing and expand their donor base in order to increase grants for use in economic development and poverty reduction;
- adopt best practices in debt recording by using an international system such as CS-DRMS; and
- observe the guidelines for external and internal borrowing, contained in the DMO Act and Fiscal Responsibility Bill, to avoid a build-up of unsustainable debt and service.

Rwanda. The national Aid and Debt Strategy Workshop took place in August (see page 3).

Institutional/Follow-up Missions

The Gambia. WAIFEM and DRI conducted an Institutional Management Mission from June 5 to 15, under a DFID-funded Intensive Assistance project. It assessed the institutional framework for debt and aid management, and underlined the need to update the Loans Act, for a coordinated policy on aid and debt to be prepared by an Aid and Debt Management

Coordinating Committee (ADMCC), for a Central Project and Aid Coordination Unit within DOSFEA, and for ensuring monthly, quarterly and annual debt reporting to all stakeholders. The mission also made many recommendations to reinforce domestic debt management, including weekly CBG-DOSFEA meetings to discuss policy, implementation of domestic debt buy-down operation, sensitisation to deepen the market, and a code of conduct for market participants. Finally, the mission agreed with Government a work programme to complete the Project by early 2007, including basic training for new staff, a national debt sustainability and new financing workshop, and missions to finalise a capacity-building plan and procedures manual.

Niger. Pôle-Dette undertook an institutional support mission from 10 to 21 July, whose main aim was to identify with the Niger authorities the key measures needed to move institutional and legal aspects of debt management closer to best international practices. The mission noted that there is a clear institutional and legal structure for debt management, and government is making important efforts to reinforce them further. However, such efforts need to be based on a comprehensive and coherent vision of national debt strategy, and to be supported by legal instruments at both the macro- and micro-administrative levels. The mission also recommended reinforcing structures to coordinate debt management with other economic policies, and a system of internal audit in the Public Debt Department. Overall, the mission's evaluation of debt strategy, operations and functional organisation, showed that Niger has a strong will to increase its debt management effectiveness, but needs to continue its efforts to implement a comprehensive strategy to meet international standards.

Sierra Leone. WAIFEM conducted an Institutional Management Mission from July 31 to August 4, which also designed a comprehensive capacity building plan. The mission found that Government has significantly strengthened its institutional framework, by amending the Loans Act and introducing a new Budgeting and Accountability Act, and including a clear statement of financing policy in the 2006 budget. Government agreed recommendations to reinforce staff levels through secondment; underpin laws with procedures manuals; and capture domestic debt and grant data in CS-DRMS. Government also stressed two priorities:

- reinforcing aid effectiveness, by training staff to design a government aid policy, improve aid management procedures, review donor and creditor policies and procedures to assess their alignment, prepare a Compendium of Donor and Creditor Policies and Procedures, and establish systems for mutual accountability between Sierra Leone and its donors.
- reinforcing domestic debt management capacity, through the design of a strategy for the deepening of domestic debt markets, the lengthening of maturity profiles and the reduction of interest rate spreads, taking into account fiscal and monetary policy needs and financial sector development plans.

HIPC CBP Methodology. In recent months there have been the following developments of the CBP's debt strategy analysis methodology:

- The criteria for analysing donor and creditor policies and procedures has been updated to incorporate the Paris indicators of mutual accountability in English and in French. Updates in the other languages are to be done and the methodology is to be further developed for weighting and for prioritising donors and creditors.
- The document explaining how to implement MDRI debt relief has been updated to incorporate the final the details of the World Bank and ADF's criteria for delivery and its impact on new disbursements.
- The domestic debt templates for fiscal, monetary and financial sector analysis and interest rates projections have been combined into one interlinked template, which enables users to assess the balance of demand and supply of domestic debt and adjust for under/over supply or demand. The domestic debt manual is to be updated to reflect these developments.
- Work is on-going on how to link the next BWI's long-term debts sustainability framework with the CBP's DSA methodology.
- Version 2006 of Debt-Pro© released earlier this year enables interest and exchange rate sensitivity analysis to be conducted and work is on-going to incorporate this into the CBP's DSA methodology.

