INTERNATIONAL MONETARY FUND

AND

WORLD BANK

HELPING DEVELOPING COUNTRIES ADDRESS PUBLIC DEBT MANAGEMENT CHALLENGES—AN IMF-WORLD BANK CAPACITY BUILDING PARTNERSHIP

March 5, 2013

EXECUTIVE SUMMARY

In 2009, the Boards of the IMF and World Bank jointly endorsed a capacity building program to help developing countries strengthen their public debt management frameworks. A key aspect of the program was to help developing countries implement the framework developed by staffs to formulate an effective medium-term debt management strategy (MTDS). The Boards also supported the continued use of the complementary framework—the Debt Management Performance Assessment (DeMPA)—developed in 2007, to assess the effectiveness of the broader institutional arrangements for public debt management. This paper provides an update on the implementation of the program since its endorsement in 2009.

The lessons of the global financial crisis reinforce the importance of the debt management agenda. Although developing countries have been relatively insulated from the direct effects, the crisis highlighted the importance of managing sovereign debt well. In addition, the scale of investment needs, coupled with potentially reduced access to concessional financing, means that many developing countries will become increasingly reliant on nonconcessional and market-based financing. This will potentially change the risk profile of their debt portfolios significantly. Consequently, it will be imperative that countries have sufficient analytical capacity to design robust debt management strategies, leverage these new financing sources effectively, and manage the resultant portfolio risks.

Since 2009, 59 countries have received technical assistance under this program. Individual country missions have been supported by extensive knowledge transfer through training and workshops. In some instances, the main pillars of the program—the MTDS and DeMPA—have been complemented by support to develop debt management reform plans or supplemented by other targeted technical assistance, including efforts to develop domestic government securities markets. A range of technical assistance providers have partnered in these efforts. Feedback from recipient governments has been very positive, and demand is growing. Country authorities have indicated that the MTDS framework is useful and sufficiently flexible to accommodate country-specific issues; some have already published a formal debt management strategy.

Experience to date indicates that Bank and Fund efforts are having a positive impact, though much work remains to be done. This is also recognized in the preliminary findings of the external evaluation of the Bank's Debt Management Facility that is being finalized. Furthermore, evidence from follow-up DeMPAs show clear gains in organizational structures, legal frameworks and borrowing procedures. There has been significant progress in the integration of debt management responsibilities and data reporting and recording, and improved procedures to mitigate operational risks. Nevertheless, despite progress in these areas, the overall DeMPA results across the full sample highlight ongoing weaknesses in critical areas.

The implementation experience suggests a number of lessons, with strong country ownership critical for success:

- Debt management reform and capacity building is complex and takes time, requiring the sustained commitment of senior policy makers. Building the capacity of debt management offices often entails significant legal, institutional and operational changes, especially given the persistence of fragmentation challenges.
- Building analytical capacity remains a fundamental challenge and is especially important as debt portfolios become more complex and the need for the authorities' to develop and implement effective debt management strategies becomes more acute.
- Progress has been more sustained where it has been complemented by related development solutions in a Bank loan or design elements of a Fund program arrangement, and the corresponding engagement of Bank and Fund country teams.
- In a number of cases, exogenous factors (such as natural disasters and conflicts) have impeded efforts to improve the institutional and operational capacity for debt management.

The agenda will remain challenging. The importance of this work program will increase as countries expand their access to nonconcessional and market-based sources in both domestic and international capital markets. Both the Bank and Fund remain committed to supporting these efforts.

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Glossary

CEMLA	Center for Latin American Monetary Studies
CPIA	Country Policy and Institutional Assessment
DeMPA	Debt Management Performance Assessment
DMF	Debt Management Facility
DMFAS	Debt Management and Financial Analysis System
DSF	Debt Sustainability Framework
ECF	Extended Credit Facility
FSAP	Financial Sector Assessment Program
HIPC	Heavily-indebted poor country
IDA	International Development Association
IMF	International Monetary Fund
IP	Implementing partners
LCBM	Local currency bond market
LIC	Low income country
MEFMI	Macroeconomic and Financial Management Institute of Eastern and Southern Africa
MTDS	Medium-Term Debt Management Strategy
MDRI	Multilateral debt relief initiative
ODA	Official Development Assistance
PDM	Public debt management
PEFA	Public Expenditure and Financial Accountability
PFM	Public financial management
PRGT	Poverty Reduction and Growth Trust
TA	Technical assistance
TFFS	Task Force on Finance Statistics
UNCTAD	United Nations Conference on Trade and Development
WAIFEM	West African Institute for Financial and Economic Management

CONTEXT

1. The importance of strengthening public debt management (PDM) frameworks in developing countries has been explicitly recognized by the IMF and World Bank since 2007.[1] At that time, country experiences were discussed and Directors of both institutions expressed concern that developing countries faced significant challenges, not least because of institutional weaknesses and scarcity of skills combined with significant underlying macroeconomic vulnerabilities. These concerns were seen as particularly relevant given the borrowing space created by the heavily-indebted poor country (HIPC) and multilateral debt relief initiatives (MDRI), and the financing needs associated with countries' infrastructure investment and broader development goals.[2] The Boards called for staff to make assistance for developing countries in this area a priority.

2. In 2009, staffs reported to the Boards on the progress in supporting efforts to strengthen PDM frameworks. A formal framework—the Medium-term Debt Management Strategy (MTDS) framework—to guide country authorities in their design of debt management strategies was put forward for endorsement. In addition, staff updated the Boards on countries' observed strengths and weaknesses based on the findings of the Debt Management Performance Assessment (DeMPA) program.

3. Bank and Fund Boards endorsed the staffs' 2009 strategy to strengthen PDM frameworks and capacity in developing countries. The strategy comprised (i) helping countries adopt and implement the MTDS framework; (ii) undertaking debt management performance assessments; and (iii) continuing the provision of other debt management and domestic debt market development technical assistance (TA) and advisory services to low- and middle-income countries.

4. Developments since 2009 have brought to the fore the critical interconnections between sound PDM and economic and financial stability, and heightened the importance of this agenda. While the direct effects of the global financial crisis were mostly felt by those developing countries contemplating accessing international capital markets, the broader lessons are relevant for all. In particular, the crisis has highlighted the importance of creating resilient and reliable sources of funding for mitigating financing risks and facilitating countercyclical fiscal policies as a crisis response. The crisis has also emphasized the risks associated with overreliance on specific

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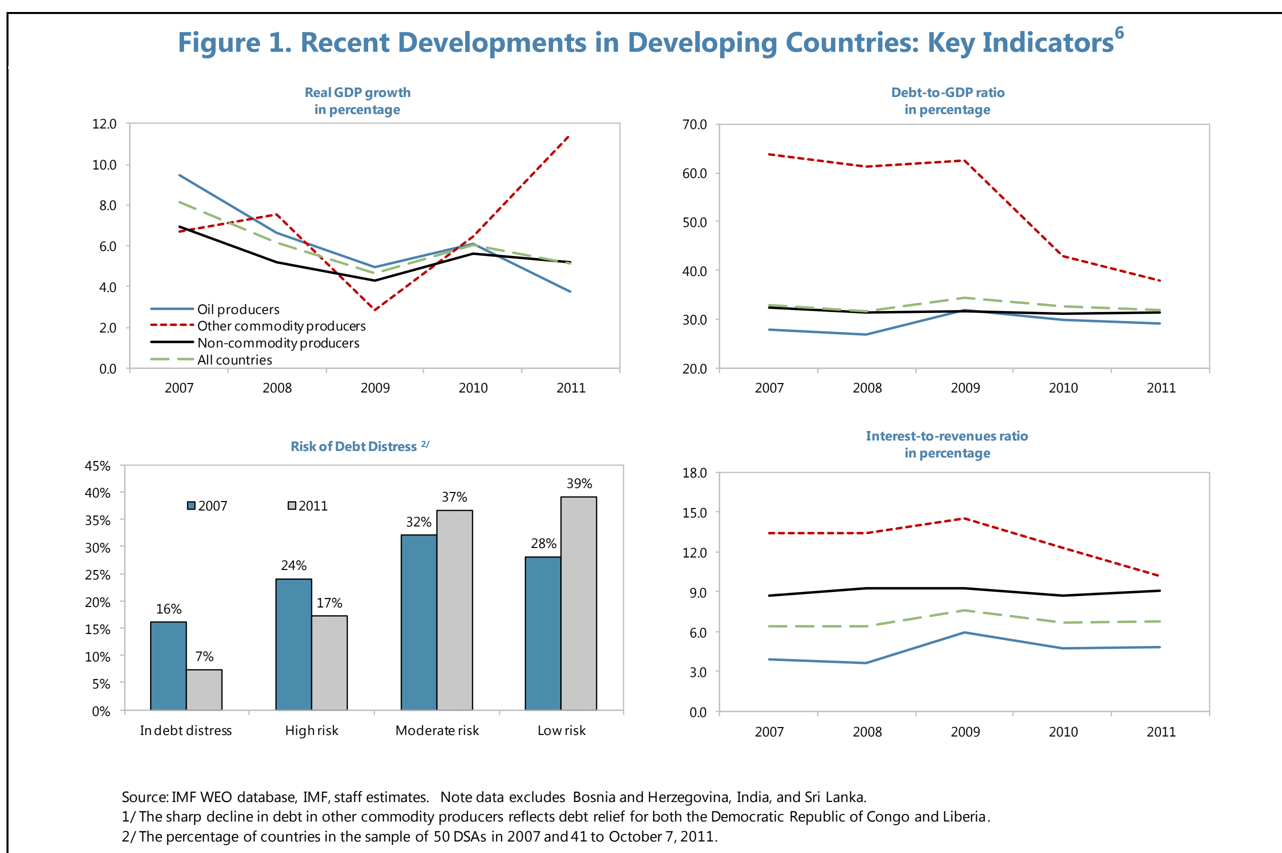
[1] This paper focuses on countries that are eligible to borrow from either the International Development Association (IDA) or the Poverty Reduction and Growth Trust (PRGT). It is the third in a series of joint Bank-Fund papers that focus on progress and challenges in strengthening public debt management in developing countries and responds to the request from the IMF Board for a subsequent update on developments. See "*Strengthening Debt Management Practices—Lessons from Country Experiences and Issues Going Forward*", IMF and World Bank (2007), and "*Managing Public Debt: Formulating Strategies and Strengthening Institutional Capacity*", IMF and World Bank (2009).

