INTERNATIONAL MONETARY FUND AND
INTERNATIONAL DEVELOPMENT ASSOCIATION

Enhanced HIPC Initiative: Possible Options Regarding the Sunset Clause

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I. Introduction

1. **A "sunset clause" was included in the HIPC Initiative to prevent it from becoming a permanent facility.** The clause has been extended three times and is now due to take effect at end-2004. During Bank and Fund Board discussions of the most recent extension in 2002, a number of Board members expressed reservations about an extension beyond 2004 and requested suggestions from staff on alternative options for dealing with the debt overhang of heavily indebted poor countries (HIPCs) that have not yet become eligible for debt relief under the Initiative.[1,2] This paper responds to the Boards' requests and presents several options to address the expiry of eligibility owing to the sunset clause. Once the Boards provide guidance, the staff will make one or more formal proposals in the HIPC Progress Report scheduled for discussion prior to the Annual Meetings.

2. The paper is organized as follows: Section II provides background on the sunset clause and discusses the implications of its expiry at end-2004; Section III outlines four policy options and the implications of each; and Section IV provides concluding remarks.

II. Background

3. **A sunset clause was stipulated in the 1996 Program of Action to prevent the HIPC Initiative from becoming a permanent facility, minimize moral hazard, and encourage the early adoption of programs of reform.** The Program of Action stated that "the Initiative would be open to all HIPCs that pursue or adopt programs of adjustment and reform supported by the IMF and IDA in the next two years, after which the Initiative would be reviewed and a decision made whether it should be continued."[3] As described in Annex I, the 1998 review of the Initiative included a two-year extension followed by two more extensions.

4. **Letting the sunset clause take effect at end-2004 would leave several HIPCs with debt in excess of HIPC thresholds after traditional relief**.[4] As of end-June 2004, eleven HIPCs had not reached their decision points and have estimated NPV debt stocks in excess

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[1] All references to debt are to public and publicly-guaranteed external debt.

[2] Countries pre-qualify for HIPC debt relief if they satisfy the following requirements before the sunset clause comes into effect: (i) they are IDA-only and PRGF-eligible; (ii) they have debt in excess of the HIPC thresholds after the application of traditional debt relief; and (iii) they have started to establish a track record of policy performance through putting in place Fund- and IDA-supported programs.

[3] "A Program for Action to Resolve the Debt Problems of the Heavily Indebted Poor Countries—Report of the Managing Director of the IMF and President of the World Bank to the Interim and Development Committees," September 20, 1996, page 2 (EBS/96/152, Revision 1 and SecM96-975/1).

[4] Hereafter "debt in excess of HIPC thresholds" refers to "debt in excess of HIPC thresholds *after traditional relief*" unless indicated otherwise.

of HIPC thresholds.[5] These countries would have to start to establish a track record of policy performance by putting in place a Fund- or IDA-supported program prior to the sunset date in order to subsequently qualify for HIPC relief. Programs that count toward meeting the track record are: an approved PRGF/ESAF arrangement or a completed mid-term review, an up-to-date Policy Framework Paper (PFP), and/or adjustment operations supported by IDA at some time since 1995 (one year prior to the HIPC Initiative). Accordingly, six of the eleven pre-decision point HIPCs with debt in excess of HIPC thresholds have met this requirement, as they have had a Fund-supported program since 1995.[6] The remaining five HIPCs (Comoros, Liberia, Myanmar, Somalia, and Sudan) have not had a Fund- or IDA-supported program because of protracted political, governance, conflict, and arrears problems (see Annexes II and III for more details). Consequently, assuming the sunset clause takes effect at end-2004 as currently envisaged, these five HIPCs would be ineligible for debt relief under the HIPC Initiative, unless they were to put in place Fund- or IDA-supported programs prior to the end of the year.

5. **The Bank and the Fund are working to assist conflict-affected HIPCs.** As suggested above, the process of putting in place a Fund or IDA-supported program has proved difficult for most of the 11 HIPCs that have not reached their decision points. The Bank and Fund have extended support to conflict-affected countries—the Bank through the Bank's Low-Income Countries Under Stress (LICUS) program and the Post-Conflict Support Fund, and the IMF through its Emergency Post-Conflict Assistance (EPCA) support fund.[7] The World Bank works with other stakeholders in the establishment of Transitional Support Strategies in an effort at facilitating re-engagement. Although the requirements for establishing a track record and other decision point conditions are substantial, the Boards have emphasized the importance of consistently maintaining the policy requirements of the HIPC Initiative.

III. POSSIBLE OPTIONS

6. **This section examines options for dealing with the sunset clause against the background described above.**

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[5] These countries are: Burundi, Côte d'Ivoire, Central African Republic, Comoros, Republic of Congo, Lao P.D.R., Liberia, Myanmar, Somalia, Sudan, and Togo. Four additional HIPCs (Angola, Kenya, Vietnam and Yemen) have estimated NPV debt burdens below HIPC thresholds and are therefore not expected to qualify for HIPC relief.

[6] Burundi, Central African Republic, Republic of Congo, Côte d'Ivoire, Lao P.D.R. and Togo.

[7] The April 2001 joint Bank-Fund paper on "Assistance to Post-Conflict Countries in the HIPC Framework" stated that: (i) Bank and Fund staffs should provide technical assistance in post-conflict societies and assess needs early; (ii) the Bank's Post-Conflict Fund should be scaled up to assist countries with arrears and broaden the scope of pre-arrears clearance IDA grants; (iii) the Fund should mobilize funds to reduce the cost to HIPCs of the Fund's Emergency Post-Conflict Assistance to low-income countries; and (iv) the track record prior to the decision point should emphasize institution building and governance, and consideration could be given to an early decision point for post-conflict countries combined with a relatively longer interim period. See Development Committee, Assistance to Post-Conflict Countries and the HIPC Framework, April 20, 2001, (DC2001-0014), http://www.siteresources.worldbank.org/DEVCOMMINT/Documentation/90015301/DC2001-0014(E)-Post%20Conflict.pdf.

