

AFRICAN DEVELOPMENT BANK



AFRICAN DEVELOPMENT FUND



**GUINEA BISSAU: EXTENSION OF THE INTERIM PERIOD
UNDER THE ENHANCED HIPC INITIATIVE**

INFORMATION NOTE ON THE EXTENSION OF THE INTERIM PERIOD FOR GUINEA BISSAU UNDER THE ENHANCED HIPC INITIATIVE

I. INTRODUCTION

1.1 The purpose of this document is to submit to the Boards of Directors of the Bank Group an Information Note on the extension of the interim period debt relief granted to Guinea Bissau in January 2006 under the HIPC Initiative. This Note is based on the Resolution of the Boards of Directors of the Bank Group on 29 June 2005 relating to the provision of additional interim period debt relief under the Enhanced HIPC Initiative¹.

1.2 Section 2 of this document summarizes the recent political and socio-economic developments in Guinea Bissau. Section 3 considers the extension of the interim period for the country as well as the financing modalities. Finally, Section 4 presents the conclusions of the Information Note.

II. RECENT POLITICAL AND SOIO-ECONOMIC DEVELOPMENTS

2.1 The Results-Based Country Strategy Paper (RBCSP) for Guinea Bissau, approved by the Boards of Directors of the Bank on 25 January 2006, gives a broad overview of recent political and socio-economic developments². This section will highlight the major socio-political and economic events which occurred in the country recently.

2.2 Guinea Bissau was marked by instability as well as political and military conflicts over the 1998-2003 period, which destroyed most of the country's economic infrastructure. However, after the peace agreements, the succession of transition regimes, with the support of the international community, culminated in parliamentary elections in May 2004 followed by presidential elections in May and June 2005. The new authorities sworn in after the elections have undertaken to implement the political, structural and economic reforms under the IMF staff-monitored programme adopted since March 2005. This programme should be converted into a post-conflict assistance programme in 2006 with the prospect of signing an economic programme supported by an IMF Poverty Reduction and Growth Facility (PRGF) towards the end of 2007.

2.3 As regards structural reforms, the Interim Poverty Reduction Strategy Paper (I-PRSP) was approved in December 2000, and the final PRSP was prepared in August 2004. On the basis of comments made by the IMF, World Bank and ADB, the Government prepared a revised version of the PRSP, as well as an action plan for 2006 and a three-year public investment programme for the 2006-2008 period. These documents are being adopted by the Government, and will be submitted to the Boards of Directors of the World Bank and IMF for a joint recommendation note for implementation of the development strategy that will be considered at a Donor Round Table scheduled for 2006.

¹Provision of Additional Interim Period Debt Relief under the Enhanced HIPC Initiative (ADB/BD/WP/2005/44-ADF/BD/WP/2005/49) of 27 May 2005.

² Guinea Bissau – Results-Based Country Strategy Paper – 2005-2009 (ADB/BD/WP/2005/ 78/Rev.2 - ADF/BD/WP/2005/82/Rev.2) of 8 December 2005 and RBCSP (ADB/BD/WP/2005/ 78/Add.1 - ADF/BD/WP/2005/82/Add.1) of 17 January 2006.

2.4 An analysis of the country's performance indicates that since the end of 2003, the Transition Government, and subsequently the Government formed following the parliamentary elections in May 2004, implemented an Emergency Economic Management Programme (PGEU) in 2004 with the assistance of the Bretton Woods institutions. There has been gradual improvement of the economic trend with the record production of cashew nuts. In view of the favourable agricultural conditions and exceptional levels of exports (93 000 tonnes of cashew nuts in 2004 as against 75 000 tonnes on average for the past three years), as well as the implementation of the PGEU, the real GDP growth rate was 2.2% in 2004, 2.3% in 2005 and projections for 2006 are 3.3%. The performance in public finance management during the staff-monitored programme should continue in 2006 thanks to pursuance of reforms under the staff-monitored programme.

2.5 The Country Strategy Paper (CSP 2005-2009) approved by the Boards of Directors of the Bank rests on two basic pillars, namely: (i) enhancement of good governance so as to increase the effectiveness of development policies and programmes for poverty reduction; and (ii) promotion of agriculture and rural sector growth in order to improve food security and the economic and social situation of people in rural areas. Through this strategy, the Bank intends to support the efforts of the new authorities in pursuing and intensifying structural reforms indispensable to economic recovery and achievement of the Millennium Development Goals (MDG) using the active portfolio and ADF X allocation amounting to UA 5.8 million. In this respect, an institutional capacity building programme for economic management was approved in 2005 by the Bank, and it is being launched. Similarly, the Bank intends to support public service reform, considered as priority by the authorities, in coordination with other development partners. Implementation of the development strategy for the private sector, which had also suffered during the country's instability, remains a priority for the Government. Revitalization of the private sector and its competitiveness will depend mainly on: (i) the rehabilitation of water, electricity and telecommunications infrastructure; (ii) the strengthening of production support services, including the port and airport; and (iii) development of the country's agricultural and fishery potential.