Future Activities

By the end of 2006, the HIPC CBP will implement the following activities:

- **Regional workshops:** Pôle-Dette on prevention of debt crises; WAIFEM on long-term debt sustainability
- **National workshops:** Angola, Bolivia, Burkina Faso, Comoros, the Gambia, Ghana, Guinea, Guyana, Kenya, Tanzania and Zambia
- **Institutional/Follow-up missions:** Angola, Benin, Burundi, Cameroon, Central African Republic, Côte d'Ivoire, Ethiopia, Guinea, Guinea-Bissau, Mali, Sudan and Uganda
- **Governance:** the 13th HIPC Ministerial Meeting in Singapore in September, and the 18th Steering Committee meeting in Tegucigalpa in October-November
- **Attachments:** a non-RO expert to DRI/Oxford, a MEFMI fellow to their mentor and the World Bank in Washington; experts from the CEMLA, Pôle-Dette and WAIFEM regions to DRI and the IMF.
- **Information products:** publications on Debt Negotiations within the Enhanced HIPC Framework, and Best Institutional and Legal Practices for Debt Management, and newsletter no.29.

Distance Learning

The first cycle of distance learning for Phase 4 started on 4 September, with 40 students from 8 countries and 3 regional organisations. The student selection process was conducted through a series of demand assessment missions (DAMs):

- In the Pôle Dette region, DAMs to Burkina Faso and Senegal selected ten students.
- In the CEMLA region, a DAM to Honduras selected six students.
- In MEFMI region, DAMs to Malawi and Tanzania selected six students.
- In the WAIFEM region, a DAM to Sierra Leone selected five students.
- In the non-RO region, DAMs to Ethiopia and Sao Tome and Principe selected six Ethiopians (two of whom are funded by a CIDA grant) and four Sao Tomeans.
- In addition, 1 MEFMI Fellow, 1 BCEAO/BEAC staff member and 1 WAIFEM staff member will study the programme.

In Phase 4, the programme content has been widened to include domestic debt strategy modules, as well as external debt strategy, new financing strategy and debt data. The programme is also available in all four CBP languages (including Portuguese). As in Phase 3, each student is assigned a mentor, a national or regional expert, who will provide comments and feedback on student assignments. A National Co-ordinator in each country is responsible for monitoring student progress and preparing the national data and documents used by the students for their studies. The CBP distance learning programme uses national data and documents, rather than a generic case study, so each student's studies can be directly applied to their work. Each student will study four modules at a distance, and will end their studies at a residential workshop in the final quarter of 2007.

UGANDA: INVESTMENT AND PROFITS RISE TRACKING NEEDED

DEVELOPMENT FINANCE INTERNATIONAL

This article summarises findings from Uganda's Foreign Private Capital Survey 2004. This collected data for 2001-3 using an enhanced questionnaire. These were used from 2005 to compile the balance of payments, but their publication has been somewhat delayed. A survey currently in course is collecting data for 2004-05 and will be published by the end of 2006.

Table 1: Foreign Liabilities (US$m)					
	2001	2002		2003	
Liabilities	Stock (MV)	Flow (net)	Stock (MV)	Flow (net)	Stock (MV)
1. Total (1+2+3)	1205	137	1416	35	1383
2. FDI	983	90	1139	102	1171
a. Equity	642	5	753	2	724
b. Reinvested Earnings	43	42	42	52	52
c. Loans (ST)	11	6	17	(9)	8
d. Loans (LT)	287	37	327	57	387
3. Non FDI	187	2	196	(38)	160
a. Portfolio Equity	8	1	10	0	12
b. Loans (ST)	12	4	16	10	27
c. Loans (LT)	167	(3)	169	(48)	121
4. Other Claims	36	45	82	(29)	53

