SUSTAINABLE LENDING AND OECD LEADERSHIP

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The financial situation of many low-income countries improved substantially in 2005 to 2006, following the implementation of the Multilateral Debt Relief Initiative (MDRI)[1], which delivered debt relief beyond that provided under the Heavily Indebted Poor Countries (HIPCs) Initiative. Lower debt levels, strengthened macroeconomic fundamentals and improved prospects in low-income countries increased – or renewed – their attractiveness to a broader range of creditors, including export credit agencies (ECAs). At the same time, many low-income countries wished to accelerate borrowing to address their development needs.

The joint IMF/World Bank debt sustainability framework

While this situation was a much welcome development, concerns were expressed at the time that a new borrowing boom could end up hindering development if resources were not well used. In particular, many observers pointed out that while the macroeconomic situation of low-income countries was much better, other economic circumstances remained largely unchanged and budgetary, project, and debt management capacities in these countries still presented weaknesses. It was also recognised that most outlays related to the Millennium Development Goals did not, by nature, generate sufficient cash flow to governments in the near term to service debt on market terms.

In response to this situation, the International Monetary Fund (IMF) and the World Bank (WB) undertook to improve their main instrument to analyse debt vulnerabilities in low-income countries – the Debt Sustainability Framework (DSF). However, it was clear that the effectiveness of the DSF ultimately depended on a broader use by debtors and creditors of the results of debt sustainability analyses conducted with the framework. Such a broader use of debt sustainability analyses would facilitate communication and co-ordination between creditors and borrowers, and among creditors.

In 2006, the use of the DSF by creditors was expanding but still limited. It was actively used by a few multilateral creditors and donors, but to a much smaller extent by others, in particular ECAs and commercial creditors. The use of the DSF and its results was (and remains) an individual choice for each creditor. The DSF has no institutional or contractual basis and does not seek to bind creditors around a given course of action such as an overall lending envelope for a borrowing country, or the appropriate degree of concessionality or the relative priority of investments; its main objective is to allow creditors and borrowers to make informed decisions about the preferred financing strategy. The ultimate responsibility for such decisions rests with borrowing governments and it is, therefore, most important that governments understand debt sustainability analyses and use them to define their borrowing strategy. Nonetheless, broadening awareness among creditors of the concept of debt sustainability and of the results of IMF/WB assessments in specific countries was seen as a way to facilitate creditor co-ordination through a shared understanding of the impact of individual lending decisions on a debtor's overall debt outlook.

In the course of 2006, IMF and WB staffs intensified outreach on the DSF with traditional official lenders, including ECAs from OECD countries. Many ECAs acknowledged that, although officially supported lending to low-income countries represented a small part of their total portfolio, it could be large in relation to the recipients' budgets. Therefore, increasing non-concessional lending to low-income countries could put debt sustainability at risk. It was recognised that debt sustainability analyses could inform ECAs' country risk analysis and provisioning decisions. Some ECAs were making efforts to develop lending practices that took into account the results of debt sustainability analyses.

In 2007, a small group of ECAs, with the critical support of the Chair of the OECD Working Party on Export Credits and Credit Guarantees (ECG), Nicole Bollen (Netherlands) and the OECD export credit secretariat, set out to design voluntary principles on sustainable lending to low-income countries, which would be consistent with the commitments made by OECD countries as members of the IMF and WB. Principles were approved by all the ECG members in early 2008, and have been implemented since.

The OECD agreement on sustainable lending to low-income countries

The ECG agreement – Principles and Guidelines to Promote Sustainable Lending in the Provision of Official Export Credits to Low-Income Countries – acknowledged that concessional lending generally remained the most appropriate source of external finance for the majority of low-income countries.

The Principles committed OECD ECAs to observing the IMF's and WB's policies on non-concessional external borrowing in low-income countries. Other commitments included taking into account the latest debt sustainability analyses jointly produced by the IMF and WB. And for any large transaction with a repayment term of two years or more, ECAs also agreed to seek assurances from government authorities in the respective low-income country that the transaction would be in line with the country's agreed borrowing and development plans. Finally, the ECG agreement cemented existing arrangements between ECAs, the IMF and the WB regarding the sharing of information on official export credits provided to the countries subject to the Principles and Guidelines.

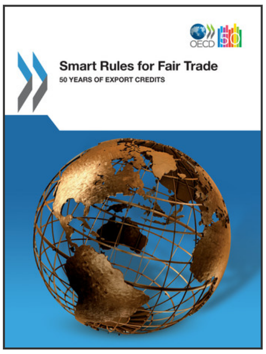
A notable aspect of the negotiation was the effort made by OECD ECAs to reach out to non-OECD countries that had been invited to participate in a number of meetings.

The IMF and the WB welcomed this OECD agreement as an important contribution to maintaining debt sustainability in low-income countries; the agreement clearly supported their call for all creditors to adhere to sustainable and transparent lending practices. The agreement was also an example of excellent co-operation between the IMF, the WB and the OECD. The design of the Principles, indeed, required frequent interaction between the staffs of these three institutions as well as ECAs. The implementation of the Principles was also facilitated by new procedures to inform ECAs of applicable IMF and WB policies in those low-income countries covered by the Principles.

The Principles remain very topical today, in a world where low-income countries face the challenge of addressing their large infrastructure gaps in a sustainable way.

Note

1. The Multilateral Debt Relief Initiative (MDRI) provides for 100% relief on eligible debt from three multilateral institutions to a group of low-income countries; the initiative is intended to help these countries advance toward the United Nations' Millennium Development Goals, which are focused on halving poverty by 2015.



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