

Development Co-operation Directorate
Development Assistance Committee

DAC Working Party on Development Finance Statistics

EXTRACTS FROM DAC STATISTICAL REPORTING DIRECTIVES BEARING ON CONCESSIONALITY

The DAC is currently considering how to clarify which loans are "concessional in character" and may therefore be eligible to be counted as official development assistance (ODA). This document presents relevant sections of existing reporting instructions.

An earlier version of this document was issued to members on 29 August 2012. This version contains essentially the same material, but is issued unclassified to facilitate broad consultation on the issue of clarifying the definition of "concessionality in character".

Contact: Ms. Julia Benn (julia.benn@oecd.org)

JT03328501

Complete document available on OLIS in its original format

This document and any map included herein are without prejudice to the status of or sovereignty over any territory, to the delimitation of international frontiers and boundaries and to the name of any territory, city or area.

EXTRACTS FROM DAC STATISTICAL REPORTING DIRECTIVES BEARING ON CONCESSIONALITY

1. **Official Development Assistance (ODA)** [DCD/DAC(2010)40/REV1, para 37]

37. Official development assistance is defined as those flows to countries and territories on the DAC List of ODA Recipients and to multilateral development institutions which are:

- i. provided by official agencies, including state and local governments, or by their executive agencies; and
- ii. each transaction of which:
 - a) is administered with the promotion of the economic development and welfare of developing countries as its main objective; and
 - b) is concessional in character and conveys a grant element of at least 25 per cent¹⁰ (calculated at a rate of discount of 10 per cent).

2. **Concessional in character** [DCD/DAC(2007)39/FINAL, para 27]

Verification of the ODA eligibility of an activity

27. Verification of the ODA eligibility of an activity involves testing its developmental objective and its concessionality. The former requires descriptive information on the purpose of the activity and the latter details on the financial terms of the transaction. Only loans with a grant element above 25 per cent are ODA eligible. In addition, an ODA loan has to be “concessional in character”. This means that its interest rate must be below the prevailing market rate. Both the developmental and the concessionality tests are completed as part of CRS Form 1 data entry procedures.

3. **Variable interest rates** [DCD/DAC(2007)39/FINAL, para 53-58]

53. Loans with variable interest rates may only be classified as ODA if concessionality is guaranteed by a specific mechanism. The mechanism needs to ensure that the variable rate is concessional and that it will be capped so that the grant element over the life of the loan is at least 25%. If the mechanism offers the borrower an opportunity during the term of the loan of obtaining a fixed interest rate, it must be *concessional in character*, i.e. more favourable than the prevailing market rate, and convey an overall grant element of at least 25%.

54. The mechanism for loans with variable interest rates takes account of the following definitions:

10. Except that capitalised interest included in reschedulings of ODA loans is recorded as ODA, regardless of the grant element of the rescheduling.

- variable rate = interbank rate, e.g. EURIBOR +/- margin.
- reference fixed rate = fixed rate that the borrower would obtain (a) in accordance with the loan commitment and (b) given market conditions applying at time of commitment for the term of the loan.
- fixed rate applied if the borrower chooses to convert the variable rate into a fixed rate.

55. The borrower's decision whether to convert the variable rate into a fixed rate will depend on the trend of the variable rate, and is not known at the time the commitment is reported. Therefore, the actual grant element cannot be calculated. To allow the Secretariat to estimate the grant element, report estimated rates.

56. Report the variable rate in item 13 *interest rate* and the reference fixed rate in item 14 *second interest rate*. The Secretariat will then calculate the estimated grant element on the basis of the reference fixed rate.

57. The loan will be classified as ODA only if:

- (i) the resulting grant element is at least 25%;
- (ii) the fixed rate and the variable rate are capped so that the actual grant element is at least 25%; and
- (iii) the variable rate, the reference fixed rate and the fixed rate are concessional in character.

58. The following types of loans are classified as OOF:

- loans extended at a fixed interest rate which is above, at or near the prevailing market rate; and
- loans extended at a floating interest rate, tied to the prevailing market rate, and above, at or near that rate.

4. Concessional in associated financing packages [DCD/DAC(2010)40/REV1, para 22, 23]

22. In an associated financing package, the availability of concessional funds is conditional upon acceptance of the linked non-concessional component, due consideration being given to any informal understandings between the recipient and the donor authority, and to a donor's intention to use ODA to facilitate the acceptability of a financing package.

23. The grant element of any officially supported export credit in an associated financing package is taken as zero by convention. [...]

5. Classification as "other official flows" of the purchase of multilateral interest-bearing securities [DCD/DAC(2010)40/REV1, para 40, bullet iv.]

40. Other official flows are official sector transactions which do not meet the ODA criteria, e.g.:

[...] iv. The net acquisition by governments and central monetary institutions of securities issued by multilateral development banks at market terms. [...]

6. Grant element [DCD/DAC(2007)39/FINAL, para 26 (box); for further details on grant element calculations, see DCD/DAC/STAT(2012)18]

Terms analysis - Calculation of the grant element

26.

The grant element reflects the financial terms of a transaction: interest rate, maturity (interval to final repayment) and grace period (interval to first repayment of capital). It is a measure of the concessionality (softness) of a loan. It is calculated as the difference between the face value of a loan and the discounted present value of the service payments the borrower will make over the lifetime of the loan, expressed as a percentage of the face value. [...]

Background:

The extent of concessionality can be measured either as the benefit to the borrower, or the opportunity cost to the lender. Both benefit and opportunity cost depend on the interest rate and duration of the loan. In a benefit calculation, concessionality would be calculated from the difference between the interest charged and the market rate of interest which the borrower would otherwise have had to pay. In an opportunity cost calculation, the concessionality would be calculated from the difference between the interest charged and the return that the lender could have expected from the next most profitable means of investing the capital. DAC statistics generally measure costs to donors, and consideration of opportunity costs played an important part in determining a reference rate of interest for calculating grant elements. For practical purposes this was set as 10%.