Table 2: Income (US$m unless indicated)		
	2002	2003
1. Net profit (2a + 2c + 3a)	60	85
a. Profit making entities	101	115
b. Loss making entities	(42)	(30)
c. Reinvested earnings	42	52
2. Return (profit to actual investment)	6	8
3. Interest due and paid	11	8
a. To related (FDI) enterprises	3	2
b. To non-related enterprises	8	7
4. Implied interest rates (%)		
a. To related (FDI) enterprises	1.0	0.4
b. To non-related enterprises	4.1	5.2

The team achieved its highest response to date (85%) thanks to better awareness and implementation. Data accounted for 90% of total foreign liabilities, which the team checked against previous surveys and financial statements, and up-rated for non-response, sample, and population, making the data the most reliable so far collected in Uganda. Nevertheless, delays in response by the private sector led to a longer collection period than past surveys. In addition, with assistance from DFI and MEFMI, Uganda officials reviewed all data from 1998 to 2003 to ensure that time series were consistent.

Findings

As Table 1 shows, total stock of foreign liabilities increased over the period in book value terms, but market value (MV) declined slightly in 2003, due to currency depreciation.

FDI was over 80% of stock, of which by far the most significant part remained equity. Stock of reinvested earnings increased significantly in 2003, reflecting high levels of profit. Loan stock increased, especially long-term. Net flows were low, but probably understated due to omissions of some new equity.

Most entities were highly specialised, with 78% operating in one sector. Direct equity stock was mostly in manufacturing (31%), finance (19%), and wholesale (18%). The largest investors were resident in the UK, USA, Mauritius, Ethiopia, Kenya and the Netherlands. New flows were low, mainly in finance, manufacturing and construction, and from Kenya and the UK. Portfolio equity stock increased significantly from a low base. It was 95% in finance and manufacturing, and from international organisations, Kenya, UK, India, Hong Kong and Egypt. Most actual investment was in new plant and machinery.

Debt levels, principal disbursements and payments increased sharply over the period. Manufacturing held the largest share of stock (33%), followed by agriculture, wholesale, and "other" sectors (including Electricity and Mining). Transport and construction also saw large increases in debt. The highest debt exposure is to France and International Organisations, and the UK, France and Germany showed the highest rates of increase. Disbursements of loans far exceeded equity, and were concentrated in agriculture and manufacturing, and sourced mainly from France, Kenya, the UK and Switzerland, although large increases were reported for the Virgin Islands, Bermuda and International Organisations.

Most debt stock was long-term and from related companies, who held an increasing share of stock and flows relative to debt from unrelated sources. As discussed in previous newsletters, related debt tends to have more flexible and concessional terms, but also to be more volatile in response to macro-economic and market developments.

Table 2 shows that overall returns on equity increased from 6% to 8%, and the number of profit-making enterprises grew from 101 to 115, sending a strong positive signal to existing and potential investors into Uganda. The level of losses, and number of loss making entities also fell. In terms of use of profits, direct equity investors received a major increase in dividends paid, but the level of earnings reinvested as additional investment rose by 25%.

Interest due and paid fell. This reflects an increased share of debt with more flexible terms from related companies, whose "implied interest" (derived from interest due and paid against average debt stock) is lower than for debt from "unrelated" sources and fell during 2003. However, implied interest rates on debt from unrelated sources rose significantly in 2003.

However, sector performance varied greatly. Those with the highest average returns were finance (18%) and wholesale (14%), but agriculture reported losses and, given its role as a key producer and employer, at the core of Uganda's anti poverty strategy, this result presents a challenge to policymakers, donors, and business. The highest levels of dividends declared were in wholesale and finance.

Performance by source country also varied. Investments from the UK, USA and Mauritius were the most profitable. Investors from the UK declared and paid the highest levels of dividends, but in percentage terms reinvested the least. By contrast, investors from Sweden, Ethiopia and Switzerland reinvested all their profits in 2002, as did investors from Ethiopia and Belgium in 2003.

