The Joint Bank-Fund Debt Sustainability Framework for LICs

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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:
  - Debt relief for the most indebted
  - Scaling up prospects from traditional creditors
  - The emergence of new private and official creditors

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