VI Prospects for Multilateral Debt Relief

As the foregoing sections have suggested, several sensible options do exist for addressing the issue of multilateral debt and the inextricably related question of new multilateral lending. But, experience and unfortunate political realities suggest the need for caution in attempting to seek any sort of global solution to the multilateral debt problem. Given the excessively bureaucratic way in which governments and multilaterals work there appears, at present, to be little likelihood of establishing a single debt reduction facility or even a single forum for coordinated reduction of multilateral debt funded by an SDR issue or by IMF gold sales.

The derivation of a common standard – or a set of common criteria – for providing such relief, to ensure burdensharing among all multilaterals or with other creditors, is also improbable, even though it would not be too difficult to design standards such as positive net transfers, or restricting multilateral debt service to agreed proportionate maxima as a percentage of either total debt service or of export earnings.

Relief is more likely to continue to be provided piecemeal by each institution separately, using its own funds, and on the basis it thinks suitable in its own circumstances.[16]

The International Monetary Fund (IMF)

Expanding Access Case-by-Case in Middle-Income Countries: SIMICs (whose debt servicing problems and concerns have not been fully addressed in this paper) have been particularly hard hit by large negative net transfers to the Fund since 1986. The IMF has done little to reverse this, because the IMF Board has recently reduced the permissible maximum multiple of quota that it lends to individual countries (this is known as *access* to Fund resources), particularly for countries regarded as poor credit risks. Publicly the Fund's position remains that where countries have strong adjustment programmes in place, the Fund will increase its exposure. There is some evidence that on a

16 Inevitably that will lead to inconsistent and inequitable treatment of debtors and will create anomalies in the system which could, with better co-ordination, be avoided. For example, it has made little sense for the World Bank to extend partial debt service relief to eligible SILICs in Africa only for the AFDB to attempt to extract full debt service from them on its own hard-window debt. To the extent that it has been successful the AfDB has been a 'free rider'; to the extent that it has been unsuccessful it has simply accumulated arrears while the debt of the World Bank has been serviced.

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net flow basis it managed to do this in the mid-1980s for countries without prolonged use of Fund resources.[17]

However, Board decisions linked to the Ninth General Review of Fund quotas in 1990 reduced access to prevent any increase in lending as a result of the quota increase. Maximum access under the credit tranches and extended facilities were reduced to an annual 68% and a cumulative 300%. Maximum access under the Compensatory and Contingency Financing Facility (CCFF) fell from 122% to 95%. This ran contrary to the arguments and projections used by Fund staff in proposing the Ninth General Review, which assumed the maintenance of 1990 access levels, or even an increase in these levels, in order to ensure continued positive net transfers to developing countries.[18] Had access been maintained at earlier levels, the quota increase in 1990 would have permitted annual lending of $12 billion in 1990-94, and positive net disbursements of $6 billion. These compare with annual lending averaging only $7.5 billion in 1990-92, and negative net disbursements of an average $1.3 billion a year.

Neither IMF staff nor independent analysts believe that restoring access to the earlier limits would pose any serious risk to the IMF portfolio as its liquidity would remain more than ample. As a result of the large negative net transfers in the 1980s, obligations to the IMF are not a large burden for most middle-income countries – with perhaps the exception of Argentina. There may be little need now for a *global* restoration of access to 1990 levels, because several heavily-indebted middle-income countries are now availing of recourse to voluntary lending from international capital markets and are the beneficiaries of unprecedentedly large inflows of direct and portfolio foreign investment. But in this group of countries there are exceptions, like Jamaica, which deserve special treatment. However, in the case of the lower-middle-income countries which do still have a debt crisis, the IMF's Board might consider applying more discretionary scope in permitting access upto pre-1990 access levels, and preferably for even higher annual credit tranches combined with the Extended Fund Facility (EFF) and CCFF limits, on a case-by-case basis.

