Unclassified **DCD/DAC(2013)37**

Organisation de Coopération et de Développement Économiques
Organisation for Economic Co-operation and Development **21-Nov-2013**

English - Or. English

DEVELOPMENT CO-OPERATION DIRECTORATE
DEVELOPMENT ASSISTANCE COMMITTEE

DCD/DAC(2013)37
Unclassified

REVIEW OF THE INCLUSION OF NON-LDC HEAVILY INDEBTED POOR COUNTRIES IN THE COVERAGE OF THE UNTYING RECOMMENDATION

This document provides background to the letter from the DAC Chair [ES(2013)55] reviewing the 2008 agreement to include non-LDC Heavily Indebted Poor Countries (HIPCs) in the coverage of the Untying Recommendation. It reviews the evolution of the situation that justified their inclusion in the Recommendation, providing support for the proposal of the DAC Chair to maintain their inclusion on the basis of their limited progress towards the MDGs, declining trends in ODA to these countries and their current debt situation.

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JT03348962

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TABLE OF CONTENTS

Tables

I. Purpose of this note and DAC action requested

1. In 2008, the DAC agreed to include under the Untying Recommendation those Heavily Indebted Poor Countries not already covered by way of their Least Developed Country status i.e. to include the non-LDC HIPCs - Bolivia, Cameroon, Côte d'Ivoire, Ghana, Guyana, Honduras, Nicaragua and the Republic of Congo. The rationale for doing so was to avoid discriminating between LDC and non-LDC HIPCs in their efforts to tackle their debt overhang and to support the HIPC group of countries as a whole in their endeavours to meet the MDGs. Clearly, untying more ODA to these countries was not the main solution to their MDG and debt problems. But it was something concrete the DAC could and did contribute to the broader international effort.

2. At the time of its adoption, it was agreed that this provision would be reviewed after five years. Should Members not agree to maintain the inclusion of the non-LDC HIPCs in the Recommendation, the terms of this provision in the Recommendation note that a donor may decide to use tied aid as part of its ODA to a non-LDC HIPC, in which case it is required to notify the country/ies concerned and the DAC Chair of its decision to do so.

3. This note reviews, in section 2, the evolution of situation initially justifying the provision, looking at progress towards the MDGs, recent trends in aid patterns to these countries and their current debt situation. The analysis of section 2 shows that:

- Progress in non-LDC HIPCs towards achieving the MDGs has been uneven and, in cases, quite limited. Overall, there do not appear to be any major differences in MDG performance between the LDC and non-LDC HIPC sub-groups that would warrant a differential treatment by donors of these two sub-groups of countries.

- ODA to the group of non-LDC HIPCs amounted to USD 3.9 billion in 2011, down USD 1.2 billion (24%) on its 2008 level. ODA has also fallen as a share of these countries' GNI. On average, 79% of the ODA to these countries covered by the Recommendation is untied. Retying such aid would compound the negative trend in volume by also reducing its value for money.

- At an aggregate level, the debt situation in developing countries has improved, although a number of HIPCs, including some non-LDC HIPCs, still show signs of debt distress. IMF/IDA review of the HIPC Initiative suggests that it will be maintained, possibly in an amended version.

4. Members should recall that in Busan in 2011 the DAC agreed to "accelerate our efforts to untie aid." If the DAC is not in a position to keep these countries included in the untying Recommendation, that would be a clear step backwards on Busan commitments. Just two years after Busan, it would send the wrong political signal to partner countries and aid watchers, just in advance of the High Level Meeting of the Global Partnership in Mexico in April 2014.

5. **In consequence, DAC Members are invited to agree to continue including non-LDC HIPCs under the coverage of the Recommendation.** If members so wish, such an extension could be again reviewed after a certain time (e.g. in 2018).

II. Evolution of the non-LDC HIPC situation

6. The HIPC Initiative was launched in 1996 by the World Bank and the IMF to ensure no poor country faced debt burdens they cannot manage and thus to work with the most heavily indebted countries to reduce their external debt burdens to sustainable levels. Relief provided under the HIPC Initiative was further intended to strengthen the links between debt burdens, poverty reduction and social policies, thereby helping countries to accelerate progress towards meeting the MDGs.

a) Progress towards the MDGs

7. An important rationale for the HIPC Initiative was to free up resources spent on debt servicing for spending on poverty reduction and social policies in order to accelerate progress towards the MDGs. But as seen from table 1, progress by the non-LDC HIPCs in this respect has been uneven and in cases limited. Only Bolivia has made broad progress (being 'on track' in seven of the eight MDGs); Ghana and Honduras are 'on track' for only half of the MDGs with the remaining countries being mostly 'off track'.