A. Option 1: Let the Sunset Clause Take Effect

7. **This option would allow the sunset clause to take effect at end-2004.** This would imply that those HIPCs that have had a Fund- or IDA-supported program since 1995—six of the eleven pre-decision point HIPCs estimated to have debt in excess of HIPC thresholds—plus any remaining HIPCs that may adopt a Fund- or IDA-supported program by end-2004—could potentially benefit from debt relief under the HIPC Initiative. However, countries that have not met the track record requirement would be left with debt levels in excess of the HIPC thresholds after the application of traditional relief.

B. Option 2: Extend the Sunset Clause

8. **A second option is to extend the sunset clause by another two years**. This option would provide more time for current HIPCs as well as other countries that may subsequently meet the HIPC eligibility requirements.

Advantages:

- This option provides the same treatment to countries that have in place a Fund- or Bank-supported program before or after end-2004, that reach the decision point before or after end-2004, and the same treatment to debt acquired before or after end-2004; and

- This mechanism, which has been utilized previously, avoids complicating modifications. It would be the simplest modality to implement the G8 statement from the Sea Island Summit.[8]

Disadvantages:

- It is unlikely that a two-year extension would provide enough time for many of these countries to meet the requirements, namely adoption of IMF- and IDA-supported programs, for reaching the decision point; and

- The credibility of a fourth extension and the resulting risk that it may need to be extended again could have adverse incentive effects. Previous extensions did not have the desired effect of encouraging the adoption of reform programs in all HIPCs.

C. Option 3: Extend the HIPC Initiative Solely for Countries Meeting Predefined Criteria

9. **A third option is to "grandfather" all PRGF-eligible, IDA-only countries found to have debt in excess of HIPC thresholds after the application of traditional relief as of**

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[8] See "Debt Sustainability for the Poorest," Press Release of the G-8 Summit in Sea Island, Georgia, USA, June 10, 2004, http://www.g8usa.gov/061004b.htm.

end-2004, for a five-year period to reach the decision point.[9] Countries meeting such criteria could include the 11 HIPCs estimated to have debt in excess of HIPC thresholds as well as a few additional countries.[10] After being "grandfathered," such HIPCs would still need to establish a track record of policy performance under a Fund- and IDA-supported program and meet the other requirements to reach the decision point, including having debt in excess of HIPC thresholds as indicated by a detailed debt sustainability analysis. Future eligibility for HIPC relief would be limited to these countries. Under this option, considerations and calculation of topping-up at the completion point would remain unchanged from the current framework.

Advantages:

- The HIPC Initiative would not become a permanent facility in the sense of providing contingent support to an unrestricted group of countries;

- Borrowing after end-2004 would not help the country qualify for HIPC debt relief; and

- Under the assumption that the five-year extension is not renewable, it provides a firm end point to new entrants into the Initiative.

Disadvantages:

- Debt acquired after end-2004 would still qualify for debt relief;

- After 2004, IDA-only and PRGF-eligible countries with similar debt burdens could receive different treatment depending whether or not they have been "grandfathered" as of end-2004; and

- Introduces pressure for a further extension after five years if some of the "grandfathered" countries had not reached their decision point by then.

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[9] The determination of NPV debt in excess of HIPC thresholds after the application of traditional relief would be determined after end-2004, when data becomes available.

[10] Preliminary estimates suggest that Haiti may have debt in excess of HIPC thresholds after the application of traditional relief at end-2003 and projected for 2004. Other potential candidates may include the Kyrgyz Republic and Tajikistan, whose projected NPV-of-debt to fiscal revenues ratios are 351 percent and 275 percent, respectively for 2004, before the application of traditional relief (see IMF and World Bank, "Recent Policies and Performance of the Low-Income CIS Countries—An Update of the CIS-7 Initiative," April 23, 2004, page 16, http://lnweb18.worldbank.org/ECA/CIS7.nsf/ECADocByUnid/85256C370063EBBE85256C1400591146/$FILE/Umbrella_050304.pdf). If their debt ratios are determined to be higher than the HIPC thresholds after the application of traditional relief as determined in a Debt Sustainability Analysis, they would meet the debt eligibility criteria for HIPC relief.

D. Option 4: Limit Debt Subject to Debt Relief by Using a Cutoff Date

10. **A fourth option is to grandfather debt as of a given cutoff date—end-2004—while not limiting the countries that could be eligible, for a five year period to reach the decision point.**[11] After 2004, any IDA-only, PRGF-eligible country with debt in excess of HIPC thresholds that meets the other requirements, would be eligible for HIPC debt relief. However, HIPC debt relief would only apply to end-2004 debt. There are several ways to implement this option.[12] Whatever the modality chosen, topping up assistance at the completion point if justified could not finance the costs resulting from additional debt incurred after 2004.

Advantages:

- Eliminates the incentive to borrow after 2004 in anticipation of more debt relief;

- Depending upon the precise operational modality chosen, provides equal access to countries that may be eligible for HIPC relief both before and after 2004; and

- Limits the debt to be covered by the Initiative to debt outstanding at end-2004.

Disadvantages:

- May not provide sufficient relief for HIPCs to have debt reduced to reach HIPC thresholds at the time of the decision point.

- Treats countries that reached decision points before end-2004 differently from those that reach decision points thereafter; and

- Introduces pressure for a further extension after five years if some of the eligible countries have not reached the decision point by then.

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[11] The list of qualifying countries would exclude post-completion HIPCs. This option would *not* preclude from debt stocks additions due to interest and penalties accrued on end-2004 debt.

