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ESTABLISHMENT OF AN IFAD HEAVILY-INDEBTED POOR COUNTRIES DEBT  
INITIATIVE TRUST FUND

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## ESTABLISHMENT OF AN IFAD HEAVILY-INDEBTED POOR COUNTRIES DEBT INITIATIVE TRUST FUND

### Preamble

1. The Executive Board and the Governing Council considered documents EB 96/59/R.73 (December 1996) and GC 20/L.6 (February 1997), respectively. The Executive Board document proposed IFAD's participation in the International Monetary Fund (IMF)/World Bank Debt Initiative for Heavily-Indebted Poor Countries (HIPC DI) as an element of IFAD's broader policy framework for managing operational partnerships with countries that have arrears with IFAD, or that face the risk of having arrears in the future because of their debt-service burden. The Executive Board endorsed the principle of IFAD's participation in the HIPC DI, and forwarded the proposal to the Governing Council. The Governing Council approved IFAD's participation (Resolution 101/XX, attached as Annex II) and delegated further approval authority to the Executive Board. Document EB 97/62/R.7 (December 1997) proposed, for Executive Board consideration, an operational policy framework for IFAD's participation in the HIPC DI including a proposal to establish an IFAD Trust Fund for the Heavily-Indebted Poor Countries Debt Initiative. The Executive Board endorsed the proposed operational framework and IFAD Trust Fund, forwarded the proposal to the Governing Council and recommended the adoption of the draft Resolution attached in Annex I hereto.

### I. Introduction

2. It is the purpose of this paper to provide the Governing Council with: (a) a summary of the basic design of the IMF/World Bank HIPC DI; (b) a synthesis of the Governing Council decision taken in February 1997; (c) a summary of the main developments in the ongoing design of the HIPC DI and the issues outstanding; (d) an overview of country-specific HIPC DI actions taken or planned for the near future; (e) the proposed elements of IFAD's operational policy framework for its participation in the HIPC DI; and (f) the decisions required from IFAD's governing bodies.

### II. The Debt Initiative for Heavily-Indebted Poor Countries: A Summary Overview of the Basic Design

3. Objective of the HIPC Debt Initiative. The objective of the HIPC DI is to reduce the net present value (NPV) of the debt of poor countries that carry unsustainable levels of debt (see Table 1 below) to a level that will no longer compromise their ongoing economic reform and poverty eradication efforts.

4. Guiding Principles. A number of principles have guided the design of the HIPC DI. They include the principles that the HIPC DI must: (i) address a country's total debt sustainability with a reliable exit strategy and involve all creditors to be effective and equitable; (ii) assist only countries with a track record of economic policy and structural reform, and that are making efforts towards poverty eradication; (iii) build on the existing mechanisms of debt relief; (iv) preserve the financial integrity of the international financial institutions (IFIs) involved; (v) secure a continued flow of new external financing on appropriately concessional terms from IFIs and from the private sector.

5. The Process. When a country has met the preliminary performance requirements (of policy reform, structural adjustment, poverty eradication measures and no arrears), a process is put in motion

that includes: a debt sustainability analysis (DSA); a debt reconciliation process, which determines the country's debt to each IFI; and consultation among all creditors (including the Paris Club and the IFIs) under the leadership of the World Bank and IMF. As a result of this consultation, agreement is reached on: the total level of debt; economic reform and social sector development performance targets for the "interim period" (in principle, the next three years); the global NPV-of-debt relief package that will be provided when these targets are met; and the burden-sharing of this debt relief. This is called the "decision point".

6. The agreed programme for the interim period is then set in motion, closely monitored against agreed performance indicators, and with periodic reviews of the DSA. During this period the countries will be supported with the additional concessional external financing envisaged at the decision point. At the end of this interim period, i.e., at the "completion point", countries are expected to have established a policy framework and economic structure that will allow them to sustain the benefits from the NPV-of-debt relief mechanism agreed upon at the decision point. At that point, in the basic design of the HIPC DI, the Paris Club would be expected to provide an 80% stock-of-debt relief operation (against 67% under the Naples Terms), the non-Paris Club bilaterals and commercial creditors would be called upon to provide relief on comparable terms (essentially flow reschedulings involving an NPV reduction of up to 80%), and the international financial institutions would deliver the residual NPV-of-debt relief required to make the debt burden sustainable (as agreed at the decision point).