[2] These debt relief initiatives created the perception of space for new borrowing, making the need to strengthen PDM frameworks particularly urgent to ensure countries did not rebuild the risk of future debt distress.

creditors or investors, and the importance of robust debt management strategies in mitigating such crises.[3]

5. Despite the virulence and persistence of the global financial crisis, recent economic performance in developing countries has been broadly positive.[4] For instance, real GDP growth is estimated at around 5 percent for the median low-income country in 2011. The robustness of the real sector outlook reflects the positive impact of countercyclical measures that many developing countries were able to adopt because of the pre-crisis build-up of buffers and the strengthening of domestic economic and market capacity. The level of public debt in developing countries has remained broadly stable (Figure 1). Overall, the interaction of past debt relief and positive economic growth has helped reduce the number of developing countries in, or at high risk of, debt distress.[5] Nevertheless, despite improvements, significant financial resources are still being used in servicing debt (on average around 12 percent of revenues), indicating the debt burden remains a critical policy constraint.

Figure 1. Recent Developments in Developing Countries: Key Indicators[6]



Source: IMF WEO database, IMF, staff estimates. Note data excludes Bosnia and Herzegovina, India, and Sri Lanka.
1/ The sharp decline in debt in other commodity producers reflects debt relief for both the Democratic Republic of Congo and Liberia.
2/ The percentage of countries in the sample of 50 DSAs in 2007 and 41 to October 7, 2011.

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[3] See discussions in "*Managing Public Debt and Debt Markets through a Crisis*", IMF (2011).

[4] See IMF (2012), "*Managing Global Growth Risks and Commodity Price Shocks—Vulnerabilities and Policy Challenges for Low-Income Countries*".

[5] See IMF and World Bank (2012), "*Revisiting the Debt Sustainability Framework for Low-Income Countries*". Debt distress signals the point at which countries face repayment difficulties.

[6] See Appendix I for the list of countries included in the sample.

6. Overall, although portfolio structures are not uniform, developing countries' debt portfolios continue to be dominated by official sector external debt.[7] This is reflected in a relatively higher level of exchange rate risk (Table 1). However, the generally long tenors and amortizing structures of multilateral and bilateral loans mitigate this risk, while their maturity and interest rate structure also helps contain refinancing and re-fixing risks.[8] These positive elements help offset vulnerabilities in domestic debt portfolios, where the still relatively short maturity of available debt instruments results in higher refinancing and re-fixing risks. Finally, the low cost of concessional borrowing and of some semi-concessional borrowing[9] also helps offset the generally higher cost of commercial and market-based borrowing (Figure 2). A key goal of an effective debt management strategy is to help manage portfolio costs and risks by identifying the mix of debt instruments (maturities, currencies and interest rate structures) that is consistent with the authorities' medium-term debt management objectives.

Table 1. Portfolio Risk in Selected Countries—Key Indicators

	Average	Max	Min
Level of debt			
Outstanding debt/GDP (%)	39%	73%	13%
Exchange rate risk			
Foreign exchange debt/Total debt (%)	71%	94%	50%
Refinancing risk			
Average time to maturity (years)	11.0	17.5	6.0
Average time to maturity (domestic debt)	3.6	9.1	0.5
Average time to maturity (external debt)	13.5	20.0	6.6
Debt maturing in next 12 months (% of total debt)	15%	34%	2%
Interest rate risk			
Average time to re-fixing total debt (years)	10.3	15.3	4.0
Debt re-fixing in next 12 months (% of total debt)	23%	56%	3%

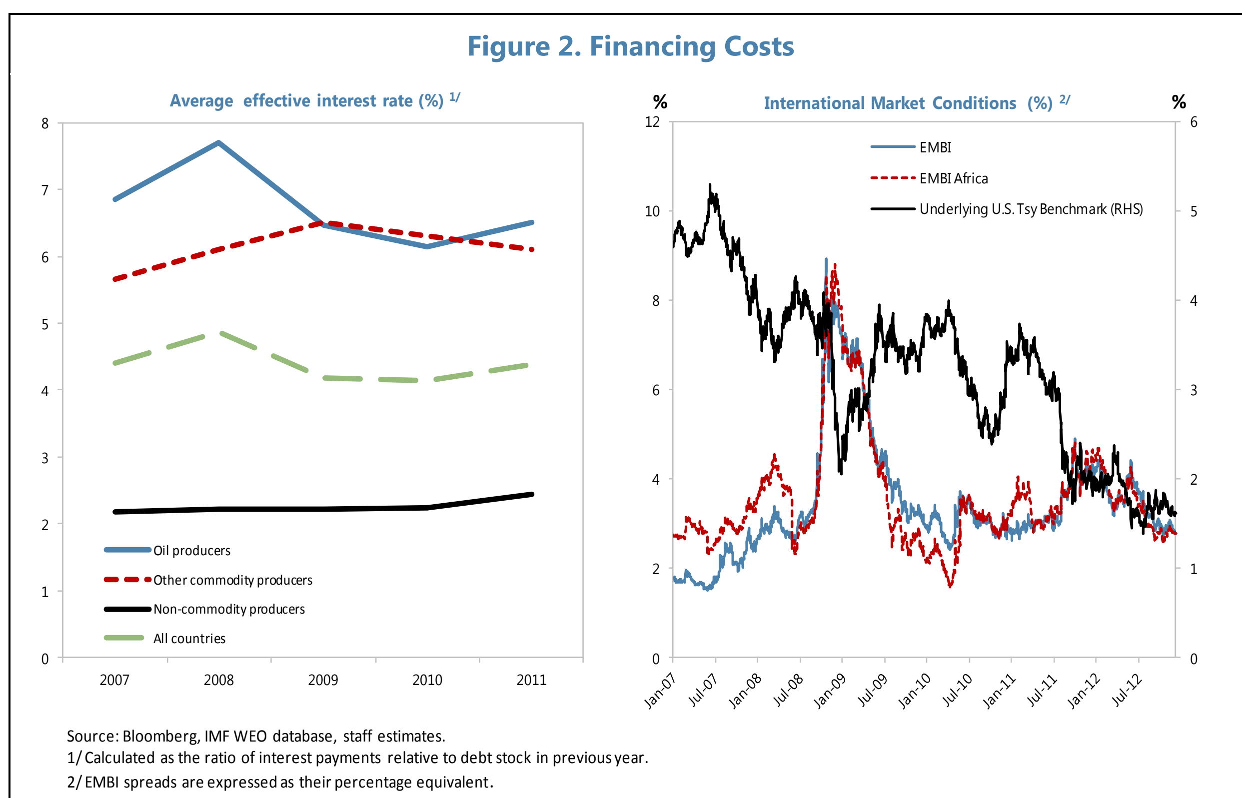
1/ Covers central government debt in countries that received joint Bank-Fund MTDS TA missions, including Armenia, Cape Verde, Côte d'Ivoire, Ethiopia, the Gambia, Ghana, Guatemala, Kenya, Kyrgyz Republic, Malawi, Moldova, Mongolia, Mozambique, Paraguay, Rwanda, Senegal and Tanzania. Data refer to the respective date of the last MTDS mission.
Source: IMF-WB MTDS TA reports.

