IV

Financial Assistance for Low-Income Members

The IMF provides financial assistance to low-income member countries in two ways: through concessional lending under the Poverty Reduction and Growth Facility (PRGF) and through debt relief under the Heavily Indebted Poor Countries (HIPC) Initiative. The PRGF (which replaced the ESAF in 1999) supports economic programs, which strengthen substantially and in a sustainable manner balance of payments positions and foster durable growth, leading to higher living standards and a reduction in poverty. The HIPC Initiative helps countries achieve a sustainable external debt position. Resources for financing these initiatives, which are separate from the IMF's general resources generated from quota subscriptions, have been provided through contributions by a broad segment of the IMF's membership, as well as by the IMF itself. These resources are administered under the PRGF and PRGF-HIPC Trusts, for which the IMF acts as Trustee. This chapter describes the financing arrangements for the PRGF and for the HIPC Initiative.

An important part of IMF assistance to low-income members is technical and capacity-building support made available at the request of such countries and at no cost to them. The IMF's technical assistance program is discussed briefly in Chapter V.[1]

Overview of Concessional Assistance

The IMF's concessional financial assistance to low-income members has been strengthened progressively over the past 25 years. The initial assistance, financed entirely through the profits from the IMF's gold sales in 1976–80, was disbursed with low conditionality, first through Trust Fund loans and later through Structural Adjustment Facility (SAF) loans. Since 1987, concessional loans financed in large part by bilateral contributions have been extended through facilities with the equivalence of upper credit tranche conditionality through the ESAF and, since 1999, the PRGF.

[1]See the section on "Voluntary Safeguards" in Chapter V. For more information, see the "Policy Statement on IMF Technical Assistance," March 31, 2000, which is posted on the IMF website (http://www.imf.org/external/np/ta/2000/index.htm).

- In 1976, the IMF initiated concessional operations through the establishment of the Trust Fund, which drew upon the profits generated from the sale of part of the IMF's gold holdings in 1976–80 and provided concessional loans to low-income developing countries for balance of payments support.[2]
- In 1986, the IMF established the SAF to provide concessional assistance to low-income countries by recycling resources lent under the Trust Fund.[3]
- In 1987, the IMF established the ESAF to foster stronger adjustment and reform measures than those under the SAF and to augment the resources available for this purpose. In contrast to the Trust Fund and SAF, the loan and subsidy resources were provided primarily by bilateral contributors.
- In 1996, the IMF and World Bank jointly launched the HIPC Initiative to reduce the external debt burden of eligible poor and heavily indebted countries to a sustainable level.
- In September 1999, the HIPC Initiative was enhanced to provide faster, deeper, and broader debt relief and the links between debt relief and poverty reduction were strengthened.[4] In October 1999, the Executive Board decided to change the names of the ESAF and ESAF Trust to the Poverty Reduction and Growth Facility (PRGF) and the Poverty Reduction and Growth Facility Trust (PRGF Trust), respectively, and to broaden the objectives of the renamed facility. The decision became effective on November 22, 1999, when all contributors to the Trust had consented to the change.[5]
- In September 1999, agreement was also reached on a financing package for the HIPC Initiative and for a continuation of the PRGF for a four-year period (the so-called interim PRGF) expected to begin in 2002

[2]Of the $4.6 billion in profits from the gold sales, $1.3 billion was distributed to developing country members of the IMF in proportion to their quotas, while $3.3 billion was made available for concessional lending through the Trust Fund.

[3]See Joslin Landell-Mills, *Helping the Poor: The IMF's New Facilities for Structural Adjustment* (Washington: International Monetary Fund, rev. ed., 1992).

[4]For a more thorough discussion of the Enhanced HIPC Initiative, see David Andrews, Anthony Boote, Syed S. Rizavi, and Sukhwinder Singh, *Debt Relief for Low-Income Countries: The Enhanced HIPC Initiative*, IMF Pamphlet Series No. 51 (Washington: International Monetary Fund, 2000).

[5]See “IMF Lending to Poor Countries—How Does the PRGF Differ from the ESAF?” (International Monetary Fund, Issues Brief, 01/06, April 2001).

after the full commitment of existing PRGF resources and before the onset of self-sustained PRGF operations.

- Loan resources of SDR 4–4.5 billion for interim PRGF lending are now being mobilized.
- In May 2001, the IMF established an account to gather resources for providing an interest subsidy on post-conflict emergency assistance to PRGF-eligible countries. The grants from this subsidy account will reduce the annual rate of charge for purchases from the GRA under the post-conflict emergency assistance facility to 0.5 percent (same rate of charge as the interest on use of PRGF resources).
- After 2005, it is anticipated that a substantial proportion of concessional lending will be provided through self-sustained PRGF operations financed by the IMF's own resources accumulating in the Reserve Account of the PRGF Trust. These resources, which derive from the IMF's gold sales in the late 1970s and related investment income, will become available as PRGF lenders are repaid and the security provided by the Reserve Account is no longer needed.

An overview of the financing of the IMF's concessional assistance is summarized in Box IV.1, while Figure IV.1 shows the level and composition of IMF concessional lending from its inception to the present.

PRGF and HIPC Operations

The IMF acts as Trustee for the PRGF and PRGF-HIPC Trusts, and through these Trusts administers the various resources supporting PRGF and HIPC operations. In this capacity, the IMF mobilizes and manages resources for both Trusts.

PRGF Trust

Eligibility, Terms, and Access for PRGF Resources

In practice, the IMF has relied on the level of per capita income and eligibility under the International Development Association (IDA), the concessional lending arm of the World Bank, to determine eligibility for PRGF loans. However, there is no automatic link between PRGF and IDA eligibility and it is up to the Executive Board of the IMF to establish the list of PRGF-eligible

Box IV.1. Overview of Financing for the IMF's Concessional Assistance

PRGF Trust

- Established as the ESAF Trust in 1987 and enlarged in 1994, with loan resources of SDR 11.4 billion provided by 17 bilateral lenders and subsidy contributions by a larger number of IMF member countries.
- Loans to the Trust are secured by a Reserve Account, which is financed through a recycling of profits from gold sales in the late 1970s (i.e., reflows of SAF and Trust Fund repayments) and investment returns on balances held in the Account; the rights accumulation gold pledge (see Chapter II); and an informal statement on security to lenders by the Managing Director (see text on the Reserve Account).