[12] One possibility would be to calculate at decision point the NPV of debt and debt relief using all relevant parameters (debt, exports, fiscal revenues, openness criteria, discount and exchange rates) as of end-2004 even though the decision point would be reached after 2004. Since the calculation would be entirely based on end-2004 data, this option could also be viewed as a subset of Option 3 that limits the debt stock subject to debt relief. Another possibility would be to calculate at decision point debt relief based on end-2004 debt data, but using the other relevant parameters as of the date of the decision point. This would be consistent with current HIPC debt relief calculations, but it would limit the debt subject to relief to that outstanding and disbursed as of end-2004 (plus interest and penalties). If the Boards recommend Option 4, then staffs will examine these operational modalities and their implications further and recommend the most appropriate modality in the September 2004 HIPC Progress Report.

E. Possible Costs

11. **The cost of providing debt relief under the various options is uncertain, but could be substantial.**[13] The cost of Option 1 is more predictable than that of other options, as only six countries are likely to be covered, and this cost, estimated at US$5.7 billion in 2003 NPV terms, has been estimated as part of the semi-annual HIPC costing exercise (see Table 1). However, the cost could change substantially because these countries have not had a formal debt sustainability analysis and may not reach the decision point for some time. The cost of Options 2 is likely to be higher than that of Option 1 since a few more countries could meet the HIPC requirements. The additional cost would depend on the countries which qualify, their debt burdens, and the timing of decision point. The cost of Option 3 is likely to be at least US$18.9 billion in 2003 NPV terms for the 11 HIPCs (discussed above) and could be higher if additional countries are grandfathered and would also depend on the evolution of key parameters. The cost of Option 4 is likely to be less (and more predictable over time) than that of Option 3, because relief would not be provided on debt disbursed after 2004.

IV. Concluding Remarks

12. **Extension of the sunset clause is desirable.** Letting the sunset clause take effect in 2004 (Option 1) would leave a number of HIPCs with debt burdens in excess of HIPC thresholds and leave the international community without a mechanism for dealing with these debts. An extension of the sunset clause as in the past (Option 2) ensures equal treatment of countries qualifying pre- and post-2004 and avoids complicating modifications, but at the risk of requiring a further extension two years hence. Grandfathering countries or debt (Options 3 and 4) allows more time for the already identified HIPCs and potentially other countries that may meet the HIPC criteria by the respective deadlines to establish a policy track record that would enable them to benefit from debt relief under the Initiative. Option 3 limits new entrants after 2004 and removes the incentive to borrow to qualify for HIPC debt relief, but maintains the moral hazard associated with accumulating debt post-2004 to maximize relief. Option 4 removes incentives to borrow in anticipation of receiving debt relief, but poses the risk that some countries may not receive sufficient relief to meet the HIPC thresholds at the decision/completion points.

13. **Any of the options chosen will need to be complemented by actions being considered under the low-income country debt sustainability framework.** Further thinking would be needed on how to assist countries that have not reached the decision point by the end of the newly agreed extension period.

[13] No provision has been made in the IMF PRGF-HIPC Trust for the financing of new potential HIPCs' debt (similar to the situation for the protracted arrears cases of Sudan, Liberia, and Somalia). Additional grant resources would, therefore, need to be mobilized before IMF HIPC debt relief can be committed to new countries.

Table 1. Breakdown of Estimated Potential Costs by Main Creditors 1/

(In millions of U.S. dollars, in 2003 NPV terms)

	Countries with Fund-Supported Programs since 1995							Other Countries						
	Burundi	Central African Republic	Congo, Rep. Of	Cote d'Ivoire	Lao PDR	Togo	*Sub-Total*	Comoros	Liberia	Myanmar	Somalia	Sudan	*Sub-Total*	**Total**
Total costs	499	279	1,961	2,694	82	206	*5,721*	97	1,409	589	1,389	9,728	*13,212*	18,933
Multilateral creditors	427	199	337	963	67	123	*2,114*	71	1,103	161	772	2,769	*4,876*	6,990
World Bank	271	107	94	460	27	65	*1,023*	19	189	80	284	720	*1,291*	2,314
Of Which: IDA	271	107	94	0	27	65	*563*	19	78	80	284	720	*1,180*	1,744
IBRD	0	0	0	460	0	0	*460*	0	111	0	0	0	*111*	571
IMF	18	21	41	175	2	15	*271*	1	629	0	272	1,172	*2,074*	2,345
AfDB/AfDF	82	43	149	240	0	15	*529*	22	186	0	83	202	*494*	1,023
Others	56	28	53	88	38	28	*291*	28	98	81	134	675	*1,017*	1,308
Other creditors 2/	72	80	1,624	1,731	15	83	*3,606*	26	307	428	616	6,960	*8,337*	11,943
Paris Club	49	20	1,239	1,063	n/a	80	*2,452*	2	236	385	518	2,287	*3,428*	5,879
Other official bilateral	23	48	45	14	n/a	3	*132*	24	70	0	85	3,806	*3,986*	4,117
Commercial	0	13	340	655	2	0	*1,009*	0	0	43	14	867	*924*	1,933
Memorandum:														
Fund-Supported and Staff-Monitored Programs	PCEA 2003 3/ PRGF 2004	PRGF 2001	PCEA 2000 3/ PRGF 2004	PRGF 2002	PRGF 2001	PRGF 1998, SMP 2001		SMP 2002	SMP 2001	None since the 1980s	None since the 1990s	SMP 2002		

Sources: country authorities and staff estimates.

1/ Data are preliminary and subject to substantial revisions and based on latest data available after full application of traditional relief mechanisms.

(Data for C.A.R., Comoros, Congo Rep. of, Cote d'Ivoire and Togo are based on the end-2000 data; data for Burundi as of end-2001; data for Liberia, Myanmar, Somalia and Sudan as of end-2002; and data for Lao P.D.R. as of end-2003).

2/ All data assumes a stock-of-debt operation on Naples terms (67 percent NPV reduction) as of the base year, and comparable treatment by other bilateral creditors.

