DEBT RELIEF AND POVERTY ERADICATION: STRENGTHENING THE LINKAGES

A paper by Andrew Hewett, Director of Public Policy and Outreach, Community Aid Abroad Oxfam Australia to a seminar sponsored by the Joint Standing Committee on Foreign Affairs, Defence and Trade, 27th August 1999.

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The continuing debt crisis, long an international sleeper which received little attention from the world's media or from the rich world generally, has become a matter of major international concern. The phenomenal growth of the Jubilee 2000 movement is one, albeit probably the most important, sign of the increased focus. The G7 meeting in mid June with the priority attached to tackling the crisis is the most visible sign of donors attempting to come to grips with the public pressure represented by Jubilee.

Quite why debt has become such a matter of international concern is beyond the scope of my paper. What I would like to do this afternoon is explore the connection between the scandal of persistent mass poverty afflicting much of the world and the debt crisis, and secondly ways in which debt relief can be used to help reduce the incidence of poverty.

Most of the focus of the discussion about debt has looked at the situation of the Highly Indebted Poor Countries (which in a previous incarnation were called SILICS - Severely Indebted Low Income Countries). It should be said from the outset that I do not claim that all poor people live in these countries- indeed they are a minority of the world's poor - and I readily acknowledge that there are many millions of people living in absolute poverty in non-HIPC countries. But nevertheless these countries are distinguished by extraordinarily low living standards and by virtue of the debt burden a significantly reduced capacity to get themselves and their people out of poverty.

A few facts and figures will give an indication of the position of HIPC countries.

- Average life expectancy in HIPC countries is 51 years - 12 years less than in developing countries as a group and 26 years less than in industrialised countries

- In HIPC countries the under-five mortality rate averages 156 per 1000 live births. This translates into 3.4 million deaths annually; most of them resulting from infectious diseases which could be averted through low cost interventions.

- There are some 47 million primary school aged children out of school - more than one third of the total worldwide. The majority of these children are girls. More than a third of the children who start school drop out before having gained basic literacy skills.

- About half of the households lack access to safe water and sanitation

- HIPCs account for 30 of the 44 countries judged to be in the "low human development' category by the UNDP Human Development Report.

- On average more than 25% of the population of these countries is not expected to reach the age of 40; this proportion rising to more than a third in countries such as Ethiopia, Niger and Burkina Faso.

These statistics are indicators of deep-rooted poverty and reflect past and continuing policy failures by national governments and the international community, including of course the failure to tackle effectively the international debt crisis.

Because of the deep poverty in these countries they are also particularly vulnerable to new threats such as the HIV/AIDS pandemic. Most of the 5,500 deaths every day from HIV/AIDS occur in HIPC countries and to instance but one HIPC country's experience - HIV/AIDS is claiming the lives of 600 Zambian teachers each year.

And the situation is getting worse.

The international community has set a series of international development targets for the year 2015. These targets cover such basic measures as access to primary school education, clean water and sanitation and well as infant mortality rates etc. In some countries the child mortality rate is predicted to rise - on current trends the child mortality rate in the HIPCs will be 134 in 2015 against a target of rate of 52 while UNESCO estimates that up to 40 million primary school age children in HIPCs will remain out of school The international goal of universal primary education by 2015 will be missed in all but seven HIPCs unless trends since 1990 are reversed.

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As I indicated earlier there are many reasons why poverty is so rampant in these countries.

But it is surely beyond debate that the debt burden is both a major reason why poverty is so deep and widespread in the HIPC countries, and why these countries find it so difficult to find a pathway out of poverty.

Unsustainable debt acts as major barrier to poverty eradication.

- Debt repayments have limited the resources available for investment in basic services which are essential to the poor. A UNICEF-UNDP study shows that six African HIPCs spent more than one third of the national budget on debt servicing but on average less than ten per cent on basic social services. This has led to inequitable growth and denied those living in poverty access to social and economic infrastructure which might enable them to raise productivity and to participate more effectively in markets.

- Debt overhang has created uncertainty for domestic and foreign investors, thereby restricting growth.

- Unsustainable debt acts as a barrier to the development of public policies capable of addressing the challenges facing the HIPC countries.

- Debt related pressures on national budgets have resulted in the burden of financing essential services being transferred away from public budgets and onto poor households. Formal and informal systems of cost recovery - usually such mechanisms as user fees - in areas such as basic healthcare and education are placing further strains on the budgets of desperately poor households.

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If it is accepted that unsustainable debt is one reason for chronic poverty in the HIPC countries, then it should also be accepted that tackling the debt crisis is an important step to enabling millions of people to move out of poverty. Debt relief has the potential to act as a catalyst for human development. The benefit will be even greater and mutually reinforcing, if it structured and provided in such a way which improves access to, and the quality of, the social and economic services used by poor people. Debt relief must be designed to support and reinforce integrated poverty reduction strategies, which are placed at the centre of macro-economic design.

While Community Aid Abroad Oxfam Australia believes that debt relief is not a sufficient condition for achieving the international community shared human development goals, we are absolutely convinced that it is a necessary condition.

