COMMISSION OF THE EUROPEAN COMMUNITIES

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COMMUNICATION FROM THE COMMISSION

TO THE COUNCIL, THE EUROPEAN PARLIAMENT
AND THE ECONOMIC AND SOCIAL COMMITTEE

on a Community participation in the debt relief initiative for highly indebted poor countries (HIPC)

EUROPEAN COMMISSION

Communication of the Commission

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The Highly Indebted Poor Country (HIPC) initiative was launched by the IMF and the World Bank in September 1996 with the aim to help relieve the debt burden of the poorest countries that make adjustment efforts in a concerted way and are committed to fight poverty. It represents a co-ordinated effort by all donors, including in particular multilateral creditors. The initiative covers those poorest countries which are eligible for highly concessional assistance from the WB and the IMF, and whose debt burdens are deemed to be unsustainable after all other debt relief measures have been applied.

As a major partner of developing countries, the Community is mainly supporting development through grants. Thus, it is only a small multilateral creditor. For instance, it will account for only about 2% of the latest total estimated cost of the HIPC initiative, or roughly 4.3% of that of multilaterals (13.3 Billion US$).

From the outset, the Community has strongly supported the HIPC initiative. It has been fully participating in it with regard to its claims to eligible ACP countries. It has made a commitment to provide in due time debt-relief to all HIPC assistance eligible ACP countries as laid down in the Council decision of July 6 1998. Furthermore, it has also attempted to address some specific problems such as interim relief through additional actions as a donor (annex 1).

At the G-7 Cologne summit, Ministers agreed to an 'expanded initiative that will provide *faster, deeper and broader* debt relief' (annex 2). As a result of the proposed enhancements, the total costs of the Initiative are now expected to more than double to US$ 27.4 bn.

If adopting the ambitious targets set at the Cologne G7 Summit, some financing is still needed in order to fully finance the multilateral share of the enhanced HIPC initiative:

Table 1: Financing needs for the HIPC initiative *(Billion US$)*

Institutions (exc. IMF)	Total Financing needs	Already Identified	Remaining	o/w. short term
World Bank	5.1	2.0	3.1	0.6
AfDB	2.0	0.6	1.4	0.8
IaDB	1.0	0.4	0.6	0.6
Other multilaterals (including EC)	2.9	1.8	1.1	0.6
Total (including IMF)	13.3	-	6.2	2.6

***Sources**: 'The Enhanced HIPC Framework: Financing the World Bank's HIPC Debt Relief', IDA, August 26,1999, and manual update after the last Bretton Woods Institutions Annual meetings*

There is growing pressure exerted on multilateral institutions to internally mobilise the required funds enabling them to meet their contributions to the enhanced HIPC in order to reduce the bilateral financing gap. For all Multilateral Development Banks, the main limit to additional contributions is the fact that further internal funding from these institutions would be at the expense of their aid programmes. As for the AfDB the exercise is almost impossible.

During the last Annual meetings of the Bretton Woods Institutions in Washington the Donor community took some far- reaching policy decisions which are expected to have significant implications for the group of highly indebted poorest developing countries. For the first time a close relation has been stressed between poverty alleviation strategies, structural adjustment programmes and a debt relief initiative. Both the IMF and the World Bank have been put at the heart of a set of more coherent, effective and co-ordinated development instruments. The concessional IMF facility for the poorest countries (ESAF) has been re-focused towards fighting poverty and transformed into a new Poverty Reduction and Growth Facility (PRGF). New Poverty Reduction Strategy papers will be jointly prepared by the World Bank and the IMF. In addition multilateral and bilateral creditors announced significant contributions to the financing of the HIPC Initiative (and to its special Trust Fund in particular).In spite of those recent pledges, the level of bilateral contributions to the HIPC Trust Fund (1.4 billions) remains insufficient to cover the 2.6 short term remaining financial gap (table 2). Moreover, although rather limited (especially when taking account of the very low US contribution to bilateral debt alleviation within the enhanced HIPC framework), the US administration pledge still needs the agreement of the US Congress, which is not secured.