PRGF-HIPC Trust

- The framework for the HIPC Initiative and the interim PRGF was agreed in 1996. Agreement was reached in late 1999 on the financing of the subsidy required for the interim PRGF (during 2002–05) and the IMF's participation in the HIPC Initiative. Contributions are provided by 94 member countries and the IMF.
- The framework and sources of loan resources for the interim PRGF of SDR 4–4.5 billion were not identified when the PRGF-HIPC Trust was established. Progress has been made in mobilizing such resources through new bilateral lending, but further efforts are needed to secure the full amount required.

Self-Sustained PRGF

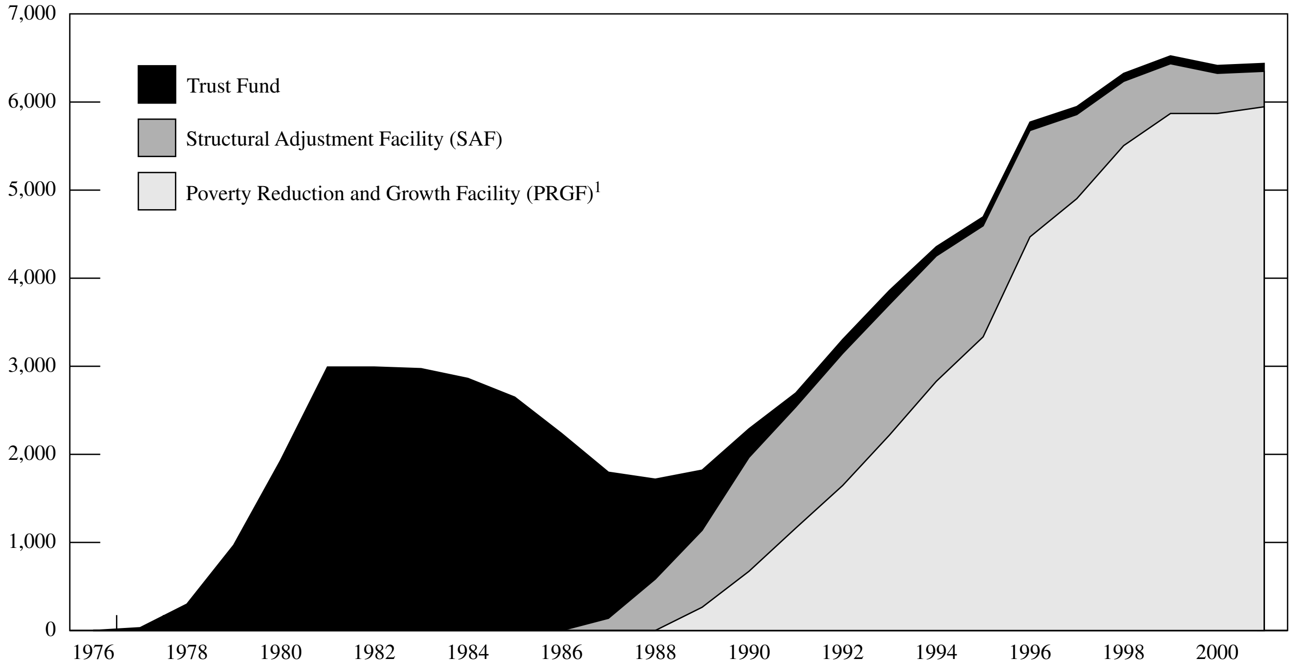
- Expected to begin operations in 2006 financed through a revolving use of the resources accumulating in the Reserve Account of the PRGF Trust. No interest subsidy contributions or loan resources will be needed from bilateral contributions.

	Loans (In billions of SDRs)	Commitment Periods	Status of Financing (In billions of SDRs)	
			Principal	Subsidies
PRGF Trust	11.4	1988–2001	Financed	Financed
PRGF-HIPC Trust				
Interim PRGF	4–4.5	2002–05	3.3[1] (committed)	Fully committed; mostly effective
HIPC Initiative	(for delivery of grants or loans)			Fully committed; mostly effective
Self-sustained PRGF	0.7/year in perpetuity	From 2006 onward	Financed	Self-financed

[1]As of end-June 2001.

FIGURE IV.1. OUTSTANDING IMF CONCESSIONAL CREDIT BY FACILITY, FINANCIAL YEARS ENDED APRIL 30, 1976–2001

(In millions of SDRs)



[1]Includes use of SAF resources under PRGF arrangements.

countries.[6] Since 1987, many countries, including some countries in transition, have become members, while others have been removed from the list. Currently, 77 members of the IMF are eligible for the PRGF (Box IV.2).

PRGF loans are provided under three-year PRGF arrangements (with a possibility of a one-year extension), with annual programs for each of the three years. Disbursements under PRGF arrangements are tied to performance criteria and reviews normally set for semiannual periods, although reviews can also be quarterly when more frequent monitoring is appropriate. Loans under the PRGF carry an annual interest rate of 0.5 percent, with equal repayments made semiannually, beginning 5½ years and ending 10 years after disbursement.

PRGF-supported programs are framed around a comprehensive, nationally owned Poverty Reduction Strategy Paper (PRSP) prepared by the borrowing country government and based on a process involving the active participation of civil society, nongovernmental organizations, donors, and international institutions. These PRSPs are then endorsed in their respective areas of responsibility by the Executive Boards of the IMF and the World Bank as the basis for the institutions' concessional loans and for relief under the enhanced HIPC Initiative. PRGF-supported programs emerge directly from the PRSPs and macroeconomic policies in such programs are integrated with social and sectoral objectives, to ensure that plans are mutually supportive and consistent with a common set of objectives to spur growth and reduce poverty. PRGF-supported programs embody budgets that are pro-poor with a reorientation of government spending toward the social sectors, basic infrastructure, or other activities that demonstrably benefit the poor. PRGF-supported programs also emphasize improvements in governance as a fundamental underpinning for macroeconomic stability, sustainable growth, and poverty reduction. The primary focus is on better management of public resources, achieving greater transparency, active public scrutiny, and generally increased government accountability in fiscal management.

An eligible country may borrow up to 140 percent of its IMF quota under a three-year arrangement, although this limit may be increased under exceptional circumstances to a maximum of 185 percent of quota. Access under individual PRGF arrangements is determined on the basis of the balance of

[6] The current cutoff point for IDA eligibility is a 1999 per capita GNP level of $885.