Going Beyond ESAF for the Low-Income Countries: In 1986 and 1988, the IMF established the Structural Adjustment Facility (SAF) and the Enhanced Structural Adjustment Facility (ESAF) for concessional lending to low-income countries. These followed the tradition of the Trust Fund. These two facilities have served to secure the IMF's role as a development finance

17 See Killick et al 1991 and Overseas Development Institute 1993.
18 See Gwin, Feinberg et al 1989.

institution (a role which it was never intended to play) by enabling it to lend for longer periods (10 years with 5.5 years of grace) at concessional interest rates (0.5%). However, funds from both SAF and ESAF have been disbursed extremely slowly partly vitiating the urgency and purpose for which they were set up. The slowness of disbursement exacerbated the debt service problems that the intended beneficiaries had with the Fund. By February 28, 1993, ESAF had disbursed only SDR 2.1 billion out of its total funding of SDR 6 billion. Apart from the general reduction of access limits and the policy of reducing lending to 'over-exposed' countries, very low limits were established for SAF. More generous limits for ESAF were reduced with the Ninth General Review of Quotas. Maximum exceptional access fell from 350% of quota to 255%; maximum normal access from 250% to 190%; average access from 150% to 110%; and access for newly ESAF-eligible countries from 80% to 60%. In the context of the current general shortage of donor concessional resources it seems almost absurd that the IMF should be persuading bilateral donors to help SILICs meet their debt service to the IMF when it could use ESAF resources which are more readily available to the Fund with no risk to its liquidity position. In addition to resorting to faster use of ESAF for SILICs the IMF should restore previous access levels at the earliest opportunity.

Two other specific factors explaining the slow disbursement of SAF and ESAF [19] have been:

(a) *Excessive Conditionality:* All countries granted ESAF facilities are being expected to implement dramatically tighter conditions in the first year of ESAF programmes, and uniformly tight conditions in later years, whether or not they began or completed SAF programmes before the expiry date of the SAF facility (March 1992). The concept of gradual progress through SAF to ESAF conditions – synchronised with gradual structural reforms under World Bank programmes and PFPs – has been discarded in favour of an emphasis on immediate and recessionary fiscal and monetary deflation. This tightening has delayed agreement for many countries, and has reduced growth and savings and increased current account deficits in ESAF programme countries compared to SAF programmes.

(b) *Balance of Payments Viability and Capacity to Repay the Fund:* Countries are informally obliged to make major progress towards balance of payments viability during the programme period and to show that they will be able to repay the Fund loan. In theory, this should mean progress towards

19 On these, see also Feinberg in Husain and Underwood 1991; Green 1993; Martin 1991, Chapter 7; and Overseas Development Institute 1993.

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ending reliance on debt relief and IMF purchases.[20] In practice, it means demonstrating that comprehensive debt relief and huge aid flows will be available to finance the programme. Because Paris Club reschedulings and some balance of payments support normally follow the making of IMF loans, several countries have been deprived of Fund lending and of exceptional financing. This vicious circle could be broken if the IMF and creditor governments agreed to provide debt relief and balance of payments support on the basis of a Fund-monitored programme without an accompanying IMF loan (as they are doing with Rights Accumulation Programmes and post-ESAF shadow programmes).

SAF and ESAF have refinanced only 40% of low-income countries' repayments of non-concessional debt to the IMF. But they have perhaps fulfilled another more invidious and questionable role: i.e. they have enabled the IMF to continue lending to low-income countries even as these countries have been compelled to meet debt service on non-concessional IMF loans. The good aspect of this development is that non-concessional IMF debt of low-income countries has fallen dramatically since 1987. At the end of February 1993 it totalled only \$6.2 billion, of which \$3.4 billion was owed by India. The SILICs owed the IMF \$2.1 billion in upper tranche obligations; but once arrears are excluded, they will owe less than \$400 million. For that reason, consideration might be given to establishing an equivalent of the World Bank's 'fifth dimension' facility, for refinancing non-concessional IMF debt of IDA-only countries, using a special SDR emission or gold sales for funding it.

The preferable approach would have been for SAF and ESAF not to have been created in the first place but to have had the resources of IDA expanded instead to fulfil the roles of SAF and ESAF. IDA would have provided a more appropriate vehicle for the IMF to withdraw from a development financing role in the low-income countries and being obliged instead to confine its activities to advice and surveillance. IDA facilities (with a maturity of 40 years and a grace period of ten years) are also far better suited to the multilateral debt refinancing needs of SILICs rather than ESAF facilities whose maturities and grace periods are much too short, resulting in the debt servicing problem caused by IMF loans being deferred for a short period and renewed rather than decisively resolved.