In spite of a strong (11%) increase in total turnover, employment grew very slowly (by only 2%). Female workers experienced higher employment growth, most notably in management and supervision positions (20%), and earnings rose by 5% (with increases concentrated in finance, manufacturing and transport). There is a strong need to ensure that employment and earnings should rise more rapidly in line with investment and profits, if FPC are to make a major contribution to growth and poverty reduction in Uganda.

The survey also captured data on foreign assets to a greater extent than in previous years, but the data remain considerably underestimated due to the difficulty of tracking overseas holdings. Most equity assets captured were in manufacturing and finance, with some in transport. There were significant trade credits to unrelated entities, and short term currency holdings, deposits and lending to related entities rose to US$187m at the end of 2003.

Recommendations
The survey suggests the following recommendations for future work:
1) Monitoring:
- Improve monitoring of assets via census and household surveys, and comparison with international data sets
- Strengthen public-private partnership and synchronise monitoring with company financial years to ensure that data are provided more rapidly
- Capture expected future earnings and profits

2) Analysis and Policy
- Establish bilateral investment treaties with main FPC source countries
- Investigate what factors influence interest rates on private sector debt
- Analyse why source countries behave so differently in terms of repatriation/reinvestment.
- Further deepen financial markets to attract portfolio investors
- Conduct a sector-specific study on how to increase investment and profits in agriculture
- Deepen questions on employment promotion and corporate social responsibility issues

For further information, visit the websites of BOU (www.bou.or.ug), UIA (www.ugandainvest.com), and UBOS (www.ubos.org.ug).

DEVELOPMENT FINANCE INTERNATIONAL

FPC CBP ACTIVITIES UPDATE

Over the last few months, the FPC CBP continued to progress at country level, moved forward on phase 3 financing, and enhanced its methodology, software and website.

COUNTRY PROGRESS
The programme countries have progressed as follows:

- Bolivia is finalising its proposal for participation in phase 3.
- Burkina Faso (Cycle 1) has finalised its fieldwork, dramatically increased its response rate, and will disseminate results in the last week of September.
- Cameroon (Cycle 1) is finalising data/analysis, with dissemination scheduled for October.
- Gambia (Cycle 2) has an 80% response rate. It is hosting a Follow Up Mission in September, and planning to disseminate findings in Q4.
- Ghana is finalising World Bank financing to launch a Demand Assessment Mission in Q4
- Honduras formally requested FPC CBP support and is lobbying donors for financing.
- Kenya is finalising its World Bank financing for the programme, for a Q4 DAM.
- Malawi (Cycle 3) has finished its fieldwork, and is checking data for advance release in Q3, and a dissemination seminar in Q4. It has also been exploring funding prospects for local donor financing of future cycles.
- Nicaragua (Cycle 1) is proceeding with its fieldwork, and a Follow Up Mission will be held in Q4, with the aim of disseminating before the end of the year
- Rwanda is finalising its project proposal, following a formal request for FPC CBP assistance
- Tanzania (Cycle 3) hosted a data quality and report writing mission in August, led and organised by MEFMI and staffed by regional experts. A closing results dissemination workshop is scheduled in Q4, to be combined with training to launch Cycle 4.
- Uganda (Cycle 5) has reached a 35% response rate in its fieldwork. It will close the cycle and publish its analysis in Q4.
- Zambia continues to explore financing prospects for participating in phase 3.

