BLESSED ARE THE POOR?

Today 41 of the world’s poorest countries are bankrupt. These nations, identified by the World Bank as “heavily indebted poor countries” (HIPC), owe some $170 billion to foreign creditors, while half of their 600 million citizens get by on less than $1 a day. Nine out of ten HIPC cannot sustain their debts, given their low export earnings and GNPS. Unless some of this debt is forgiven, they will be paying in perpetuity. Their creditors, on the other hand, include the wealthiest countries in the world, as well as the international financial institutions that are meant to support economic development.

In the spirit of the Jubilee (a semicentennial forgiveness of debts described in the Old Testament), a diverse and powerful coalition of political and religious leaders, Nobel Peace Prize winners, economists, rock stars, and rioting activists has rallied for a complete debt write-off. Arguing that high interest payments “crowd out” government spending on the poor, these advocates claim that forgiving national debts will help relieve the world’s worst poverty. Using powerful emotional rhetoric, they offer heart-wrenching descriptions of the millions of people lacking security, adequate food, clean water, and basic health care and education. But as moving as this testimony may be, the reality is that the windfall of the current HIPC Initiative—a $28 billion debt-relief package administered by the International Monetary Fund (IMF) and the World Bank—does not go to the poor. Instead, it goes to the same governments that racked up the debt in the first
Getting Debt Relief Right

place, many of which are weak, corrupt, and authoritarian—hardly the best intermediaries to carry out a philanthropic agenda.

IN THE RED

During the late 1970s, many HIPC countries experienced a surge in the prices of their primary export commodities, such as oil, cocoa, tin, and coffee. Based on exceptionally strong export earnings, these countries borrowed from private banks and official export credit associations and then dramatically expanded government spending. But commodity prices quickly tumbled in the 1980s, and as a result, many HIPC countries suffered dramatic downturns in their terms of trade (the prices of exports relative to imports). Ethiopia, for example, suffered a 90 percent degradation in its terms of trade between 1980 and 1993, while Côte d’Ivoire’s terms of trade fell by nearly half. Meanwhile, a serious drought persisted in the Sahel, and high population growth continued across the board.

Under such circumstances, many HIPC countries had trouble paying their creditors, both foreign and domestic. Borrowers and lenders alike initially saw this setback as temporary; HIPC countries continued to borrow to make up the shortfall and stimulate economic growth based on optimistic predictions of recovering export prices. But even when it became clear that prices would not return to their previous highs, some countries were reluctant to cut government spending. They continued to borrow from other governments and multilateral institutions such as the IMF, the World Bank, and the African Development Bank. During the 1980s, long-term HIPC debt more than tripled before peaking in 1995. In 1997, 42 percent of this debt was owed to other governments, 22 percent to the World Bank and the IMF, and 10 percent to other multilateral institutions.

Still, the debt crisis might have been avoided if not for the bad economic policies and poor governance of many HIPC countries. Many of them maintained money-losing public enterprises, created government posts to provide employment, imposed artificially high exchange rates and formidable trade barriers, and unduly concentrated on the production of just a few commodities. Many HIPC governments, moreover, have been riddled with corruption.

FOREIGN AFFAIRS · September/October 2001 [37]
2000 survey, which ranks countries according to perceived corruption, 9 out of the 15 HIPCs included were ranked in the bottom quartile.

Although total losses due to high-level corruption are impossible to estimate, individual cases indicate losses in the millions and billions of dollars. Foreign creditors continued to lend to Zaire, for example, even while President Mobutu Sese Seko amassed a personal fortune estimated to be as much as $5 billion; to Côte d'Ivoire, even after President Félix Houphouët-Boigny built a basilica that cost an estimated $300 million of his "own money"; and to Kenya, even as government officials siphoned up to $1.1 billion from the national treasury and central bank.

Studies of petty corruption also present troubling results. A 1996 budget-tracking exercise in Uganda showed that in 1991, only 2 percent of nonwage public spending on education actually arrived at the schools; in 1995, only 20 percent did. Although the country has since addressed this problem, a contemporaneous study found that Ugandan health-care workers were stealing and selling 78 percent of drug supplies for their personal profit, dramatically reducing public health care for the poor.