Table 2: Bilateral support to the HIPC Trust Fund *(Million US$)*

	Contr°	Old Pledges	Recent Pledges	*Total*		Contr°	Old Pledges	Recent Pledges	*Total*
Australia	5			*5*	Luxembourg	1			*1*
Belgium	4	8		*12*	Netherlands	61	70		*131*
Canada	27			*27*	Norway	41			*41*
Denmark	26			*26*	Portugal	15			*15*
France		21		*21*	Spain	15			*15*
Finland	14			*14*	Sweden	29			*29*
Germany		27	54	*81*	Switzerland	28			*28*
Greece	1			*1*	UK	36	135	50	*221*
Ireland	16			*16*	USA			650?	*650*
Italy		70		*70*					
Japan	10			*10*	***Total***	***329***	***331***	***754***	***1414***

***Source**: 'HIPC Initiative: Perspectives on the Current Framework and Options for Change', IDA, April 2, 1999, with partial update with information available to the Commission.*

During the same meeting, and following an 'information note' from the Commission's services on a possible Community contribution to the enhanced HIPC, the Presidency of the European Council made the following statement:

"The EU is prepared to use funds in the framework of existing EDF instruments for the purpose of making a substantial contribution towards attenuating the debt burden of ACP States which are eligible for the HIPC initiative, and will approach the ACP States with a positive proposal to that end. The treatment of non-ACP States should be a fair one, in the global effort of the international Community. This initiative would include contributions for debt cancellation of the order of magnitude of one billion euros".

The proposal of the Commission, which follows on the above-mentioned 'information note', is to be seen in this perspective.

* *

The decision adopted by the Council on 6 July 1998 on a proposal of the Commission confirmed the Community's full participation in the original initiative both as a donor and as a creditor:

- as a donor, by making available supplementary resources under the 8th EDF structural adjustment facility for countries having reached their "decision point";
- as a creditor, by using, in the first place, interest earned on EDF funds to deal directly (at the agreed level for multilateral donors) with the debt of countries having reached their "completion point".

As those two dimensions did not concern non -ACP HIPCs, funding (40 million Ecus) was only drawn from EDF.

The reduction in the eligibility ratio, the retroactive application of new criteria, the greater number of countries and the speeding-up of decision will increase the cost of the enhanced initiative in such a way that the interest earned on EDF funds or possible reflows, as provided for in the Council Decision of July 1998 will not be sufficient.

The overall EU contribution can be financed mainly with non-allocated 8th and previous EDF resources. However, in view of the enhancement of the Initiative, the Commission proposes that also the external indebtedness of non-ACP HIPCs be addressed and supported with budgetary resources. As regards the ACP countries, available EDF-based resources, which are in excess of € 1 bn, are derived as follows: co-operation with non-performing countries for which programmable resources have not been allocated; some are also the result of programming by tranche under the revised Lomé IV, which means that the second tranche of programmable resources has not been mobilised for a number of underperforming countries; finally, unused Stabex funds may become available after the expiration of Lomé IV on February 29, 1999.

However, for any mobilisation of EDF resources, a decision of the ACP-EC Council of Ministers will be needed, as the proposed Community action is outside the normal procedures of the Lomé Convention. To prepare for such a decision, a dialogue has to be opened in the very near future between the European Community and its ACP partners. Similarly, the use of funds from the General Budget to support the initiative for non-ACP countries will be implemented in coherence with the Commission Cooperation Strategies towards them. The legal basis for the Community's action will be the ALA Regulation n. 443 / 92 which emphasises a new commitment towards poverty alleviation (art. 4) and Community's support to enable EU partner countries to overcome macroeconomic and structural problems (art. 5).

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The Commission's proposal is based on three elements:

Role of the Community as a creditor:

For all multilateral creditors, it is impossible, at this stage, to give definitive figures on their contribution to the initiative. Indeed, some countries will only qualify, if they do, in 2001 or later, and reliable analysis of their debt situation will only be available by then. Accordingly, the degree of future debt alleviation can only be very approximately estimated for the totality of eligible countries (annex 3).

Going by current estimates and setting them against a Community claimable debt, including arrears, in the order of € 1.3 bn in net present value, the cost of the Community's contribution for potentially eligible countries would be in the region of €550 Million (annex 4), out of which 40 MEUR already secured by the July 1998 decision, through interest from former EDFs.

The mobilisation of the required financing reaffirms the strong political commitment by the European Community to the Initiative. These resources will however be mobilised on a case-by-case basis, including with respect to the level of arrears to be taken into account, following a favourable opinion of the EDF Committee, in such a way that each of the countries involved would, on reaching its "completion point", be able to prepay part of its debt to the Community on a Net Present Value basis (annex 5).