3/ EPCA stands for Emergency Post-Conflict Assistance.

HISTORY OF THE SUNSET CLAUSE

1. **The sunset clause stems from the 1996 Program of Action, which established a two-year limit to the HIPC Initiative "at the end of which a comprehensive review would be held to decide whether to continue with the program."** The 1998 review indicated that the sunset clause "reflects the intention that the HIPC Initiative would not be a permanent facility. The sunset clause gives countries an incentive to adopt IDA- and IMF-supported adjustment programs. It also limits the time available for build-up of new debt, and thus provides for relief on debt which mostly predates the Initiative." The 1998 review proposed a two-year extension. The countries which did not meet the entry requirements for the HIPC Initiative at that time were: Angola, Burundi, the Democratic Republic of the Congo, Equatorial Guinea, Liberia, Myanmar, Sao Tomé and Príncipe, Somalia and Sudan. Seven of these countries (all except Angola and Equatorial Guinea) were, in the staffs' view, potentially eligible for assistance as they appeared to have had unsustainable debt ratios (with the caveat of very poor data). Some of these countries were just emerging from conflict, and thus had not reached the stage to be able to enter into IDA- and Fund-supported programs. Furthermore, for some, access to new loans—and thus moral hazard—seemed to be limited. Given these considerations, the Executive Directors of IDA and the Fund agreed to an extension of the original deadline for meeting the entry requirement until end-2000.[14]

2. **In 2000, the sunset clause was extended for a second time.** The countries which still did not meet the entry requirement by then were Angola (which was later dropped from the list, since it was estimated not to require HIPC relief), Burundi, the Democratic Republic of Congo, Liberia, Myanmar, Somalia, and Sudan.[15] The HIPC Progress Report noted that a preliminary analysis of the countries which had yet to pass the entry requirement suggested that it would be very likely that they would need comprehensive debt relief, including from multilateral institutions. Since many of the countries were conflict-affected and undergoing social and political strife, there was considerable uncertainty about the timing of a possible decision point. Staff, therefore, recommended the elimination of the sunset clause so that no time limit would constrain these countries to reach the decision point. However this suggestion was rejected by the Boards of the Bank and the Fund, and a decision was taken to extend the sunset clause by another two years.[16]

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[14] "The Initiative for Heavily Indebted Poor Countries—Review and Outlook," (EBS/98/152, 8/25/98), http://www.imf.org/external/np/hipc/progrept.htm, and September 22, 1998, (DC/98-15), http://www.worldbank.org/hipc/hipc-review/hipc-review-and-outlook.pdf.

[15] Guinea and São Tomé and Príncipe had met the entry requirements.

[16] "The Enhanced Initiative for Heavily Indebted Poor Countries—Review of Implementation," (EBS/00/166, 8/14/00), http://www.imf.org/external/np/hipc/, and September 7, 2000, (SecM2000-487), http://www.worldbank.org/hipc; and "Summing Up by the Chairman of the IMF Executive Board: Enhanced Initiative for Heavily Indebted Poor Countries (HIPC) and Poverty Reduction Strategy Papers (PRSP)—Progress Reports and Review of Implementation," Executive Board Meeting of September 5, 2000 (BUFF/00/147, 9/11/00), http://www.imf.org/external/np/hipc/2000/ehipc.htm, and http://www.imf.org/external/np/hipc/2000/091100.htm.

3. **In 2002, the sunset clause was extended for the third time**. From end-2000 to September 2002, only the Democratic Republic of Congo had started an adjustment program with the IMF and the World Bank. However, the list of HIPCs that were yet to be considered was expanded to 12 countries: Côte d'Ivoire, Burundi, the Central African Republic, Comoros, the Republic of Congo, the Democratic Republic of the Congo, Lao P.D.R, Liberia, Myanmar, Somalia, Sudan, and Togo. Staff proposed that the sunset clause be extended by another two years to end-2004 to provide an opportunity for these countries to begin to establish a policy track record that would allow their consideration for HIPC relief.[17] While the Directors agreed to this extension, several expressed concern about further extensions of the clause in the future, on reputation and moral hazard grounds. Recognizing that the extension up to 2004 would not be sufficient to help all the remaining HIPCs join the Initiative, some Directors suggested extending the sunset clause in the future only on a case-by-case basis.

[17] "Heavily Indebted Poor Countries (HIPC) Initiative—Status of Implementation," (SM/02/264, 8/16/02), http://www.imf.org/external/np/hipc/2002/status/092302.htm, and September 23, 2002, (IDA/SecM2002-0467), http://www.worldbank.org/HIPC.

CHALLENGES TO REACHING THE DECISION POINT BY REMAINING HIPCS

1. Fifteen countries are currently identified as HIPCs, of which four are believed to have debt burdens below the HIPC thresholds after the application of traditional relief. Eleven pre-decision-point countries are therefore potentially eligible for HIPC relief.[18] In addition, an estimated three PRGF-eligible and IDA-only countries may have debt burdens in excess of HIPC thresholds after traditional relief. Since 1996, six countries (Burundi, Central African Republic, Republic of Congo, Côte d'Ivoire, Lao P.D.R., and Togo) have had a Fund-supported program and they are judged technically to have established a track record leading to the decision point.

2. It is useful to review a few characteristics of the eleven countries that are yet to reach the decision point:

- One group of countries has been hindered in reaching the decision point due to continuing difficulties in resolving conflict (Burundi, Central African Republic, Republic of Congo, Côte d'Ivoire, Liberia, Sudan, Somalia and Togo) that have hampered effective policy implementation and institution building.

- A second set of countries has large and protracted arrears, including to multilateral creditors. A concerted international effort would be required for arrears clearance operations (Central African Republic, Comoros, Republic of Congo, Cote d'Ivoire, Liberia, Myanmar, Somalia, Sudan, and Togo).

