# The Joint Bank-Fund Debt Sustainability Framework for LICs

Paris, May 23, 2007

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# Outline of the presentation

- Why a specific framework is needed for low-income countries
- Description of the debt sustainability framework for low-income countries
- Use of the framework and challenges

# The Debt Sustainability Framework

- Developed by the IMF in 2002 in the context of surveillance, to better monitor debt issues in emerging markets

- The DSF is intended to serve as an “early warning system” of potential risks of debt distress so that preventive action can be taken in time

- It helps countries in determining appropriate financing strategies to maintain/achieve debt sustainability

# Why a special framework is needed for low-income countries

- Their debt has special features
  - A large part is granted on concessional terms
  - Longer maturities than emerging market debt
- Their economies have special features
  - They are more vulnerable to exogenous shocks
    - Higher incidence of natural disasters, terms of trade shocks, conflicts
    - Higher impact of shocks on their economies
  - They have more limited institutional capacities
- Information on their macroeconomic and debt situation is scarce, segmented

# A growing need in the current environment

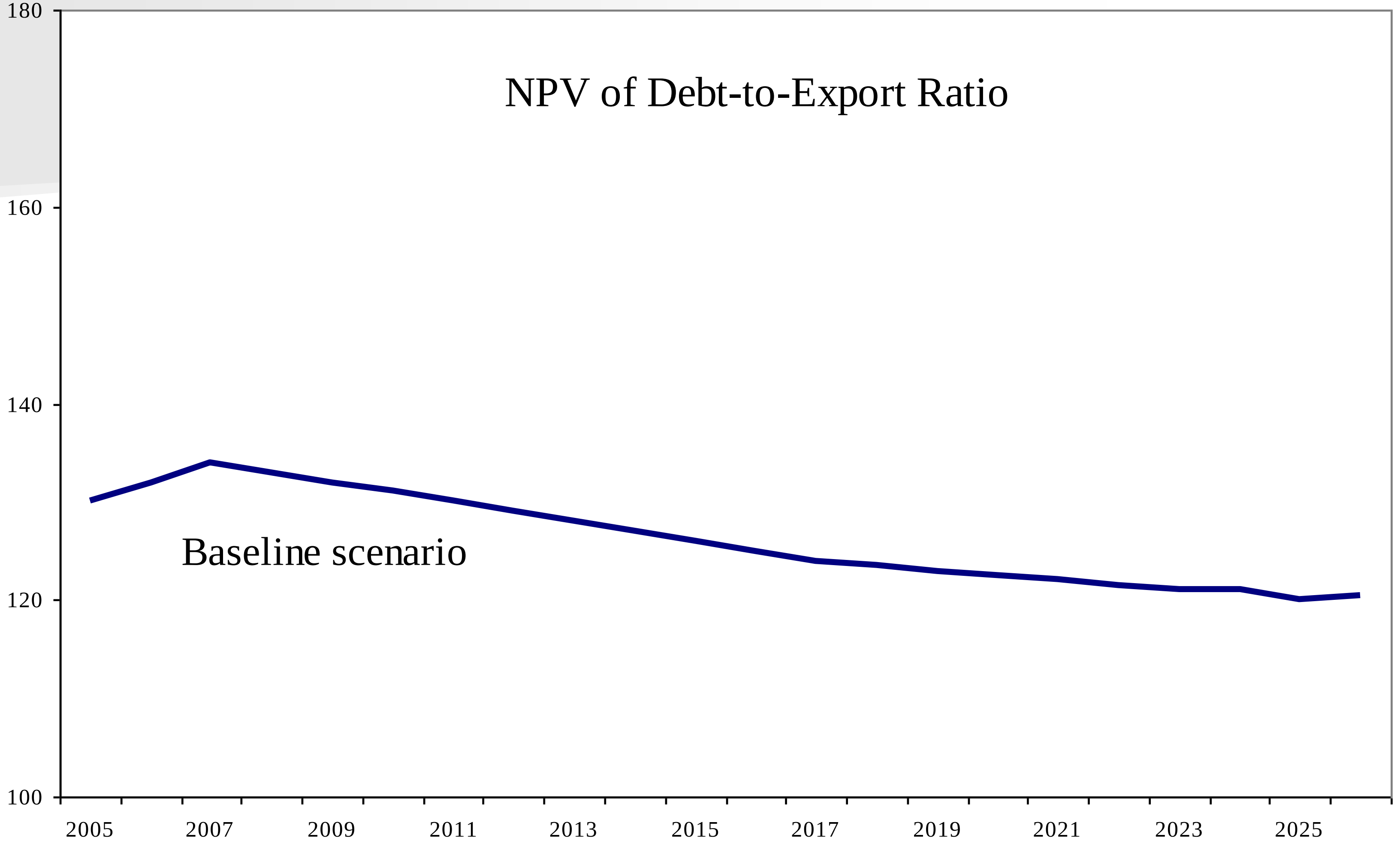
- LICs have larger borrowing opportunities:
  - <u>Debt relief</u> for the most indebted
  - <u>Scaling up</u> prospects from traditional creditors
  - The emergence of <u>new private and official creditors</u>
- These changes provide *opportunities* for faster output and income growth…
- … But they need to be *managed* in order to avoid too rapid a build-up of debt