It is manifestly clear that so far the HIPC process has not had a sufficient anti-poverty focus. It is this realisation that no doubt prompted the G7 Finance Ministers in their report on HIPC reform to call for a mechanism to "lay out specific priority steps needed to ... enhance social sector investment, focusing in particular on poverty reduction".

Why has HIPC not delivered the goods?

I won't repeat all the problems - these have been widely canvassed. Suffice to say that in contrast to the current HIPC process, a renewed debt relief mechanism needs to deliver deeper, quicker, more flexible debt relief, linked to poverty reduction measures. From a human development perspective, the requirement that a qualifying country adhere with two successive IMF programs was probably one of its biggest weaknesses.

The Cologne initiative agreed to by the G7 leaders addresses some of these problems, though in many aspects the jury is still out. There are some real positive aspects:

- The lower debt sustainability thresholds will double the NPV value of debt stock reduction

- The provision of interim debt relief by the international financial institutions in advance of completion Point could significantly reduce the cash-flow burden of debt service payments

- The commitment to "front-load" debt relief in the early years could generate a substantial increase in resource flows

- The G7 statement unambiguously transforms the HIPC framework into a mechanism for poverty reduction: "The central objective of this initiative is to provide a greater focus on poverty reduction by releasing resources for investment in health, education and social needs".

But substantial problems still remain.

Some of the countries with the most severe social development indicators, with the greatest incidence of poverty, will still be paying too much in debt servicing relative to spending on basic services.

- Mozambique will continue to spend twice as much on debt servicing as on primary education, even though there are 1.2 million children out of school

- Burkina Faso will continue to spend more on debt servicing than on primary health care, despite an average life expectancy of 46 years

The funding of the Cologne initiative is another area of major concern. At this point there is no indication as to how the initiative is to be funded. Our fear is that it may be funded by a diversion of development assistance, either from funds originally destined for non-HIPC countries to HIPC countries, or within individual HIPCS. Yet many of the non-HIPC countries also suffer from deep and chronic poverty. Further, such a diversion does little or nothing to strengthen poverty reduction attempts within the HIPC concerned. And such a diversion of funds would come from decreasing aid budgets.

Community Aid Abroad Oxfam Australia has other concerns about the Cologne initiative including its ambiguities regarding the timing of debt relief, eligibility for such relief and the apparent contradiction with other moves and stated intentions of donors, especially regarding a greater sense of national ownership.

So how can the HIPC framework and the Cologne initiative be improved to give a greater linkage to poverty reduction measures?

First, HIPC, no matter how good, cannot do it alone. It needs to be considered in the light of a number of other efforts to develop integrated poverty reduction strategies.

These efforts include:

- The Comprehensive Development Framework (CDF) being piloted by the World Bank. This is an attempt to integrate macro-economic and financial policy reforms in a single planning matrix with social and human development concerns

- The Principles of Good Practice in Social Policy which emphasise the achievement of universal access to basic social services, through an integrated strategy which places social capital development at the heart of macro-economic planning and institutional development. The World Bank-IMF Development Committee has adopted these principles.

- The 20/20 initiative which seeks to enhance the equity and efficiency of public spending by both donors and national governments in pursuit of shared human development goals.

Together these initiatives are helping to develop a policy environment which is conducive to poverty reduction measures. At a program level there are at least three other important developments, namely:

- Sector-Wide approaches (SWAPs) which are an attempt to move away from project-based financing to longer-term sector strategies

- Improved budget management and Medium Term Expenditure Frameworks (MTEFs)

- More participatory approaches to development, the "essential oil'.

Given these developments how can debt relief be geared most effectively towards poverty reduction goals? Critically there is no magic blueprint which can be applied without modification to each country concerned. Strategies and mechanisms are needed which adapt to processes and problems on a country by country basis, taking into account the state of national planning for poverty reduction.

Debtor countries have already developed a number of innovative approaches to poverty reduction which provide some very useful experiences. Uganda, for instance, has established the Poverty Action Fund which has provided a framework for channelling budget savings from debt relief into financing for priority social sector investments. Two million more children are now in primary education as a result of the limited debt relief from the HIPC.

The Ugandan experience is a powerful one for two main reasons. First, it is an integral part of a national human development strategy - the Poverty Eradication Action Plan - which is in turn a central element of a well-defined Medium Term Expenditure Framework. Secondly, the Ugandan Government has designed and administered the Poverty Action Fund in a manner which combines budget transparency with a high level of civil society participation. The Uganda Poverty Action Fund demonstrates a high level commitment to poverty reduction, as does the recent proposal by the Ghanaian government to establish a Debt for Development Fund. This Fund would link budget savings from debt relief to broad targets for raising expenditure in key social areas.

So how can the HIPC initiative truly become a vehicle for poverty reduction?

As indicated above there is a need to avoid detailed blueprints and rather the focus should be on developing a broad and flexible framework. Community Aid Abroad Oxfam Australia proposes a two-phase approach. One of the by-products of this approach would be to strengthen the hand of those countries which are in the process of developing poverty reduction strategies and plans in collaboration with partners.