What percentage of foreign aid is lost to such corruption? That is the wrong question to ask. Because money is fungible, aid dollars that are actually spent on social services can free up government money for other purposes. That is why so many people looked askance last year when Uganda concluded the purchase of a presidential jet within days of receiving HIPC debt relief. The only way to determine whether earmarked funds add to or substitute for government spending is to track all poverty-related spending and social-service provision. But according to a recent report by the IMF and the International Development Association (IDA), none of the HIPCs currently receiving debt relief are capable of doing so. These countries lack the practices and procedures necessary for budgeting, monitoring, and reporting on the use of public resources. More fundamentally, they lack basic institutions of accountability.

**BREAKING ALL THE RULES**

**Good budget execution** starts with a good budget. But many HIPCs are unable to formulate good budgets because they lack access to reliable information. In Uganda, for example, official figures indicate that primary school enrollment remained stagnant from 1991 to 1995,
even though it actually increased by 60 percent. Many HlPCs do not account for foreign aid that is controlled and spent by donors because the donors fail to provide them with the necessary information. And many HlPCs deliberately keep certain revenues off-budget.

This weakness in budgeting contributes to what the IMF/IDA report calls the “significant differences between planned and actual expenditures” in more than a third of the countries now receiving debt relief. What is budgeted is often not disbursed, and what is disbursed often does not arrive. Salaries go unpaid for months, operating funds do not materialize, and government debts remain unsettled. At the same time, the executive branch makes unbudgeted expenditures throughout the year. These loose practices make public spending data extremely spotty—and the data that does exist is often inaccurate or even falsified.

When making government purchases, moreover, HlPCs routinely violate the rules of public contracting. Officials award contracts to favored companies, despite laws requiring competitive bidding; manipulate bid criteria; violate the confidentiality of bid documents, which are not standardized; and privately negotiate the terms of contracts after the contracts are already awarded. As a result, these governments persistently purchase unnecessary, inappropriate, overpriced, or low-quality goods and services. Many HlPCs do not archive contract documents, making subsequent audits impossible. And complicated spending procedures prompt even well-intentioned officials to evade the rules.

HlPCs also fail to follow standard procedures of human-resource management. Recruitment is not transparent and does not correspond to actual staffing needs. Minimum qualifications for positions often do not exist, and where they do, they are not respected. Orders jump the official hierarchy, so that supervisors do not know what their subordinates are doing or to whom they are reporting. Bosses do not evaluate the performance of their employees, or they do so based on punctuality and dress rather than the quality and quantity of work. Promotions are given without regard to objective criteria, even where laws establish them. Records of work performance and of disciplinary sanctions are either incomplete or missing. Governments perpetually struggle with the problem of “ghost workers”—people collecting salaries without actually working for the government—and some HlPCs do not even know how many civil servants they have.
OUT OF CONTROL

In many HIPCs, procedures and laws are violated in part because systems of monitoring and sanction are either weak or nonexistent. In many government agencies, supervisors do not visit, and inspections are not performed. And without reliable means of communication and transportation, remote local administrative units become isolated, independent fiefdoms. Audit offices are typically understaffed, undertrained, and underfunded. According to the IMF/IDA report, only a third of the HIPCs currently receiving debt relief have active audit systems—and even these are ineffective. Many governments do not close their books at the end of the fiscal year, and some government units—particularly local ones—keep no books at all.

When government officials violate the law, justice systems often cannot hold them accountable. Police forces are untrained and unequipped, subject to political interference, and no match for sophisticated white-collar criminals. Judiciaries are weak, underfunded, and corrupt. Case files are heaped in dirty corners or kept in rooms open to the public, making them easy to lose or manipulate. Judges lack access to law books and even paper on which to write opinions. The application of laws varies from city to city, based on the availability of texts. The executive branch firmly controls judicial appointments and promotions and constantly interferes in the judicial process. Administrative law—the basis on which orders from the executive branch are challenged—is underdeveloped, and most citizens do not know that the government is subject to the law, even if just in theory.

To make matters worse, legislatures cannot hold the rest of the government accountable. According to the IMF/IDA report, audited accounts are forwarded to legislatures within 12 months of the end of the fiscal year in fewer than one-fifth of the HIPCs now receiving debt relief. And even when legislators do see the accounts, they usually do nothing about them. With few exceptions, legislatures are firmly controlled by the president’s party. Even those that strive to act independently are hampered by weak capacity. Many legislators are unable to read budgets, understand government documents, or draft legislation. Some cannot even communicate in the government’s official language. And many legislatures have only a few technical staff.
Finally, the ultimate guarantor of accountability—the electoral process—is either weak or nonexistent in many HIPCs. Of the 41 HIPCs, 11 do not hold multiparty democratic elections. Of the other 30, fewer than 10 have been able to vote governments out of office. As a consequence, most HIPC government officials do not fear losing an election if they fail to respond to the people’s needs. This lack of accountability plays out in the theft and waste of public resources, in routine torture and extrajudicial killings, and in the prevalence of government impunity.