7. Funding Mechanisms. The HIPC DI involves two basic sets of financial movements with regard to the IFI participants: (a) agreed reduction of debt repayments from debtor countries to IFI creditors; and (b) payments to the loan fund accounts of IFIs to compensate for the loss of the financial reflows implicit in the reduction of debt repayments. A basic principle of HIPC DI is that although participating IFIs will adopt a common target for debt reduction in the case of each eligible and confirmed country participant, the modality of debt reduction to the agreed level will be decided independently by each IFI according to the instruments available to it, considerations of institutional financial integrity, and specific country circumstances (e.g., the modality for debt reduction employed by the World Bank/International Development Association (IDA) will be different in the case of Bolivia compared to that of Uganda). Equally, each IFI will decide upon the mechanism most appropriate to itself for the mobilization and management of resources to compensate loan fund accounts for the reduction of reflows. The IMF will use a special Enhanced Structural Adjustment Facility (ESAF) HIPC Trust managed by the IMF, which Trust will be financed from IMF's own resources. The World Bank will use a World Bank component of the HIPC Trust Fund, which will receive resources from the International Bank for Reconstruction and Development (IBRD) to compensate IDA for debt repayments foregone as part of debt reduction under HIPC DI. Many other participating IFIs have not yet identified the specific mechanisms they will employ for debt reduction and loan fund account compensation, although a number have indicated that they will also use mechanisms entirely internal to themselves. For those institutions that may decide that it is either inconvenient or not cost-effective to establish their own mechanisms, the World Bank/IDA has established an HIPC Trust Fund to assist in the mobilization and management of resources to support IFI participation in the HIPC DI. To date, this Trust Fund (excluding its World Bank/IDA component dedicated to the management of resource flows within the World Bank group) has been used exclusively as a repository of bilateral (i.e., "external") funds to support the HIPC DI operations of the two IFIs (the Nordic Development Fund and the African Development Bank) that have decided not to establish internal handling mechanisms. With regard to the two IFIs, it is not yet clear whether the African Development Bank will employ the HIPC Trust Fund to handle all resources required to cover HIPC DI operations or only to handle bilateral/external contributions in support of the same.

Table 1: Projected Country Participation in the HIPC DI:  
Possible Timing of Decision Points a/

1997 First Half	1997 Second Half	1998	1999	2000-2001
Uganda <u>b/</u>	Bolivia <u>b/</u> Burkina Faso <u>c/</u>	Chad Guinea-Bissau Mauritania Sierra Leone Togo Viet Nam Côte d'Ivoire Ethiopia Guyana <u>b/</u> Mali Mozambique <u>c/</u> Senegal	Congo Guinea Madagascar Nicaragua Niger Tanzania, United Republic of Yemen Zambia	Angola Burundi Cameroon Central African Republic D.R. Congo Equatorial Guinea Honduras Myanmar Rwanda Sao Tome and Principe

Source: World Bank and IMF.

a/ This table includes 33 of the 41 HIPCs. The table excludes 8 countries: Liberia and Somalia (for lack of information); Nigeria (which is not IDA-only); Ghana, Kenya and Laos (which have never received a concessional rescheduling from the Paris Club); The Sudan (for which no allowance has been made for possible participation in the HIPC DI); and Benin (debt is considered sustainable).

b/ Completion point assumed to be one year after decision point.

c/ Completion point assumed to be two years after decision point.

### III. IFAD's Governing Council Decision

8. Governing Council Resolution 101/XX on IFAD's participation in the IMF/World Bank HIPC DI was approved in February 1997 (see Annex II). With this resolution, the Governing Council endorsed the approach of the HIPC DI and decided that IFAD will participate, mainly on the grounds of the link between the manageability of debt and the sustainability of poverty eradication efforts.

9. The Governing Council decided that IFAD will participate on a country-by-country basis. It was understood that IFAD will abide by the general conditions and targets established for each country HIPC DI in which it participates. Authority was delegated to the Executive Board to approve, on a country-by-country basis, the debt-relief required from IFAD as part of the overall HIPC DI effort to reduce a country's debt to a sustainable level. The Governing Council also gave the Executive Board the authority to amend ex post the lending terms and conditions of approved loans to reflect this debt relief under the HIPC DI. It delegated authority to the Executive Board to approve any general or country-specific agreements between IFAD and the World Bank related to IFAD's participation in the HIPC DI. The Governing Council also retained the two options of participation in the HIPC DI, depending on the country circumstances: through the IDA-administered Trust Fund; or in parallel but in full coordination.