The funds of the current ESAF will be exhausted during 1993-94. There is, unfortunately, a broad consensus among developed and developing country governments in favour of a successor concessional facility within the IMF modelled after its predecessor. The optimal solution would be

20 See Goreux in Gwin, Feinberg et al 1989

expanding IDA rather than financing ESAF-II. However, once an institutional dynamic takes over, and vested interests in support of one institution over another become entrenched, it is very difficult to achieve sensible rationalisation in the multilateral system. Accepting a new ESAF as a sub-optimal reality, it could however be improved by giving the facility the following features:

(a) *Less Rigid Conditionality:* based on the length of prior adjustment and degree of prior stabilisation rather than some uniform standard for ESAF successor programmes. For countries progressing from third or fourth year ESAF programmes to its successor, there should be no requirement to accelerate progress towards balance of payments viability: they should only have to maintain it at the current pace.
(b) *Larger Loan Size* with increased access limits.
(c) *More Concessionality in Terms:* at least 67% grant element to match the Paris Club's Trinidad terms (IDA terms would be preferable for SILICs), achieved by lengthening the grace and maturity periods to 8 and 15 years and maintaining the current 0.5% interest rate.
(d) *A Longer Period* allowed for achieving balance of payments viability, thereby easing disbursement restrictions for some countries.
(e) *A Larger Replenishment:* of at least SDR 8 billion over three years, considerably larger than the original ESAF, because eligibility has now been widened from low-income debt-distressed to all 72 IDA-eligible countries and because several newly-eligible countries may follow Zimbabwe in abandoning their earlier decision not to use ESAF resources.[21] Eligibility may need to be further expanded to include 7 more Caribbean and Pacific states.
(f) *Capital Funding for ESAF from normal General Resources Account* funds rather than from loans by donors. This is vital because it avoids the need for a specific reserve to ensure the repayment of donor loans.[22] The SDR 1 billion of gold pledged to back this reserve, and the net earnings from investment of donor contributions to the ESAF could then be freed to cofinance an interest subsidy on the larger total funds, along with additional gold sales of approximately SDR 3.3 billion.

Beyond ESAF-II, consideration must be given to removing the development financing function altogether from the Fund before it becomes an embedded perversion of the Fund's role. The Fund could still fulfil its role of gatekeeper

21 Countries added in 1992 are Albania, Angola, Côte d'Ivoire, Dominican Republic, Egypt, Honduras, Mongolia, Nicaragua, Nigeria, Philippines and Zimbabwe.

22 It would also reduce the current complexity of proliferating multiple accounts and facilities in the Fund.

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to rescheduling and new aid, by approving and monitoring the monetary, fiscal and external sector policies and targets of an adjustment programme as it currently does. Creditors would accept a role of monitoring with negative net transfers (as they have during the 1980s) whereas they would be unlikely to accept a complete transfer of programme design to the World Bank. This role would also ensure that staff time and attention were not diverted away from low-income countries to other borrowing countries, and might reduce political pressure to lend, allowing staff to focus still more on the viability and consistency of adjustment programmes; as has recently been shown by post-ESAF Fund-monitored programmes in Ghana and Gambia.

As noted above, the development financing function should be more appropriately fulfilled by IDA, with bilateral donor grants being used to augment IDA rather than ESAF. The SDR 3 billion provided for ESAF would have increased IDA-10 by 23%. In order to begin moving in this direction, the interest subsidies inherent in ESAF-II should be financed not by donor grants but by sales of IMF gold instead. The Fund's financing role in low-income countries should revert to its earlier role in the 1970s: i.e. that of providing quick, ready access first line liquidity and longer-term contingency finance to offset sudden, unprojected external shocks.[23] The quantum of recyclable concessional funds already built up in the Fund appear adequate to meet that requirement for the foreseeable future.

The World Bank

The World Bank has been at the vanguard in taking several creative and helpful steps in recent years to help SILICs cope with the problems created by debt service obligations to the IBRD, and to maintain positive net flows and transfers to borrowing countries.[24] It has focussed particularly on former IBRD borrowers whose creditworthiness has deteriorated sufficiently for them to now be classified as IDA-only countries, many having fallen from middle-income to low-income status. Since 1988, IDA has earmarked a portion of repayments on earlier credits (IDA reflows) to assist eligible SILICs in meeting part of their interest payments on IBRD loans borrowed when they were middle-income countries.[25] Initially this was established as

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23 For more discussion of this issue, see Green 1993.