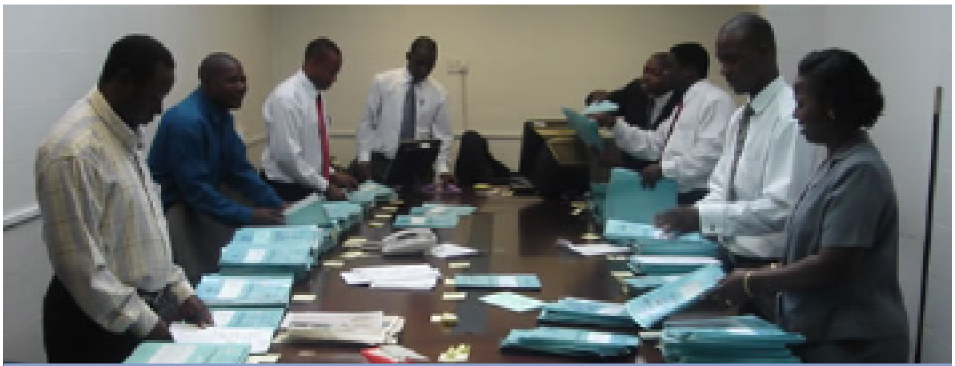
OTHER ACTIVITIES
Among other activities, the FPC CBP has:

- Finalised the phase 3 document including major increases in financing from regional implementing organisations, as well as the timetable for disbursing core funding for phase 3 of the FPC CBP.
- Enhanced FPC CBP Software. The new version (1.70.1.2) enables much faster processing of data, and includes improvements requested by country experts during the Training for Trainers Workshop in September 2005. Users are urged to download it and give feedback to DFI. The EIS website now provides information on technical updates for the attention of software experts. Users are encouraged to download both from the EIS website, and get back to EIS and DFI with comments: Users are encouraged to download both from the EIS website, and get back to DFI with comments: http://www.evinsol.co.uk/software.
- Conducted a donor seminar, in collaboration with Seco, in September, to disseminate programme findings to Seco and other donor agencies.
- Designed improved methodology for investor perception and corporate social responsibility

FPC CBP ACTIVITIES UPDATE *(continued)*

questionnaires.

- Continued to disseminate electronic FPC CBP Briefings every six weeks, and uploaded previous Briefings on to the FPC CBP website.
- Uploaded country analytical reports on the CBP website under a new page, Country Reports, on the open site, including quoting links to country sites where available.
- Updated the Country Status page on the FPC CBP website.
- Created a new Software page on the FPC CBP website.
- Enhanced its liaison with the OECD FDI statistics and analysis units.



Training Workshop and Data Time Series Mission, Tanzania

FORTHCOMING WORK PROGRAMME

In the forthcoming months, the FPC CBP will:

- Conduct follow up missions to the Gambia (Q3) and Nicaragua (Q4), closing workshops in Burkina Faso (Q3), Cameroon (Q4), Malawi (Q4), Nicaragua (Q4), Tanzania (Q4) and the Gambia (Q4), and demand assessment missions to Ghana and Kenya (Q4).
- Finalise the draft of the publication on analytical findings (Q4)
- improve and update the website, software and technical materials
- produce and disseminate electronic FPC CBP Briefings in 3 languages every 6 weeks

FOREIGN PRIVATE CAPITAL: FREQUENTLY ASKED QUESTIONS

How Should Countries Analyse Corporate Social Responsibility?

Before 2002, the FPC CBP focussed largely on collecting and analysing data on balance of payments and investor perceptions/intentions. These have been of major use to public and private sector decision makers and donors.

However, at an international level, it is also widely accepted that FPC can make a major contribution to poverty reduction and sustainable development through corporate social responsibility (CSR). Nevertheless, most monitoring and analysis of these efforts has been through self-reporting by TNCs, and has excluded developing country governments and private sector organisations. The OECD for example, has established a system of "National Contact Points" (NCPs), responsible for encouraging awareness, understanding and observance of *OECD MNE Guidelines* at a national level, and dealing with complaints from trade unions and NGOs, but they do not formally monitor company performance against the *Guidelines*, or liaise with national authorities.

