A NEW TOOL FOR DEBT MANAGEMENT

The debt crisis in its present proportions erupted in 1982 when Mexico, the world's largest Third World debtor, suspended its debt service payments. Reasons for the crisis can be traced back to the mid-1970s when a combination of macroeconomic shocks in the world economy, imprudent borrowing policies in the debtor countries, and imprudent lending by commercial banks, left many countries in the developing world unable to meet their loan obligations.

A resolution to the crisis was sought through a combination of policies, including debt forgiveness, debt reduction, debt rescheduling with varying degrees of concessionality, and structural adjustment programs negotiated with the World Bank and the International Monetary Fund (IMF). As part of this solution, developing countries were encouraged to improve their economic management capacity by establishing appropriate debt-management operations, as real interest rates rose, commodity prices fell and the world entered a recession.

The complexities of international debt management have plagued many Third World governments. Given the size and technical complexity of developing-country debt, the task of recording and organizing loans has proved beyond the capacity of many countries. This has led to massive confusion with respect to information and procedures regarding debt payment. One government, for example, incurred additional interest and penalty charges simply because the officer who was handling the payments was on leave and the instalment was late. Another government paid the same instalment twice. Yet another saved millions of dollars only after recognizing that a high-interest loan could be refinanced and replaced with one bearing a much lower interest rate.These particular examples are neither isolated nor hypothetical; they are indications of the often chaotic state of debt management and data collection in developing countries. Indeed, these instances illustrate the importance of proper loan administration and well-informed debt management — factors now recognized as critical in dealing with the current debt crisis. Effective debt management is the first in a multitude of steps toward surmounting the debt crisis.

In 1983, the Technical Assistance Group (TAG) of the Commonwealth Fund for Technical Cooperation (CFTC), Commonwealth Secretariat (CS), established a program of advisory services in external debt management. The objective of the program was twofold: to address the "information crisis" resulting from countries' inability to cope with the volume of data on external debt, and to provide a low-cost, microcomputer-based, user friendly system for the accurate recording and quick recall of debt-related data. At this point, TAG/CFTC turned to IDRC for technical and financial support for the development of the specialized software required to run this system, which is now known as the Commonwealth Secretariat Debt Recording and Management System (CS-DRMS).

Apart from assisting in the development of CS-DRMS, IDRC has also been active in disseminating and enhancing use of the system. These activities include the installation of the system in Sri Lanka on a pilot-project basis; cofinancing, with CFTC, the development and testing of training materials to help prepare staff in the use of the software; and assisting the Eastern Caribbean Central Bank (ECCB) to make CS-DRMS available to its eight member States.

To date, the system has been installed in 26 Commonwealth countries. These countries now have an overall legal and institutional framework to enable them to monitor the contracting, spending and repayment of loans. They can practice both "passive debt management" (e.g., they now know when payments are due) and more active management (e.g., the development of an effective borrowing policy to, inter alia, keep debt service costs to the minimum).

The CS-DRMS system has two basic advantages. It enables governments to develop the ability to make a payment on time, and to view their "payment profile" (the "bunching" of due payments) to assess whether a loan could be refinanced and paid off with one bearing lower interest. In fact, one government saved close to US $5 million in interest payments using this method on the basis of the data supplied by the system. Another government department recognized, after implementing the system, that it was owed money by other local bodies to which proceeds of a loan had been on-lent. CS-DRMS, therefore, notifies governments of who they owe money to, and who, in turn, owes them money.

It is important for Third World governments to consider such benefits in deciding to introduce a system like CS-DRMS. Clearly, there will be costs of time and money beyond those donated by IDRC, the CS, or any other donor. These costs, however, could be paid off by a single instance of interest savings or through an advantage gained in a loan negotiation.

Many of the benefits of CS-DRMS are as a result of the reports that it generates. The system generates nearly 100 different reports, which can be produced virtually at the push of a button. As well, an agency can produce its own original report(s). The system generates two very useful reports — one that states the payments due on a day-to-day basis over a 1-month period, and an "arrears report." Moreover, CS-DRMS produces reports specifically required by the World Bank and the IMF.

The fact that various international financial institutions require different reports has given many a developing-country official nightmares. Despite the difficulties involved in building and maintaining the data base, the potential benefits to be derived from the effective use of the system are tremendous.