24 Sadly, the Bank has taken full credit for doing so unilaterally when the real impulse for these initiatives (especially the fifth dimension facility) have come from concerned donors; in particular, the Nordic donors.

25 Until 1987, reflows were used largely to cover exchange rate losses on IDA contributions.

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the 'fifth dimension' of the Special Programme Assistance (SPA) for Africa; it has since been expanded to cover all IDA-only borrowers.[26]

Disbursements are made as supplements to adjustment credits, and therefore have sometimes been delayed by failure to agree or implement programmes. In 1988, the funds available were a maximum of 10% of IDA reflows or approximately $400 million, which financed only 60% of interest payments due from eligible countries. However, due to favourable exchange rate changes, improvements in IDA's financial position,[27] and because not all eligible countries agreed to implement acceptably tough adjustment programmes, the Bank was able to refinance 90% (and in 1992-93 almost 100%) of interest due on IBRD loans for the remainder. The total amount allocated under the programme during 1988-92 has been more than $520 million In addition, Finland, Norway and Sweden have provided additional donor support to refinance IBRD interest *and principal* payments.

Under IDA-10 the 'fifth dimension' will continue, but there seems currently little prospect of expanding it to refinance principal payments on IBRD loans by IDA-only borrowers (as proposed by several donor governments since 1987). One objection in principle is that refinancing all IBRD principal would make the terms of IBRD loans softer than IDA loans. However, a formula could easily be devised to refinance a proportion of principal payments which equalised the net present value of IBRD and IDA loans. The greater barrier is that all but 10-15% of IDA reflows are needed to enhance IDA-10 commitment authority (see below). Any extra amount allocated to the fifth dimension will be a 'safety margin' to cover interest subsidy financing requirements for additional countries which may soon become eligible.[28] For that reason the case is strong for using exceptional financing sources to refinance the principal of IBRD loans owed by IDA-only countries, through a one-off, up-front formal refinancing using some of the Bank's reserves.

Few would argue that similar measures should be taken to maintain a positive net transfer from the IBRD to middle-income developing countries,

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26 Countries currently eligible are Bangladesh, Bolivia, Ghana, Guinea, Guyana, Honduras, Kenya, Madagascar, Malawi, Mauretania, Nicaragua, Senegal, Sierra Leone, Tanzania, Uganda and Zambia. Honduras and Nicaragua have recently become IDA-only countries.

27 These improvements in IDA's financial position are caused by larger earnings on investment of donor contributions, because donors contribute more than is scheduled to be disbursed or because disbursements are delayed. In addition, the proportion of IDA funding which comes from transfers of IBRD net income is now able to be "called" simultaneously with donor contributions (whereas before it was called only after donor contributions).

28 For example, when the CFA franc is eventually devalued (as it must be to restore a semblance of equilibrium in the franc zone economies) Côte d'Ivoire will become a low-income debt distressed country and might alone absorb 6% of total reflows if it becomes eligible.

given that many are now receiving large private capital inflows. However, there may be a case for considering the extension of IDA loans on an exceptional basis to severely-indebted lower-middle-income countries with a heavy IBRD service burden (particularly Bolivia, Côte d'Ivoire, Jamaica and Morocco). IDA credits could be used to refinance a proportion of the existing hard-window IBRD debt and to restructure debt service on intermediate terms.

Debt owed to IDA is not an issue which requires any urgent solutions. Instead, the issue is whether IDA *should* or *can* continue to bail out other multilateral creditors. To a large extent during the late 1980s, IDA has acted as the international financial system's 'lender of last resort' for SILICs by attempting to provide positive net flows to low-income countries. The most recent IDA replenishment (IDA-10) agreed in 1992, for commitment between 1994-96, totals SDR 13 billion (or approximately $18 billion). Viewed in the context of severe donor budget constraints the replenishment amount was generous. Viewed in the context of SILIC and other low-income country financing needs, it was insufficient, for the two reasons noted earlier: (a) more middle-income countries are continuing to fall into low-income status, increasing eligibility and demand for IDA loans; and (b) many IDA countries are reaching their existing commitment ceilings and require more credits for gap-filling in growth-oriented adjustment programmes.