The first phase of our approach is to the decision point.

Debtors would be required to establish a track record indicating a commitment to a continued economic reform process and to poverty reduction. The current eligibility criteria would be reformed and our preferred option would be for the World bank, IMF, United Nations agencies and other donors to reach an agreement with the government on more flexible criteria for macro economic adjustment, geared towards poverty reduction goals. Alternatively the IMF's ESAF targetting parameters must be brought into line with the policy requirements for the 2015 targets.

The length of the track record should be set in a more flexible manner, depending on country-specific events, shocks and other conditions. It should be no longer than two years.

In this initial track record period, governments would be expected to:

- Demonstrate progress towards an effective poverty reduction strategy.
- Develop a national poverty assessment - a clear profile of the underlying causes of poverty and inequality, including regional and gender inequalities.
- Develop a poverty reduction plan, addressing the challenges set out in the poverty assessment.

All these documents would be developed in collaboration with civil society and would be public documents. The aim would be to develop clear priorities for action, timetables for implementation and evaluation and monitoring procedures.

Performance benchmarks would be developed with the view of capturing the pace, scale and quality of reform, rather than absolute levels of achievement. While there would be no fixed time frame for the preparing a poverty reduction strategy -such a strategy would be a requirement for proceeding to Completion Point. Countries reaching the Decision Point with a strong national poverty reduction plan in place could proceed straight to Completion Point.

Importantly, under this arrangement delayed progress towards Completion Point should be seen not as a means for punishing bad performance or delaying debt relief, but as a means of ensuing that the flow of debt relief after the Completion Point is used with maximum efficiency and effectiveness.

Moving to Phase 2.

At the Completion Point, governments will receive debt stock reduction and will exit from the HIPC framework. To reach this point countries will be required to meet just one condition - a demonstrable capacity to absorb debt relief into the national poverty reduction strategy. Some countries could proceed immediately to the Completion Point, others with less well-developed poverty reduction strategies would benefit from interim debt relief flows which would substantially reduce the costs of delayed progress.

Performance criteria for measuring progress in the development of a poverty reduction strategy would include macro-economic and social policy indicators, including such things as:

- Progress towards poverty-focused public spending priorities
- Strengthened budget management
- Development of a Medium Term Expenditure Framework

In order to demonstrate the capacity to absorb debt relief into the national poverty reduction strategy, governments will be required to develop in cooperation with civil society and donors, a Debt for Development Plan. This would detail:

- The proportion of debt relief which will be channeled into basic social services

- The outcome targets related to increased spending on basic services, over and above those already envisaged in existing sector strategies and projected trends

- Infrastructural investments specifically benefiting the poor, such a support for rural feeder roads, irrigation and marketing support, specifying the regions and districts to be targeted

- Monitoring and evaluation arrangements with civil society to assess outcomes.

It is clear that we are proposing conditionality - but it is a positive conditionality to help tackle the most serious global social crisis. It is a way to help put some substance into the international agreed to 2015 social development targets. It is a way to ensure that the way out of the debt crisis becomes a permanent one for HIPC countries. It is a way to help strengthen civil society in HIPC countries and relations between civil society and governments.

It flows from all that I have said that we want the rich world, including Australia, to help solve the debt crisis- and solve it quickly.

Decisions about the future of HIPC and of debt relief more generally are to be made in the next two months. Community Aid Abroad Oxfam Australia believes it's essential that the Australian government join with other governments - and indeed joins with the growing international movement - to ensure that from all the negotiations and discussions a mechanism emerges which delivers faster, deeper and more flexible debt relief. And, importantly one which strengthens the linkage between debt relief and poverty reduction.

Specifically, at next month's annual meetings of the World Bank and IMF, Community Aid Abroad Oxfam Australia proposes a seven-point plan for the Australian government:

- Support the thrust of the G7 Cologne Communiqué as an important but limited step forward in recognition of the failure of the 1996 HIPC initiative.

- Publicly recognise that the Cologne Communiqué does not go far enough. The HIPCs are amongst the world's poorest countries, and the majority will remain offtrack by a wide margin for meeting the human development commitments made at Copenhagen in 1995.

- Advocate for debt relief to be linked to poverty reduction through the provision of incentives for quicker and deeper debt relief to HIPC countries committed to chanelling resources into poverty alleviation programs such as basic education and primary health care.

- Advocate for HIPC repayments to be limited to no more than 10% of Government revenue for HIPCs as part of advocating a more poverty focused approach to debt relief.

- Advocate that countries with viable poverty reduction strategies should not have to wait at all - let alone up to three or six years - for debt relief, and for generous interim relief to be provided as an incentive to those countries which have yet to develop plans for converting debt liabilities into pro-poor spending.

- Commit to finance deeper and faster debt relief for the enhanced HIPC through additional resources - not out of the existing aid budget.

- Support the proposed IMF gold sales as a measure for partially funding debt relief measures.

The debt crisis will be with us for ever more unless governments and people in the rich world are prepared to take the necessary steps to ensure a sustainable solution. The next two months could be our once in a lifetime opportunity.