**WATER IN A SIEVE**

The lack of procedures and institutions to ensure accountability is not simply a technical problem to be fixed with more money and more training. Rather, the root of the problem lies with the nature of governance itself. In many HIPCs, illegality permeates the highest levels of government, implicating presidents, ministers, legislators, and supreme court justices. These officials fill posts with cronies and pressure them to grant personal favors and remit money (often collected through bribes and embezzlement). This top-down pressure for illegal activity trickles down to all levels of government, creating hierarchies of wrongdoing.

At the same time, government officials protect themselves by deliberately destroying the fabric of accountability. It is misleading to say simply that systems of accountability are weak or nonexistent: rather, someone is actively weakening or neglecting them. People charged with maintaining records falsify or destroy them; people responsible for nominating judges choose those who are obedient rather than those who are independent and honest; people allocating resources underfund judiciaries and audit offices. In the absence of control, all types of abuses become possible, from petty corruption to human rights violations. When most of the government is corrupt, the government is unable to sanction its own members or reform itself.

Such corruption is fueled by the public’s demand for private goods rather than public policies, supporting a system of “patronage politics.” The very definition of corruption—the abuse of public office for private gain—assumes the existence of public purposes for which the office should be used. But in the HIPCs that were forged under colonialism,
M. A. Thomas

many citizens do not yet have a sense of belonging to a public larger than their families, villages, or clans. Familial roles and social obligations take precedence over formal roles and legal obligations, which do not carry the authority of either tradition or legitimate government. People look to the government as a collection of resources for private consumption, and those aspiring to public office must satisfy the demands of their constituents—the army, the civil service, or their own ethnic clans. If systems of planning, public resource management, and service delivery are exceptionally weak in HIPC governments, it is because the constituencies they serve do not demand public accountability or public services.

Despite all this, debt-relief advocates continue to press the international community to forgive HIPC debt in the name of the poor. One advocacy Web site states, for example, that “more than 18,000 children die each day because loan repayments to rich countries come before health care to the poor.” This statement assumes that high interest payments trade off with government spending on social services, and that low spending is the principal cause of poor service delivery. But in the case of some HIPCs, where the largest part of every dollar spent can “go missing,” bad governance—not low spending—is the immediate cause of poor service delivery. Increasing social spending will not necessarily improve service delivery because water cannot be carried in a sieve. Moreover, interest payments do not necessarily “crowd out” social spending; left to their own devices, HIPC governments would not necessarily use the funds now allocated to debt payments to tackle the problems of the poor. In fact, some HIPCs had no policy responses to poverty, AIDS, or corruption until they were required to develop them as conditions for debt relief under the HIPC Initiative.

Ensuring the proper use of debt-relief dollars requires HIPC governments not only to commit those funds to poverty-reducing programs but also to address the serious governance problems that hamper effective resource management and social-service delivery. The necessary reforms are deep and painful and unlikely to be taken voluntarily. Therefore, unless debt forgiveness is effectively conditioned on both the proper use of funds and the pursuit of structural reforms, it is unlikely to help the poor. Even worse, debt-relief funds may be used
Getting Debt Relief Right
to support activities that actually aggravate poverty, such as war. Or they may get illegally diverted by government officials, who protect themselves by further undermining institutions of accountability.

Although conditions alone cannot guarantee sustainable reform, they can establish new precedents, catalyze local constituencies for change, and open public dialogues about social and policy issues—provided that the conditions are well chosen and enforced. Unfortunately, the current political pressure for faster debt relief undermines the design and enforcement of such conditions.

FASTER, FASTER
Although public attention to debt relief peaked last year because of the Jubilee 2000 campaign, debt payments were already being rescheduled in the 1980s. And as the crisis deepened in the late 1980s and the 1990s, debt-relief efforts continued on increasingly concessional terms. In 1996, the IMF and the World Bank launched the HIPC Initiative, under which individual creditors pledged to reduce debt to sustainable levels. Three years later they introduced the Enhanced HIPC Initiative, which more than doubled the amount of relief to be provided. This expanded program had two objectives: to accelerate the delivery of debt relief and to link it more closely to poverty reduction. Unfortunately, pursuing the first goal has made the second one more difficult to achieve.