As a result, IDA contributions from donors have traditionally been supplemented by using transfers from the investment income of IBRD and, more recently, by IDA reflows from credits made in the 1960s and 1970s which are now being repaid.[29] IDA reflows will grow sharply in the mid-1990s. But, in the current IDA commitment period 90% of IDA reflows will still be needed to meet planned commitments for IDA-10 recipients. There is therefore little room for IDA to do more than it is already doing to overcome multilateral debt problems unless present allocations to much better-off countries such as China – whose continued access to IDA might be questioned in view of its highly favourable economic circumstances – are deployed for higher priority purposes. If the political problems associated with such perfectly sensible reallocations could be satisfactorily dealt with, there may be more room for manoeuvre than meets the eye.

29 IBRD profits from investment income have also been used to finance buybacks of commercial debt owed by low-income countries - the so-called "sixth dimension" of the SPA. As of mid-1993, these funds had been used for only 5 countries (Bolivia, Guyana, Mozambique, Niger and Uganda), but several operations were close to conclusion and the Bank is asking its Board for more funds to replenish the account.

The Regional Development Banks

The African Development Bank: As discussed earlier, debt service payments to the African Development Bank are now becoming a significant burden for most African countries as grace periods on loans made in the mid-1980s expire and disbursements on commitments made between 1987-92 rise dramatically. The bulk of AfDB's portfolio remains of generally high quality but is beginning to show signs of structural deterioration. Time is running out for finding remedies which will arrest and reverse the future growth of what might become a serious problem. The most important measure that needs to be taken is to rectify the imbalance between the concessionality of funds available for lending and the income level (and creditworthiness) of most of its borrowers. A debt servicing problem has arisen because the substantial expansion of AfDB's lending between 1987-93 was financed by the wrong kind of resources, using hard-window (IBRD-type) AfDB loans instead of softer (IDA-type) AfDF credits. Surprisingly, during those years when the debt crisis was at its peak, the AfDB was making relatively large amounts of AfDB loans to patently uncreditworthy African countries which were already severely debt-distressed and which had, even then, been downgraded by the World Bank from 'IBRD-eligible' to 'IDA-only' status. As observed earlier, this lending was not simply the fault of AfDB management alone – though it must bear the main burden of responsibility. Such lending was approved by its Board (indeed actively promoted by regional members of the Board) and endorsed by all its shareholders (including OECD donors). Implicitly it was also encouraged by the IMF and World Bank when AfDB funding was sought to close financing gaps for Bank-Fund designed adjustment programmes in low-income African countries.

Thirty-four of the AfDB's forty-eight borrowing members are now low-income, and this number will almost certainly grow during the 1990s. The AfDB's major concessional window, the African Development Fund (AfDF) provides credits on the most concessional terms available to developing countries – they are interest-free with a service charge of 0.75%, a 50-year maturity and a 10-year grace period. For the fifth (1988-90) and sixth (1991-93) replenishments of the African Development Fund, donors pledged unexpectedly large amounts ($2.7 billion and $3.4 billion equivalent respectively).[30] The sixth replenishment represented a 14% increase in real

30 For additional analysis of African Development Bank funding, see Jerlstrom, B., "Banking on Africa: An Evaluation of the African Development Bank", Swedish Ministry for Foreign Affairs, Stockholm, 1990; the African Development Bank 1990; Larrecq in Husain and Underwood 1991, and the AfDB Annual Reports.

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terms, exceeding the increases for any other soft window multilateral. Yet these amounts remain insufficient to address the financing requirements of African countries and to avoid a marginalisation of the AfDB's role as a significant regional multilateral institution. Moreover, the trebling of the AfDB's capital in 1986 permitted a much higher level of AfDB lending than was warranted or justifiable, so that AfDB disbursements in 1990-92 continued to be twice those of the AfDF – exactly the reverse of what was needed given the low and declining income levels and creditworthiness of most African borrowers.

In view of the overhang of AfDB hard window debt for low-income countries, several donors have been discussing establishing an interest subsidy facility for AfDB loans to IDA-only countries, similar to the World Bank's fifth dimension. However, there have been two constraints:

(a) *Inadequacy of Own Resources:* AfDB's levels of net profit after provisioning are very low (averaging around $160 million between 1989-92) as are AfDF reflows ($31 million in 1991). These internally-generated funds are therefore inadequate in permitting AfDB to take the kind of action which the World Bank has done. Therefore any substantial contribution to a fifth-dimension type facility will require diverting a much larger proportion of financing provided by donors under AfDF-7 to support the current commitment authority of AfDF.