8. More generally, looking at all HIPCs (LDC plus non-LDC), the picture is quite similar. There is good progress across HIPCs in relation to the MDGs on health, gender and HIV/AIDS, but only about one quarter of those HIPCs that have received full debt relief are on track to meeting the poverty MDG, progress towards the maternal health MDG is also uncertain and only a few countries are on track to meet MDG8 (Global Partnership for Development). Overall, therefore, there is no strong difference between the LDC HIPCs and their non-LDC counterparts in respect of performance in meeting the MDGs and thus no reason to differentiate between the two groups in respect of efforts to help them reach the MDGs.

b) Evolution of aid patterns

9. Since 2008, when non-LDC HIPCs were added to the coverage of the Recommendation, overall ODA trends to these countries are as follows:

- The volume of bilateral ODA to the group in 2011 was USD 3.9 billion, 3.4% of total DAC bilateral ODA. This represents a fall of USD 1.2 billion (24%) from the 2008 level (table 2).

- The relative importance of ODA in these countries' budgets (as measured by their ODA/GNI ratios) has generally decreased, now ranging from 1.9% for Honduras to 4.6 % for Côte d'Ivoire (table 3). The main reason has been the growth of national income in these countries but the fall in ODA receipts has also contributed.

- The main donors in 2011 (in volume terms and in descending order) are France, EU, United States and Germany, which collectively accounted for 70% of the total (table 2).

- The main recipients in this group in 2011 (in volume terms and in descending order) are Côte d'Ivoire, Cameroon, Ghana and Bolivia. Only in Côte d'Ivoire and to a much lesser extent, Guyana, has the volume of ODA risen since 2008 (table 3).

- The share of ODA to these countries that is covered by the Recommendation and is delivered as untied aid averaged 79% in 2011, which is on a par with the average untying ratio for all developing countries. Overall, it has increased since 2008 (73%) resulting from the inclusion of these countries in the coverage of the untying Recommendation. Inclusion under the Recommendation has thus had the desired effect of increasing the share of their aid that is untied. The vast majority of donors untie all of the aid that should be untied under the Recommendation, with only three donors (Austria, EU and Italy) falling below the 50% mark (table 2).[1]

10. The high average level of untying and its associated value for money benefits has at least partially offset the impact of falling ODA volume. Removing such countries from the coverage of the Recommendation and retying their ODA would compound reduced ODA volume with reduced value for money.

c) Debt evolution and the future of the HIPC Initiative

11. For developing countries as a whole and up until around 2008, there was strong improvement in their debt indicators, both in terms of the debt sustainability as well as the ability to service it and absorb external shocks. Strong growth performance, a sharp rise in export earnings, high international commodity prices and a shift from debt to equity financing in some countries all contributed, as did large scale debt forgiveness under the HIPC Initiative for low income countries. Progress was interrupted in 2009 with the global economic and financial crises, as falling export earnings were coupled with recourse to increased external borrowing. Nevertheless, despite continued global uncertainty, the majority of developing countries saw their economies rebound in 2010/11, which has translated into improved debt ratios.

12. Looking at the evolution of debt sustainability in the non-LDC HIPCs (as measured by the ratio of external debt stocks to GNI), table 4 shows a mixed picture. Some countries (Bolivia, Cameroon, the Republic of Congo) have significantly reduced their debt stock ratios since 2005. But in others (Ghana, Guyana, Honduras, Nicaragua) initial progress after 2005 has turned around and debt vulnerability has again increased since 2008. Other debt indicators for the non-LDC HIPC group (e.g. debt service/exports as an indicator of liquidity/ability to service debt and reserves/external debt as an indicator of the availability of a cushion for external shocks) are broadly better in that they have generally moved in a positive direction over the period 2005 – 2011 for most of the countries concerned.

13. For the HIPCs as a group (LDC plus non-LDC), about one-quarter of the countries that have received full debt reduction are rated as still having a high rate of debt distress. While new debt initiatives are seen as not warranted, debt vulnerabilities will need to be addressed by sustained efforts, including from donors, to improve the terms of their external borrowing and the effectiveness by which partner countries use ODA. The IMF has recently reviewed the status of the implementation of the HIPC Initiative and is considering proposals for its future[2]. Discussions in the IMF and IDA Boards suggest little support either for making the HIPC Facility a permanent one or for closing it down. This suggests the Initiative will continue, either as it presently stands or in an amended version.

