Poverty Reduction and Economic Development

Report from G7 Finance Ministers

to the Heads of State and Government

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Poverty Reduction and Economic Development

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A. A Comprehensive Approach to Development

1. With the dramatic change in the world economy that has come as a result of the rapid progress in globalization, it is vital that the international community take action to ensure that developing countries have the opportunity to benefit from the forces of globalization and to play their role in the world economic system. It is a key objective to take a forward-looking approach in a strategic and intensive manner, in order to assist these countries in their efforts to attain sustained poverty reduction and economic development, and achieve the International Development Goal of a reduction by one half of the proportion of people living in extreme poverty by 2015.

2. Experience has shown the importance of sustainable growth as a necessary condition for poverty reduction. All development partners should focus on priorities that will bring about the robust growth necessary to meet the 2015 goals. These priorities should include achieving macroeconomic stability, encouraging private sector development, promoting good governance, investing in social development, accelerating trade liberalization, and strengthening financial sectors.

3. While growth is crucial in the fight against poverty, greater attention must be paid to a more equitable distribution of the benefits of growth. To this end, the right social policies are essential, including institution building, education and skills development, and the improvement of health including through the fight against infectious disease. These are the foundation for poverty alleviation and greater social equity. Social investment secures high returns over the longer term.

4. Combating global poverty requires a multi-dimensional approach. To achieve this, poor countries need to produce their own comprehensive Poverty Reduction Strategies, centered on the International Development Goals. These strategies will provide a vital link between social and economic policies needed to reduce poverty and increase growth. They should emphasize transparency, accountability, elimination of wasteful expenditure, and good governance. These strategies should also be developed through participatory processes involving civil society. The International Financial Institutions (IFIs) and bilateral donors should assist countries in developing and

implementing these strategies, including through technical assistance.

B. HIPC Debt Relief

5. For the heavily indebted poor countries (HIPCs), debt relief through the enhanced HIPC Initiative is a crucial part of establishing a virtuous circle of poverty reduction and economic development. Last year in Cologne, we agreed to launch the Initiative to deliver faster, broader, and deeper debt relief, releasing funds for poverty reduction. We welcome the endorsement of this initiative by the international community last autumn.

6. Since then, the implementation of the Initiative has begun. Nine countries have reached decision points and are receiving debt relief under the new framework which should total more than US$15 billion in nominal terms (US$8.6 billion in net present value). Up to eleven further countries could reach the decision points by the end of this year. Further details on the progress of the enhanced HIPC Initiative are set out in the attached annex.

7. We encourage those HIPCs that have not done so to embark quickly on the process by beginning to develop Poverty Reduction Strategies, in close cooperation with the World Bank and the IMF, and thus benefit from debt reduction. We will work together to ensure that as many countries as possible reach their decision point, in line with the targets set in Cologne, giving due consideration to the progress of economic reforms and the need to link debt relief to poverty reduction. In this respect, we are concerned by the fact that a number of HIPCs are currently involved in military conflicts, which prevent poverty reduction and delay debt relief. We call upon these countries to end their involvement in conflicts and to embark quickly upon the HIPC process. In that eventuality, we stand ready to strengthen our efforts to help them prepare and come forward for debt relief.

8. We encourage the World Bank and the IMF to continue to make efforts toward speedy and effective implementation of the Initiative. In this regard, we welcome the establishment in April of the new Joint Implementation Committee by the World Bank and the IMF, and urge the Committee to effectively facilitate the implementation of the HIPC Initiative and provide regular information on the status of individual countries.

9. We note the progress made in securing the required financing of the IFIs for effective implementation of the enhanced HIPC Initiative. We encourage

effective and timely participation of all multilateral and bilateral creditors, including non Paris Club members. Resources for the IMF and World Bank's share of the costs of debt relief have been identified and substantial contributions to the financing needs of other IFIs have been pledged. We urge MDBs' active engagement in the Initiative through the maximum use of internal resources. We welcome the recent progress made in putting together financing that will promote debt relief for HIPC countries in Latin America and Africa.

10. We reaffirm our commitment to make available as quickly as possible the resources we have pledged. In this context, we recognize the importance of fair burden sharing among creditors. We encourage new contributions by bilateral donors to the HIPC Trust Fund.

11. We reaffirm our commitment to bilateral debt reduction within the HIPC framework. In this respect, we have now committed ourselves to grant 100% debt forgiveness on our commercial claims eligible for treatment in the framework of the Paris Club. We welcome the announcement made by some other countries that they too will provide 100% debt forgiveness, and we urge other creditors to follow suit.

C. Going beyond Debt Relief

12. Official Development Assistance will continue to be crucial to support and encourage efforts for poverty reduction and economic development by poor countries. In this context, we welcome the recent reversal in the trend of declining aid levels. In order to ensure that those countries to which the Initiative is applied do not face again excessive debt burden, we have committed ourselves to extend ODA mostly in the form of grants for these countries.

13. Experience shows that economic assistance to countries with sound management raises growth and improves social conditions. Donors can play their part by directing aid more effectively to those poor countries that are serious about tackling economic reforms and poverty reduction. Donors should also improve the effectiveness of their support by coordinating their aid better in support of well-considered and recipient-led programs, and simplifying, and where feasible harmonizing, aid procedures.

