The Debt Reduction Facility for IDA-Only Countries: An Overview

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Objective of the presentation

- A brief overview the Debt Reduction Facility for IDA-Only Countries (DRF)
- A few key messages for Paris Club members and private creditors

Mandate and financing

- The DRF was established by the Boards of IBRD and IDA in July 1989
- Role is to help heavily indebted, low-income countries resolve external commercial debt
- Financed from IBRD net income (about $218 m. used to date) and grant contributions from other donors (about $207 m. used to date)
- With approval of the DRF Oversight Committee and the IDA Board, the DRF provides:
  - preparation grants to fund legal and financial advisers
  - implementation grants to finance debt buybacks

Why the DRF is needed

- Many commercial creditors have not provided “proportional burden sharing” debt relief
- Share of commercial debt is high in upcoming HIPC Initiative cases
- Concerns about aggressive acquisition and litigation by commercial creditors
- The DRF is a proven instrument for catalyzing commercial creditor participation in debt relief
- For these reasons, in April 2007 the IDA Board extended the DRF until 31 July 2012

Eligible countries

- "IDA-only" countries which have reached the "decision point" under the Heavily Indebted Poor Countries (HIPC) Initiative
- Acceptable progress with a medium term program for economic development
- A strategy for debt management involving:
  - addressing commercial debt comprehensively
  - substantial relief from official bilateral creditors
  - and which enhances country's growth and development.

Pre-Decision Point HIPCs

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- Afghanistan
- Comoros
- Côte d'Ivoire
- Eritrea
- Central African Rep.
- Kyrgyz Rep.
- Liberia
- Nepal
- Somalia
- Sudan
- Togo

Interim HIPCs

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- Chad
- Congo, Dem. Rep.
- Congo, Rep.
- The Gambia
- Guinea
- Guinea-Bissau
- Burundi
- Haiti

Completion Point HIPCs

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- Sao Tome and Principe
- Sierra Leone
- Benin
- Bolivia
- Burkina Faso
- Cameroon
- Ethiopia
- Ghana
- Guyana
- Honduras
- Madagascar
- Malawi
- Mali
- Mauritania
- Mozambique
- Nicaragua
- Niger
- Rwanda
- Senegal
- Tanzania
- Uganda
- Zambia

Eligible debt

- Public and publicly guaranteed uninsured medium and long-term external commercial debt in arrears
- Public and publicly guaranteed uninsured short-term external commercial debt (trade financing, suppliers credit and overdrafts)
- Debt must have been contracted and disbursed before the end of the HIPC "reference year"

Ineligible debt

- Bilateral debt or multilateral debt
- Domestic debt
- Third-party guaranteed debt
- Debt contracted after end of the HIPC "reference year"
- Debt that is time-barred under statutes of limitation

Characteristics of an operation

- Debt buyback prepared and implemented by the Government and its advisers – not by IDA
- Debt purchased at deep discount
- Principal, interest and penalties extinguished
- Comprehensive operation – high participation essential
- Best possible deal – but "proportionate burden sharing" required
- Typically at least 50% of costs of a buyback from other donors

22 DRF operations in 21 countries

Around US$8 billion of debt has been extinguished:

– US$ 4.5 billion of principal

– plus US$ 3.5 billion of interest arrears and penalties

1991-1995	1996-2000	2000-2005
10	8	4
Niger (91)	Ethiopia (96)	Yemen (01)
Mozambique I (91)	Mauritania (96)	Honduras (01)
Guyana I (92)	Senegal (96)	Cameroon (03)
Uganda (93)	Togo (97)	Tanzania (04)
Bolivia (93)	Vietnam (98)	
Sao Tome Principe (94	Cote d'Ivoire (98)	
Zambia (94)	Guyana II (99)	
Albania (95)	Guinea (00)	
Sierra Leone I (95)		
Nicaragua I (95)		

Future operations

- DRF-supported operations are currently under preparation in Mozambique and Nicaragua
- A DRF preparation grant has been approved for the Democratic Republic of the Congo, with work expected to start soon
- Discussions are under way with a number of other countries including Sierra Leone

Pricing and participation: the past

- To date, buybacks have been priced as a percentage of principal only:
  - Price per dollar of principal has fluctuated from 8 cents to 26 cents
- This has resulted in:
  - uneven treatment of creditors (those with older claims/more interest got a lower effective price)
  - sometimes in low participation (participation has fluctuated from 100% down to as low as 62%)
  - in some cases, need for "clean up" second buybacks (e.g. Guyana, Mozambique, Nicaragua)

Pricing and participation: the future

- In future, buybacks will be priced as a percentage of a broader definition of debt (including interest components)
- Proportionate burden sharing is called for by the Paris Club and the HIPC Initiative
- DRF beneficiary governments and their advisers are required to negotiate the best possible deal
- However, "best possible deal" will be assessed in terms of <u>participation</u> as well as <u>pricing</u> so as to eliminate the need for second buybacks

Future financing

- The DRF can play a bigger role in encouraging commercial creditor participation in the HIPC Initiative
- But only if other donors, including Paris Club members contribute:
  - IBRD net income contributions to the DRF are limited
  - Future DRF demands on IBRD net income will need to be weighed against the competing needs of IDA
- And only if responsible commercial creditors continue to provide debt relief as part of buybacks