Box IV.2. PRGF- and HIPC-Eligible Countries

1. Afghanistan, I.S. of
2. Albania
3. Angola*
4. Armenia
5. Azerbaijan
6. Bangladesh
7. Benin*
8. Bhutan
9. Bolivia*
10. Bosnia and Herzegovina
11. Burkina Faso*
12. Burundi*
13. Cambodia
14. Cameroon*
15. Cape Verde
16. Central African Republic*
17. Chad*
18. Comoros
19. Congo, Democratic Republic of the*
20. Congo, Republic of*
21. Côte d'Ivoire*
22. Djibouti
23. Dominica
24. Eritrea
25. Ethiopia*
26. Gambia, The*
27. Georgia
28. Ghana*
29. Grenada
30. Guinea*
31. Guinea-Bissau*
32. Guyana*
33. Haiti
34. Honduras*
35. India
36. Kenya*[1]
37. Kiribati
38. Kyrgyz Republic
39. Lao, P.D.R.*[2]
40. Lesotho
41. Liberia*
42. Macedonia, F.Y.R.
43. Madagascar*
44. Malawi*
45. Maldives
46. Mali*
47. Mauritania*
48. Moldova
49. Mongolia
50. Mozambique*
51. Myanmar*
52. Nepal
53. Nicaragua*
54. Niger*
55. Nigeria
56. Pakistan
57. Rwanda*
58. Samoa
59. São Tomé and Príncipe*
60. Senegal*
61. Sierra Leone*
62. Solomon Islands
63. Somalia*
64. Sri Lanka
65. St. Lucia
66. St. Vincent and the Grenadines
67. Sudan*
68. Tajikistan
69. Tanzania*
70. Togo*
71. Tonga
72. Uganda*
73. Vanuatu
74. Vietnam*
75. Yemen, Republic of*[1]
76. Zambia*
77. Zimbabwe

* HIPC-eligible countries.

[1]One of two HIPC-eligible countries that have sustainable debt as defined in the Initiative. In July 2000, the IMF and World Bank confirmed that the Republic of Yemen does not need HIPC Initiative assistance to reach debt sustainability.

[2]Country has indicated that it does not want to make use of the HIPC Initiative.

payments need of the member, the strength of the adjustment program, the member's outstanding use of IMF credit, and the record of such use in the past. Access is subject to review, both at the approval of a three-year arrangement and at the periodic reviews thereafter. Over the years the access policy has evolved to provide for different access levels according to circumstances. There is substantial differentiation in access in individual cases because of a variety of factors:

- In some cases, where there is a balance of payments need, a convincing strengthening of the adjustment effort, and capacity to repay, actual access within existing limits tends to be higher now than in the past, with the expectation that continued strong performance should both elicit support from others and permit a steady decline over time in the need for exceptional balance of payments support, including from the PRGF. Where the balance of payments need is not clear cut, lower access is set appropriately on a case-by-case basis.
- No access is appropriate in cases that have relatively weak track records and are not able to implement sufficiently strong policies. In these circumstances, the IMF seeks to continue to play an active role through the provision of policy advice and technical assistance in helping countries elaborate and implement strong policy reforms that could eventually merit support from the IMF and other sources.
- Since repeat users are likely to have IMF credit outstanding, access is expected to be lower than for first-time users in otherwise similar situations; this does not, however, preclude an IMF response through higher access in support of suitably strong policies.
- For poor countries that are heavily indebted, greater emphasis is given to the outstanding use of IMF credit in setting access. There are wide variations across countries in the ratio of quotas to exports, which implies that similar access levels in relation to quotas result in widely differing debt-service burdens to the IMF. Thus, access in individual cases is more closely tied to countries' current and prospective payments capacity than to quotas.
- The "blending" of concessional PRGF with market-based GRA resources through parallel arrangements continues to be an option for those countries that have the capacity to service nonconcessional debt, allowing greater scope for access by others more in need of PRGF resources.

Sources and Uses of Financing

PRGF operations are conducted through three accounts within the PRGF Trust: the Loan Account, Reserve Account, and Subsidy Account (Figure IV.2.)

The Loan Account borrows resources generally at market-related interest rates from central banks, governments, and official institutions, and lends them on a pass-through basis to PRGF-eligible countries.[7] At the end of April 2001, the IMF had entered into 28 bilateral borrowing agreements with 17 creditors for SDR 11.4 billion for on-lending to PRGF-eligible members; Saudi Arabia has provided additional loan resources through an associated lending agreement between the Saudi Fund for Development and the IMF (Table IV.1). Most of these loans are remunerated at a six-month SDR interest rate, with a maturity typically set to match the maturity profile of loan repayments from borrowing members (i.e., with a 5½-year grace period and 10-year maturity).

Since July 1988, 54 of the 77 PRGF-eligible members have made use of PRGF loans. Many of these members have had multiple PRGF or ESAF arrangements as they endeavor to achieve sustainable economic growth and poverty reduction. At end-April 2001, about SDR 10 billion of the total available loan resources of SDR 11.4 billion was committed to borrowing members, and SDR 7.9 billion was disbursed. It is expected that the remainder of resources will be fully committed around late 2001 or early 2002.

The Reserve Account of the PRGF Trust is designed to:

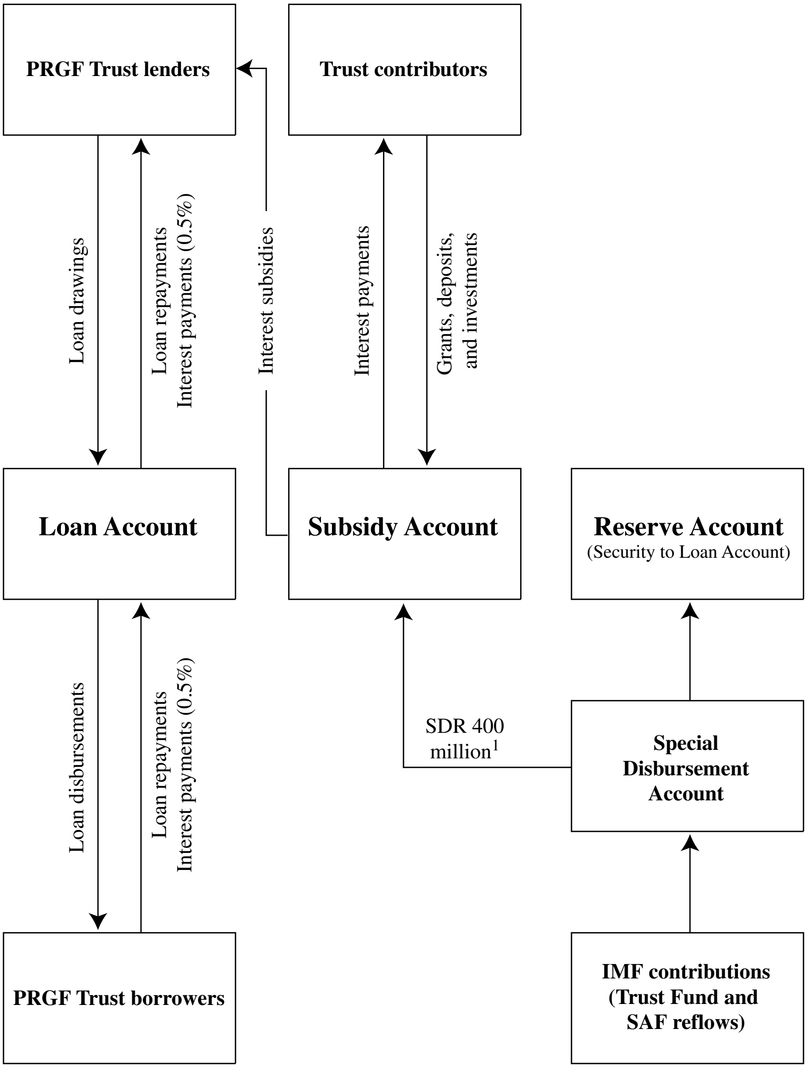
- provide security to the lenders to the Loan Account of the Trust in the event of delayed or nonpayment by PRGF borrowers;[8]
- meet temporary mismatches between repayments from borrowers and payments to lenders; and
- cover the IMF's costs of administering PRGF operations.[9]

[7]Lenders have extended resources to the PRGF Trust on various interest terms, in some cases at highly concessional rates.

[8]Additional security to lenders includes the gold pledge for rights accumulation programs financed from the PRGF Trust (see Chapter II) and an informal statement of the Managing Director of the IMF in 1987 which made clear that the IMF would take "all such initiatives as might be necessary" to ensure repayment of PRGF loans to PRGF lenders. This statement is understood to include the possible use of a portion of the IMF's holdings of gold.

[9]In April 1998 and April 1999, the IMF's Executive Board decided that no reimbursement would be made from the Reserve Account to the GRA for the annual cost of administering the PRGF Trust for FY1998–2000 and that, instead, an equivalent amount would be transferred from the Reserve Account to the PRGF-HIPC Trust. On December 8, 1999, the Executive Board agreed to extend the earlier decision to cover FY2001–04. These transfers are estimated to amount to SDR 0.6 billion for FY1998–2004.

FIGURE IV.2. FINANCIAL STRUCTURE OF THE PRGF TRUST



[1]A one-time transfer.

TABLE IV.1. LENDERS TO THE PRGF TRUST, AS OF APRIL 30, 2001[1]
(In millions of SDRs)

1.	National Bank of Belgium	200
2.	Government of Canada	700
3.	Government of China	100
4.	National Bank of Denmark	100
5.	Central Bank of Egypt	100
6.	Agence Française de Développement	1,900
7.	Kreditanstalt für Wiederaufbau (Germany)	1,750
8.	Bank of Italy	830
9.	Japan Bank for International Cooperation	4,350
10.	Bank of Korea	93
11.	The Netherlands Bank	250
12.	Bank of Norway	150
13.	OPEC Fund for International Development[2]	40
14.	Bank of Spain	341
15.	Government of Spain	67
16.	Swiss Confederation	200
17.	Swiss National Bank	152
	Total	11,322

Note: Numbers may not add to total due to rounding.
[1]Excluding associated loans from the Saudi Fund for Development in the amount of SDR 49.5 million.
[2]The loan commitment is for the SDR equivalent of $50 million valued at the exchange rate of April 30, 2001.

As of end-April 2001, the balance in the Reserve Account amounted to SDR 2.7 billion, equivalent to 47 percent of outstanding obligations to PRGF lenders. Thus far, the PRGF Trust has experienced a good track record of payments by PRGF borrowers, with only two cases of principal arrears exceeding one month in duration.

The balance in the Reserve Account is projected to be sufficient to cover all outstanding PRGF Trust obligations to lenders by around 2007. Factors that affect the pace of further accumulation of balances in the Reserve Account include:

- repayments of SAF and Trust Fund loans, including those by countries with protracted arrears to the IMF;
- the investment return on resources in the account; and
- the level of transfers to meet the cost of administering PRGF operations.

The primary factor driving Reserve Account accumulations is the investment return on resources in the account. The annual rate of return on investments in the account has averaged about 4.8 percent over the life of the PRGF Trust through end-April 2001. Assuming that the return on investment remains at about 5 percent a year, the cumulative balance in the Reserve Account is projected to increase from SDR 2.7 billion at end-April 2001 to SDR 3.9 billion at end-2005, when the self-sustained PRGF is expected to begin (Figure IV.3)