Best practice says that self-reporting by TNCs needs to be verified against other sources. As a result, the countries participating in the FPC CBP demanded that phase 2 (see also issue 12) and phase 3 should enhance CBP monitoring and analysis of these aspects. This article discusses how this can be achieved.

CSR focuses on the non-financial benefits (or costs) of investment, and its impact on development and poverty reduction. This involves monitoring and analysing its impact on the environment, society, and governance. This article covers potential benefits, international codes, implementation challenges, and implications for methodology, analysis, and policy.

Contributions from Business

Views as to how business should contribute to poverty reduction and development diverge very widely, from "everything should be left to the market", to "business should make charitable donations", to "business should make national development integral to its core activities". The latter approach is described by the UK Commission for Africa (2005) as:

- Improving local employment numbers, levels, gender balance and training
- Enhancing links of foreign investors with local medium, small and micro-enterprises
- Lobbying to ensure that governments improve the investment climate
- Improving production processes to ensure that goods are produced with greater choice, at lower cost, for maximum access by the poorest,[1] and with minimal negative environmental impacts
- Providing social services: either by paying taxes to government, or by paying directly for the education, housing and health services for the workforce and their families.

International Initiatives

There are a huge number of international initiatives to promote CSR, including guidelines promoted by international organisations (ILO, OECD, UNCTAD), national standards, certification schemes (ISO), voluntary initiatives (UN Global Compact), mainstream financial indices (FTSE4Good), and reporting guidelines (AccountAbility, and the Global Reporting Initiative - GRI). Keeping track of developments in all these initiatives would imply huge workloads for developing countries.

Fortunately, there is a growing consensus to focus on codes such as the UN *Global Compact*, OECD *Guidelines for MNEs* and *Bribery Convention*, the *GRI*, and *ILO Tripartite Declaration of Principles Concerning MNEs and Social Policy.*

...and challenges in their application

While environmental standards are sophisticated and well established, those on social responsibility are much less consistent. Many codes are written with MNEs in mind, and need to be adapted to large local enterprises and SMEs.

The crucial aspect is to ensure that monitoring and analysis is focussed on delivery, rather than the existence of policy guidelines and systems. International analysis indicates that TNCs are more advanced on guidelines and systems, which allow them to promote a positive image in headquarters

countries, whereas SMEs show more progress on delivery.
Most international codes are voluntary, relying on moral suasion, which means suppliers of FPC are under little pressure to apply them, except to achieve positive publicity. Even where developing country laws insist on strict application of standards, LICs have no capacity to monitor and enforce enterprise compliance.

Monitoring
Governments need to focus on monitoring corporate actions and encouraging conduct consistent with sustainable development strategies. Each of the areas above requires country teams to:

- Consult widely with relevant stakeholders (public and private sectors, donors, civil society) to define priorities and data needs
- Assess existing information sources (self-reporting by enterprises, direct reporting to line ministries, corporate watch organisations etc)
- Identify data that would need to be collected through direct surveys
- Agree on methodology, information sharing and policy action plans among stakeholders

Given the novelty and sensitivity of certain questions, countries often decide to introduce CSR questions gradually. They formulate a shortlist of questions from the following:

- *Job creation* by types: gender, nationals (and indigenous groups) versus foreigners, role (eg, management, skilled, unskilled…)
- *Training* by types: ratio of training budget to annual operating costs; numbers trained; average hours of training per employee per year; skills transferability
- *Remuneration* and benefits by types: amount spent on wages, salaries, illness and injury benefits, education for employees' children, maternity, disability, housing, retirement benefits; (ratio of lowest to highest paid)
- *Worker rights*: freedom of association and collective bargaining; percentage of workforce unionised; days lost to industrial action; share of Board represented by workers; spend on health and safety; number of injuries
- *Human rights:* hours in the working day; minimum recruitment age; indigenous rights
- Links to local enterprises: spend on supporting local SMEs; monitoring suppliers; percentage spend on local rather than foreign suppliers
- *Distribution of goods to poorer consumers:* amount spent adapting or providing lower cost goods to the poor, on infrastructure and distribution networks, and on training customers in their use
- *Social services:* amount spent on the wider community: housing, health services, HIV and AIDS programmes, infrastructure and utilities, schools.
- *Environment:* amount spent on new technologies, encouraging renewable resources, mitigating environmental damage, recycling, reducing emissions and energy use
- *Bribery and corruption:* spending on anti-bribery education, amount of money lost.