[7] IMF and World Bank (2009), "*Managing Public Debt: Formulating Strategies and Strengthening Institutional Capacity*."

[8] The risk that interest rates move against the sovereign when it comes time to re-fix an interest rate; this differs from refinancing risk to the extent that the portfolio contains variable (or floating) rate debt.

[9] Semi-concessional or quasi-concessional borrowings are loans from bilateral or multilateral creditors that are contracted at rates less than those the country could secure in the market, but which do not meet the minimum grant element of 35 percent.

Figure 2. Financing Costs



Source: Bloomberg, IMF WEO database, staff estimates.
1/ Calculated as the ratio of interest payments relative to debt stock in previous year.
2/ EMBI spreads are expressed as their percentage equivalent.

7. The importance of effective capacity to manage debt is reinforced by recent changes to Bank and Fund debt-related policies. The review of the Bank-Fund Debt Sustainability Framework (DSF) for Low Income Countries (LICs) and greater flexibility in limits on nonconcessional borrowing in Bank and Fund programs reflect the recognition that countries may need to borrow on nonconcessional terms to finance key infrastructure investment. The shift towards nonconcessional sources of financing is further aggravated by the potential decline in official development assistance (ODA). For example, net ODA by members of the OECD Development Assistance Committee fell by 2.7 percent in 2011, with country programmable aid anticipated to stagnate between 2013 and 2015.[10]

8. This paper reviews progress in strengthening debt management practices in developing countries since the program was endorsed in March 2009. It responds to the request from the IMF Board for a progress report. It focuses on the delivery and results of the capacity building program and on challenges identified through its implementation.[11] It also discusses how changes in the Bank and Fund policy frameworks support these capacity building efforts. The following sections cover: delivery of the Bank-Fund TA program, status of performance

[10] See the *UN Secretary General Report on the International Financial System and Development* (2012).

[11] Initially the program was targeted at low-income countries; however, it was subsequently expanded to include some lower middle-income countries that are IDA-eligible. See Appendix I for a full list of countries included in the sample.

and areas of progress, links with the broader Bank-Fund policy agenda and lessons and challenges going forward.

DELIVERY OF THE BANK-FUND TA PROGRAM

9. Since 2009, Bank and Fund staffs have provided debt management support through a range of TA channels (Figure 3). An integrated architecture of instruments has been developed that has proven to be flexible enough to meet the large variety of individual country situations, including taking a programmatic approach when needed. At the core of the engagement is an understanding of countries' needs, which can be achieved through (i) a formal diagnostic, such as the DeMPA; (ii) a focused TA mission, including, for example, a joint Bank-Fund MTDS mission; (iii) a more general TA mission; or (iv) country self-assessment. Once needs are identified, a capacity building action plan can be developed, for example, through a Bank-assisted Debt Management Reform Plan mission. Tailored TA on key analytical and operational issues can then be delivered to help implement specific elements of the action plan. For instance, the Bank and Fund have provided tailored TA on the legal and institutional aspects of debt management that are critical for enabling the design and implementation of an effective debt management strategy, while other TA partners have helped address deficiencies in debt recording, another critical enabling element.[12]

10. The key components of the work program are:

- The Debt Management Performance Assessment (DeMPA), which assesses the strengths and weaknesses of a country's institutional arrangements for PDM.

- The MTDS program, which provides technical and operational guidance on how to determine a medium-term debt management strategy that targets a composition of the debt portfolio consistent with the government's preferences with regard to the cost-risk trade-off and long-term debt sustainability.

- The Debt Management Reform Plan which sets out a detailed and sequenced country-owned action plan that aims to alleviate the weaknesses identified in PDM institutions and operations. It details expected outputs and outcomes, actions, sequencing and milestones.[13]

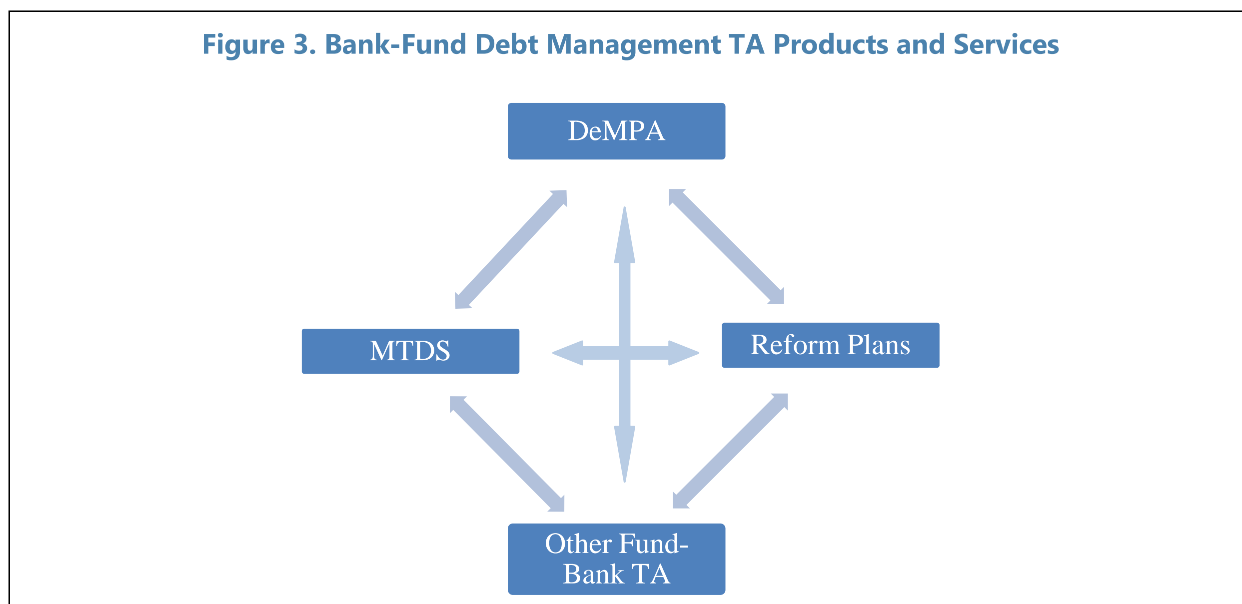
- Targeted capacity building and TA, that can be provided on request in specific areas of PDM (e.g., drafting a legal framework to underpin borrowings and guarantees). These activities are customized and sequenced according to country specific needs, priorities, and absorption capacity.

[12] See "Developing a Medium-Term Debt Management Strategy (MTDS)—Guidance Note for Country Authorities", IMF and World Bank (2009) for a discussion of the enabling framework.

[13] In the case of Bank-assisted Debt Management Reform Plans, it will also provide an estimate of budget and resources required to implement the plan.

11. These activities complement one another in supporting overall PDM reform. They also complement other related capacity building and TA efforts, including financial sector TA related to the Financial Sector Assessment Program (FSAP), other domestic debt market development initiatives, such as the Global Emerging Markets Local Currency Bond Program, or targeted Fund TA and other macro-fiscal TA related to strengthening public financial management (PFM). Overall, these activities are supported by broad knowledge sharing activities, including an extensive program of training and outreach, and the dissemination of related policy, research and operational papers.[14]

Figure 3. Bank-Fund Debt Management TA Products and Services



12. Under this overarching program, 59 developing countries have received some assistance from the Bank and/or Fund to support capacity building efforts in the area of debt management.[15] Depending on countries' needs and preferences, support has either involved a discrete engagement or more comprehensive and sustained follow-up programs (see Figure 4 and Background Paper, Table 1). The pace of delivery of the DeMPA and MTDS programs has been broadly in line with that originally envisaged.[16] Collaboration and coordination between the Bank and the Fund staff in the area of PDM has been reinforced by the joint delivery of the MTDS TA program. The delivery and positive impact of this overall TA program illustrates the benefits of a

[14] This includes activities supported by the Bank's Debt Management Facility (such as the Debt Managers' Practitioners' Program (DMPP), the Debt Managers' Peer Network, and the Annual Stakeholders' Forum), along with the joint regional workshops on the MTDS framework.

[15] See chapter 1 of the accompanying background paper for a detailed analysis of the delivery of the TA program.