#### IV. Developments in the Design of the HIPC DI and Outstanding Issues

##### Design Developments: Lessons Learned from Implementation

10. The HIPC DI is a process-based initiative, and, as such, its design is expected to evolve over time. It is important to assess progress on an ongoing basis and to learn from experience. After a year of implementation of the HIPC DI, the IMF and World Bank have learned lessons that have now been built into the HIPC DI. These adjustments relate to almost every aspect of the HIPC DI (the technical parameters, the process, the modalities and the instruments) and include the following:

11. Export Denominator. Debt sustainability relates the NPV of a country's future aggregate debt to its projected revenue from the export of goods and services. Originally, workers' remittances were to be included in the export revenue calculations. However, given the absence of reliable data in most HIPCs, and in order not to penalize countries with better statistics, it has been decided to exclude workers' remittances from the export base. Where available, they will be included in the vulnerability assessment or sensitivity analysis as a factor of strength. Henceforth, the analysis will also use the simple three-year average of actual exports in the years prior to the completion point to define a country's underlying export capacity on a more stable basis.

12. Debt Service in Relation to Fiscal Resources. Initially, debt sustainability analyses related a country's NPV-of-debt to its export base. Other indicators of debt-servicing capacity, including debt service in relation to fiscal revenues and to Gross Domestic Product (GDP), were used only as vulnerability factors and to establish the target range for the NPV-of-debt to exports ratio. This approach puts open economies with relatively large export sectors at a disadvantage, even though their debt burdens may be similar to less-open countries when measured in terms of other indicators of a government's debt-financing capacity. Participating IFIs have agreed to broaden the primary (essentially export-related) eligibility criteria to include a fiscal ratio, mainly to capture the question of fiscal sustainability of debt servicing. The Boards of the IMF and the World Bank have endorsed the approach of considering, on a case-by-case basis, an NPV-of-debt to exports target below 200% at the completion point, provided that the country concerned meets two criteria at the decision point: an exports-to-GDP ratio of at least 40%; and a minimum threshold of fiscal revenue in relation to GDP of 20%. For countries meeting these thresholds, the NPV-of-debt to exports target will be set at a level that achieves a 280% ratio of the NPV-of-debt to revenue at the completion point; this methodology implies that countries that meet these thresholds will also have a high external-debt-to-GDP ratio.

13. Debt Sustainability Target Range. It was originally considered that a country's debt was "unsustainable" when the NPV-of-debt to exports ratio exceeded 250%, and "stressed" when it was in the 200-250% range; with the debt-service ratio above 25% and 20-25%, respectively. Based on the experience gained with a three-phased vulnerability assessment, it has now been decided that the target range for NPV-of-debt relief will be in the bottom half of the range, i.e., 200-225%, to ensure the robustness of the exit from the unsustainable debt burden.

14. Policy Conditionality. The HIPC DI debt relief, which will be provided at and subsequent to the completion point, is committed at the decision point in the context of an agreement on an appropriately strong structural adjustment, policy reform and social sector development agenda. The HIPC DI documents, even in their preliminary stages, will indicate which macroeconomic, structural, social development and poverty eradication policy actions and indicators will be monitored during the interim period. The World Bank and IMF have retained their own ESAF and Structural/Sector Adjustment Programme conditionality, with further allowance for social-sector/ poverty eradication policy objectives. Other participating IFIs have the opportunity to add to or modify conditionalities in

the process of production of the final country HIPC DI document, which establishes the common conditions for release of assistance by all participating institutions.

15. Length of the Interim Period. The basic design of the HIPC DI envisages a three-year interim period between the decision point and the completion point (after having met the basic eligibility criterion of a track record - of at least three years - of economic policy reform and structural adjustment). It has now been decided that the length of the interim period will be determined with more flexibility, in order to take into account the pre-eligibility track record of a country. This is resulting in shorter interim periods in the early country cases under the HIPC DI, in recognition of good policy performance. This will not constitute a precedent for HIPCs that do not have similarly strong performance records.

16. Interim Assistance. The World Bank and IMF reiterate the importance of adequate additional financial resources on appropriately concessional terms to ensure that the adjustment (and poverty eradication) programmes are fully financed during the interim period (and also after the completion point and the delivery of the debt relief). IFIs are also encouraged to provide during the interim period, at their discretion, part of the assistance they would be committed to provide at the completion point.

17. Debt-Management Capacity. The HIPCs continue to face severe constraints in their capacity to: collect and manage debt information; analyse their debt-servicing capacity and debt sustainability; assess the implications of their debt-servicing capacity for debt relief requirements and for their future borrowing strategies; and integrate their debt-management system into their macroeconomic management and policy-making process. It has been decided that from now onward these elements will appear in all HIPC DI documentation; and IFIs will be encouraged to identify ways in which a country's capacity could be strengthened and how local ownership of capacity-building efforts could be enhanced.