Role of the Community as a donor:

Over and above this amount, which corresponds to the Community's role as a creditor, the Commission advocates to remain on the lines defined by the Community's involvement as a donor under the original HIPC framework. This refers to a bonus on the structural adjustment support to eligible countries having reached their "decision point", so that they have adequate financing for their macroeconomic reforms, which in turn will facilitate their efforts to reach their "completion point" (annex 1). The evaluation of the size of the bonus should in the future also take into account the beneficiary country's past track record in servicing its debt towards the Community.

Such a contribution would be in line with two key elements of the Cologne proposal: the need for adequate support to HIPCs during the interim period, and the need to enhance the social content of the whole exercise (annex 6).

In the past, this additional support was financed by reallocations of funds within the Structural Adjustment Facility with no increase in the overall amount. If this instrument is to be deployed extensively in the near future, bearing in mind the large number of countries that will become eligible for the initiative over the next 24 months, there will not be a sufficient margin to cover the additional requirements of the countries concerned. The Facility will thus have to be given more resources. An additional argument in favour of such an increase is that the next EDF is unlikely to enter into force before 2002.

The Commission estimates that the Community's contribution to the HIPC initiative as a creditor should be mirrored by an increase, as a donor, to the tune of €150 Million in the 8th EDF Structural Adjustment Facility. This amount will also need to be mobilised from unallocated 8th and previous EDF money.

The additional SAF support will be mobilised on a case-by-case basis on top of the structural adjustment programme whenever a country reaches its "decision point".

Role of the Community as a major development stakeholder:

As a major development partner, the Commission feel that, on top of its participation stricto sensu to the enhancement of the HIPC Initiative, the Community should make a contribution to the overall financing of the HIPC initiative, and specifically to the HIPC Trust Fund.

Such an additional contribution would be in line with the Community support to development in general. This policy spans from the Community strategy to better integrate developing countries into the world trading system to its support for global debt alleviation and fighting poverty.

This participation, however, should be considered keeping in mind the need to ensure a minimum of fair burden sharing among stakeholders. The Community cannot, on its own, fully finance the remaining gap, and other donors would have to play their fair part in the financing of the Initiative.

Moreover, it would make sense that a contribution of this kind should not be exclusively funded from unallocated EDF resources. It should rather be seen as a contribution to global debt relief of the highly indebted poorest countries, which also includes non-ACP countries. As such, it should comprise an adequate mix of EDF and appropriate complementary financing from the general budget, and contributions from all stakeholders in an agreed EU context.

While preserving adequate funding for existing programmes, this funding from the general budget would imply a redeployment of resources within the financial envelope allocated to the concerned non-ACP geographical co-operation programmes, covered by subsection B7 (external action) of the Community Budget.

The amount of the Community contribution to the HIPC Trust Fund could be of an order of magnitude of 200 to 300 MEUR, depending on final decisions on fair burden sharing. 82% would be financed from unallocated EDF resources (annex 4), and the rest from the Community budget. Taking into account the geographical distribution and eligibility for debt relief of the countries concerned, the approximate breakdown over a period of three years beginning in 1999 could be 15% from chapter B7-31, 'Cooperation with Latin American developing countries', and 3% from chapter B7-30, 'Cooperation with Asian developing countries'. However the precise split remains to be determined, including in the course of discussions with the World Bank on modalities/

The Community contribution to the HIPC Trust Fund would be earmarked. Resources originating from the EDF would be earmarked for the ACP countries, and in principle for the AfDB's claims on African HIPCs belonging to the group of ACP countries (with specific dispositions for the sole non-African ACP HIPC: Guyana). Resources originating from the budget would help financing the reduction of claims towards Asian or Latin American HIPCs. Specific dispositions will be taken to ensure that, following EU financing to the Multilateral Debt Relief Initiative, beneficiary countries will use further domestic resources for social sector development.

The technical modalities of such a combined financing of a possible EU contribution to the enhanced HIPC Initiative would have, of course, to be considered carefully in their details. In particular, specific provisions will be taken to ensure adequate visibility, monitoring and financial control of the EU contribution to the Initiative in general and to the Trust Fund in particular.