[16] The initial program envisaged up to 20 DeMPAs per year and applying the MTDS framework in 4-6 countries (implying up to 12 missions taking into account the anticipated need for a follow-up mission) per year; this level of activity was costed in the 2007 paper. On average, 13 DeMPAs have been undertaken and 7 MTDS missions delivered per year. Over the same period, an average of 6 Debt Management Reform Plan missions per year—following up on DeMPAs but not costed in the 2007 paper—were also delivered. Note these figures also do not include DeMPAs or MTDS missions delivered beyond the set of developing countries identified in Appendix I.

broad-based partnership with country authorities and other TA providers (Box 1).[17] The positive impact and partnership benefits have also been recognized in the early findings of the forthcoming external evaluation of the Bank's Debt Management Facility (DMF).

Box 1.The MTDS Program—Partnership in Action

Collaboration and coordination between the Bank and the Fund in the area of PDM has been reinforced by the joint delivery of the MTDS related TA program. This builds on the long history of collaboration on these issues, such as the drafting of the joint "*Guidelines for Public Debt Management*" and follow-up publications, as well as related TA activities. Bank and Fund staffs continue to work together to enhance the quality of the program. In particular, the Bank and Fund MTDS Practitioners Group meets regularly to coordinate mission delivery, brainstorm on technical and analytical issues and form a consensus on key issues. These activities complement other coordination efforts covering broader TA requests in the area of debt management and debt market development, which have been recognized as one area of progress in SM/10/54, "*Implementation of the Joint Management Action Plan on Bank-Fund Collaboration*".

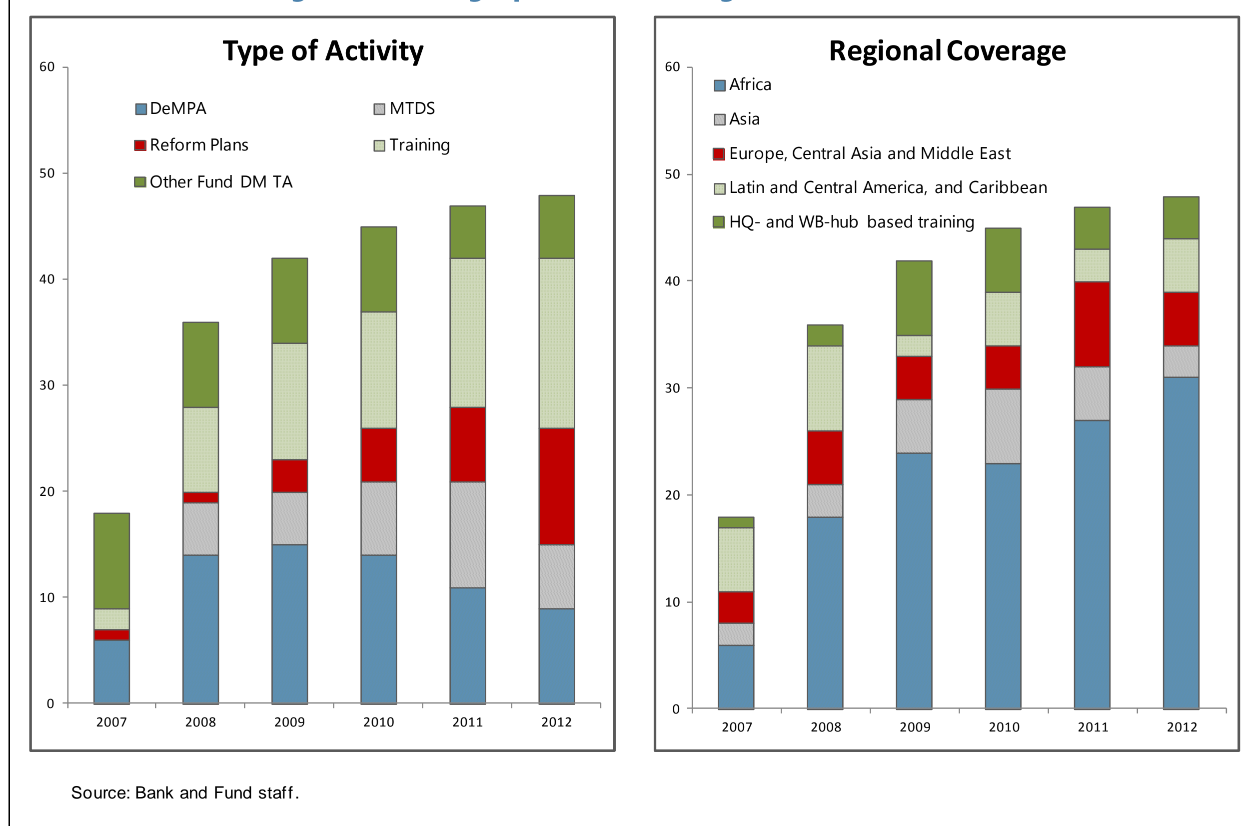
Partnership with country authorities has proved critical in the effectiveness of MTDS missions. Bank and Fund staffs have built on their shared experience to enhance the effectiveness of country-level TA interventions. In particular, mission teams have adapted their approach to more actively engage TA-recipients in the hands-on design of the analyses and reports. For instance, in the initial stages of the program, the Bank-Fund team would present the outcome of the strategy analysis at the conclusion of the mission; now, technical counterparts are encouraged to take responsibility for presenting the analysis to senior policymakers, with the support of the Bank-Fund team. These changes have contributed to a 'learning by doing' culture and enhanced country ownership, fostered the active use of MTDS analysis by country authorities, and further facilitated the production of a formal debt management strategy.

In addition to Bank-Fund collaboration, partnership with other providers of TA has proved beneficial. The MTDS program was designed to include the participation by other international and regional TA providers in debt management, such as the Center for Latin American Monetary Studies (CEMLA), the Debt Management Section of the Commonwealth Secretariat, the Debt Management Program of the United Nations Conference on Trade and Development (DMFAS-UNCTAD), Debt Relief International, the Macroeconomic and Financial Management Institute of Eastern and Southern Africa (MEFMI), and the West African Institute for Financial and Economic Management (WAIFEM). Their participation is supported through the DMF, which has the coordination in service delivery with these implementing partners (IPs) as a key objective.[1/] This collaboration and continuous engagement helps build the capacity of IP staff and consultants, and enhances the quality and consistency of advice to client and developing countries while also reducing duplication.

1/ Launched in November 2008, the DMF for Low-Income Countries (LICs) is a grant facility financed through a multi-donor trust fund to support the scaling up and accelerated implementation of the Bank's debt management work program in DMF eligible countries. To date the DMF has supported work in over 50 developing countries See http://go.worldbank.org/BO5WOYO460.

[17] Of those 23 countries that have received an MTDS TA mission, several have published a formal debt management strategy (including Ghana, The Gambia, Kenya and Tanzania) while others have presented a formal MTDS to ministers, cabinet or parliament as relevant (including Cape Verde, Kyrgyz Republic, Malawi, Moldova, Mozambique, and Rwanda).

Figure 4. Scaling Up of Debt Management TA Activities



Source: Bank and Fund staff.

13. Building on this experience, the Bank has expanded its debt management TA program to strengthen capacity at the sub-national level. This responds to increased demand from sub-national entities that are borrowing either in the markets or from bi- and multi-lateral sources. To reflect the critical differences between sovereign and sub-national debt management, staff developed a sub-national DeMPA tool[18] that takes into account the specific inter-governmental framework, and the fiscal and procedural rules of the country on incurring debt.[19]

14. The involvement of other TA partners has supported the delivery of the program. In addition to the Bank's IPs, a variety of short-term external experts also helped resource the delivery of the TA work program. Their participation on missions has had the added benefit of ensuring the wider population of debt management experts and consultants share a common understanding of the key issues. This means that follow-up TA, or a more prolonged TA engagement, can be effectively delivered by other experts, allowing Bank-Fund staff to focus on priority cases.

[18] The tool has been subject to external review and has been piloted in Lagos and Ondo states in Nigeria, Rio de Janeiro State in Brazil, DKI Jakarta in Indonesia and the metropolitan municipality of Lima, Peru. The subnational DeMPA tool and Guide are available at http://go.worldbank.org/5AHEF2KF70.

[19] For instance, in most countries sub-national debt management activities may only marginally affect monetary policies. As such, these aspects are not given prominence in the sub-national tool.

STATUS OF PERFORMANCE AND AREAS OF PROGRESS

15. The application of the DeMPA tool over the past five years provides a rich information set on the status of debt management practices in developing countries.[20] Since 2007, a total of 54 developing countries have been assessed using the DeMPA tool, about sixty percent of which have received subsequent TA under the program. The results across all countries assessed post-2009 highlight the key analytical, institutional and operational challenges countries continue to face (Figure 5).