#### Outstanding Issues

18. As a process-based initiative, the HIPC DI also has a number of outstanding issues that need to be pursued; they include the following:

19. The Consultation Process. The World Bank and IMF are aware of the need to improve further the debt reconciliation process considerably and for an early consultation of all creditors, including IFIs, if a timely, reliable and collective response is sought. They are also aware of the need to strengthen the process in order to lead all IFIs in a coordinated fashion to the decision point - as a group with common terms and policy conditions - with the debtor countries.

20. The Executive Boards of the World Bank and IMF have had to approve or endorse the first three country cases (Bolivia, Burkina Faso and Uganda) without debt reconciliation having been concluded. A more intensive consultative process for debt reconciliation has been launched simultaneously addressing the methodological issues related to calculation of NPVs-of-debt for each IFI.

21. The dependence of the volume of debt relief to be supplied upon the debt:export ratio at completion point (i.e., a time in the future) makes it impossible to fully quantify the IFI burden at decision point, and this has created problems for IFIs which would like to quantify their obligations at the point at which commitments are made (i.e., the decision point). This concern has been answered by establishing commitments at the decision point in terms of a fixed percentage reduction of debt actually disbursed at that point. Should the debt:export ratio at completion point vary significantly from the

estimate, IFIs may be requested to increase the NPV-of-debt relief by no more than 10% and on a purely voluntary basis.

22. Paris Club Burden-Sharing. The Paris Club has committed itself to a case-by-case approach and an understood objective of topping-up NPV-of-debt relief to 80% (from the Naples Terms of 67%). The IMF and the World Bank have opened discussions with the Paris Club on opportunities for establishing full proportionality between IFI and Paris Club debt relief in individual HIPC DIs.

23. Evolving Cost Estimates. The cost to IFIs of the HIPC DI will undergo review and revision and will depend on: (a) the overall cost of the HIPC DI and (b) the burden-sharing approach<sup>1/</sup>. The overall cost is determined by revisions in the country-specific DSAs (taking into account actual debt figures, better definitions of eligible debt, a simulated full application of traditional debt-relief mechanisms, and higher export or revenue projections); application of the three-year export average; application of the fiscal ratio criterion; the choice of NPV-of-debt target ratios; and the timing of the completion points.

24. The most recent available estimate (7 July 1997), shown in the table below, assesses the total cost of the HIPC DI at USD 7.4 billion, for a target NPV-of-debt to exports ratio of 200%, and USD 6.3 billion for a 220% target ratio, in 1996 NPV terms. Costs expressed in 1997 present value terms would be about USD 500 million higher. With the earlier estimates of IFAD's share of IFI debt-relief requirements (of 1.28%), the base scenario cost to IFAD would amount to USD 50-60 million (depending on the burden-sharing approach), and USD 41-50 million, respectively. Figures are also provided for a scenario of lower rates of export growth.

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<sup>1/</sup> The basic design foresaw, briefly: (a) Paris Club relief up to 80% of NPV relief, if required; and (b) IFIs provide residual debt relief to secure exit.

The modified residual approach: (a) Paris Club creditors provide up to 80% NPV reduction on eligible debt; (b) if this 80% NPV reduction is insufficient, IFIs would provide sufficient assistance to achieve debt sustainability; but (c) if this latter IFI relief action would imply higher assistance (in relation to the NPV of their IFI claims at the completion point) than that provided by the bilaterals (after full application of Naples Terms), then proportional action is expected (in relation to the NPV-of-debt after the full application of Naples Terms) from both bilateral and IFI creditors.

The approach proposed by the Paris Club creditors: (a) proportional action by all creditors (after Naples Terms by the bilaterals) up to a cap of 80% NPV reduction by the Paris Club (and other non-IFI creditors); and (b) IFIs provide any additional assistance required under the HIPC DI beyond this level.

The fully proportional approach: IFIs would provide proportional assistance with bilateral creditors at all levels of assistance. This will require an equal percentage reduction in outstanding NPV-of-debt, measured at the completion point, from IFI and bilateral creditors (after full application of Naples Terms).