14. In order to ensure responsible lending practices, it is vital that donors

reaffirm their commitment to discourage unproductive expenditure. In this context, we call upon the OECD to review through its export credit group strengthened measures toward ensuring that export credit support to HIPCs and other low income developing countries is not used for unproductive purposes. The result of this review should be published and could include the review of the relevant existing national rules and regulations. We encourage the OECD to complete this work as soon as possible. In addition, we welcome efforts by the IFIs and other donors to encourage poor countries to pursue sound debt management policies to ensure the productive use of resources.

15. Global public goods such as environment and health deserve priority attention and require strong involvement of the IFIs, in particular the World Bank and the regional development banks, and also by bilateral donors. To be effective, the involvement of the international community in global public goods should be built on the principles of comparative advantage and priority-setting.

D. Improved Trade and Investment Environment

16. In view of the close link between trade and investment growth and economic growth, trade and investment will play a critical role in promoting effective poverty reduction and sustainable economic growth. We must find ways to give HIPC and other low-income developing countries a stake in world trade and to improve access for these countries to international markets. We should ensure that the forthcoming WTO round actively promotes the interests of these countries, so that they too can benefit from trade liberalization. We should also promote regional cooperation among these countries in accordance with WTO rules, which often represent a welcome first step towards further integration in global economy. We call on the relevant international organizations, particularly the WTO and the World Bank, to strengthen their efforts to help build trade-related capacity in the poorest countries. We should also support the efforts of poor countries to create a welcoming environment for productive investment.

E. Faster Integration into the Global Economy

17. In view of the rapid progress of globalization and the IT revolution, it is important for developing countries including the poorest to harness the benefits of new advances in IT and prevent digital divide. It is crucial that

the international community emphasize capacity and institutional building including those related to IT, such as investment in human capital.

18. In the longer term, there will be a need to ensure that all developing countries have the ability to progress up the ladder of development. In many countries, domestic savings and private capital flows already play an important role in financing development. Putting in place the conditions for increased levels of stable forms of private financing and investment is key to achieve sustainable development.

19. While many developing countries will continue to be reliant on concessional aid flows for the foreseeable future, the IFIs should give some consideration to ways for these countries to participate in the global financial marketplace in the future. The objective must be to provide a "roadmap" to support developing countries make the journey from isolation to integration, growth and development.

ANNEX— The Heavily Indebted Poor Countries Initiative: Progress in Implementation

1. The enhanced HIPC Initiative launched at Cologne last year is aimed at providing faster, broader and deeper debt relief for the HIPC countries and at ensuring that the benefits of debt relief are used to reduce poverty. The link between debt relief, economic and social policy reforms and poverty reduction in the HIPC process is made through the development of comprehensive Poverty Reduction Strategy Papers (PRSPs). PRSPs are developed by the HIPC country itself, through a participatory process involving civil society and with the support of the International Financial Institutions and donors.

2. Nine countries (Benin, Bolivia, Burkina Faso, Honduras, Mauritania, Mozambique, Senegal, Tanzania, and Uganda) have reached their decision points under the enhanced initiative. For the nine countries, debt relief has been agreed that will provide savings of more than US$15 billion in nominal terms (US$8.6 billion in net present value). This represents, on average, a reduction in countries' stock of debt of about 45 per cent in addition to traditional debt relief mechanisms. This figure will be further increased by the reduction in Official Development Assistance (ODA) debt which we agreed at Cologne and by the commitment we have now made to grant 100 per cent debt forgiveness on eligible commercial debt owed to us by HIPCs which achieve debt reduction under the initiative.

3. Going forward, according to the latest IMF and World Bank estimates, up to eleven further countries could reach decision points before the end of this year (Cameroon, Chad, Cote d'lvoire, Guinea, Guinea-Bissau, Guyana, Malawi, Mali, Nicaragua, Rwanda and Zambia). This would bring total debt relief agreed under the HIPC initiative of around US$35 billion in nominal terms (around US$20 billion in net present value). Again this amount will be increased by the reduction in ODA debt and our commitment to grant 100 per cent debt forgiveness on eligible commercial debt.

4. The decision point for these countries will depend on their commitment to poverty reduction and economic growth, as demonstrated by their progress in developing poverty reduction strategies and their performance in relation to their IMF programmes. Progress in implementing these commitments would clearly be undermined by situations of armed conflict or significant political unrest.

5. There remain 20 HIPC countries. Of these:

- Four countries (Angola, Kenya, Vietnam and Yemen) are not expected to meet the indebtedness thresholds for the higher, enhanced HIPC debt reduction;

- Two countries have decided not to seek relief under the enhanced initiative (Ghana, Lao PDR);

- Two countries with IMF programmes are in the process of establishing the necessary track record. In the meantime, both countries are receiving traditional debt relief (Paris Club Naples Terms (67%)) in the context of their current IMF programme (Madagascar and Sao Tome and Principe);

- Twelve countries have not at present agreed programmes under the IMF's Poverty Reduction and Growth Facility, performance against which is necessary for decision point (Burun¥di, Central African Republic, Democratic Republic of Congo, Republic of Congo, Ethiopia, Liberia, Myanmar, Niger, Sierra Leone, Somalia, Sudan and Togo). The speed at which these countries can go forward to decision point will vary greatly. A few are close to embarking on the process. Ten countries are affected by conflict. Some are experiencing political unrest and macro economic instability. In such circumstances, many remain unable to commit to the HIPC framework which is intended to ensure that the resources made available through debt relief are used for poverty reduction within a policy framework directed to economic growth.