16. In general, performance in the areas of legal framework, debt recording, and coordination with monetary policy has been relatively strong. At the same time, deficiencies in key analytical functions, including development of a robust debt management strategy, assessment of cost effective and beneficial terms for external borrowing, and cash flow forecasting and cash management, have been revealed. These weaknesses have the potential to become more acute, and will often impact more adversely, as the characteristics of the debt portfolio change and become more complex.

17. Poor performance in the area of debt management strategy was generally related to the quality of the exisiting strategy and weaknesses in the associated governance process. While many countries do have some form of strategy, it is often unpublished, does not have the approval of the highest policy makers and is not supported by an institutional decision making process that ensures its regular production, implementation, and updating. Moreover, most strategies are not underpinned by robust cost-risk analysis of the debt portfolio.[21]

18. Weaknesses associated with policies and procedures related to external borrowing are of particular concern given the likely shift in countries' borrowing choices. Less than one-third of countries in the sample analyzed met the minimum requirements in this area. Scores on this indicator show that there is: (i) a low degree of assessment of the most beneficial/cost-effective borrowing terms and conditions; and (ii) a general absence of documented procedures for borrowing in foreign markets.

19. Weaknesses in operational and institutional factors further aggravate deficiencies in countries' analytical capacity. Deficiencies in operational controls, business continuity planning, and staff responsibilities significantly increase overall risk as the range of borrowing instruments increases. The absence of effective and independent auditing of debt management policies,

[20] Using a set of standardized criteria, DeMPA measures performance across the following functions: (1) governance and strategy development; (2) coordination with macroeconomic policies; (3) borrowing and related financing activities; (4) cash flow forecasting and cash balance management; (5) operational risk management; and (6) debt records and reporting.

[21] Note that these results may precede country efforts to strengthen specific areas. In particular, several countries have received a joint Bank-Fund MTDS mission subsequent to their initial DeMPA and have made progress in the area of strategy development.

functions and performance undermines accountability and becomes an increasing problem as decisions about borrowing choices become more complicated.

Figure 5. Cross-Country Summary Assessment of Debt Management Performance

Source: World Bank, Results aggregated from 28 countries that conducted DeMPAs and finalized reports during 2010-12.

Note: Results in each category are aggregated to show the share of the sample meeting the minimum requirements as defined in the DeMPA tool.

20. While the overall results show weaknesses in critical areas, progress is evident in those countries that received subsequent TA support. In particular, where Bank-Fund TA engagement—through MTDS missions, debt management reform plan missions or other TA—has been sustained, countries appear to show most progress. Results of DeMPA follow-up missions show improvements in many aspects of debt management, including organizational structures, the legal framework, debt management strategy development and operational risk management (Table 2). At the same time, there were hardly any improvements in the areas of audit and evaluation of debt management operations, and cash management. This highlights the importance of ensuring that senior policy makers remain committed and focused on strengthening capacity. Progress has also been more sustainable where it has been complemented by the inclusion of debt management reform elements in the design of a Bank loan or Fund program arrangement.

21. Experience also illustrates the importance of training in sustaining country authorities' capacity to understand and utilize the debt management TA received. Since 2009, 51 training events covering a range of debt management related issues have been delivered by the Bank and Fund, training over 300 country participants during the period. In addition, hands-on training is a key element of Bank-Fund MTDS missions and plays a key role in ensuring country authorities can

apply the framework and analytical tool in their specific country circumstance. Training events have also promoted the development of peer networks where learning and experiences can be shared among practitioners.

22. Key areas of progress and challenges that countries continue to face are detailed below.

Table 2. Progress in Strengthening PDM Capacity—A Summary[1/]

DeMPA Indicator	Steps taken	Country
Legal framework	Strengthened legal framework	Burundi, Haiti, Malawi, Sierra Leone, Togo, Mongolia, Sao Tome Principe, Sierra Leone
Managerial structure	Upgraded or modernized organizational structure	Burundi, The Gambia, Ghana, Kenya, Maldives, Malawi, Tanzania, Senegal
	Enhanced institutional framework governing loan guarantees	Malawi, Senegal, Sierra Leone,
Debt management strategy	Strengthened middle office	Bangladesh, Papua New Guinea, The Gambia, Liberia, Malawi, Nicaragua, Sierra Leone, Moldova
	Debt management strategy development based on cost-risk analysis	Bangladesh,Burkina Faso, Ethiopia, Maldives, Cape Verde, The Gambia, Ghana, Malawi, Mali, Moldova, Mozambique, Nigeria, Nicaragua, Rwanda, Tanzania
Audit	Strengthened audit function	Malawi, Mongolia
Domestic Borrowing	Deepening domestic market development	Bangladesh, Kenya
Cash Flow Forecasting & Cash Balance Management	Strengthened cash management	Burkina Faso, Malawi, Maldives
Segregation of Duties, Staff Capacity & BCP	Reduced operational risk	Bangladesh, Bhutan, Maldives, Rwanda, Togo
Debt Records and Debt Reporting	Improved debt recording and reporting	Bhutan, Burundi, Liberia, Burkina Faso, Malawi, Mali, Mozambique, Nigeria, Togo

1/ This reflects areas where countries have taken explicit steps to enhance capacity; it does not measure the effectivensess or completeness of the steps taken. This is based on information at the time of a mission visit.

Source: DeMPA and Reform Plan updates, mission staff, and country authorities.

A. Debt Management Strategy Development

23. Analytical capacity remains constrained and initiatives are needed to augment incentives and retain skilled debt management staff. The results of initial DeMPAs show that some countries did have a formal debt management strategy in place, but there were deficiencies with respect to analysis of cost and risk. This is of particular concern where countries contract (or could contract) significant amounts of nonconcessional or market-based debt.

24. To help address this deficiency, capacity building efforts have centered on the MTDS TA program. The objective of the MTDS TA program is to help country authorities assimilate the MTDS framework for developing a debt management strategy, as well as build capacity in the use of the associated quantitative tool (MTDS Analytical Tool).[22] TA missions are complemented with workshops that provide training for country officials on the conceptual and operational aspects of debt management. Sound understanding of the framework, along with focused training, should, over time, enhance the quality of debt management strategies and strengthen portfolio risk analysis.

25. Several countries have made progress in developing a formal and explicit debt management strategy. Ghana and Kenya have published and regularly updated their debt management strategy. Others (e.g., Cape Verde, Malawi, Moldova, Mozambique, and Tanzania) recently presented their first formal debt management strategy to ministers, cabinet or parliament as relevant. Other countries (e.g., Bangladesh) have yet to publish a formal strategy, but are using the MTDS analysis internally to inform policy making. Reflecting these developments, the results of follow-up DeMPAs show progress in almost half the assessed countries (e.g., The Gambia, Malawi, and Mongolia).

26. Success in developing a debt management strategy is reflected in the improved coordination between debt management and fiscal and monetary policies. Given the explicit recognition of key policy inter-linkages in the MTDS framework, success in understanding and using the toolkit should reinforce the importance of sound medium-term fiscal, monetary and financial sector policies. In addition, by providing insight into the country's debt dynamics, strengthened capacity to formulate debt management strategy will enhance countries' public debt sustainability analysis.

27. The flexibility of the MTDS toolkit has helped countries better evaluate changes in the structure of borrowing. The quantitative analysis has proved especially relevant to countries that have or anticipate graduating from IDA-only access. For instance, in Malawi the quantitative tool helped quantify the potential cost-risk mix of increasing access to international capital markets versus further reliance on domestic debt markets. The quantitative tool has also allowed borrowing constraints defined in the context of an economic program (e.g., limits on net domestic financing) to be examined.

28. Country authorities have proved capable of using the MTDS quantitative tool to evaluate the impact of alternative macroeconomic scenarios on their preferred borrowing compositions. For instance, country authorities in Cape Verde, Ghana, Kenya, Nigeria, and Tanzania used the MTDS quantitative tool to examine the potential implications of contingent liabilities.[23]

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[22] The tool helps quantify the costs and risks of alternative borrowing strategies. In response to user feedback—both Bank and Fund staff, and country authorities—the tool has been revised to make it more user friendly and operationally more robust. The new version has been extensively tested in the field and reviewed by external peers, and has been released on the Bank and Fund websites.

[23] The nature of contingent liabilities may differ—including guarantees, on-lending to state owned enterprises (SOEs) and to parastatals, and support to the banking sector.

This analysis has helped country authorities better understand debt dynamics by showing that the ranking of various strategies in terms of their cost and risk does not necessarily change with the size of the financing requirement.[24] However, it does challenge country authorities to consider whether their preferred strategy remains feasible when the financing requirement rises. For instance, while the preferred strategy might entail meeting 50 percent of financing needs through concessional financing, limits on the availability of that financing might render that strategy infeasible when the gross financing requirement increases.