Table 2: HIPC DI: Cost Estimates for Alternative Scenarios  
(in USD millions, in 1996 present value)

		Baseline Assumptions	NPV-of-Debt to Exports Target of 220% Rather than 200%	Export Growth Rate 2% Lower in Every Year before the Completion Point
Total Cost		7 400	6 300	8 500
Modified Residual Approach	Bilateral and commercial creditors	3 600	3 100	3 900
	Multilateral creditors	3 900	3 200	4 600
	of which IFAD	50 (1.28%)	41 (1.28%)	52 (1.13%)
Paris Club Approach	Bilateral and commercial creditors	2 700	2 300	3 000
	Multilateral creditors	4 700	3 900	5 400
	of which IFAD	60 (1.28%)	50 (1.28%)	61 (1.13%)
Fully Proportional Approach	Bilateral and commercial creditors	3 200	2 600	3 700
	Multilateral creditors	4 200	3 600	4 800
	of which IFAD	54 (1.28%)	46 (1.28%)	54 (1.13%)

Source: World Bank and IMF.

Table 3: HIPC DI: Countries for Which Costs are Projected in the Current Estimates a/

Cost Projection Based on:			
Decision point commitments in principle (agreed target for NPV-of-debt to exports shown in parentheses)	Preliminary HIPC document discussed by the Executive Boards of the IMF and the World Bank (NPV-of-debt ratio target assumed for costing purposes shown in parentheses)	Additional countries that may be eligible for assistance under the openness/fiscal criteria (costs based on NPV-of-debt to fiscal revenue target of 280%)	Countries with NPV-of-debt to exports ratio exceeding 200% at the assumed completion point, after full use of traditional debt relief mechanisms
Uganda (target 202%)	Bolivia (target 225%) Burkina Faso (target 205%) Côte d'Ivoire (NPV-of-debt to fiscal revenue target of 280%)	Guyana Mauritania	Burundi D.R. Congo Ethiopia Guinea-Bissau Madagascar Mauritania Mozambique Myanmar Nicaragua Niger Rwanda Sao Tome and Principe Tanzania, United Republic of Zambia

Source: World Bank and IMF.

a/ No costs are expected for Cameroon and The Congo.

25. Arrears. Even though the HIPC DI focuses on future debt repayment obligations, several IFIs have raised the issue of outstanding arrears (past dues) negatively affecting these institutions' capacity to remain operational in the debtor countries concerned. Even though the HIPC DI framework does not include any formal instruments to deal with the arrears issue (except for the inclusion, in the basic good performance eligibility criteria, of the condition that the country would not have arrears), it has been agreed that the process leading to decision point will be used to review the existing arrears issues and options.

#### V. Specific Country Cases and IFAD's Participation

26. So far IFAD has been approached by the HIPC DI in relation to Bolivia, Burkina Faso, Côte d'Ivoire and Uganda. The table below highlights some of the main features of the HIPC DI for these countries.

Table 4: Comparative Table of HIPC DI Action

	Uganda	Burkina Faso	Bolivia	Côte d'Ivoire
Current Debt Ratio	248.9	249.8	259.1	188.6
Current Debt-Service Ratio	21.3	18.1	28.3	21.8
Main Export Sensitivity	coffee	cotton	zinc	cocoa, coffee
Target Debt Ratio to be Achieved with Debt Relief	202%	205%	215-235%	-
Proposed Decision Point	April 97	October 1997	September 1997	1997
Proposed Completion Point	April 98	April 2000	September 1998	2000

Source: World Bank and IMF

27. In the case of Uganda, the World Bank and IMF Executive Boards have formally approved their participation in the HIPC DI, and the World Bank and IMF have requested an early formal commitment from IFAD to "provide assistance at the completion point (April 1998) equivalent to 21% NPV-of-debt relief on its claims on Uganda at the decision point (April 1997, based on 30 June 1996 data), with the actual amount of assistance implied by this commitment to be determined before the completion point on the basis of the reconciled data". The Executive Board approved IFAD's participation in the Uganda HIPC DI at its Sixty-First Session in September 1997 (document EB 97/61/R.14 ). The Executive Board approved IFAD's participation in the Burkina Faso HIPC DI at its Sixty-Second Session in December 1997 (document EB 97/62/R.10), with IFAD's commitment (USD 2 000 000 in NPV terms) representing 17.1% of Burkina Faso's debt (NPV terms) to IFAD at the decision point (based on December 1996 data). A proposal to the Executive Board for IFAD participation in the Bolivia HIPC DI is under preparation.

28. Future Plans. The most recent information (see Table 1) indicates future action for the following countries:

- (a) Côte d'Ivoire: a final HIPC DI proposal to the Executive Board of the World Bank and IMF is expected in early 1998;
- (b) Guyana: entering the HIPC DI on the grounds of fiscal unsustainability of debt, with the preliminary HIPC DI document having been circulated in late-August 1997;

- (c) Mali, Senegal, and Ethiopia: the options are under review, with the DSA expected for the fourth quarter of 1997;
- (d) Togo; and
- (e) Mozambique: the former Soviet Union's debt issue is being reviewed (Russia having joined the Paris Club, as agreed during the Denver Summit), with the preliminary HIPC DI document having been circulated at end-August 1997.