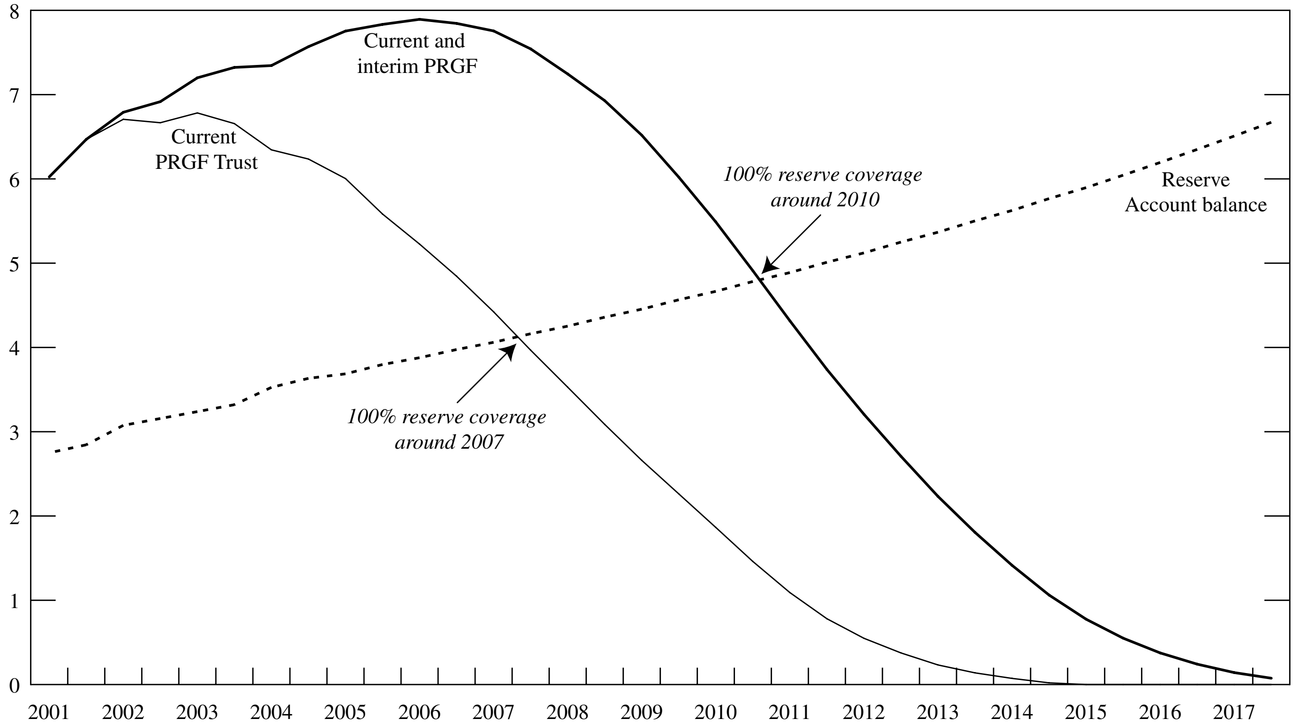
The Subsidy Account of the PRGF Trust receives contributions from bilateral sources and contributions from the IMF's own resources to subsidize the rate of interest on PRGF loans to borrowers at ½ of 1 percent a year. These resources finance the difference between the market rate of interest paid to PRGF Trust lenders and the rate of interest of ½ of 1 percent a year paid by the borrowing members. Subsidy resources are typically provided through either grant contributions or deposits and investments placed by contributors with the PRGF Trust at below-market interest rates. In the latter case, the interest rate differential between the rate of interest earned on the deposit or investment by the PRGF Trust and the rate of interest paid to the contributor represents a subsidy contribution to the PRGF Trust.[10] As of end-April 2001, the Subsidy Account had received contributions, including investment income, totaling SDR 3.0 billion, of which SDR 2.6 billion was provided by 40 bilateral contributors, with the rest (SDR 0.4 billion) provided by the IMF.

The adequacy of the resources in the Subsidy Account to support PRGF lending depends critically on the future rate of interest paid to PRGF Trust lenders, the investment return on balances held in the Subsidy Account, and the level and pace of PRGF lending. Based on an assumed annual investment return of 5 percent and a similar interest rate on loans extended by PRGF Trust lenders over the remaining life of the Trust (around 2015), subsidy resources are expected to exceed estimated needs by a small margin.

[10]In certain cases, the PRGF Trust may receive subsidy contributions through the provision by lenders of loan resources to the Trust at below-market interest rates. The IMF has also, at contributors' requests, agreed to receive and place deposits or investments in the Administered Contribution Account.

FIGURE IV.3. PRGF TRUST: PROJECTED OUTSTANDING OBLIGATIONS AND RESERVE ACCOUNT BALANCES

(In billions of SDRs)



Financial Statements of the PRGF Trust

The sources and uses of resources of the PRGF Trust are summarized in its balance sheet (Table IV.2). The sources are identified as "Resources and liabilities," while the uses are shown as "Assets." The bulk of resources reflects borrowings and the accumulated resources of the Reserve Account. The major assets are loans receivable, reflecting outstanding PRGF loans to low-income countries, and investments of the Reserve Account.

The Income Statement for the PRGF Trust for FY2001 is shown in Table IV.3.

PRGF-HIPC Trust

Resources for debt relief under the HIPC Initiative and subsidized PRGF loans are administered by the IMF under the PRGF-HIPC Trust, established in February 1997.

The HIPC Initiative

The IMF and the World Bank jointly launched the Heavily Indebted Poor Countries (HIPC) Initiative to support a growing recognition by the international community that the external debt burden of a number of low-income countries, mostly in Africa, had become unsustainable. The HIPC Initiative entails coordinated action by the international financial community, including multilateral institutions, to reduce the external debt burden of these countries to sustainable levels. The Initiative complements traditional debt relief mechanisms, concessional financing, and the pursuit of sound economic policies, which together are designed to place these countries on a sustainable external footing.

Under the HIPC framework, the IMF and the World Bank determine the eligibility of a member and the amount of HIPC assistance to be committed at the decision point—the point at which the member completes its first record of good policy performance under programs supported by the IMF and the World Bank (Box IV.3).[11] Beginning from the decision point, an eligible member may receive interim assistance from the IMF of up to

[11]The IMF's Executive Board has agreed to be flexible in assessing the track record prior to the decision point in order to deliver interim HIPC assistance to eligible post-conflict countries as rapidly as possible.

TABLE IV.2. PRGF TRUST: COMBINED BALANCE SHEETS, AS OF APRIL 30, 2001
(In millions of SDRs)

	Loan Account	Reserve Account	Subsidy Account	Combined
Assets				
Cash and cash equivalents	159.6	519.7	181.1	860.4
Investments	215.5	2,200.5	1,762.2	4,178.3
Loans receivable	5,899.5	—	—	5,899.5
Accrued account transfers	27.2	30.6	(57.9)	—
Interest receivable	13.2	5.1	0.4	18.7
Total assets	6,315.1	2,756.0	1,885.8	10,956.8
Resources and liabilities				
Borrowing	6,244.0	—	108.8	6,352.8
Interest payable	71.0	—	1.7	72.7
Other liabilities	—	12.5	—	12.5
Total liabilities	6,315.1	12.5	110.5	6,438.0
Resources	—	2,743.5	1,775.3	4,518.8
Total resources and liabilities	6,315.1	2,756.0	1,885.8	10,956.8

Note: Numbers may not add to totals due to rounding.

20 percent annually and 60 percent in total (25 percent and 75 percent, respectively, in exceptional circumstances) of the committed amount of HIPC assistance between the decision point and the floating completion point—the point when the member has fulfilled all policy-related conditions for HIPC assistance. Remaining undistributed HIPC Initiative assistance is delivered at the completion point.