B. Institutional and Organizational Areas

29. Work to strengthen institutional and organizational arrangements has been delivered through Bank-assisted debt management reform plan missions and other Bank and Fund tailored TA. The focus of these TA activities included helping to strengthen the legal framework (e.g., Malawi, Sao, Tome & Principe, and Sierra Leone), address technical deficiencies in key back-office functions, and develop the evaluation and audit capacities of countries' debt operations (e.g., Bhutan and Mongolia).

30. There has been significant progress in the integration of debt management responsibilities. A number of countries have taken steps to improve the coordination of debt management responsibilities to help enhance efficiency and reduce impediments to the development of an effective debt management strategy. While similar in purpose, the approaches have taken different forms. Some (e.g., Bangladesh, Bhutan, and Togo,) set up institutional coordinating committees, while Ghana upgraded the existing debt office. Some countries (e.g., Moldova, Maldives, Malawi, Tanzania, and Vietnam) set up a front, middle and back-office structure, while others (e.g., Bangladesh and Papua New Guinea), with a more complex division of responsibilities, have tried to strengthen the middle office capacity to analyze the total debt portfolio and formulate a debt management strategy. However, fragmentation of operations remains a challenge in a number of countries (e.g., Vietnam, Pakistan, and Zambia). In addition, when the central bank is (de facto) involved in the exercise as the principal (e.g., Zambia, Bhutan, and Tanzania), lack of clarity in its role in managing domestic or external public debt may contribute to potential policy conflicts.

31. Improvements have been seen in data reporting and recording, and in procedures to mitigate operational risks. The availability of timely and good quality debt data can mitigate some of the impediments to debt management strategy formulation that arise from organizational fragmentation, and support evidence-based policy-making and transparency. Some countries (e.g., Bhutan, Burkina Faso, Mali, Mozambique, and Nigeria) improved the quality of debt data reporting and /or prepared a debt statistical bulletin presenting the key risks of their existing debt portfolios. Guinea Bissau and Tanzania strengthened the debt data recording and management software systems; while others (e.g., Maldives, Bhutan, and Togo) improved operational risk management through enhanced back-up procedures. More than half of the countries in the sample now meet

[24] Provided the change in the level of borrowing does not change the credit risk premium.

DeMPA requirements for timely and accurate debt data records for both external and domestic debt; this has facilitated enhanced debt monitoring across developing countries.[25] However, obtaining timely data on commitments, disbursements, and loan guarantees remains a challenge for several countries (e.g., Bangladesh). And weaknesses in debt recording have resulted in some countries accumulating debt arrears, although these weaknesses are now being addressed. In addition, while the framework for debt monitoring focuses on public and publicly guaranteed debt, country authorities should also consider the potential risks associated with private sector debt, especially external debt, and potential strategies to monitor that.

32. Progress in supporting the development of domestic government securities markets has been facilitated by improvements in cash management practices.[26] Improvement in countries such as the Maldives, Malawi, and Bangladesh centered on the publication of Treasury bills/bonds issuance calendars and borrowing procedures, and, in some instances, establishing a single treasury account or setting up a cash management committee to improve cash forecasting and enhance coordination. These developments are expected to help improve adherence to the pre-established auctions calendar and further support market development.

LINKS WITH BROADER BANK AND FUND POLICY AGENDA

33. The strengthening of debt management practices is often explicitly recognized as a critical component of a country's economic program. A number of Fund programs incorporate structural conditionality aimed at enhancing the country's debt management practices and, in particular, its debt management strategy. Improvements in countries' institutional arrangements and operational approaches have been targeted to help sustain the benefits of policy adjustment and improved macro-economic performance (Box 2).

34. Bank-Fund policy frameworks for nonconcessional borrowings allow more flexibility to countries with enhanced debt management capacity.[27] Where the latest Country Policy and Institutional Assessment (CPIA) and Public Expenditure and Financial Accountability (PEFA) assessment measures of debt management capacity conflict, staff consider both the availability and quality of the debt management strategy, plus a country's track record of accessing market financing and managing nonconcessional borrowing, coupled with the availability of timely debt data, as necessary conditions for effective debt management. This highlights the complementarity between the staffs' TA-program and the broader policy agenda.

[25] A joint IMF/World Bank public sector debt database covering 40 developing countries can be found at: http://www.worldbank.org/qpsd.html

[26] These include better cash forecasting.

[27] See "*Debt Limits in Fund-Supported Programs—Proposed New Guidelines*", IMF (2009) and "*IDA's Nonconcessional Borrowing Policy: Progress Update*", World Bank (2010).

Box 2. Examples of Country Program Support for Enhanced Debt Management

- In Ghana, efforts to incorporate and embed the MTDS framework have been supported by two successive program structural benchmarks related to the publication of a medium term debt management strategy in both 2010 and 2011. That has helped ensure that the analytical capacity developed with the support of Bank and Fund advisory and technical assistance missions has been fully incorporated into the operational routines of the Aid and Debt Management Department.

- In Kenya, the debt management operations were fragmented and disorganized before 2003. In 2004, the Bank recommended a sequenced capacity building plan based on the previous needs assessment. The Bank has led the effort in collaboration with other implementation partners. By 2009, all but one of the proposed reform actions had been completed. Subsequently, the 2011 Article IV report praised the authorities' prudent medium term debt strategy, despite challenges driven by the increase in domestic financing costs and the depreciation of the currency. The MEFP for the three-year ECF arrangement, approved on January 31, 2011, incorporates the authorities' commitment to reflect exposures to contingent liabilities, including those that arise through projects funded through public private partnerships, into the medium term debt management strategy.

- In Cape Verde, given the impact of the worsening of the global outlook, Fund staff and the authorities recognized the need to enhance debt management and continue to strengthen oversight of contingent liabilities to safeguard debt sustainability. Consequently, the authorities committed to present to the council of ministers a medium-term debt strategy report discussing debt levels, composition and desirable trends as a structural benchmark under the policy support instrument (PSI). This commitment was met, with the presentation of the country authorities' first medium term debt management strategy in November 2011.

- In Mauritania, the IMF ECF (2010) included the requirement to design an overall external debt management strategy. Given problems signaled in institutional arrangements and capacity (identified by the DeMPA 2010), the Bank, at the authorities request, sent a reform plan mission (March 2012) with a joint Bank-Fund MTDS mission following in June 2012.

- In Burundi, the IMF ECF (2008) included the requirement to undergo a DeMPA and develop an action plan to increase staff capacity. Accordingly, to ensure sustained engagement, the DeMPA mission in April 2012 was followed by a debt management reform plan mission in July 2012.

- In Comoros, the Bank-Fund HIPC Decision Point document (2010) included three triggers on debt management: installation of debt management software, publication of reports, and alignment of the debt management office mission with staff capacity. To support this agenda, a DeMPA followed in 2011, with a debt management reform plan mission in 2012.

- Other IMF programs also incorporate measures focused on the development and publication of a strategy as part of the core structural conditionality. Examples include Kyrgyz Republic (2011) and Burkina Faso and Côte d' Ivoire (both 2012).

35. The recent enhancement of the Bank-Fund DSF for LICs has strengthened the links with the MTDS work. The MTDS program, with a main focus on debt composition complements the LIC DSF which focuses on the sustainability of debt and evaluates the risk of debt distress. The outcome of the MTDS analysis supplements a country's debt sustainability analysis (DSA) by providing a more granular assessment of how the characteristics of different financing instruments and the debt redemption profile can transmit shocks into the stock of debt and be reflected in interest payments in the medium term.[28]

36. Improvements in debt management play an important role in enhancing overall public financial management (PFM) at the country level. The design of an effective debt management strategy requires consistency with the medium-term fiscal framework. Furthermore, debt management is strongly linked to core aspects of PFM as it requires predictability in the budget process and of fiscal outturns, as well as sound cash management practices. Recognition of these complementarities and of the relevance of integrating debt management institutional reform into PFM capacity building programs has helped improve the downstream implementation of debt management TA. For example, in Bangladesh a project on implementing downstream PFM reforms included debt and cash management as core components. Similar projects to ensure downstream implementation and strengthening of debt management functions are being developed in Vietnam and Tanzania, among others. Likewise, linking with the PEFA yielded positive externalities in the case of Nigeria, where the DeMPA findings informed the PEFA exercise.

37. Work on debt management practices is complemented by a number of other initiatives led by the international community. In 1998, the Inter-Agency Task Force on Finance Statistics (TFFS) reconvened to enhance the quality of external debt and international reserves data. To improve debt data reporting, the TFFS prepared the *External Debt Statistics Guide* (2003); this is currently being updated, with the pre-publication version expected to be released in 2013. And to complement that, the TFFS published the *Public Sector Debt Statistics Guide* in December 2011.