- Several countries have had limited relationships with the Fund. Myanmar and Somalia have not had any Fund-supported programs since the early 1980s and 1990s, respectively. Moreover, since the launch of the Initiative, relationships between the Fund and Comoros, Liberia, and Sudan, respectively, have been limited to Staff Monitored Program (SMPs), which have not counted towards meeting the track record requirements of the decision point.

3. Under the original framework for the HIPC Initiative, the length of the track record of IDA-and Fund-supported programs prior to the decision point was set at three years. With the enhancement of the HIPC Initiative in September 2000, the Boards indicated that this three-

[18] Burundi, Comoros, the Central African Republic, Cote d'Ivoire, the Republic of Congo, Lao P.D.R., Liberia, Myanmar, Somalia, Sudan and Togo. A Board paper and Debt Sustainability Analysis was prepared for Yemen in 2001 concluding that the country's debt levels were insufficient to qualify for HIPC relief. IMF staff conducted a preliminary debt sustainability analysis on Lao P.D.R. in 2002, which will be updated in the context of the Article IV consultation discussions in July 2004. The results of the analysis are sensitive to the outcome of ongoing discussions between Lao P.D.R. and Russia on debt to the former Soviet Union. A Board paper and Debt Sustainability Analysis has been prepared for Vietnam with the same objective and is expected to be finalized shortly. Angola and Kenya are both not expected to qualify for HIPC relief. It should be noted that all of these countries except Cote d'Ivoire were indicated as subject to the World Bank's Low-Income Countries under Stress (LICUS) approach and most are categorized as conflict-affected.

year requirement should be generally maintained, but agreed that some of the three-year track record could be established between the decision and completion points.[19]

[19] See IMF "Summing Up of the Chairman, Enhanced Initiative for Heavily Indebted Poor Countries—Review of Implementation," (EBM/00/90, 9/5/00). See also IMF "Modifications to the Heavily Indebted Poor Countries Initiatives—Proposed Decision to Amend the PRGF-HIPC Trust Instrument," (EBS/00/9, 1/20/00), in Section III paragraph 2(c). Members could receive credit toward the decision point for programs that were underway prior to the adoption of the Initiative.

COUNTRIES THAT COULD REACH THE DECISION POINT AFTER JUNE 2004[20]

Burundi

Burundi has had post-conflict emergency assistance programs in 2002 and 2003 and more recent progress in the peace process has culminated in the approval of a PRGF-supported program in January 2004. The program for 2004 aims at consolidating the peace process and stabilizing the macroeconomic situation. The World Bank is currently supporting Burundi with the Economic Rehabilitation Credit and a number of other projects planned in the context of a Transitional Support Strategy. That strategy, approved by the World Bank Board on March 7, 2002, has underpinned IDA assistance to Burundi. In addition to the Economic Rehabilitation Credit, it envisages exceptional World Bank assistance to Burundi for HIV/AIDS, capacity building, health care, demobilization and reintegration, and social action.

The Arusha agreement of August 2000 represented a turning point. All but one of the major rebel groups have joined the peace process. After intensive political discussions, including with regional country partners to the peace process, the timing of national elections to end the transitional process has been set for October 2004. A new constitution and electoral and communal law remain to be agreed, however, as does an agreement on military integration of rebel forces leading up to the IDA-funded Demobilization, Disarmament and Rehabilitation (DDR) process.

PRSP Status: Burundi launched its PRSP process in July 2000 and a Joint Staff Assessment of the I-PRSP was reviewed by the Directors of the World Bank and the IMF in January 2004. The World Bank has been providing assistance in consultation and participatory diagnostic analysis. The Burundi authorities recently requested further assistance in this area within the context of preparing the full PRSP. Burundi is one of the first countries to seek assistance under the Diagnostic Trade Integration Study program; the study was done in 2003. A full PRSP is scheduled for mid-2005.

HIPC Status: Burundi faces unsustainably heavy debt service obligations. A Paris Club rescheduling on Naples terms was granted in March 2004. It is expected that a full DSA and preliminary HIPC document will be prepared at the time of the first PRGF Review in late 2004. Subject to satisfactory program implementation, the HIPC decision point could be reached by the time of the second review in mid-2005.

[20] These notes are intended to provide information on the status of countries that have yet to reach their decision points and the factors that affect it. They are based on similar notes in the recent Board document "Initiative for Heavily Indebted Poor Countries—Statistical Update," (SM/04/109, 4/1/04), http://www.imf.org/external/np/hipc/2004/033104.htm and March 31, 2004 (IDA/SecM2004-0184), http://www.worldbank.org/hipc/. The earlier notes have been updated for more recent information and greater focus has been placed on factors and requirements that influence a country's ability to reach the decision point.

Central African Republic

An ESAF/PRGF program was approved in 1998 (and expired in 2002) for the Central African Republic (C.A.R.). The C.A.R. successfully completed a six-month Staff Monitored Program (SMP) in June 2002 but has been unable to establish an IMF-supported program since the onset of civil conflict in October 2002, which culminated in a coup d'état in March 2003. Civil conflict has taken a heavy toll on most sectors of the economy and on physical and economic infrastructure. A Fund team visited Bangui in May 2004 to initiate negotiations on a program to be supported by the Emergency Post-Conflict Assistance (EPCA) policy. The mission reached understandings, ad referendum, on a program. The program would cover the period July-December 2004 and could lead to a PRGF in early 2005 if performance under the EPCA is satisfactory and the administrative capacity of the authorities is restored to an appropriate level.

The political situation has been generally calm since the transitional government has been installed. A constitutional referendum is scheduled for October 2004, before legislative and presidential elections in early 2005.