(b) *Donor Conditionality limiting AfDB Lending:* Most donors have specified the precondition that there should be no more AfDB disbursements to IDA-only countries. This would considerably reduce the AfDB's ability to operate in many of its borrowing member countries, and make it difficult for the AfDB to sustain continued positive net flows and transfers towards 2000. However, the latter difficulty must be resolved by expanded AfDF lending (and therefore by a much larger AfDF-7 replenishment) and not by continued AfDB lending which would only enlarge and worsen the problem.

To surmount these two problems, the African Development Bank needs a fundamental restructuring of its resource base to reflect the changed income level of its borrowing members. The current negotiations for the seventh replenishment of the AfDF need to aim for an amount of at least $5 billion. Almost all of the increase ($1.6 billion) should be set aside for refinancing AfDB loans to IDA-only countries on AfDF terms, in conjunction with donor cofinancing if necessary.[31] To facilitate this major shift away from non-concessional to concessional lending for the remainder of the 1990s, the next

31 On this issue, see also Mistry 1991.

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AfDB Capital Increase should be deferred for as long as possible towards the end of the decade.[32]

The Asian Development Bank: Given the small stock of AsDB debt, its negligible impact on the debt service ratios of its borrowers, and the fact that only two of them are SILICs, there is currently no need for special mechanisms to restructure its portfolio or to refinance its hard-window debt onto soft terms. If a refinancing facility were felt necessary for reasons of keeping up with other development banks, the amounts would be tiny and could easily be funded out of the AsDB's profits. In the longer-term, as it continues to expand its lending programme, the AsDB will need to monitor closely developments in some of its major borrowers, particularly Bangladesh, India, Indonesia, Pakistan, the Philippines and Sri Lanka, which are already classified as 'moderately-indebted' though they all have particularly heavy multilateral debt burdens. As has been observed earlier, if the present processes of economic reform which all these countries have embarked on take hold and bear fruit, none are likely to pose a problem. But if these reforms falter or fail then the burdens of debt incurred to finance these reforms may become too onerous for countries to meet without some form of relief. Moreover, the AsDB confronts new challenges in the low-income countries of Indo-China, Afghanistan and Myanmar (assuming that political developments in these two countries will make them eligible for borrowing during this decade). In these countries the resources provided will need to be mainly concessional in nature to avert, at the outset, any debt problem from emerging in these fragile economies.

The Inter-American Development Bank: The major problem posed by outstanding obligations to the IDB is the drain on scarce convertible resources caused by the need to meet IDB hard-window debt service obligations for a handful of its smaller, severely-indebted members: three SILICs (Guyana, Honduras and Nicaragua) and two SILMICs (Bolivia and Ecuador). Yet, because of an inadequacy of soft-window resources the IDB has been shrinking the proportion of its FSO lending to low-income countries. The Seventh General Increase of IDB capital saw a rise of $26.5 billion, a 45% increase in real terms over the Sixth GCI, which enabled a 50% rise in commitments (40% in disbursements) during 1990-93, compared to the previous four-year period. In contrast, FSO resources were boosted by

32 The current proportion of overall paid-in capital is 12.5%, and a zero increase in real terms with 6.25% paid in would keep it well above 10%. This compares with much lower paid-in ratios for the other MDBs (2.5%), and should easily preserve its international credit rating.

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only $200 million when a more appropriate amount would have been around $1 billion.

The IDB has been very creative during 1990-93 in augmenting the lending capacity of FSO by using resources generated internally. It funded the interest rate subsidy for its intermediate facility (the IFF) from FSO reserves until the year 2010, and financed additional FSO commitments by using FSO reflows expected during 1994-97. This has enabled soft-window lending to be maintained at nine times the donor-funded level. Because of these measures, the IDB has been able to maintain a marginally positive net transfer to its low-income members. Nevertheless, the proportion of FSO funds in total disbursements has fallen from 12.9% in 1987 to 8.7% in 1991. All low-income members except Haiti are still receiving hard-window disbursements. In the lower-middle-income countries of Central America and the Caribbean that is causing problems. For these latter countries what is needed is a 'blend' of IDB and FSO resources on what are then effectively intermediate terms – not quite as concessional as FSO but not quite as onerous as IDB either.