38. Enhanced debt management also plays a critical role in supporting broader initiatives to develop domestic debt capital markets. An effective and published debt management strategy should provide a medium-term perspective on the volume and type of new domestic debt; this, coupled with clear operational procedures, provides a degree of transparency that can support more active markets. In turn, deeper and more liquid domestic debt markets increase the range of feasible debt management strategies, enabling country authorities to achieve different cost-risk trade-offs. Recognizing the importance of developing domestic debt markets for enhancing financial stability and economic growth, the G20 heads of state endorsed an action plan to support the development of local currency bond markets (LCBMs) in November 2011. Both the Bank and Fund are actively supporting this initiative, which will complement their respective debt management work.

[28] This complements other efforts to enrich the DSA, such as recent work to explore the impact of public investment surges in LICs. See, Buffie, E., et al, (2012) "*Public Investment, Growth, and Debt Sustainability: Putting Together the Pieces*", IMF Working Paper 12/144.

LESSONS, GAPS AND CHALLENGES GOING FORWARD

39. The implementation of the program suggests a number of relevant lessons. Debt management reform and capacity building is complex and takes time. Country authorities' capacity to develop and implement effective debt management strategies is affected by both their analytical capacity and the enabling institutional structure. Lessons from the past three years of program implementation include:

- Effective debt management cannot be seen in isolation. Building robust capacity requires efforts to strengthen practices across a number of parallel work streams, and often involves organizational and legal changes that require sustained commitment of senior policy makers.
- Capacity building requires on-going support. To encourage country ownership and policy makers' ongoing commitment, efforts are made to engage and coordinate with Bank and Fund country teams on the delivery of the TA work program. Close involvement of the country team ensures not only a continued connection with the authorities, but helps place the various debt management reforms into the broader context of the country program to ensure their further implementation. This also helps ensure debt management reform plans and specific TA are tailored to country-specific requirements and priorities.
- The role of effective debt management within broader Bank and Fund policies has supported the absorption of TA efforts. Progress has been more sustained where it has been complemented by related design elements in a Bank loan or Fund program arrangement, or where TA engagement has been more extensive. This is reflected in their follow-up DeMPAs. For example, progress is evidenced in the legal framework (e.g., Haiti, Sierra Leone and Sao Tome & Principe), debt management strategy development (e.g., Cape Verde, Ghana, Kenya, Malawi and Nigeria), and operational risk management (e.g., Bangladesh and Bhutan).
- Strong country ownership of the reform effort is critical for success. This has both increased demand for, but also helped secure commitment to, capacity building. It is critical that support is prioritized to countries where senior policymakers are committed to follow-through.
- Demand for debt management TA is growing significantly. This partly reflects an increase in countries' awareness of the MTDS and DeMPA frameworks, and their links to the debt limits and nonconcessional borrowing policies, but also the broader recognition of the significance of debt management challenges.

40. Capacity constraints and institutional fragility remain acute in many developing countries. Exogenous factors and prioritization conflicts have also impeded efforts to improve the institutional and operational capacity for debt management. This argues for continued support from the Bank and Fund if PDM policies and practices are to become fully resilient. Such progress also requires significant time and sustained commitment on the part of country authorities.

41. The systematic management of operational risk must be improved in most countries. Most countries do not have adequate, explicit, and well understood procedures governing their debt management operations. For example, debt transactions that are entered into and verified by the same individual increase the risk of mistakes and fraud, and put at risk the integrity of the data. Codes of conduct guiding debt management operations are often missing or rarely implemented; these are especially important where regular interface with the market is involved. These risks are amplified by staff turnover and dependence on very limited resources, with many debt offices depending on only one or two key qualified staff. Consequently, the preparation of formal procedures manuals and implementation of systematic business process has been factored in as a key element in the staff-delivered TA.

42. Overall, the current work program has made significant progress in responding to demand by authorities for improving their debt management capacity. The program has earned a reputation for facilitating the delivery of quality debt management services and products. Country authorities reported their capacity has increased as a consequence of receiving support under the program. Preliminary findings from the forthcoming external evaluation of the DMF also affirm the program has contributed to positive achievements on the ground.

43. Looking forward, the economic landscape will remain challenging. The near-term economic outlook remains broadly favorable, with positive growth rates supported by domestic demand, including from investment. The main risks to the outlook include the risk of an intensification of financial stress in the euro zone and a sharp fiscal adjustment in the United States.[29] Vulnerabilities are accentuated by the fact that policymakers have not had time to restore policy buffers to pre-crisis levels. This would limit the scope for any counter-cyclical measures were these risks to materialize.

44. In parallel, the nature of financing challenges facing developing countries is changing. Economic growth has led to higher income levels but it also implies that some countries will graduate from International Development Assistance (IDA) eligibility. This will change the nature of available official sector financing and reduce a country's access to concessional financing. While this will likely imply higher cost, the financial choices available will increase. Furthermore, the depth and length of the current economic crisis is increasing fiscal pressure on official donors, which might also reduce the medium- and longer-term availability of aid.

45. Substituting market-based sources of financing may be viable for some. In the current low interest environment, foreign investors are aggressively searching for yield, with strong demand for bonds from new issuers (Appendix II).[30] However, accessing the international capital markets brings its own challenges. While the direct portfolio risks—refinancing and exchange rate risks—are

[29] See *World Economic Outlook* (Fall 2012), *Sub-Saharan Regional Economic Outlook* (Fall 2012) and *Global Economic Prospects for Development* (January 2012).

[30] A record $3.75 billion has been raised by debut issuers in international capital markets in 2012, with Bolivia's public issue being three times over-subscribed and Zambia's offering also being about 16 times over-subscribed, reflecting high investor demand.

generally recognized, the indirect challenges of absorption and cost of carry are often not adequately assessed (Box 3).[31] And, in most cases, domestic markets remain very constrained in both size and tenors. This points to a need for continued progress on both the macroeconomic front (to generate greater capacity for savings) and broader financial sector development (to provide a robust regulatory environment or enhance market intermediation) if domestic debt is to become a stable source of financing.

Box 3. Market-Based Sources of Financing: Challenges

Access to international capital markets is often seen as a viable alternative source of financing (e.g., Kenya, Tanzania and Zambia). While market conditions—though volatile—remain relatively favorable for a number of developing countries (Figure 2 above), refinancing risks linked to "sudden stops" cannot be overstated, especially in the current turbulent global outlook.

Country authorities need to carefully consider the trade-offs involved in determining the size of any issue. Access to foreign markets is often contemplated for large amounts that cannot be readily absorbed. This increases risks (including of inefficient uses of borrowed resources) and the cost of carry (i.e., the costs incurred while the funds are under-utilized).[1/] However, a larger size is more likely to be liquid and will allow inclusion in key indices; these factors can broaden the investor base and reduce the direct cost of borrowing. In contrast, a smaller issue size would be easier to absorb, mitigating the cost of carry, but typically carries an illiquidity premium. Anecdotal evidence suggests that a country could pay up to 200–250 basis points on an illiquid issue. Given the scale of the potential costs and risks involved, the trade-offs need to be well understood so that country authorities can make informed choices and not simply respond to market demand.

The syndicated loan market may prove a suitable funding channel in testing access to international markets.[2/] The lower volumes and more tailored structures that can be accessed can alleviate some of the problems associated with the cost of carry and absorption capacity. Also, this instrument may complement eventual international bond issuance (e.g., Kenya), and help mitigate potential rollover risks. However, costs in this market can be high and maturities may not be as long as in the bond market so, again, the trade-offs need careful consideration.

Countries' ability to rely on domestic market resources tends to be constrained by the relatively low level of market development. Countries with an already-established and relatively robust local institutional investor base may be able to access long-term funding for public investment purposes (e.g., Kenya, Nigeria) in their domestic market. However, the strategy needs to be carefully designed to mitigate the risks of "crowding out" and avoid creating unnecessary obstacles to private sector activity. However, in countries where banks are the only viable investor, domestic markets remain small, with short maturities; in this case, long-term financing is likely to be limited and very costly. More broadly, enhancing domestic debt market access will require a sustained policy commitment to financial sector deepening supported by a sound macroeconomic environment. Consequently, it will take considerable time to expand capacity in a meaningful way.

1/ For instance, assume a country borrows $750 million for five years to finance a three-year investment at an all-in-cost of 5 percent. Then, given returns on safe assets are effectively zero, the carry cost could amount to $25 million in the first year, with a further carry cost of $12.5 million in year two. This means the return on the associated investment has to be equivalent to at least 6 percent per annum over the five years of the bond just to help cover this cost. The broader challenges facing countries in accessing international capital markets are discussed in Appendix II.