Using the data
Verification
Self-reporting needs to be verified, by consultation with:

- National bodies: ministries, investment promotion agencies, regulatory authorities, private sector organisations
- Companies: websites and reports
- Dedicated NGOs monitoring corporate performance (eg, OECD Watch, Friends of the Earth, Amnesty, Corporate Watch…)
- International and Local Media
- OECD National Contact Points and non-OECD diplomatic counterparts.

Analysis and Policy Implications
Several analytical and policy steps should emerge from better monitoring:

- creation of company profiles to assess performance, compliance with codes, progress, and next steps, reviewing company performance over time.
- Using profiles (or information from other countries) to provide positive media coverage and awards for best performing enterprises, to encourage private sector best practice to increase shareholder value, employee gains, or market opportunities for the poorest.
- design of sectoral and overall policy action plans to improve CSR performance.
- refining of investment promotion strategies and tax incentives to focus on CSR aims.
- working with the *international community* (eg via OECD NCPs and NGOs) to encourage improved corporate performance - see www.oecdwatch.org for updates on the status of cases presented to NCPs.

As a result of CBP efforts, many countries already monitor CSR partially through a list of selected questions. But a much more comprehensive approach is needed in methodology, analysis, policy, and consultation with a wide group of national and international stakeholders, making full use of international and national initiatives and laws. The next issue of the FPC CBP newsletter will present more precise questions for CSR surveys.

[1] *See: http://www.12manage.com/methods_prahalad_bottom_of_the_pyramid.html*

DEBT RELIEF TECHNICAL QUESTIONS

Legal Support to HIPCs Advocates for International Development (A4ID)

Since 1997, HIPCs have been requesting assistance to prevent or defeat lawsuits by creditors which do not wish to provide HIPC-comparable debt relief. Finally in 2006 structures have been established to provide such assistance.

A4ID is a new independent organisation based in London providing free legal advice and assistance to developing countries and development NGOs. A4ID's aim is to harness the skills of the highest-quality international lawyers, in order to provide access to justice to further the UN Millennium Development Goals, in the areas of trade, debt & finance, intellectual property, development, governance and capacity building. A key area of our work is in helping developing countries to overcome legal problems relating to debt. A4ID is concentrating on providing;

- *Advice on lawsuits and arbitration claims relating to existing loans*. A4ID member firms are already representing a number of debtor countries in defending legal or arbitration claims brought by a range of creditors, working through the most experienced international litigation and arbitration lawyers. In addition to providing this representation, A4ID is conducting due diligence studies of potential litigants, so that the information can be used to assist other countries in future, and preparing best practice case study documents for developing countries and lawyers to use to defend litigation and arbitration actions.
- Advice and training on future finance initiatives and loan agreements. A4ID is planning a series of training workshops to build the capacity of, and share knowledge with, representatives of debtor countries in order to ensure that they are better able to defend themselves against litigation, especially at the national level, and that future loan agreements are less susceptible to legal actions. These will examine best practices in litigation, as well as key aspects of new loans such as jurisdiction, applicable law, what should or should not be included so as to protect the interests of the debtor, sovereign immunity and assignment of debt instruments.

All assistance from A4ID is provided on a pro bono basis (ie free), even though it mobilizes the skills of the top international lawyers. For more information about A4ID and its debt work, contact Nick Flynn at Nick.Flynn@Weil.com or Katie Frith at katie.frith@a4id.org.