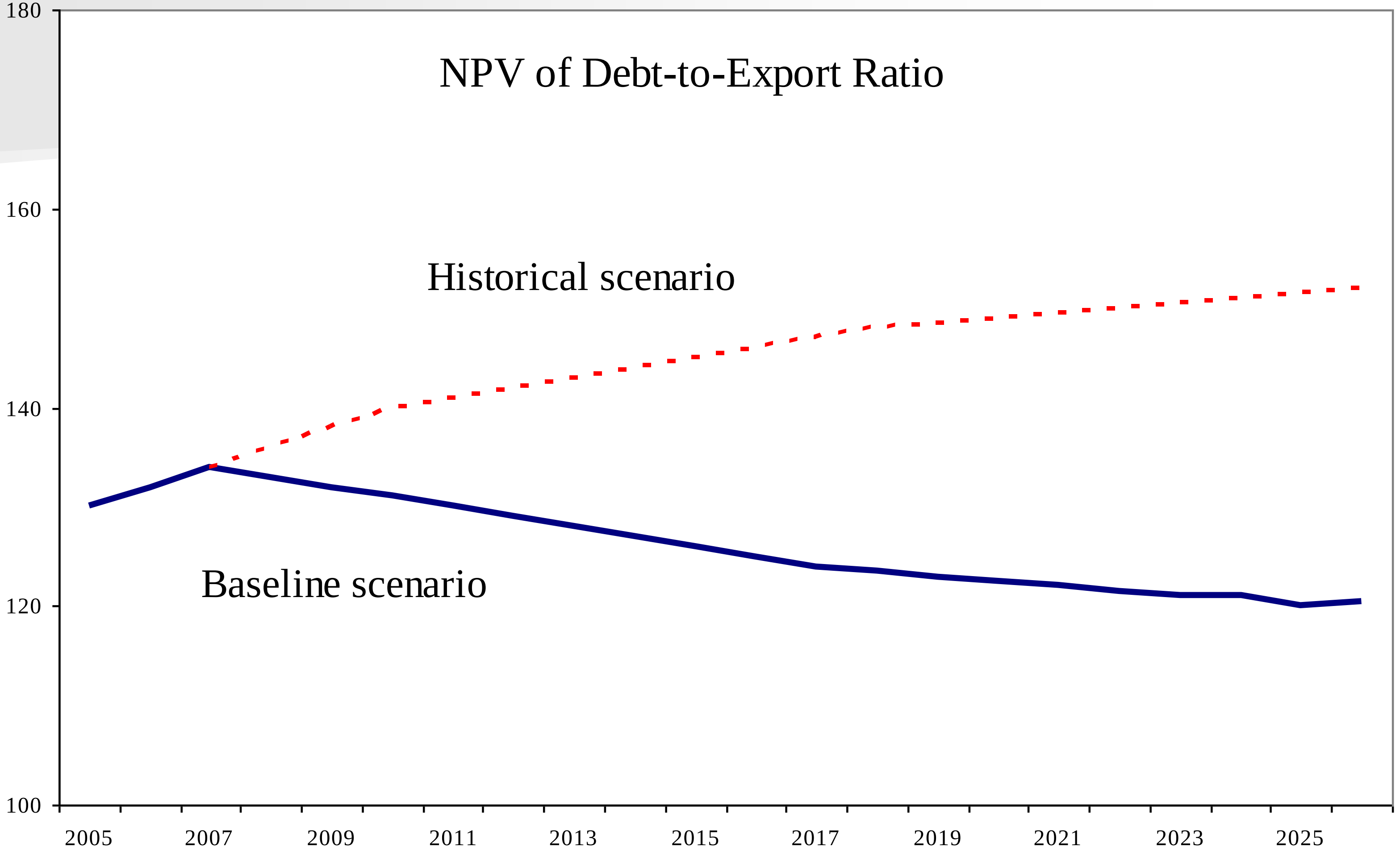
# The Joint Bank-Fund DSF

- The Bank and Fund have jointly developed – and recently strengthened – an instrument to analyze debt challenges in LICs:
  - The Debt Sustainability Framework for Low-Income Countries (DSF)
- It takes a long-term perspective (20-year forecasts) and uses NPV terms to account for the specificities of LIC debt
- It explicitly links the risk of debt distress to the size of the debt burden, the type of exogenous shocks, and the quality of policies and institutions
- It generates a debt distress risk rating for each LIC
- The DSF is not the framework used in the context of the HIPC Initiative; it serves a different purpose.