2/ For instance, Kenya recently accessed this market with a $500 million two-year floating rate loan. Given the then volatile macroeconomic conditions, there was a risk that a debut bond would not have been well received by the market. The loan allowed them to secure the needed financing in a low key manner that helped mitigate reputation and execution risk. It has also provided scope to resolve some key macroeconomic challenges (e.g., inflation has declined) before going to the wider market.

[31] In addition, an over-reliance on international capital markets could undermine efforts to develop the domestic debt market.

46. As countries move towards more commercial borrowing, a robust debt management strategy, coupled with sufficient capacity to implement it, becomes critical. To the extent available, maximizing concessional financing tends to be a preferred debt management strategy for developing countries. However, this strategy becomes less feasible as income rises. As countries substitute nonconcessional and market-based financing sources, higher financing costs could contribute to deterioration in debt dynamics. This shift in debt composition will also aggravate portfolio risks. In particular, the typical bullet-payment structure of market-based debt increases refinancing risk and, to the extent countries need to continue their reliance on external debt, exchange rate risk.[32] In this context, the analytical capacity to measure and monitor portfolio risks and evaluate effectively alternative borrowing choices becomes critical.

47. Reflecting these factors, demand for TA is likely to increase further. Limited TA resources—both skills and financial, imply competing demands will need to be prioritized so that TA resources can be used most effectively. In particular, given the criticality of country ownership for success, TA delivery will need to prioritize countries that show strong commitment to the reform process. For instance, a two-track approach could be adopted with priority given to those countries with explicit commitments set out in a Bank loan or Fund program, while also maintaining a broader pipeline to meet the needs of other countries that have set out a clear commitment to capacity building. Similarly, requests for follow-up TA could be explicitly dependent on the implementation of earlier recommendations, or other evidence of progress. In addition, a country's financing situation could also be taken into account, especially with respect to demands for Bank-Fund MTDS TA. Here, priority could be given to countries facing a near-term phasing out of IDA-financing and / or with specific plans to borrow from international capital markets or increase significantly domestic debt. For other countries, more emphasis could be given to strengthening key elements of the enabling framework, such as debt recording or institutional arrangements, than delivery of a Bank-Fund MTDS mission.

48. The importance of the Bank-Fund TA work program will increase as countries expand their access to nonconcessional and market-based sources. To ensure such developments do not aggravate underlying vulnerabilities, analytical and risk management capacity will need further development, coupled with a strengthening of institutional and governance arrangements in many countries.

49. Bank and Fund staffs are committed to providing continued support in this area. However, this will be subject to the resource constraints that both the Bank and Fund face. Work is ongoing on addressing these constraints to ensure this work program can be sustained into the medium-term.

[32] Exchange rate risk increases because of its higher concentration on one point in time and dependence on the exchange rate value at the date rather than a smoothing effect coming from the currency fluctuations over time.

Appendix I. List of Developing Countries

Countries covered by the TA program described in this paper consist of all IDA-eligible countries.

Oil & Gas producers

Angola
Bolivia
Cameroon
Chad
Congo, Republic of
Mauritania
Nigeria
Papua New Guinea
São Tomé and Príncipe
Sudan
Timor-Leste, Dem. Rep. of
Yemen

Other commodity producers

Congo, Dem. Rep. of
Ghana
Guinea
Kyrgyz Republic
Liberia
Mongolia
Sierra Leone
Uzbekistan

Others

Afghanistan
Armenia
Bangladesh
Benin
Bhutan
Bosnia and Herzegovina
Burkina Faso
Burundi
Cambodia
Cape Verde
Central African Rep.
Comoros
Côte d'Ivoire
Djibouti
Dominica
Eritrea
Ethiopia
Gambia, The
Georgia
Grenada
Guinea-Bissau
Guyana
Haiti
Honduras
India
Kenya
Kiribati
Kosovo
Lao People's Dem. Rep.
Lesotho
Madagascar
Malawi
Maldives
Mali
Marshall Islands
Micronesia, Fed. Sts.
Moldova
Mozambique
Myanmar
Nepal
Nicaragua
Niger
Rwanda
Samoa
Senegal
Sri Lanka
Solomon Islands
Somalia
St. Lucia
St. Vincent & Grenadines
Tajikistan
Tanzania
Togo
Tonga
Uganda
Tuvalu
Vanuatu
Vietnam
Zambia
Zimbabwe

Appendix II. Trends in Accessing International Capital Markets

50. Several developing economies have started to explore new funding alternatives to expand their financing sources. In particular, countries have accessed, or are considering accessing, international capital markets for the first time. This may be a reflection of limitations in domestic market financing in these countries.

51. The prospect of accessing international capital markets gained considerable traction prior to the crisis. Global liquidity was abundant and international investors were actively searching for diversification and yield. Improvements in underlying macroeconomic conditions in issuing countries also supported this trend. However, the crisis resulted in effectively a "sudden stop" in international capital market access in late-2008, This brought to the fore one of the key risks involved in reliance on this market—sudden stops can be unpredictable and of uncertain length.

52. Market access appears to have been reestablished. Although established emerging market issuers began to regain access early in 2009, the first low-income country to test the waters post-crisis was Senegal with its debut bond in December 2009 (Table 3). Since then, seven different sovereigns have tapped the international capital markets for the first time, issuing a total of US$5.6 billion. Three of these issuers were African—Angola, Namibia, and Zambia. Activity in these frontier markets has been further supplemented with a new issue and debt exchange by Senegal, and a further novel issuance by Namibia (South African rand-denominated bond).

53. Despite the historical low levels of interest rates (Figure 6), these new funding sources are not without challenges.[33]

- The broad macroeconomic environment needs to be supportive: Typically, a track record of good economic performance and a stable macroeconomic outlook are necessary preconditions for an issuance to be successful.

- The external environment also needs to be supportive, with significant investor interest and risk appetite in evidence.

- The issuer requires sufficient technical capacity. These operations tend to be highly specialized and require specific technical knowledge. Although legal and financial advisers can provide some of this expertise, the issuer needs sufficient in-house capacity in order to make the right decisions.

[33] See Das, et al., "*Strategic Considerations for First-Time Sovereign Bond Issuers*," IMF Working Paper 08/261; November 1, 2008.

- Transaction costs can be significant. Issuance in international capital markets involves an array of other transaction costs. These range from fees for advisory services, to engaging trustees and paying agents, to fees for any related transactions (e.g., currency swaps).

54. In addition, there are some key risk exposures that need careful management.

- **Dealing with large issuance proceeds.** In many circumstances, the issuance size is larger than the amount of resources needed for the country at that immediate point in time. This means that there is an associated carry cost until resources can be invested; it also increases the potential risk that resources are allocated inefficiently or wasted.

- **Substantial refinancing risk.** The typical bullet structure of these bonds concentrates refinancing exposure. In particular, issuers are exposed to the risk of a "sudden stop" in market access when the bond is due. The closure of the market for several months post-Lehman is one example of this. Similarly, concentrating large repayments of debt at one point in time also increases the impact of any shock to exchange rates.

Table 3. Recent Debt International Issuance by Emerging and Developing Countries

Country	Issuance Date	Maturity Date	Yield at issue (%)	Tenor	Volume ($ mn.)	Currency
Ghana	27-Sep-07	4-Oct-17	8.500	10	750	USD
Sri Lanka	17-Oct-07	24-Oct-12	8.250	5	500	USD
Gabon	6-Dec-07	12-Dec-17	8.250	10	1,000	USD
Georgia	7-Apr-08	7-Apr-13	7.500	5	500	USD
Senegal	15-Dec-09	22-Dec-14	9.473	5	200	USD
Belarus	26-Jul-10	3-Aug-15	9.207	5	600	USD
Montenegro	7-Sep-10	14-Sep-15	8.000	5	254	EUR
Albania	28-Oct-10	4-Nov-15	7.625	5	407	EUR
Jordan	8-Nov-10	12-Nov-15	4.125	5	750	USD
Nigeria	21-Jan-11	28-Jan-21	7.126	10	500	USD
Namibia	27-Oct-11	3-Nov-21	5.835	10	500	USD
Angola	14-Aug-12	16-Aug-19	7.186	7	1,000	USD
Zambia	13-Sep-12	20-Sep-22	5.625	10	750	USD
Bolivia	22-Oct-12	29-Oct-22	4.875	10	500	USD
Mongolia	5-Dec-12	5-Jan-18	4.125	5	500	USD
Mongolia	5-Dec-12	5-Dec-22	5.125	10	1,000	USD
Average			6.930	7	607	

Figure 6. Selected African Countries—Bond Yields