In a nutshell, the Commission proposal is as follows:

Contribution to the initiative as a creditor:	550 MEUR
Increase of the Structural Adjustment Facility:	150 MEUR
Contribution to the HIPC Trust Fund:	200-300 MEUR
Total	900-1000 MEUR

ANNEXES

to the

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ANNEX 1

IMPLEMENTATION OF THE COUNCIL DECISION OF 6 JULY 1998

Eight ACP countries reached "decision point" in 1997 and 1998 and so are covered by the Decision of 6 July 1998. With the new criteria all, rather than merely six of them, should eventually qualify for debt alleviation.

Of these eight, only three have so far reached "completion point" in the framework of the HIPC initiative: Uganda, Guyana and Mozambique. Following the financing decision adopted by the Commission on 24 July 1998, all Uganda's remaining obligations in the form of special loans were wiped out to the tune of ECU 4 590 000. A financing proposal for Guyana will shortly go before the EDF Committee. Naturally, in both cases an additional alleviation will take place once the new debt alleviation objectives are known. Mozambique is a trickier case because a lot of risk capital has to be paid upfront, something which poses a number of technical problems. Since the completion point has only just been decided, the Commission proposes to wait a few weeks/months while the alleviation objectives are revamped so as to move straight into the finalised version of the alleviation plan.

Ever since it joined the HIPC initiative the Commission has considered that simply fully meeting its commitments as creditor was not sufficient in view of the scale of the ACP countries' debt problem. Hence its decision to readjust the share-out of the structural adjustment facility (SAF) and raise the HIPC allocations during the interim period by 15% (or by 10% for countries already enjoying a 15% bonus in the form of regional integration support). Annex 3 shows that a good many countries will gain from this measure in their 1999-2000 allocations.

Note that this Community initiative anticipated the G7's call for support to the HIPC initiative at the beginning of the interim period, as well as its intention to enhance the social content of the process linked to the initiative (see Annex 6).

ANNEX 2

THE MAIN FEATURES OF THE ENHANCED INITIATIVE

Following a series of initiatives taken by a number of member States, the G7 meeting at Cologne in early June this year decided to facilitate and reinforce the highly indebted poor countries' access to the HIPC initiative.

The proposals made at Cologne, which have since been endorsed by the Bretton Woods institutions, have three main planks, which can be summed up by the slogan "*deeper, broader and faster*".

- "Deeper" debt alleviation:
    * reduce the NPV debt-to-export qualification ratio from 200-250% to 150%;
    * make the access conditions for the "fiscal window" more flexible by lowering the qualifying thresholds concerning the openness of the beneficiary economies and revenue as a proportion of GDP[1];
    * retroactive application of these new criteria to countries which already reached their 'decision/completion points', so that they are not penalised for having met the conditions more quickly;
    * fix final debt reduction objectives when the decision point is reached, namely when it is decided that a country qualifies (with no possibility of revision, as hitherto, at completion point, i.e. when it is acknowledged that a country has met the conditions laid down and creditors actually start to reduce the country's stock of debt), meaning that an increase in GDP or exports will not penalise the beneficiary.
- "Broader" coverage of the initiative:
    * thanks to these changes the number of the 41 HIPCs that should ultimately qualify for the initiative should rise from 26 to 33, and even 36 if Liberia, Sudan and Somalia are included.
- "Faster" relief:
    * the international financial institutions (IFIs) and other multilaterals that so desire, will provide debt servicing relief during the interim period, i.e. between the decision and completion points;
    * the completion point will become floating in the sense that the countries will enjoy a final alleviation of their debt as soon as they have met all the conditions set, even if they do so before the three years hitherto laid down as interim period.

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1 To benefit from the "fiscal window", namely qualify even when the net present value of the debt is less than 150% of exports, it is now enough that the NPV debt-to-revenue ratio is over 250% (against 280% previously), that exports account for only 30% of GDP (against 40% previously) and that revenue exceeds 15% of this same GDP (against 20% previously).

ANNEX 3 :
LIST OF POTENTIALLY ELIGIBLE COUNTRIES

Decision point reached in 1997
Benin, Bolivia Burkina Faso, Guyana, Uganda

Decision point reached in 1998
Côte d'Ivoire, Mali, Mozambique, Senegal.

Decision point expected in 1999
Chad, Ethiopia, Ghana, Guinea, Honduras, Laos, Malawi, Mauritania, Nicaragua, Niger, Tanzania, Togo, Zambia.