The IMF provides its share of assistance under the HIPC Initiative to eligible members in the form of grants or loans or both, which are used to help meet debt-service payments to the IMF. So far, HIPC Initiative assistance has been extended only through grants. Between the decision point and the floating completion point, interim assistance may be provided in annual installments to an account of the member administered by the IMF. These resources are used for debt-service payments to the IMF as they fall due. The member's account earns interest on any balance during the interim period. At the completion point, the IMF deposits the remaining amount of

TABLE IV.3. PRGF TRUST: COMBINED INCOME STATEMENTS,
FINANCIAL YEAR ENDED APRIL 30, 2001
(In millions of SDRs)

	Loan Account	Reserve Account	Subsidy Account	Combined
Balance, April 30, 2000	—	2,558.4	1,747.4	4,305.7
Investment income	—	155.8	116.6	272.5
Interest on loans	28.9	—	—	28.9
Interest expense	(237.5)	—	(2.1)	(239.6)
Other expenses	(0.1)	(1.6)	—	(1.6)
Operational income (loss)	(208.7)	154.3	114.5	60.1
Contributions	—	—	127.0	127.0
Net income	(208.7)	154.3	241.5	187.1
Transfers from SDA	—	25.9	—	25.9
Transfers between				
Reserve and Subsidy Accounts	—	1.1	(1.1)	—
Loan and Reserve Accounts	(3.9)	3.9	—	—
Loan and Subsidy Accounts	212.6	—	(212.6)	—
Net changes in resources	—	185.1	27.9	213.0
Balance, April 30, 2001	—	2,743.5	1,775.3	4,518.8

Note: Numbers may not add to totals due to rounding.

undisbursed committed assistance to the member's account. After the completion point is reached, the member will continue to draw on the resources of its account for debt-service payments to the IMF according to a schedule agreed between the IMF and the member.

Continuation of PRGF Lending

The framework for the PRGF envisages continued commitments to borrowers under the current PRGF Trust through late 2001 or early 2002, to be followed by a four-year interim PRGF with a commitment capacity of about SDR 1 billion a year. The objective of the interim PRGF will be the same as that of the current PRGF, that is, to promote sustainable economic growth and achieve durable poverty reduction. The subsidy needs of the

Box IV.3. Enhanced HIPC Initiative: Qualification Criteria

A country must satisfy a set of criteria to qualify for special assistance. Specifically, it must:

- be eligible for concessional assistance from the IMF and World Bank;
- face an unsustainable debt burden, notwithstanding available debt-relief mechanisms such as Naples terms (where low-income countries can receive a reduction of eligible external debt of 67 percent in net present value (NPV) terms), defined as:
  - —a debt-to-export ratio of more than 150 percent (in NPV terms), or
  - —a debt-to-government revenue ratio of more than 250 percent (in NPV terms)
- establish a track record of reform and sound policies through programs supported by the IMF and the World Bank.

All countries requesting HIPC Initiative assistance are normally expected to (1) have a Poverty Reduction Strategy Paper (PRSP) developed through a broad-based participatory process and accepted by the Executive Boards of the IMF and World Bank by the time of the decision point, and (2) have made progress in implementing this strategy for at least one year by the time of the completion point.

interim PRGF are included in the financing arrangements for the PRGF-HIPC Trust, while new loan resources are being sought from bilateral lenders.

Sources and Uses of Financing

The financing required for the IMF's cost of HIPC assistance and interim PRGF subsidies are estimated at SDR 3.0 billion in end-2000 net present value (NPV) terms,[12] with the HIPC Initiative accounting for about two-thirds of the total. These financing requirements are to be met through bilateral contributions to the IMF amounting to SDR 1.2 billion in NPV terms and contributions by the IMF itself of SDR 1.8 billion in NPV terms (Table IV.4).

[12]These estimates exclude projections of use of PRGF resources and HIPC assistance by Liberia, Somalia, and Sudan, which presently have protracted overdue financial obligations to the IMF.

TABLE IV.4. PRGF-HIPC TRUST: FINANCING REQUIREMENTS AND SOURCES OF FINANCING, AS OF APRIL 30, 2001

	In Billions of SDRs (End-2000 NPV)
Total IMF financing requirements	3.0
PRGF subsidy requirement	1.1
Cost of the HIPC Initiative to the IMF	1.9
Sources of financing	3.0
Effective	
Bilateral contributions	1.1
IMF contributions	1.8
Investment income from gold proceeds	1.4
Other contributions	0.5
Pending	
Bilateral contributions	0.1

Bilateral pledges from member countries come from a wide spectrum of the IMF's membership, demonstrating the broad support for the HIPC and PRGF initiatives. In all, 94 member countries have pledged their support: 27 industrial countries, 58 developing countries, and 9 countries in transition. As of end-April 2001, effective bilateral contributions amounted to SDR 1.1 billion in NPV terms, or 93 percent of total pledged contributions.

The bulk of the IMF's contribution comes from the investment income on the net proceeds equivalent to SDR 1.4 billion in NPV terms generated from off-market transactions in gold of 12.9 million fine troy ounces. The off-market gold transactions were completed in April 2000, generating net proceeds of SDR 2.226 billion. These resources have been placed in the SDA and invested solely for the benefit of the HIPC Initiative. Transfers of the investment income on gold to the PRGF-HIPC Trust can only be made when all other available resources for the delivery of HIPC assistance have been exhausted (see the discussion of off-market gold transactions in Chapter II).

The IMF also contributes about SDR 0.5 billion in NPV terms by forgoing compensation for the administrative expenses related to PRGF operations for the financial years 1998 through 2004. The equivalent amount is transferred from the Reserve Account of the PRGF Trust to the PRGF-HIPC Trust. In addition, part of the interest surcharge on financing provided in 1998 and 1999 under the SRF related to activation of the NAB have also been transferred to the PRGF-HIPC Trust.[13]

At end-April 2001, the IMF had committed enhanced HIPC Initiative assistance of SDR 1.3 billion in NPV terms to 22 member countries that had reached decision points under the enhanced HIPC framework, one of which, Uganda, had reached the completion point.[14] Of this amount, SDR 0.5 billion in NPV terms was disbursed (Table IV.5). Since interim PRGF operations have not begun, no resources have been committed for interim PRGF subsidies.

To ensure the continuity of PRGF operations after existing loan resources in the PRGF Trust are fully committed, additional loan resources of SDR 4–4½ billion need to be mobilized for an interim period until PRGF operations become self-sustained after 2005. As of end-April 2001, a number of member countries had indicated their readiness to provide new loans for this purpose.

Financial Statements of the PRGF-HIPC Trust

The sources and uses of resources under the PRGF-HIPC Trust are summarized in its balance sheet (Table IV.6) and income statement (Table IV.7), as discussed above for the PRGF Trust.