Currently, the C.A.R. has accumulated arrears to all its external creditors (except for the Fund) including multilateral creditors, notably the World Bank and the AfDB. The C.A.R. has been in non-accrual status with the World Bank since June 2002. As part of a concerted international effort in the event of a program with the Fund, the European Union and France would provide budgetary grants. The World Bank is preparing a country re-engagement note and could provide support under its Low-Income Countries Under Stress (LICUS) facility to finance technical assistance in economic management and to support the rehabilitation of the social sectors.

PRSP Status: The JSA of the I-PRSP stressed that the PRSP would need to address weaknesses in the preparation of the I-PRSP. In particular, the work leading to the preparation of the PRSP would need to improve the statistical database; strengthen the participatory process; better prioritize the objectives for poverty reduction; clearly define quantitative targets for poverty reduction in the context of a detailed costing and financing exercise; and design an effective system for monitoring progress in reducing poverty, including the tracking of poverty outlays.

The work on the full PRSP was delayed due to political instability and violent conflict. However, the authorities have made it a priority to finalize the PRSP and recently resumed the preparation of the full PRSP. Donors, including the World Bank, are to undertake a joint assessment mission, working with local authorities to assess the constraints and opportunities for socio-economic recovery in the C.A.R. and identify entry points where actions by the government and appropriate donor support will lead to visible and quick pay-offs for the citizens of the C.A.R., as well as strengthen the foundation for sustainable peace and poverty reduction. The priority areas for intervention have already been identified, namely infrastructure, HIV/AIDS, health, and food security. A full PRSP is expected to be completed by 2005.

HIPC Status: The C.A.R. external debt situation is difficult. It has a sizable stock of arrears and a very heavy debt burden over the medium term. The country could be in a position to benefit from the Initiative but would need to establish a track record of policy implementation either under a EPCA or a PRGF program. A full PRSP is expected to be completed by 2005.

Comoros

Comoros has not had a Fund arrangement in place since 1991. Disputes between Union and Island governments over competencies and revenue sharing led to a mixed performance under the SMP covering the period July 2001-June 2002. A Transitional Agreement establishing joint governance between Union and Island governments was signed on December 20, 2003. In June 2004 the newly elected National Assembly, in which the opposition to President Azali has a two-thirds majority, met for the first time. It remains unclear whether cooperation between the President, the Assembly, and the Island presidents is possible. The IMF staff feels that discussion on an SMP requires assurances on cooperation for coherent economic management, including the establishment of a consolidated budget. In addition, a broader and more timely flow of information and statistics has been urged to permit a meaningful monitoring of an SMP. The president has promised to advance on these issues and present the Fund staff with the required information. Once this happens, an SMP mission can be fielded.

PRSP Status: The PRSP process was initiated in March 2002, when the country was in the process of overcoming its secessionist crisis. Since then, for at least some time, the PRSP process proved to be a useful tool to facilitate discussions between the conflicting parties. An I-PRSP was produced and discussed through participatory workshops in May 2003. Since then, the process came to a virtual halt, reflecting the uncertain political environment. The process could be revived under the auspices of the new National Assembly. Modifications would need to concentrate on issues of decentralization and the design and implementation of coherent economic and social policies for the country as a whole. After such updates, the revised I-PRSP could be presented to the Boards of the World Bank and the IMF.

HIPC Status: The country's debt situation is clearly unsustainable, with NPV debt stocks of over 500 percent of exports of goods and services, and of more than 400 percent of domestic revenue in 2003. In early October 2003, a Comorian delegation met with Fund management to explain the country's need for debt relief under the HIPC Initiative. Fund management concurred with the need, but insisted on a track record under an SMP which would lay the basis for an arrangement under the PRGF and allow Comoros to meet the entry requirements for the HIPC Initiative. In late December, a Fund mission discussed with the authorities the modalities for the negotiation of a SMP. Since then, the authorities have on a number of occasions repeated their call for steps toward debt relief under the HIPC Initiative. Large arrears to the African Development Bank/Fund complicate the issue.

Congo, Republic of

The Republic of Congo has benefited from a Fund EPCA program in 2002. Since then despite some encouraging results during the 2003 SMP, overall performance was not sufficiently strong to allow a move to a PRGF-supported program. A new six-month SMP (covering January-June 2004) provides the authorities with an opportunity to develop a sufficient track record of policy implementation for a possible move to a PRGF-supported program. The implementation of the 2004 staff-monitored program (SMP) was broadly satisfactory through end-April. Particularly noteworthy are the efforts being made to enhance transparency and governance in the oil sector operations and management.

PRSP Status: The preparation of an I-PRSP is at an advanced stage and is expected to be completed in the third quarter of 2004.

HIPC Status: With respect to the HIPC Initiative, it would be important for the Republic of Congo to establish the necessary track record for a PRGF-supported program. On the basis of the broadly satisfactory implementation of the SMP so far, the IMF staff initiated negotiations in May 2004 on a program that could potentially be supported by a new three-year arrangement under the PRGF. The conclusion of these negotiations would be conditional on continued good implementation under the SMP through end-June 2004, and obtaining full financing assurances. A Fund mission is planned for August 2004 to assess the implementation of the SMP through June and to continue negotiations on a possible PRGF-supported program.

Côte d'Ivoire

PRGF progress in Cote d'Ivoire has been derailed since the outbreak of a crisis in September 2002 resulting in Côte d'Ivoire not being able to reach the decision point in that year. The implementation of the Bank's Economic Recovery Credit (ERC), which had been approved before the crisis in June 2002, was also interrupted. On the political front, progress toward reconciliation has proven difficult in a deeply polarized country. The disarmament, demobilization and reintegration process has stalled, and the fundamental issues at the core of the crisis—nationality, rural land ownership rights, and eligibility for the presidency—are yet to be addressed. The security and political situation has worsened further since March 2004. The fiscal situation suffered in 2003 and 2004, as lack of progress in political reconciliation and in normalizing the security situation complicated budget implementation. Without access to fresh financing, the government accumulated large external arrears, with the stock estimated at 10 percent at end-March 2004.

