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Report on Workshops on Debt Sustainability in Low-Income Countries in Paris, Berlin, and Accra in May/June, 2003

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1. Staff participated in three workshops on debt sustainability and development financing in low-income countries in May/June 2003. The workshops were organized by the Agence française de Développement (AfD), in Paris (May 14), InWEnt, Capacity Building International, Germany, in Berlin (May 19-20), and the Commonwealth Secretariat and the World Bank in Accra (June 9-10). Besides Fund and Bank staff, participants included government officials from both creditor and donor countries and representatives from academia and NGOs. While covering a broad agenda, the workshops provided an opportunity to exchange ideas on many of the issues outlined in the paper on "Debt Sustainability in Low-Income Countries—Toward a Forward-Looking Strategy". This statement summarizes the exchange of views, as background for an informal Board seminar on the topic. Taking account of Directors' comments in that seminar, Fund and Bank staff will jointly organize a workshop in Washington, in September, with a view of preparing an operational paper with specific policy proposals for Board discussion before the end of the year.

2. Participants in the three workshops broadly agreed with the paper's main premise that prudent debt management strategies are an essential complement to strong policies in achieving and maintaining long-term debt sustainability. Many speakers highlighted, in particular, the challenges in ensuring that the financing necessary to help achieve the millennium development goals (MDGs) is provided on terms that are consistent with sustainability. The general view was that resolving this tension requires both sound policies in the countries concerned and a substantial increase in the grant share of aid from the international community. Attempts to finance the MDGs on terms that would lead to reemerging debt problems would undermine their achievement. Indeed, financing on appropriately concessional terms and in support of strong policies and institutional reform was seen as critical in achieving the higher growth rates necessary to meet the MDGs.

3. There was general agreement on the need to base sustainability assessments on a range of indicators, to monitor and assess the level and composition of both domestic (public) and external debt, and to follow a flexible, country-specific approach. While various speakers

recognized the NPV of debt relative to GDP, exports, and government revenues as important indicators of debt crises in the past, many pointed to the critical role of debt-service indicators, particularly in relation to fiscal revenues. In this context, some participants argued that debt sustainability assessments should not focus rigidly on NPV-based indicators, but that countries should have flexibility to increase NPV ratios as long as debt service relative to fiscal revenues remained sustainable. Other participants observed that even if an economy were able to generate foreign exchange, the government could still lack the ability to mobilize these revenues to service its external debt, particularly if a large fraction of export earnings accrued to foreign investors. While a comprehensive coverage of debt was generally considered appropriate to assess sustainability—including, in particular, the domestic claims on the public sector—a number of speakers expressed concerns that inclusion of public-enterprise debt could create difficulties in obtaining financing for these enterprises, as creditors feared requests for debt forgiveness in the future. Others were concerned that exempting public enterprise debt could lead financing to be channeled in a roundabout and non-transparent way, resulting to buildup of debt in public enterprises enjoying implicit government guarantees.

4. Many participants highlighted the danger of overly optimistic projections, which were considered a key factor behind the buildup of unsustainable debt levels in the past. While stressing the need to attain a better understanding of the factors that drive sustainable growth, they encouraged the Fund and the Bank to be more cautious in future projections and to make rigorous use of stress tests and sensitivity analyses to assess the risks to debt sustainability in the event of weaker-than-expected outcomes. A number of speakers emphasized the extreme vulnerability of many low-income countries to exogenous shocks, particularly in the form of declining commodity prices, and the need for developing mechanisms that assist countries in dealing with these shocks. Specific proposals included counter-cyclical lending (perhaps with floating tranches), domestic-currency lending, and procedures to delay or waive debt service in the event of adverse movements in commodity prices—which is complicated, however, by the experience that such movements have often proven to be persistent. Participants generally agreed that vulnerability to shocks made it all the more important for countries to pursue a prudent borrowing strategy in good times, to create room for counter-cyclical borrowing when the economy is hit by adverse shocks.

5. Finally, participants emphasized the importance of low-income countries' gaining improved access to foreign markets, so that they can successfully promote and diversify exports to grow out of poverty, reduce their vulnerability to shocks, and to eventually graduate from reliance on aid. While domestic policies play an important role in this strategy, its success equally hinges on export market access, particularly to the industrial world.