Operational Structure

When the PRGF-HIPC Trust was established in 1997, it was envisaged that financial contributions could be earmarked for either PRGF subsidies or HIPC Initiative assistance. To permit such earmarking, three separate subaccounts were established (Figure IV.4):

- the HIPC subaccount for resources earmarked for HIPC Initiative assistance;
- the PRGF subaccount for resources earmarked for interim PRGF subsidy operations; and
- the PRGF-HIPC subaccount for unearmarked resources.

[13]On April 28, 1999, the participants in the NAB unanimously decided that, as a condition for the activation of the NAB to finance purchases by Brazil, one-third of the surcharge on outstanding purchases made under the SRF by Brazil be transferred to the PRGF-HIPC Trust. As of end-April 2000, Brazil completed all NAB-financed SRF repurchases, which generated transfers of SDR 72.5 million in support of HIPC operations.

[14]As noted in Table IV.5, one additional country, Côte d'Ivoire, had resources committed under the original HIPC Initiative. On June 8, 2001, Bolivia also reached its completion point.

TABLE IV.5. HIPC ASSISTANCE BY THE IMF, FINANCIAL YEAR ENDED APRIL 30, 2001
(In millions of SDRs)

Member[2]	Amount[1] Committed	Amount[1] Disbursed[3]
Benin	18.4	3.7
Bolivia	62.4	21.2
Burkina Faso	31.3	17.8
Cameroon	28.5	2.2
Côte d'Ivoire[4]	14.4	—
Gambia, The	1.8	0.1
Guinea	24.2	2.4
Guinea-Bissau	9.2	0.5
Guyana	56.2	31.7
Honduras	22.7	—
Madagascar	16.6	0.7
Malawi	23.1	2.3
Mali	44.4	11.5
Mauritania	34.8	9.9
Mozambique	104.8	95.5
Nicaragua	63.0	—
Niger	21.6	0.4
Rwanda	33.8	6.8
São Tomé and Príncipe	—	—
Senegal	33.8	4.8
Tanzania	89.0	26.7
Uganda	120.1	120.1
Zambia	468.8	117.2
Total	1,322.9	475.5

Note: Numbers may not add to totals due to rounding.
[1]Amounts may include interest on amounts committed but not disbursed during the interim period between the decision and completion points.
[2]Twenty-three members, of which 22 under the enhanced HIPC framework.
[3]These amounts are grants from the PRGF-HIPC Trust Account to member accounts to be used for repayments to the IMF as they fall due.
[4]Under the original HIPC framework.

Resources earmarked for the HIPC subaccount include investment income on the net proceeds derived from off-market gold transactions and certain bilateral contributions. Together these resources amount to SDR 1.7 billion

TABLE IV.6. PRGF-HIPC TRUST AND RELATED ACCOUNTS: COMBINED BALANCE SHEETS, AS OF APRIL 30, 2001

(In millions of SDRs)

	PRGF-HIPC Trust Account	Subaccount			Umbrella Account for HIPC Operations	Post-SCA-2 Administered Account	Combined Total
	PRGF-HIPC	PRGF	HIPC	Combined			
Assets							
Cash and cash equivalents	536.9	6.4	3.9	547.2	304.4	92.1	943.7
Investments	444.1	7.5	—	451.7	35.0	—	486.7
Transfers receivable	12.5	—	—	12.5	—	—	12.5
Transfers to and from subaccounts	214.2	—	(214.2)	—	—	—	—
Interest receivable	5.3	0.1	0.1	5.5	4.0	1.2	10.7
Total assets	1,213.1	14.0	(210.3)	1,016.8	343.4	93.3	1,453.6
Resources and liabilities							
Borrowings	477.2	—	—	477.2	—	—	477.2
Interest payable	0.9	—	—	0.9	—	—	0.9
Total liabilities	478.0	—	—	478.0	—	—	478.0
Resources	735.1	14.0	(210.3)	538.8	343.4	93.3	975.5
Total resources and liabilities	1,213.1	14.0	(210.3)	1,016.8	343.4	93.3	1,453.6

Note: Numbers may not add to totals due to rounding.

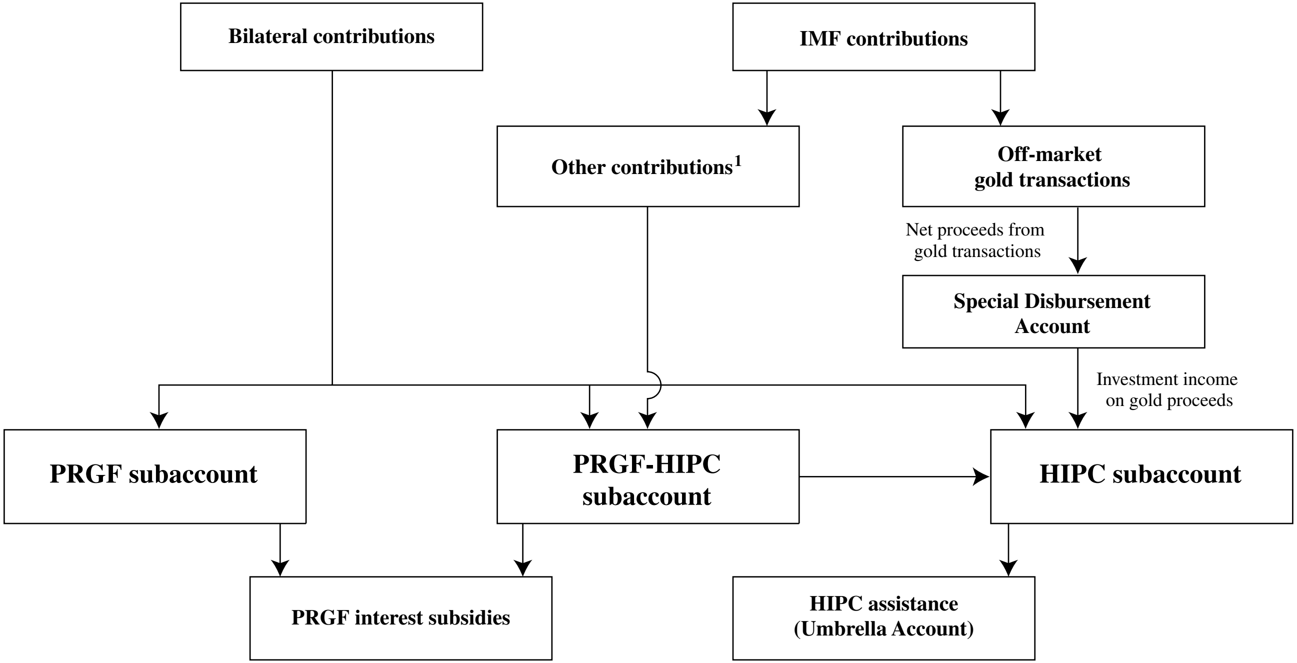
TABLE IV.7. PRGF-HIPC TRUST AND RELATED ACCOUNTS: COMBINED INCOME STATEMENTS, FINANCIAL YEAR ENDED APRIL 30, 2001