With reflows having been fully committed, the financing base of the FSO needs to be made more secure, by formal replenishments to increase its lending capacity to levels which enable the IDB to curtail hard window lending to low-income members. In addition, the IDB needs to look actively at using part of its profits to extinguish the hard window debt of the low-income countries through informal refinancing, preferably of the entire stock.

Other Multilateral Institutions

The European Community Multilaterals: Of themselves, debt service obligations to the EC are not a serious problem for any developing debtor country. This is because European Development Fund (EDF) aid is provided almost entirely on grant terms. In addition, EC capacity to disburse has expanded dramatically in the early 1990s, particularly as a result of the 25% real increase in funding for the Fourth Lome Convention (Lome-4) for 1991-95. This has more than refinanced debt service payments due to the EC, and has made the EC a crucial source of net transfers for low-income ACP countries. In addition, the EC has recently taken a further step to reduce the burden of its debt. Under Lome-4 it has agreed to cancel the STABEX/SYSMIN debt of low-income countries, and to make future transfers to these countries on grant terms.

However, the **European Investment Bank,** continues to lend non-concessional resources to low-income countries, even for feasibility studies rather than bankable investment projects. EIB loans carry an interest rate subsidy which reduces the rate by up to 4% (to a rate of between 2-6%) and

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have relatively short grace and maturity periods – as low as 2 and 5 years on some loans from the mid-1980s, and even now only 5 and 11 years. These terms, though intermediate, are still too 'hard' for low-income countries. Like the other multilaterals the EIB raises most of its loanable resources by borrowing on international capital markets, and therefore resists rescheduling. However, it would be possible to refinance EIB service using a Trust Fund equivalent to the 'fifth window' of the World Bank, and preferably on EDF-equivalent (i.e. grant) terms. Up-front refinancing of such debt for the SILICs would cost a total of $835 million, and would reduce total debt service to the EIB from SILICs by $125 million a year during the 1990s.

EIB also lends 'risk capital' as a managing agent for EDF funds; and EDF makes 'Special Loans'. Both these types of debt could be rescheduled on Paris Club-comparable terms without any discernible impact on EIB's credit rating. Alternatively, reflows from previous loans under these facilities could continue to be treated as an additional source of financing for EDF above the amount agreed in the Lome Convention; or, they could contribute to refinancing EIB debt.

Arab-OPEC & Islamic Multilateral Institutions: These institutions receive most of their loanable funds from various Arab and OPEC governments. Until recently, other multilateral creditors have tended to refinance current debt service due to them with equivalent amounts of new loans for fast-disbursing balance of payments support, often on concessional terms (especially for the SILICs). However, most Arab and OPEC governments suffered a collapse in revenues when the real price of oil collapsed in 1986 and their capacity to keep funding these institutions was dramatically curtailed as a result. In addition, these institutions have always been reluctant to disburse aid for quick-disbursing adjustment support, (believing that function not to be the business of development banks) and have preferred to concentrate on financing slower-disbursing projects. For these reasons, it is unrealistic to expect that these institutions will be able to refinance debt service in the same way that other multilaterals have (as the recent negative net transfers confirm). This group of multilaterals cannot expect new capital or concessional funding to enable them to continue net new lending to developing countries; nor do they play any sort of role as gatekeepers for debt rescheduling and new aid to guarantee their preferred creditor status. Given these limitations, they face a particularly difficult challenge in coming up with creative ways of reducing the burdens of debt which their developing country borrowers owe them in the 1990s.

The simplest method would be cancellation of part of their claims or rescheduling of their service on Paris Club-comparable terms. There have

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already been some steps taken in this direction, with the rescheduling of arrears for selected countries by BADEA. However, these reschedulings have generally been on terms considerably harder than 'Enhanced Toronto' terms. The next step could be for these institutions to ensure 'uniformity of treatment' among debtors, and 'comparability' with other rescheduling bilateral creditors, by rescheduling on 'Enhanced Toronto' terms for all SILICs. Another option would be to consider debt-equity conversions on their project portfolios, especially if such conversions could be designed to have other collateral benefits.

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