The results of a recent survey indicate that governments have continued to use the system, at least to provide them with their reporting requirements, after it has been installed. However, its use in active debt management — to generate "what if" scenarios, for example — varies from case to case. Nevertheless, a number of governments have used the software for working out scenarios in preparation for Paris Club reschedulings. One of the limitations of the Commonwealth Secretariat's program, from a wider Third World perspective, is that the distribution and installation of the CS-DRMS software is confined to the 49-member Commonwealth, although it has been installed in Mozambique and Thailand through special arrangements.

Recently, this restriction was addressed in a joint project by IDRC and the Canadian International Development Agency (CIDA). This project aims to establish an in-house capability, in IDRC, to deliver a program of advisory services in debt management to non-Commonwealth countries, with a focus on the countries of Francophone Sub-Saharan Africa. IDRC has already conducted an in-depth survey, in conjunction with the United Nations Institute for Training and Research (UNITAR) and the French Ministry of Cooperation and Development, to determine the state-of-the-art with respect to debt management and to assess the needs of specific countries in Francophone Sub-Saharan Africa. The IDRC/CIDA project will also look into the feasibility of developing a French-language version of the software.

This initiative is, in fact, the Canadian government's response to one of the recommendations contained in the House of Commons External Affairs Standing Committee's report on the debt crisis. The Committee recognized IDRC's contribution in the Commonwealth program, but pointed to the need for an expanded Canadian contribution in the field of debt management. The IDRC/CIDA program is modelled on that of the Commonwealth and uses the CS-DRMS software, which has been made available to IDRC under a Distributor Agreement signed between IDRC and CFTC. The CS will, however, retain responsibility for not only maintenance but also for any enhancement in the software.

A basic tenet of IDRC is that research and related activities on developing-country issues should, where appropriate, be carried out in the South. In keeping with this philosophy, IDRC hopes that, perhaps during a second phase of the joint IDRC/CIDA project, up to three regional CS-DRMS resource centres could be eventually established to assume the task being executed by the in-house project.

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IMPLEMENTING A DEBT MANAGEMENT SYSTEM

Governments interested in implementing an effective debt-management system will likely need to keep the following steps in mind:

- A thorough **needs assessment study** should be carried out with regard to the country's internal capacity for external debt management.
- A **detailed plan for coordinated debt-information management** should be developed before the system is actually implemented. As well, problems of mandate, overlap, information flows, and data standards should also be resolved at this time.
- A **Debt Management Office (DMO)** should be established at an appropriate location to deal with the organizational arrangements for debt management. It is essential that the terms of reference of the DMO are drawn up and accepted by the government. These should be circulated within the adminstration and to all creditors. Staff with skills in loan operations and loan accounts, basic computer literacy, and knowledge and experience of loan instruments and capital markets should be recruited for the DMO if they are available in the country. It is also necessary to appoint a high-level Debt Policy Committee to provide guidance on borrowing and guarantee levels and the terms of such loans and establish ceilings for relevant debt indicators.
- **Training should be provided to the staff of the DMO in aspects of debt management** that are relevant to the needs of the country. The training will be staggered during project implementation and take place at different stages.
- A **well-defined legal and institutional framework** should be set up to monitor the contracting of loans, their utilization, and repayment. The framework will cover loans by the government, parastatals, and the private sector.
- Data requirements for a DRMS project should be set out and **administrative arrangements** made for their compilation. These will cover all aspects of loan operations including historical transactions for the period for which the government wishes to collect data. The information should cover the basic loan details and terms of repayment, which are available from loan agreements, and actual transactions covering loan disbursements and all debt-service payments. When a project is being implemented, an inventory of past loans should be built up and the data updated regularly.
- Once the data have been compiled, **facilities are necessary for their storage, retrieval, and analysis**. Projects may initially involve the establishment of a sound manual system with computerization introduced when this is fully operational. At this stage, appropriate microcomputers, the Xenix operating system that facilitates multiuser access, and the INFORMIX 4GL/SQL data base management system, need to be purchased for the installation of the CS-DRMS software.
- Once the system has been installed and the data have been compiled, planners can use the reports generated from the resulting data base on national external debt as a **decision-making support tool**.