Decision point expected in 2000
Cameroon, Congo, Guinea-Bissau, Madagascar, Rwanda, Sierra Leone.

Decision point expected in 2001 or later
CAR, Burundi, Myanmar, Sao Tome & Principe, DRC, Liberia, Somalia, Sudan.

ANNEXE 4
METHOD OF CALCULATING THE COMMUNITY'S CONTRIBUTION

To be able to deduce the level of the Community contribution from what is set out in Annexes 3 and 5 we would need a reliable estimate of the percentages of debt reduction that will be decided. But this is impossible as we are in a period of transition.

- In the case of countries that have already reached the decision point qualifying them for debt alleviation, we need to update the figures calculated earlier in the light of the new Cologne principles and this can be done only roughly.[2]

- The data available for other eligible but not yet qualified countries are even more unsatisfactory since we do not have any good estimate of the economic ratios and we do not know the discount rate that will be used for calculating the net present value.

We therefore cannot claim to give anything but rough estimates and a large margin of error must be allowed for. The Bretton Woods institutions have tried. They have calculated that the total cost of the initiative will rise from USD 6.2 billion to 13.3 billion for all the multilateral creditors, meaning that the principles adopted at Cologne will more or less double its cost.

The table below, drawn up on the basis of current estimates, gives a geographical breakdown of this total.

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[2] In principle the cost of participation in the initiative is henceforth fixed at the decision point on the basis of current economic data. But the way in which the criteria are to be applied retroactively to the countries that have already reached it is not clear. Will account be taken of the evolution of macroeconomic ratios and data – exports, earnings, GDP and, above all, discount rates – or will the new ratios be mechanically applied to the original data?

Table 3: geographical breakdown of the total cost (%)

	% of the total cost, all HIPCs	% of total cost, all HIPCs except SSL
ACP	86	113
of which: non-SSL ACP	*62*	*82*
of which: non-African ACP	*1*	*2*
ALAT	11	15
Asia	2	3

***Source**: World Bank*

In the particular case of the Community, note that the "European" claimable debt is of three types: special loans, risk capital and loans on EIB own resources. When it comes to participation in the HIPC initiative, the Community will assume the two former types of debt and the EIB the third (the Bank having accepted the Council's request contained in the Decision of 6 July 1998). The respective responsibilities are thus clearly identified.

The problem arises from the fact that it is technically not possible either to make direct use of the Bretton Woods estimates[3] or to make country-by-country estimates, however approximate.[4]

In view of these constraints, a pragmatic approach had to be adopted. It was decided to apply, on the basis of figures supplied by the EIB (which gives the schedules and thus the net present values of each of the special loans and risk capital operations) the least unfavourable reduction percentage available, namely the one derived from the *average* estimates of the Bretton Woods institutions.

In the preliminary document provided by these institutions,[5] the figure put forward for the European participation is USD 731 million in 1998 terms. This figure represents 41% of the net present value of the ACP debt to the Community and EIB including arrears (USD 1.8 billion). In relative terms, this order of magnitude matches the increase in the total cost of the initiative to multilaterals – a 20% average reduction of debt was used as a working hypothesis in the earlier report (1998) on the Community's participation in the initiative.

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[3] Not only do they not distinguish between the different types of European claims referred to above but also their estimate of the net present value is altogether excessive in the light of the information available to us. Furthermore, using the Bretton Woods estimates means adopting dollar calculations and the Commission has always made clear that it works only in euros and that in the framework of its participation in the initiative it would be bound only by NPV percentage reductions (not units). Indeed, the main cause of the difference between the Bretton Woods figures and those of the EIB would appear to stem from the exchange rates used.

[4] The World Bank, which centralises the information gathered under the HIPC initiative, has such estimates. With them it established a matrix of reduction coefficients, on the basis of which it calculated the debt reductions for each of the potentially eligible countries. It did not, however, want to publish this matrix or any table that would enable deductions to be made on the grounds that it could give rise to false hopes and give mere estimates too official a status. If the Commission were to try to gather the information to make its own estimates, it would be faced with the same problem.

[5] Preliminary costing for individual MDBs – EIB/EU, MDBs meeting, Friday June 25 1999.