(In millions of SDRs)

	PRGF-HIPC Trust Account Subaccount				Umbrella Account for HIPC Operations	Post-SCA-2 Administered Account	Combined Total
	PRGF-HIPC	PRGF	HIPC	Combined			
Balance, April 30, 2000	491.0	7.3	12.7	511.1	160.8	257.1	928.9
Investment income	52.7	0.6	5.6	45.3	11.2	7.9	64.3
Interest expense	(1.4)	—	(13.5)	(1.4)	—	—	(1.4)
Other expenses	(0.2)	—	—	(0.2)	—	—	(0.2)
Operational income (loss)	51.0	0.5	(7.9)	43.6	11.2	7.9	62.7
Contributions received	138.0	6.1	47.7	191.9	262.8	—	454.7
Grants	—	—	(262.8)	(262.8)	—	—	(262.8)
Disbursements	—	—	—	—	(91.4)	—	(91.4)
Net income (loss)	189.1	6.7	(223.0)	(27.2)	182.6	7.9	163.2
Transfers	55.0	—	—	55.0	—	(171.6)	(116.6)
Net changes in resources	244.1	6.7	(223.0)	27.8	182.6	(163.7)	46.6
Balance, April 30, 2001	735.1	14.0	(210.3)	538.8	343.4	93.3	975.5

Note: Numbers may not add to totals due to rounding.

FIGURE IV.4. FINANCIAL STRUCTURE OF THE PRGF-HIPC TRUST



[1]Includes transfers equivalent to the cost of administering PRGF operations for FY1998–2004 and transfers of part of the interest surcharge on certain outstanding purchases under the Supplemental Reserve Facility.

in NPV terms, compared with the estimated HIPC Initiative financing requirement of SDR 1.9 billion in NPV terms. Since expected HIPC financing requirements exceed resources earmarked for the HIPC Initiative, and the investment income on the net proceeds derived from gold sales accrues only slowly over time, the structure of the PRGF-HIPC Trust allows the HIPC subaccount to borrow resources from the PRGF-HIPC subaccount for HIPC operations.

All HIPC Initiative assistance provided by the PRGF-HIPC Trust is disbursed from the HIPC subaccount to the beneficiaries. The investment earnings on resources generated from gold sales held in the SDA will be made available to the HIPC subaccount to meet the costs of the HIPC Initiative. As the HIPC subaccount is replenished over time, any borrowings from the PRGF-HIPC subaccount are to be repaid. To preserve the value of resources for the continuation of PRGF operations, the HIPC subaccount will pay interest on the temporary use of resources of the PRGF-HIPC subaccount at a rate equal to the average return on investment of SDA resources.

Self-Sustained PRGF

Following the interim PRGF, the IMF intends to continue to provide concessional lending to eligible members under PRGF-like arrangements. It is expected that both loan and subsidy resources for this purpose will be provided through a revolving use of the balances currently accumulating in the Reserve Account of the PRGF Trust.

New Investment Strategy

In March 2000, the IMF initiated a new investment strategy for the assets of the SDA and other resources of the PRGF and PRGF-HIPC Trusts with the objective of supplementing returns over time while maintaining prudent limits on risk. The supplemental income will be used to enhance the level of protection accorded to lenders to the PRGF Trust, provide an additional margin for subsidizing PRGF lending, generate additional subsidy and grant resources for interim PRGF and HIPC operations, and expand the size of the self-sustained PRGF.

Under the new approach, the maturity of SDA, PRGF, and PRGF-HIPC investments was lengthened by shifting the bulk of assets previously invested in short-term SDR-denominated deposits with the BIS to portfolios

BOX IV.4. INVESTMENT STRATEGY

At the core of the investment mandate given to external bond managers is the one- to three-year benchmark bond index, which embodies the IMF's baseline risk and return preferences for longer-term bond investments and is the neutral position toward which external bond managers are expected to gravitate. The bond benchmark is a customized index[1] comprising the Merrill Lynch one- to three-year government bond indices for Germany, Japan, the United Kingdom, and the United States with each market weighted to reflect the currency composition of the SDR basket.

The new strategy is implemented on the IMF's behalf by the BIS, the World Bank, and three private investment managers. Assets are actively managed and invested in domestic government bonds of the euro zone, Japan, the United Kingdom, and the United States, as well as bonds issued by eligible national and international financial organizations in SDRs or a currency included in the SDR basket. Managers are permitted to invest in eligible securities across the maturity spectrum, provided that the sensitivity of the portfolio to changes in market interest rates remains broadly in line with that of the benchmark index.

Investments may be made only in cash securities; positions in derivative securities are not permitted. There may be no short selling or any form of leverage. Foreign exchange risk is to be tightly controlled through regular portfolio rebalancing.

[1]In contrast, the MTI benchmark employs the J.P. Morgan one- to three-year government bond indices for Germany, Japan, the United Kingdom, and the United States, weighted to reflect the composition of the SDR basket.

of bonds and other medium-term instruments (MTIs)[15] structured to reflect the currency composition of the SDR basket (Box IV.4). Remaining short-term deposits are held at a level sufficient to meet liquidity requirements[16]

[15]MTIs perform similarly to domestic government bonds, but are claims on the BIS that offer ready liquidity and the possibility to benefit from a credit spread over domestic government bonds.

[16]Short-term deposits held to meet liquidity requirements are kept at a level sufficient to meet three-months' projected cash outflows for PRGF subsidies and HIPC grants, plus a margin for deposits that may be withdrawn by depositors in case of balance of payments need and for possible delays in the repayment of PRGF obligations.

and to conform with the administrative arrangements agreed with certain contributors.

In the first 12 months since its inception, the new investment strategy added about 220 basis points (on an annualized basis, net of fees) to returns over the previous approach of investing in SDR-denominated deposits—generating supplemental income of nearly SDR 140 million in support of PRGF and PRGF-HIPC operations.