29. The DSA for Benin has been finalized. The country's debt is considered as being sustainable, and hence Benin would not qualify for HIPC DI debt relief.

#### VI. IFAD's Operational Policy Framework for Participating in the HIPC DI

30. The Governing Council made the basic policy decision authorizing IFAD's participation in the HIPC DI on a country-by-country basis in its Twentieth Session. It is the purpose of this section to provide an operational policy framework for IFAD's concrete engagement in the HIPC DI. This framework aims at guiding the staff concerned in their country-by-country participation in the HIPC DI process, while securing a degree of institutional consistency of approach across regions and countries, and safeguarding IFAD's financial integrity. The Governing Council is requested to approve this framework for HIPC DI action by IFAD.

#### Establishment of an IFAD-Administered Trust Fund

31. As indicated in paragraph 7, major IFI HIPC DI stakeholders (e.g., the IMF and the World Bank) have established internal mechanisms for managing resources dedicated to supporting debt reduction operations. The internal nature of these mechanisms reflects the fact that all or a major portion of the resources involved will be sourced from the institutions themselves, and compensatory shifts of resources will involve movement from one internal account to another, in relation to which it would not be either necessary or cost-effective to organize the transfer of funds through a third and external account managed by another institution. Correspondingly, and for the same reasons, it is proposed that IFAD will establish its own Trust Fund, i.e., the parallel mechanism provided for in the Governing Council Resolution 101/XX approved in February 1997. This Trust Fund would receive resources, from within IFAD and from other sources, specifically dedicated as compensation to the loan fund account(s) for agreed reductions in loan repayments under HIPC DI. The draft resolution to actually establish the Trust Fund is attached as Annex I for consideration and adoption by the Governing Council. The draft resolution also defines the financial/legal instruments to be used by IFAD to transfer the country's eligible debt obligation to the Trust Fund, for both modalities referred to in paragraph 33 (f). It is planned that all decision point commitment under HIPC DI will have been made by 2001/2, with actual reductions in scheduled loan repayments beginning at the subsequent completion points at each agreed country HIPC DI.

#### Country Eligibility for IFAD Participation in the HIPC DI

32. IFAD has committed itself to participate in the HIPC DI on a country-by-country basis. The Governing Council resolution established the link between the sustainability of debt and the sustainability of poverty eradication efforts as the main rationale for IFAD's involvement in the HIPC DI. The main issues IFAD will address during the preparation of each specific HIPC DI are: the country's policy focus on poverty eradication; the strength of the country's poverty eradication and rural development programme; and the sensitivity to poverty eradication of the ongoing structural adjustment efforts.

### The Process and Modalities of IFAD's Participation

33. The Executive Board would be requested to consider each HIPC DI country case on the basis of a recommendation of the President of IFAD. To develop this recommendation IFAD would:

- (a) fully participate in the established HIPC DI process (see section II), coordinated by the World Bank. As only a first step to this effect, IFAD will provide the World Bank with the information related to the debt owed to it by the different HIPCs; and the World Bank will facilitate IFAD's debt reconciliation;
- (b) where relevant, initiate the dialogue on the issue of arrears, in consultation with the other HIPC DI partners; and identify, for management consideration, the issues and options for addressing the arrears problem, in line with IFAD's policy on the matter;
- (c) after consultation on the basis of the DSA documentation, adopt the World Bank/IMF decisions regarding the length of the interim period and the timing of the completion point; the target NPV-of-debt to exports ratio, after a review of the sensitivity analysis in the DSA; and the aggregate debt-relief requirement;
- (d) contribute to the development of the HIPC DI conditionalities for adoption by all participating IFIs, reflecting: IFAD's poverty eradication concerns; the supplementary assurances already built into IFAD's current Loan Agreements; the need to enhance fiscal resource allocations for rural poverty eradication; and define IFAD's role in the follow-up to these issues;
- (e) define IFAD's percentage share of total debt at the decision point, which will also be IFAD's percentage share of debt relief at the completion point; the absolute amount of NPV-of-debt relief IFAD would need to provide at the completion point, assessing also the implications of the sensitivity analysis for the possible costs to IFAD; the cap on IFAD's debt-relief exposure, taking into account the need for a reliable exit strategy;
- (f) provide IFAD management with a proposal regarding the options for the modalities of NPV-of-debt relief. The main options include:
  - (i) for countries where the short-term debt-service problem (indicated by the debt-service ratio) is more acute than the long-term debt burden (reflected by the NPV-of-debt to exports ratio), IFAD could provide debt relief by drawing, on the IFAD Trust Fund, a number of early debt repayment obligations due after the completion point (simultaneously writing-down the country's own obligations to IFAD), till the required debt relief has been achieved;
  - (ii) for countries where the debt burden is mainly a long-term problem, the reduction of the country's NPV-of-debt to IFAD could be achieved by redefining the profile of the country's repayment obligations to IFAD. This would entail consideration of a number of elements, including: grace periods; reassessment of the profile of instalments; reassessment of the maturity period of specific loans; and combinations of these elements. The Trust Fund would finance the NPV-loss to IFAD that results from this modality of NPV-of-debt relief; and
  - (iii) a combination of the two approaches;