About including arrears in the claimable basis, it is worth recalling that the application of the rules has been relaxed. In the past, the treatment of arrears to multilaterals in the context of the HIPC Initiative had been guided by the principle of clearing all arrears before a HIPC could become eligible for assistance under the initiative (*at the decision point*) so that it would enable all donors to take part in the debt relief action[6]. This remains true: the final settlement of actual debt relief will not be decided until all arrears are cleared towards all multilateral creditors. However, the estimates provided by the World Bank now include arrears in the base for calculating the reduction ratio by treating them as part of the regular debt. On this issue, there has been an understanding reached together with all multilaterals taking part in the Initiative, and which was reconfirmed during the October 1st Multilateral Development Banks meeting in Washington.

According to EIB figures (see table 4 below), at 31 December 1998 the NPV at 4.5% of the special loans and risk capital covered by the initiative stood at €1209 million excluding arrears and at €1340 million including arrears. By applying the rates of 41% to this last amount, we obtain €549 million (or €516 million excluding Sudan, Somalia and Liberia). In view of the margin of error induced by the estimation methodology we used[7], even if Sudan, Somalia and Liberia are very unlikely to benefit from the initiative, it would be preferable to secure a sufficient security margin and take a conservative figure of around €550 million[8].

This figure includes an estimate of what our contribution would be to the debt alleviation of Somalia, Sudan and Liberia, plus countries with which the Community has suspended cooperation. From the methodological point of view, note that all the figures cited above were calculated at 31 December 1998. In other words, the sums reimbursed by the HIPCs up to the start of debt alleviation will have to be deducted.

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6 So far the Community, which is treated as a preferred creditor, has always strictly adhered to this principle in its assistance to third countries, and the assistance provided under the HIPC framework has not called for an exceptional treatment to date (Uganda being the only ACP country having received Community debt relief assistance and having no arrears to the Community).

7 Applying to the EIB database the "European' average reduction rate derived from the World Bank estimates, on top of above mentioned quality problems, is definitely a 'second best'. First there are great differences in the geographical breakdown of loans on own resources, on the one hand (fewer in number and concentrated in a small group of countries), and special loans and risk capital, on the other. One of the EIB's main debtors in terms of loans on own resources is Côte d'Ivoire, and in its case the debt reduction will be well below average. Therefore the use of the "European" average rate (i.e. including the EIB) for all claims relating to special loans and risk capital tends to underestimate the debt reduction necessary under the initiative. Moreover, the data supplied by the EIB gives the NPV at 31 December 1998, which means that all new disbursements after this date but before the cut-off date fixed for calculating the NPV at decision point will have to be added. But while these first two elements tend to lead to underestimates, the choice of a discount rate appropriate to what would be the reference rate for a decision point at end 1998 (4.5%) would overestimate the NPV of the Community debt. For countries that have already reached their decision point the reference discount rate is in fact higher, and the NPV thus lower. If the upwards trend in interest rates continues, the same will apply for countries qualifying in 2000 or after. Added to this, disbursements that continue to be made under the drawing rights have to be taken into account, as do the repayments made up to the completion point that then have to be deducted from the value of Community debts at 31 December 1998. Failing any information that will help us determine which factor will predominate, we shall just have to work on the assumption that they will cancel each other out, but this implies to accept taking a significant security margin, when presenting the outcome of the estimate.

8 Out of which 40 MEUR already secured by the July 1998 decision, through interest from former EDFs.

How to deal with the countries with which cooperation is suspended is a difficult matter. It is hard to see how the Commission could commit itself to participating in the initiative in respect of these countries unless cooperation had resumed[9]. But we cannot rule out cooperation resuming with these countries, even in the short term. It would thus be wise to include the potential cost of these countries' becoming eligible, even though the Community's participation is likely to come much later in their case than that of other multilateral creditors.

On a more general note, the Community's participation in the initiative will be staggered over several years and its cost should be viewed in a timescale beyond the provisional schedules in Annex 3. Since the completion point will henceforth be floating, the schedule of costs is more tentative than ever. And even if some countries qualify earlier than predicted, it is highly likely that this will be counterbalanced by others doing so later. In other words, the completion point may come more than three years after the decision point. Furthermore, in spite of the 'enhanced' treatment of arrears, a practical risk remains, leaving aside geopolitical vicissitudes (some potential beneficiaries are at war or politically very fragile) that many could fail to reach their theoretical completion point dates on time, due to their incapacity to completely clear arrears.