Under the Enhanced HIPC Initiative, countries seeking debt forgiveness are required to develop poverty-reduction strategies outlining specific goals and programs. HIPCs qualify for temporary debt relief (known as “passing the decision point”) after they have formulated interim poverty-reduction strategies; they receive permanent relief (known as “passing the completion point”) after they have “implemented a set of key, pre-defined social and structural reforms and maintained good macroeconomic performance.” No fixed date is set for the completion point, but the interim period is expected to last an average of 15 months.

This ambitious schedule leaves little time for HIPCs to effectively develop multisector poverty-reduction strategies. Because countries receive interim debt relief before they finalize their plans for some
sectors or even start to develop programs for others, they are unable to use the strategies to prioritize their spending for poverty reduction. As a result, they are unlikely to use their debt-relief dollars effectively. In the absence of good planning, for example, governments have strong incentives to spend on infrastructure, given the profitability of public contracting. But putting a hospital in every village and a court in every town is not necessarily the best way to improve the quality and quantity of health and judicial services, particularly where fundamental institutional problems remain unaddressed, local demand is unknown, and funds for staffing, operation, and maintenance are unavailable.

Under the Enhanced HIPC Initiative, moreover, the HIPCs themselves are responsible for managing debt-relief funds. They are also responsible for monitoring their own poverty-reducing spending, even though none of the HIPCs currently receiving debt relief is capable of doing so. The IMF/IDA report estimates that only two HIPCs—with the proper technical assistance—could be brought up to speed within a year; seven others could be ready within two years. Sixteen will require “substantial upgrading,” for which no time estimate is ventured. In other words, most HIPCs will not be able to report on their use of debt-relief funds before the end of the anticipated interim period. And after they pass the completion point and receive irrevocable debt relief, they will no longer have incentives to monitor and report on spending or to pursue reforms.

Nevertheless, some debt-relief advocates are pressuring the IMF and the World Bank to speed up their schedules. But accelerating interim debt relief will only further reduce the time available to develop meaningful poverty-reduction strategies, negotiate substantive conditions, implement monitoring mechanisms, and establish oversight institutions. By the same token, expediting permanent debt relief will reduce the number of reforms and the amount of benefits to the poor that can be monitored and assured. For some HIPCs, accelerating disbursements will serve no purpose, as they are already receiving money faster than they can spend it.

Unfortunately, both donors and recipients of debt relief have gotten the message that speed should take precedence over assuring benefits for the poor. The IMF and the World Bank initially envisioned that
countries would become eligible for debt relief only after they had established a three-year good track record. But this requirement has been subsumed by arbitrary numerical targets: in 2000, the two organizations announced that they would see 20 HIPC's pass the decision point by the end of the year. And instead of considering conditions that will provide the greatest benefits for the poor, some staff are now looking for conditions that can be easily satisfied in six months.

HIPC's are also aware of the political pressure for fast debt relief. Some governments—particularly those that are not reform-minded—may well predict that they can pass the completion point by simply making pro forma reforms and stalling for a few months. One HIPC that recently qualified for interim debt relief is already falling far behind schedule—even on easy, inexpensive measures. Very shortly, the international community will have to decide how serious it really is about tying debt relief to poverty reduction. But so far, no one has even discussed what will happen to countries that fail to meet conditions.

The indebtedness of the world’s poorest countries is untenable. A long-term response to the problem must involve changes to the system of international aid, including the curbing of lending to heavily indebted countries and the establishment of minimum accountability requirements for governments managing aid money. But fresh lending to HIPC governments continues today—even as they benefit from debt relief.

A short-term response to the problem must entail debt relief, whether or not it has any impact on poverty. After all, poverty reduction is just one reason for forgiving HIPC debt. But if debt relief is to help the poor, advocates must give HIPC governments enough time to develop credible spending plans before interim debt relief is granted. They must monitor the implementation of key reforms and the delivery of social services to the poor. They must allow more time for the poor to realize gains before debt relief is made irrevocable. And they must send early and consistent signals that countries will not pass the completion point unless they use their debt-relief dollars to help the poor and satisfy their reform commitments. Having demanded and obtained debt relief in the name of the poor, advocates have a special responsibility to make sure that the needy actually benefit from it. The hardest work is still ahead—and the poor are watching.