- (g) negotiate an agreement with the debtor country that would establish the amortization schedule of the aggregate outstanding debt due to IFAD after debt relief. This agreement would replace the amortization schedules of the individual loan agreements, and would become effective from the completion point;
- (h) define the level of resources required from the Trust Fund; the schedule of draw-down of these resources; and the Trust Fund replenishment requirements;
- (i) define IFAD's plans to enhance its support on appropriately concessional terms to the country's policy and poverty eradication efforts during the interim period. This will preferably relate to the elements of vulnerability identified in the DSA. This may also include proposals for IFAD to participate in multi-donor programme to enhance debt management capacity-building.

## VII. Decisions Required

34. IFAD's management requests the Governing Council to:
- (a) review the proposed operational policy framework and provide further guidance;
  - (b) approve the proposed policy framework (see section VI);
  - (c) adopt draft resolution (in Annex I).

DRAFT RESOLUTION ON THE ESTABLISHMENT OF AN IFAD TRUST FUND  
FOR THE HEAVILY-INDEBTED POOR COUNTRIES DEBT INITIATIVE

Resolution .../XXI

The Establishment of an IFAD Trust Fund for the Heavily-Indebted Poor Countries Debt Initiative

The Governing Council of IFAD,

Recalling its Resolution 101/XX on IFAD's Participation in the Debt Initiative for Heavily-Indebted Poor Countries (HIPC DI), adopted on 21 February 1997;

Further recalling its Resolution 16/IV on the Establishment of a General Reserve, adopted on 11 December 1980, of which one of the objectives is to cover possible delinquencies in the receipt of loan service payments;

Noting the establishment of the HIPC DI Trust Fund by the World Bank and noting the full support of all other international financial institutions therefor;

Having considered document GC 21/L.6 on the Establishment of an IFAD Heavily-Indebted Poor Countries Debt Initiative Trust Fund and the draft Resolution contained therein;

Decides that:

1. For the purpose of paragraph 3(ii) of Resolution 101/XX, a trust fund for the HIPC DI shall be established ("the IFAD HIPC DI Trust Fund").
2. IFAD is hereby appointed the administrator of the IFAD HIPC DI Trust Fund.
3. The IFAD HIPC DI Trust Fund is authorized to receive the following resources:
  - (a) subject to the approval of the President of IFAD, contributions made in a freely-convertible currency by non-Member States of IFAD, other entities and private individuals;
  - (b) funds, in such amounts as it shall specify, that the Executive Board may, from time to time, decide to transfer from the resources of IFAD, including the General Reserve of IFAD;
  - (c) contributions made in a freely-convertible currency directly by Member States of IFAD;
  - (d) the investment income received on the resources of the IFAD HIPC DI Trust Fund; and
  - (e) funds from other resources, subject to the approval of the Executive Board.