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9. This is clear if you consider that reducing these countries' debt is in some way equivalent to giving them budgetary aid because it releases resources that would otherwide be devoted to debt servicing.

Table 4: Theoretical cost on the basis of average reductions (EUR)

	Total claims Nominal	Total claims NPV (1) (a)	of which special loans Nominal	of which special loans NPV (1)	arrears (b)	Cost Theoretical(4) 0.41 x (a+b)
Angola	2.107.710	**1.676.812**	0	**0**	978.881	1.088.834
Benin	15.885.850	**10.264.038**	2.796.735	**1.591.466**		4.208.256
Burkina	45.536.152	**32.201.534**	11.629.399	**6.930.186**	10.477	13.206.925
Burundi	54.201.588	**32.300.611**	42.689.409	**23.511.196**	5.680.753	15.572.359
Cameroon	83.838.177	**46.607.965**	81.171.648	**44.511.617**		19.109.265
CAR	13.916.421	**10.790.989**	4.454.571	**2.595.257**	1.303.805	4.958.865
Chad	8.142.926	**5.824.017**	5.331.606	**3.601.913**	30.913	2.400.521
Congo	47.480.297	**29.494.208**	37.085.907	**21.376.347**	16.323.192	18.785.134
Congo (DRC)	138.731.707	**86.595.910**	108.529.321	**63.171.978**	44.378.977	53.699.704
Côte d'Ivoire	82.059.529	**50.724.419**	66.246.525	**38.505.539**	11.400	20.801.686
Ethiopia	81.595.071	**55.827.759**	32.650.644	**18.248.946**	11.000	22.893.891
Ghana	47.409.459	**33.638.739**	29.437.474	**18.416.877**		13.791.883
Guinea	145.616.087	**94.177.740**	63.971.201	**35.123.489**	4.402.095	40.417.732
Guinea-B.	5.610.600	**5.610.600**			902.140	2.670.223
Guinea Eq.	4.403.616	**3.346.207**			2.602.258	2.438.871
Guyana	51.096.680	**29.316.417**	43.174.114	**23.072.409**		12.019.731
Kenya	144.989.180	**95.773.260**	87.432.193	**51.447.287**	1.596.039	39.921.413
Liberia	6.400.453	**3.877.330**	5.828.853	**3.305.730**	1.286.313	2.117.094
Madagascar	49.098.029	**32.068.513**	30.170.338	**16.967.571**		13.148.090
Malawi	89.070.772	**57.431.596**	31.088.890	**17.418.722**	23.733	23.556.685
Mali	57.263.432	**39.994.067**	26.078.948	**14.742.812**		16.397.567
Mauritania	59.223.561	**40.951.983**	28.176.598	**15.692.864**		16.790.313
Mozambique	45.115.734	**30.361.150**	7.687.004	**3.235.408**	1.205.131	12.942.175
Niger	34.272.625	**21.140.877**	24.256.962	**13.051.789**	6.169.543	11.197.272
Rwanda	35.652.251	**23.535.877**	23.735.701	**13.886.726**	7.073.035	12.549.654
Sao T. & P.	1.103.932	**941.410**	0	**0**		385.978
Senegal	93.860.217	**58.439.695**	66.365.451	**37.302.249**	24.762	23.970.427
Sierra Leone	34.368.124	**22.078.084**	17.479.696	**9.745.864**	2.243.708	9.971.935
Somalia	19.022.338	**16.403.094**	0	**0**	5.558.634	9.004.308
Sudan	37.676.792	**30.105.038**	12.471.873	**7.878.929**	23.340.592	21.912.708
Tanzania	75.067.684	**51.887.432**	36.289.449	**22.940.210**	569.059	21.507.161
Togo	29.459.809	**19.489.507**	23.005.303	**14.484.995**	1.166.281	8.468.873
Uganda (3)	41.664.619	**36.089.050**	(4)	**4.590.000**		14.796.510
Zambia	161.261.860	**100.477.562**	136.403.621	**80.297.394**	3.558.294	42.654.701
Total HC (2)	1.542.271.432	**1.009.753.649**	894.067.425	**516.006.485**	**46.306.967**	**432.984.853**
Total - SSL	1.779.103.698	**1.159.058.028**	1.067.338.707	**616.461.110**	**100.265.476**	**516.322.637**
Total	1.842.203.281	**1.209.443.489**	1.085.639.433	**627.645.769**	**130.451.015**	**549.356.747**

(1) NPV=net present value at 4.5% on 1 January 1999.
(2) Total HCS = Total excluding countries with which cooperation is currently suspended: Somalia, Sudan and Liberia (SSL) + DRC, Niger, Sierra Leone and Togo
(3) In the case of Uganda there are no more special loans because they were cancelled as part of the Community's participation in the HIPC initiative. But, applying the principle of retroactivity, we have added to the NPV of our claims the value these special loans had at the time of their early repayment.
(4) Theoretical cost of the Community's participation applying a rate of 41% to the NPV of the Community's claims including arrears.