PRSP Status: The IMF and the World Bank Boards endorsed the I-PRSP in March 2002. A first draft of the full PRSP was prepared in September 2002 and reviewed by World Bank and IMF staff. The intervening conflict, however, delayed completion of the PRSP and implementation of anti-poverty measures. It is estimated that poverty increased from an official 38 percent of the population before the conflict to about 42-44 percent after the conflict, including the large number of refugees. The PRSP process has been reactivated, but the completion of the PRSP will have to take into account worse economic and social "initial conditions" for mapping out a post-conflict poverty reduction strategy than had been envisaged at the time of the I-PRSP. The Bank has prepared a draft Interim Transitional Support Strategy (I-TSS) and taken proactive measures to restructure its portfolio toward the most urgent post-conflict needs. The political and security situation deteriorated during the opposition protests in May 25-27, 2004 that claimed at least 120 lives. In the aftermath, more ministers of the opposition suspended their participation in the government, which as of mid-June 2004, led to a complete political impasse.

HIPC Status: With respect to the HIPC Initiative and reaching of the decision point, this cannot be envisaged before a new program is put in place and the authorities have re-established a policy implementation track record. Such a track record could be established under the IMF EPCA program, for which Côte d'Ivoire could qualify, provided understandings are reached on an appropriate macroeconomic framework and minimum structural reforms. In terms of key actions to reestablish a track record for the Bank and the Fund, there are likely to be three preconditions: (i) re-establishing and maintaining the policy of no debt service arrears to the Bank and the Fund, (ii) re-establishing a credible government of national reconciliation, and (iii) making some progress towards demobilization and disarmament. In addition, putting in place a post-conflict program with the Fund with minimum macroeconomic policy and structural measures would constitute key actions toward attaining a satisfactory track record.

Lao People's Democratic Republic

The third review of Lao P.D.R.'s PRGF arrangement was completed in September 2003 at which time, the IMF Board agreed on a one-year extension of the arrangement. During the delay in the third review, measures to address the shortfall in budget revenue in 2002/03 were undertaken and structural reform measures in the banking sector were strengthened. However, reforms in state-owned enterprises lagged. Recent macroeconomic performance has been mixed, as GDP growth slowed to 5.3 percent in 2003 because of tighter commercial bank credit and weaker tourism, and inflation declined more gradually than expected and reached 12 percent (12-month basis) in April 2004. Concerns over the decline in fiscal revenue have caused the fourth review to be delayed. A joint IMF Article IV and PRGF review mission is planned for the second-half of July 2004.

The first tranche of the World Bank Financial Management Adjustment Credit was disbursed in January 2003 and the second tranche was released in May 2004, following the completion of all 17 actions.

PRSP Status: The World Bank and IMF Boards considered the country's I-PRSP in April 2001. The first draft of the PRSP was delivered by the Lao authorities at the end of May 2003. The final PRSP called the National Growth & Poverty Strategy (NGPES) was approved by the National Assembly in October 2003, delivered to the Bank and Fund on April 1, 2004 and is expected to be presented to the Boards in August 2004.

HIPC Status: IMF staff conducted a preliminary debt sustainability analysis in 2002, which will be updated in the context of the Article IV consultation discussions in July 2004. The results of the analysis are sensitive to the outcome of ongoing discussions between Lao P.D.R. and Russia on debt owed to the former Soviet Union. Although it is likely that Lao P.D.R. would qualify for HIPC assistance after traditional relief, it is uncertain if the authorities will seek HIPC relief. The decision point could be reached fairly quickly provided Lao P.D.R. decides to participate in the HIPC Initiative (the DSA shows debt in excess of HIPC thresholds after traditional relief), and stays on track with its PRGF programs.

Liberia

Liberia's relations with the IMF deteriorated steadily prior to the NTGL (National Transitional Government of Liberia) taking office in October 2003. Liberia has been in continuous arrears to the IMF since 1984 and the IMF Board decided to suspend the country's voting and related rights in March 2003 due to a protracted lack of cooperation. Liberia has not yet engaged in the PRSP process.

Intermittent civil wars have largely destroyed Liberia's physical and economic infrastructure, and the government's capacity to devise and implement policies. However, the NTGL has shown commitment in implementing a first set of fiscal and governance measures. Cooperation with the Fund has improved in terms of implementation of policies, and token payments to the Fund resumed in early 2004. On March 1, 2004, the IMF Board decided to resume technical assistance to Liberia.

In December 2003, the UN, the World Bank and the IMF assisted the government in a needs assessment covering 10 priority sectors that led to a time- and cost-bound action plan, the Results Focused Transitional Framework (RFTF), which was presented at an international conference held in New York in February 2004. Donors pledged US$440 million for reconstruction needs and US$85 million for humanitarian assistance. Should arrears clearance be achieved, a post-conflict World Bank allocation would be sought and a Transitional Support Strategy (TSS) would be prepared. This sequence is likely to monitor Liberia's transition from the RFTF to a PRSP framework.

HIPC Status: The stock of Liberia's external public debt amounted to about US$2.9 billion (600 percent of GDP) at the end of 2003. Nearly all of Liberia's external debt is in arrears. For purposes of establishing a track record, first relations with the Fund will need to be normalized and policies put in place that will help start the process of establishing a track record to meet the entry requirements (i.e., either a EPCA or a Fund-supported PRGF program). In recent Board discussions, Fund Directors have welcomed the resumption of monthly token payments towards arrears. They stressed the need for a continued track record of cooperation and strong policies to lay the basis for normalizing relations with the Fund (and other creditors) over time.