# Three "Pillars"

1. Twenty-year projections of debt burden ratios under baseline and alternative scenarios


NPV of Debt-to-Export Ratio
Baseline scenario
180
160
140
120
100
2005
2007
2009
2011
2013
2015
2017
2019
2021
2023
2025


NPV of Debt-to-Export Ratio
Historical scenario
Baseline scenario
180
160
140
120
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2005
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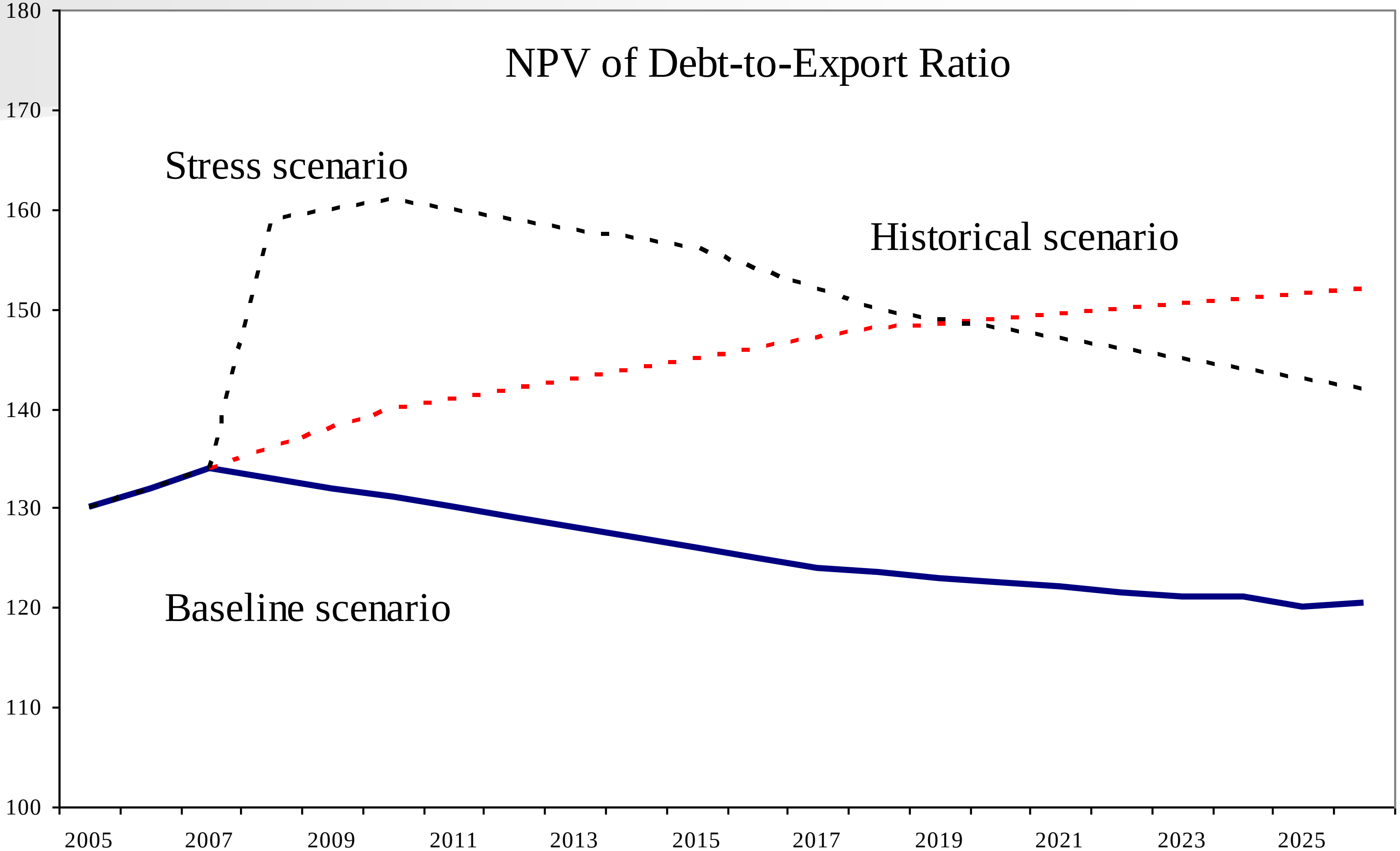
NPV of Debt-to-Export Ratio
Stress scenario
Historical scenario
Baseline scenario
180
170
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