ANNEXE 5

PRINCIPLES GOVERNING THE COMMUNITY'S CONTRIBUTION

The European Community shall fully participate in the HIPC initiative by assisting the countries which will qualify for this initiative, with a view to helping them reducing the net present value of their external financial obligations towards the Community. For this purpose, the Community shall make available grant resources to be utilised by the eligible countries to meet outstanding debt and debt service obligations towards the Community. This assistance, together with resources provided by other creditors, shall allow the eligible countries to achieve their country-specific debt sustainability target agreed within the framework of the HIPC initiative.

This assistance referred shall primarily be used by the beneficiary countries to prepay outstanding special loans on a net present value basis. If such action is not sufficient to attain the agreed level of net present value debt reduction, the beneficiary country shall use the allocated grant to meet any outstanding risk capital obligations towards the Community.

The Commission shall take, on a case-by-case basis, specific decisions providing assistance to each eligible ACP country, in accordance with the rules and procedures laid down in Chapter IV of the Internal Agreement. The Commission's decision on the amount of assistance to be provided in each case shall allow for the necessary reduction in the net present value of that country's outstanding external financial obligations toward the Community and be consistent with the HIPC initiative methodology. The country specific decisions shall also take into account the structure of the country's exposure towards the Community, the desire for administrative simplicity in the case-specific proposals chosen and the need to ensure an equitable and fair treatment between the eligible countries. Each country decision shall make explicit the modalities, terms and conditions for the implementation of the 6th July 1998 decision.

ANNEX 6
THE LINK BETWEEN THE INITIATIVE AND POVERTY REDUCTION

The G7 did not rest on its laurels with a "deeper, broader and faster" initiative; it formally requested the IMF and the World Bank to give poverty reduction a much higher priority in their operations as well as in the debt relief process. The IMF's Enhanced Structural Adjustment Facilities were explicitly mentioned.

It is not yet quite clear what the operational response of the Bretton Woods institutions will be but we are obviously heading for a radical change in the way structural adjustment programmes and policy framework papers are drawn up in future.

This strengthening of the social link is in perfect accord with the Community's longstanding concerns and with the Commission's new guidelines for structural adjustment.

Indeed, the Community's structural adjustment support programmes were designed to underpin and expand the social dimension to programmes negotiated with the IMF. From the start the main aim was to secure social spending and ensure that adjustment was not achieved at the expenses of social standards. Another aim was to extend the necessary process of adjustment beyond the purely monetary/budgetary sphere in order to make the public administration of social sectors more efficient. In other words, the Commission has always tried to emphasis the social dimension of adjustment, even to the extent of establishing its own forms of conditionality specific to social considerations. Seen in this light, the G7's call is a response to longstanding Community concerns.

It also fits in perfectly with the Commission's new structural adjustment guidelines. Discussions between most major donors in the SPA framework have revealed ever more clearly that a reform of conditionality has to be envisaged. The Commission has played in key role in this process. A pilot scheme it carried out in Burkina Faso produced a number of tools that could radically change the very concept of structural adjustment programmes, above all by making aid depend on performance indicators mainly focused on the social needs of the population.

The Commission's last communication on structural adjustment drew conclusions from these efforts and it has already been decided to start implementation, in Madagascar and Senegal for example. The basic idea is to concentrate on the results of reforms rather than the reforms themselves. This will mean that: (i) the focus of reform programmes will become longer term; and (ii) the countries concerned will have to assume greater responsibility for the choice of measures and the pace and order of reforms; transparency will be encouraged, objectives will become more explicit and programmes will be assessed by results. These efforts will have poverty reduction and institutional building as priority objectives.

The Commission hopes that the Bretton Woods institutions will draw on these experiences and come up with an operational response to the G7's request that is in accordance with SPA principles.

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