Myanmar

Myanmar has not had an IMF-supported program since 1981/82 and relations have been limited to annual Article IV consultations. The last consultation, finalized in March 2004, concluded that Myanmar's macroeconomic situation has deteriorated, although official statistics point to continued double-digit growth. The fiscal deficit spiked in 2000/01 and, despite some declines since, remains unsustainable. The deterioration in the institutional infrastructure (including a distortionary dual exchange rate regime) declines in various aspects of human capital, and governance problems continue to erode Myanmar's potential. Near-term prospects have been further undermined by an intensification of international sanctions and a weak banking sector. The World Bank has approved no new lending since 1987 and does not have an active program in Myanmar. However, a participatory assessment has been completed by UNDP in collaboration with the Ministry of Planning and a household expenditures survey is expected to be launched in April 2004. Without active engagement with the World Bank and the IMF, Myanmar is not engaged in the PRSP process.

HIPC Status: Myanmar is in arrears to the World Bank and to other multilateral and bilateral agencies. Poor debt statistics make assessment of the debt burden difficult. Highly tentative estimates indicate that Myanmar's debt ratios exceed the HIPC thresholds. Given Myanmar's poor relations with the international community and the lack of economic reforms, there is little prospect for moving beyond IMF surveillance and the World Bank's LICUS approach at this stage. Without an active engagement with the World Bank and IMF, Myanmar is not engaged in a process to proceed with preparing an I-PRSP or working to develop a track record of economic performance to receive HIPC relief.

Somalia

Given the lack of a fully functional national authority and continued domestic conflict, Somalia is not expected to proceed with preparing an I-PRSP.

On January 29, 2004, a broad cross-section of Somali leaders concluded negotiations on the framework for the structure and composition of the future government of Somalia. The signed agreement, Transitional Federal Charter (TFC), provides a basis for elections of the 275-member parliament, whose members will elect the president and draft the constitution. This represents the start of the third and final phase of the peace process which was launched in October 2002 under the auspices of the Intergovernmental Authority on Development (IGAD). The World Bank provided technical expertise during the second phase of the process to the committee on economic recovery and trade. The World Bank is also an active member of the Somalia Aid Coordination Body (SACB), which provides a framework for UN agencies, international and Somali NGOs, and donors to develop a common approach for the allocation of development assistance to Somalia. There is no PRSP process in place.

HIPC Status: The Fund has had no relations with Somalia and the country is also in arrears. The World Bank has not had an active lending program in Somalia since 1991 and is also in arrears. A joint World Bank/UNDP Country Re-engagement Note was approved in June 2003 by the World Bank's Board of Directors and is currently being implemented in Somalia. The following areas of intervention are being pursued: (i) support to macroeconomic data analysis and dialogue; (ii) creation of an enabling environment for the livestock and meat industry; (iii) coordinated action plan to address HIV/AIDS issues; and (iv) capacity-building for skills development and training centers. In collaboration with other development partners and the donor community, these activities are being implemented with the support of a Post-Conflict Grant of US$4.6 million. The World Bank is also currently undertaking a Conflict Analysis Framework for Somalia to ensure conflict-sensitive development assistance. The World Bank is also providing access to global electronic knowledge and resources to tertiary educational institutions.

Sudan

Sudan has not had a Fund-supported program since 1984, but has been implementing SMPs since 1997. On the peace front, an agreement in May 2004 between the Government of Sudan and the Sudan People's Liberation Movement/Sudan People's Liberation Army resolved all outstanding issues. The formal signing of the comprehensive agreement is expected in late summer. Since mid-2003, the security and humanitarian situation has deteriorated in Darfur (western Sudan) due to tribal clashes and local insurrection. The government has made good progress in preparing an I-PRSP, which is near completion, and work on a full nationwide PRSP, to be developed in collaboration with civil society, will begin once peace agreement is in place.

HIPC Status: Sudan's economic performance under the 2003 SMP was broadly on track. The IMF Board has agreed that the SMP for 2004, like the 2002 and 2003 SMPs, is comparable in strength to a Rights Accumulation Program (RAP). Once the peace agreement is finalized, the situation in Darfur is stabilized, and the appropriate financing assurances secured, a RAP may be in place by end-2004. Some work has been completed in recent months to lay the groundwork for a possible arrears clearance for Sudan in the event that conditions improve sufficiently to allow for re-engagement by the international community. With the establishment of a Fund-supported program, Sudan would have met the entry requirements and commenced the establishment of a track record. To this end financing assurances are being sought for clearing arrears to the Fund.

Togo

Togo had a Fund-supported PRGF program approved in 1998. The stabilization program for 2002 yielded mixed results as did the April-December 2001 SMP, with some progress on the structural front but a disappointing macroeconomic and fiscal performance. Second, as indicated in the last Article IV staff report (SM/04/125, 4/14/04), while the Togolese authorities are eager to enter into a new SMP, the possibility of an SMP hinges on the track record of policy implementation, and the normalization of relations with the EU.

The government issued a draft I-PRSP in November 2002 on which donors' feedback was sought. In March 2004, the I-PRSP was presented and discussed in the Council of Ministers and a *communiqué* was issued. The final I-PRSP will be validated in a national seminar and then adopted by the government. It will be submitted to the Boards of the Bank and the IMF once a satisfactory macroeconomic framework is in place.

The World Bank is currently preparing a Country Re-engagement Note scheduled for Board discussion in the third quarter of 2004. The Note will lay out an interim assistance strategy for Togo that describes the key steps towards the normalization of relations between Togo and the Bank. In April 2004, the government and the European Union launched consultations under Article 96 of the Cotonou Partnership Agreement, that could lead to the resumption of financial assistance from the EU in the medium term.

HIPC Status: In the context of the November 2003 Article IV IMF staff visit, the authorities discussed with Fund staff a macroeconomic framework for 2004 that aims to demonstrate commitment to improving revenue mobilization and strengthening expenditure management, to sustain the on-going rehabilitation of the phosphate sector, and to lay a foundation for normalizing relations with external creditors.