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[1] 2011 data are not available for Greece and Portugal.

[2] Heavily Indebted Poor Countries (HIPC) Initiative and Multilateral Debt Relief Initiate (MRDI) – Status of Implementation and Proposals for the Future of the HIPC Initiative. IMF, March 2013

Table 1. Non-LDC HIPCs: Progress towards the MDGs

	Bolivia	Cameroon	Republic of Congo	Ghana	Guyana	Honduras	Nicaragua
Poverty	✓	X	NA	✓	X	X	✓
Education	✓	✓	✓	✓	✓	✓	X
Gender	✓	X	X	✓	✓	✓	✓*
Child Mortality	✓	X	✓*	X	X	✓	✓
Maternal Health	✓	X	✓*	X	X	X	✓*
HIV/Aids	✓	X	NA	X	X	X	X
Environment	✓	X	✓*	✓	X	✓	X
Global Partnership for Development	X	X	NA	X	X	X	X

Source : HIPC Initiative and Multilateral Debt Relief Initiative : Status of Implementation and Proposals for the future of the HIPC Initiative, IMF, 8 November 2011.

Key: ✓ : on track
✓*: possibly on track
X: off track

Note: No data available for Côte d'Ivoire

Table 2. Bilateral ODA to non-LDC HIPCs

	Total bilateral ODA to non-LDC HIPCs (USD million)		Share untied as covered by the Recommendation	
	2008	2011	2008	2011
Australia	0	6	100.0	100.0
Austria	11	21	98.9	24.4
Belgium	88	86	31.5	52.5
Canada	396	113	97.7	99.9
Denmark	171	47	100.0	99.8
EU Institutions	819	637	0.0	43.2
Finland	21	54	98.3	53.9
France	807	1 114	100.0	98.6
Germany	738	453	100.0	100.0
Greece	1	1	57.1	..
Ireland	12	6	100.0	100.0
Italy	58	14	19.4	48.7
Japan	161	204	100.0	100.0
Korea	46	221	12.9	58.7
Luxembourg	17	13	100.0	100.0
Netherlands	463	29	91.5	100.0
New Zealand	1	2	..	100.0
Norway	25	20	100.0	100.0
Portugal	0	0	100.0	..
Spain	385	129	56.3	76.1
Sweden	65	35	100.0	100.0
Switzerland	63	45	100.0	100.0
United Kingdom	114	104	100.0	100.0
United States	642	545	80.6	77.0
Grand Total	**5 104**	**3 899**	**73.0**	**79.0**

Source: OECD DAC/CRS aid activity database.

Table 3. Bilateral ODA to Non-LDC HIPCs and share ODA/GNI

	2008		2011	
	USD million	ODA/GNI (%)	USD million	ODA/GNI (%)
Bolivia	507	3.1	466	2.0
Cameroon	1 070	4.6	742	3.0
Republic of Congo	445	5.1	256	2.3
Cote d'Ivoire	268	1.2	1 052	4.6
Ghana	1 806	7.1	664	1.8
Guyana (1)	80	4.2	98	..
Honduras	416	3.1	302	1.9
Nicaragua	512	8.2	318	4.5
Total	**5 104**		**3 899**	

Source: OECD DAC/CRS aid activity database.

(1): GNI data for Guyana not available

Table 4. Non-LDC HIPCs: Debt Ratio's (%)

	External debt/GNI			Debt service/Exports			Reserves/External debt		
	2005	2008	2011	2005	2008	2011	2005	2008	2011
Bolivia	76	37	28	15.7	13	4.9	19.1	116.7	153.1
Cameroon	48	12	12	19.3	6.1	3.5 (1)	12.3	109.2	104
Republic of Congo	155	68	23	2.3	NA	NA	11.7	64.6	223.6
Côte d'Ivoire	76	56	52	3.5	9	4.7 (1)	11.4	17.8	35.9
Ghana	68	22	30	8.5	4.2	2.4	24.4	31.1	48.6
Guyana	154	45	65	5	2.6	2.7 (1)	20.4	41.9	43.4
Honduras	56	26	28	10	7.1	16	45	70.9	59.2
Nicaragua	106	69	101	12.1	14.3	14.8	14.6	26.7	26.6

Source : World Bank, 2013, International Debt Statistics.

(1) 2010 data