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From the Principal Private Secretary

30 March 1988

When you saw me this morning, you said that my Japanese colleague, Mr. Kitamura, would like to see the note on debt of poorest countries which our representative recently circulated at a meeting of the Paris Club.

I now have pleasure in enclosing a copy of this paper. You will see it takes the form of a note by Sir Geoffrey Littler, the Second Permanent Secretary at the Treasury.

I have spoken to Sir Geoffrey and to Mr. Peter Mountfield, an Under-Secretary in the Treasury, who is our representative at the Paris Club, and either would be willing to give you further information about the approach suggested in the paper if you cared to be in touch with them.

N.L. WICKS

Mr. Sezaki

DEBT OF THE POOREST COUNTRIES

(Note by Geoffrey Littler)

At our recent meeting in Val David I promised to circulate a note about ways in which we could ring-fence special treatment of Paris Club commercial debt of the poorest countries.

2. I think the main worry is that concessions for the poorest might spread to the middle-income debtors, or others who do not have anything like the same need, because they have the long-term potential to grow out of their debt problem. There is a second worry that concessions might weaken the pressure on debtors to undertake the urgent and necessary task of adjustment of their own domestic policies.

3. What we need is a framework of agreement among creditors which will provide a sufficiently robust basis of demarcation. I believe we could readily build such a framework on three key qualifications, all of which would have to be fulfilled:

- first: the scheme should benefit only the very poorest countries - which could conveniently be defined by reference to the 'IDA-only' criterion of per capita income of $425 or less at 1986 prices;

- second: the scheme should be confined to those countries regarded as 'debt-distressed' - which could be defined on the UK proposal of an interest/exports ratio of 15%, or the IBRD definition used in their Special Programme of Assistance in Africa;

- third: it should be a pre-requisite that beneficiaries were undertaking long-term structural reforms with appropriate Fund and Bank programmes.

4. There may of course be a few marginal cases - there are few perfect definitions in applied economics! - but I believe the criteria I have suggested are clear and potentially robust, and they cover the countries we would want to cover.

5. The modalities of a scheme should be constructed to reflect the need and the criteria:

- on the scale of interest abatement, to ensure reasonable burden-sharing I envisage something like a reduction of, say, three percentage points; other possibilities might include, say, halving of the interest rate charged by each creditor: this needs discussion;

- in order to link with conditionality, I would envisage annual agreements, or staging on the lines David Mulford has been exploring, or possibly packages in which new aid or credit would be withheld on disappointing performance: this also needs discussion.

6. Finally two comments on the problems for creditors:

- additionality: the UK is prepared to provide the limited proposed relief of interest as an addition to our planned aid programme; we hope others could do the same, but it is up to them;

- alternative methods: if legal and other impediments for some creditors prove insuperable, we would be willing to explore alternative ways of channelling funds to achieve the equivalent of direct interest-rate abatement, such as recycling of moratorium interest in the form of relending on something like IDA terms, provided this were genuinely additional to existing flows.

7. I hope to persuade Jean-Claude Trichet that it would be worth arranging discussion of these ideas in a small expert group at the time of the March Paris Club meeting.

(Geoffrey Littler)
3 March 1988