HOW SHOULD COUNTRIES ACCOUNT FOR MDRI DEBT RELIEF?

1) IMF relief

The liability to the Fund rests with the central bank as the borrower. Therefore, debt relief from the Fund results in a reduction of the central bank's foreign liabilities and either

- a corresponding increase in the central bank's domestic liabilities (ie government deposits with the central bank) or in its capital equity (ie central bank profits); or
- a corresponding decrease in the central bank's claims on government.

As a result, net foreign assets increase and net domestic assets decrease by the amount of IMF debt relief, while the monetary base remains unchanged.

The following table outlines three cases depending on the arrangements agreed within a country for the transfer of IMF debt relief resources between the central bank and the government:

Case A: liability to the IMF rests with the central bank and the loans were not on-lent to government:

Alternative 1: agreement that debt relief proceeds are i passed on to government

Alternative 2: debt relief reflected in central bank's higher profits

Case B: liability to the Fund rests with the central bank and the loans were on-lent to government

Case C: liability to the Fund rests directly with the fiscal authorities

All post-HIPC countries have had to agree arrangements between their central banks and governments regarding the transfer to the budget of IMF debt relief. These arrangements vary from the total resources being placed in special accounts at the central bank (Madagascar, Mozambique, Rwanda and Tanzania) to agreed ad hoc transfers (Ghana) and transfer being effected by the central banks in line with previously scheduled debt service (Guyana, Honduras, Uganda and Zambia). In addition, countries have adopted different timeframes for use of the resources, such as 3 years in Ghana, 4 years in Mozambique and 10 years in Madagascar.

The treatment of MDRI relief in fiscal accounts involves two steps:

- reflecting the grant component of MDRI stock relief, which will be different depending on modalities of the transfer of the grant component and on whether a country compiles its fiscal accounts on a cash or accrual basis. This will appear under the grant line item of revenues
- reporting of new interest and amortisation schedules for the remaining, outstanding external liabilities.

In the balance of payments, MDRI relief is reported as a credit entry (inflow) in the capital account under general government (or other sectors if the central bank is the debtor), with a corresponding debit entry showing an equivalent reduction of liabilities to the Fund in the financial account under other investment - liabilities. Gross international reserves are initially unaffected.

2) IDA and AfDB relief

This involves direct debt cancellation to the fiscal authorities. Therefore relief from these two institutions is not expected to have any affect on the monetary accounts, while the impact on the balance of payments will be similar to that for the Fund. The impact of IDA and AfDB relief on the fiscal account depends on whether a country's fiscal accounts are compiled on a cash or accrual basis. The table below shows the impact on a cash accounting basis.

Impact on monetary accounts of IMF MDRI relief				
	Case A		Case B	Case C
	Alternative 1	Alternative 2		
Net foreign assets	+ 500	+ 500	+ 500	0
Foreign assets				
Foreign liabilities	- 500	- 500	- 500	
Net domestic assets	- 500	- 500	- 500	0
Net claims on government	- 500	0	- 500	
Claims on government	0	0	- 500	
Government deposits	+ 500	0	0	
Other items net	0	- 500	0	
Assets		0		
Liabilities and capital		- 500		
Monetary base	0	0		0

Impact of IDA/AfDB MDRI relief on fiscal accounts - cash basis	
	Budget changes for MDRI
Revenue	
Expenditures	
Interest of IDA & AfDB	-5
Overall balance	+ 5
Financing:	- 5
Foreign, of which IDA & AfDB	35
Domestic, of which	
MDRI related government deposits*	- 40
Memorandum items:	
Public sector debt (after MDRI)	-750
MDRI debt relief from IDA & AfDB	750
MDRI debt relief from AfDB	250
MDRI amortisation savings from IDA & AfDB	35
MDRI interest savings:	5

* this amount arises due to 'excess' financing in the base case, prior to any post-MDRI adjustment of financing (eg reduction) or spending (increase)

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