4. The adequacy of the resources of the IFAD HIPC DI Trust Fund shall be reviewed periodically by the Executive Board. In that context, the Executive Board shall decide, from time to time, the maximum amount of resources that may be held by the IFAD HIPC DI Trust Fund.
5. IFAD shall invest the resources of the IFAD HIPC DI Trust Fund in a prudent and non-speculative manner according to the same rules, guidelines and criteria as may apply to its regular resources.
6. The IFAD HIPC DI Trust Fund shall be used to reduce the debt burden of Member States declared eligible under the HIPC DI to a sustainable level, through a Debt Relief Package relative to the debt of each Member State to IFAD.
7. Upon the eligible Member State receiving approval at Completion Point for its Debt Relief Package from the World Bank, IMF and other participating multilateral creditors, the Trust Fund administrator shall establish a sub-account for that Member State and pay into such sub-account the agreed amount of the Debt Relief Package to be provided by IFAD from the resources of the IFAD HIPC DI Trust Fund. All payments made under that Member State's Debt Relief Package by IFAD shall be made thereafter from the said sub-account.
8. Withdrawals from the IFAD HIPC DI Trust Fund for the purposes stated in paragraph 6 above shall be made by the President of IFAD, in accordance with the Debt Relief Package approved by the Executive Board for each Member State, in the following manner and in accordance with an agreement to be entered into by IFAD and the Member State concerned: (a) either the IFAD HIPC DI Trust Fund shall make to IFAD payments or repayments on behalf of the borrowing Member State every six months until the full amount of the IFAD Debt Relief Package for that country shall have been disbursed; or (b) the IFAD HIPC DI Trust Fund shall pay to IFAD the NPV-loss incurred in adjusting that Member State's repayment schedule for one or more loans received from IFAD.
9. The incremental administrative expenditures directly incurred by IFAD in administering the IFAD HIPC DI Trust Fund shall be paid to IFAD from the resources of the IFAD HIPC DI Trust Fund.
10. The Executive Board shall terminate the IFAD HIPC DI Trust Fund upon a proposal from the President of IFAD at an appropriate time. At that time, the Executive Board shall decide upon the arrangements for the termination of the IFAD HIPC DI Trust Fund and the disposal of the resources of the IFAD HIPC DI Trust Fund.
11. The President of IFAD shall report periodically to the Executive Board on the operations of the IFAD HIPC DI Trust Fund and the resources held by the IFAD HIPC DI Trust Fund, as well as providing the Executive Board with financial statements thereon for each year.

IFAD'S PARTICIPATION IN THE  
DEBT INITIATIVE FOR HEAVILY-INDEBTED POOR COUNTRIES

Resolution 101/XX

IFAD's Participation in the Debt Initiative for Heavily-Indebted Poor Countries

The Governing Council of IFAD,

Recalling the Lending Policies and Criteria, adopted in December 1978, its Resolution 83/XVII on IFAD's Lending Terms and Conditions, adopted on 28 January 1994, its Resolution 89/XVIII on the Amendment of the Lending Policies and Criteria, adopted on 26 January 1995, and its Resolution 94/XIX on the Amendment of the Lending Policies and Criteria, adopted on 18 January 1996, all of which amended the Lending Policies and Criteria;

Concerned by the effect that a high level of indebtedness has upon the rural poor of the countries in such a position and on the sustainability of a country's poverty eradication efforts;

Noting the important role that Member Countries have played in accelerating the establishment of the Heavily-Indebted Poor Countries (HIPC) Debt Initiative (DI) and noting the call of the Development Committee of the World Bank and the International Monetary Fund (IMF) ("the Development Committee") on the World Bank to present a progress report thereon to its Spring 1997 meeting;

Further noting the establishment of the HIPC DI Trust Fund ("the Trust Fund") by the World Bank and noting the full support of all other international financial institutions therefor;

Taking into account the link between development, including poverty eradication efforts, and manageable levels of debt and, consequently, the rationale for IFAD's participation in the HIPC DI;

Having considered the draft Resolution contained in document GC 20/L.6/Add.1;

Decides that:

1. IFAD shall participate in the HIPC DI.
2. The Executive Board may authorize the President of IFAD to conclude, on the basis of a recommendation from the President of IFAD, such agreements as may be necessary with the World Bank for IFAD's participation in the HIPC DI and the Trust Fund.
3. IFAD's participation in the HIPC DI shall be either: (i) through direct participation in, and contribution to, the Trust Fund that is to be established; and/or (ii) through IFAD working in parallel, but in full coordination, with the said Trust Fund, dependent upon particular circumstances relating to heavily-indebted poor countries to be assisted under the DI and/or such conditions as may be attached to specific bilateral donor contributions to IFAD for this purpose.



4. The Executive Board may authorize the President of IFAD to approve for each country declared eligible under the HIPC DI a Debt Relief Package coordinated with the Trust Fund Administrator, the International Development Association (IDA), with the objective of reducing that country's debt to a sustainable level.
5. In **Paragraph 32 of the Lending Policies and Criteria** (document IFAD 8/Rev.2) the following text shall be added after sub-paragraph (d) thereof as follows (the text to be added is underlined):

"For the purposes of implementing the Heavily-Indebted Poor Countries Debt Initiative, the Executive Board may amend the terms upon which an approved loan is provided to a country. In determining the grace period, the maturity date and the amount of each instalment for the repayment of Loans, the Executive Board shall take into account an assessment of a country's debt sustainability produced under the Heavily-Indebted Poor Countries Debt Initiative."