2.6 Three major challenges will face the country's economic and social development in the coming years. *The first challenge* concerns consolidation of the country's political and social stability over the medium term. The *second challenge* concerns institutional and human capacity building, which is a fundamental requirement for implementation of the PRSF and post-conflict assistance programme, in view of the current weaknesses of public administration. Lastly, *the third challenge* concerns sustainability of the country's debt, which depends on the success of the ongoing staff-monitored programme and subsequent implementation of the post-conflict assistance programme with the IMF. The success of this post-conflict programme and implementation of a PRGF-supported economic programme will, to a great extent, determine the waiting period of the HIPC Initiative completion point, which is fundamental to solving the problem of the country's debt sustainability. The Bank intends to support the authorities in reducing risks relating to these challenges by deepening economic policy dialogue with the authorities and satisfactorily implementing its active portfolio operations.

III. EXTENSION OF INTERIM RELIEF AND FINANCING CONDITIONS

3.1 The Boards of Directors will recall that Guinea Bissau reached its decision point under the HIPC Initiative in December 2000. Within this context, the Bank Group undertook to grant a debt relief estimated at US\$ 50.84 million, in Net Present Value (NPV) terms, to enable the country to reach its completion point not later than the end of December 2003. However, due mainly to instability of the socio-political situation during the 2000-2003 period, Guinea Bissau recorded is far behind schedule with respect to fulfilment of the conditions for reaching the completion point. Consequently, after a detailed review of the special circumstances arising from the successive governance problems in the country, the first extension of interim assistance was obtained for the 2004-2005 period.³ This extension, which took into account public finance cash flow problems and delays in the implementation of reforms to reach the completion point, made it possible to mobilize US\$ 6.96 million. Consequently, under the extension, it was proposed that the completion point be reached before the end of December 2005.

3.2 Despite this extension by the Bank Group, the country was placed under sanction in August 2005 for failure to repay the external debt service balance estimated at US\$ 450 102, which was the difference between the debt relief allocation approved under the HIPC Initiative and the effective debt service owed. Guinea Bissau could not reach its completion point the second time as scheduled. However, it should be noted that the country made satisfactory progress in reforms and good governance. In this respect, the new Government formed following the Presidential elections in June 2005 and the new authorities undertook to pursue the reforms. Accordingly, following consultations with the Bank Group, the above-mentioned arrears were quickly cleared in November 2005, thereby leading to the lifting of the related sanctions. The Results-Based Country Strategy Paper for the 2005-2009 period was approved by the Boards in January 2006.

3.3 In order to make a well-targeted contribution to poverty reduction efforts in Guinea Bissau, the Bank determined two areas of focus consistent with PRSP priorities and the Government Agenda for the 2004-2008 period (see paragraphs 2.5 and 2.6). Consequently, taking into account the second CSP pillar relating to the promotion of agriculture and rural sector growth, the Boards in January 2006 approved a project for a total amount of UA 5.8 million.⁴ Furthermore, in support of its selectivity-based strategy for operational activities in Guinea Bissau, the Bank Group recently awarded to the country a grant amounting to US\$ 500,000 as emergency humanitarian aid for cholera control.⁵

3.4 In view of the commitment and efforts made by the new authorities in pursuing and deepening the ongoing reforms, the Bank remains committed to intensifying its support to the country by granting it a second extension of the interim debt relief. This decision is based on consultations between the Bank Group and the HIPC Trust Fund aimed at enabling Guinea Bissau to reach the authorized maximum of 40% of the interim period under the HIPC Initiative financing mechanism. The support is consistent with the Board Resolution of 29 June 2005 relating to the extension by Management of the of the debt relief under the Initiative. Indeed, the

³ Guinea-Bissau: Extension of the Interim Period under the Enhanced HIPC Initiative (ADB/BD/WP/2004/ 58 - ADF/BD/WP/2004/61) of 18 May 2004.

⁴ See ADF/BD/WP/2005/74 – ADF/BD/WP/2005/74/Corr.1.

⁵ Document (ADB/WP/2006/07/Approved on 1 February 2006.

relevant resolution clearly defines the following four eligibility criteria for any HIPC member country which should have: (i) reached decision point and implemented reforms for at least three (3) years; (ii) exhausted the Interim Period debt relief approved at decision point; (iii) received less than forty (40) per cent of the total debt relief, in NPV terms, approved at decision point; and (iv) making significant progress towards reaching completion point as supported by evidence from the other multilateral Financial Institutions and the Bank Group's own assessment.

3.5 An analysis of these criteria supports Management's decision to grant an additional extension of the interim period to Guinea Bissau. Indeed, the country has been in the interim period since 2000, which satisfies the first criterion.⁶ Concerning criteria (ii) and (iii) above, it is important to stress that the resources allocated to the country for interim assistance were exhausted in July 2005, and the debt relief granted is lower than the authorized ceiling of 40% of the total debt relief. Indeed, as at the end of December 2005, the debt relief granted to Guinea Bissau was estimated at a total of US\$ 16.78 million, in Net Present Value (NPV) terms, which is 33.01% of the approved total debt relief. As for the fourth criterion, recent field missions of the Bank Group confirmed that the new authorities remain committed to pursuing reforms indispensable to the development of the country, as well as to implementing the staff-monitored programme with the IMF. Satisfactory progress has been made, as shown by the conclusions of the IMF technical assistance mission in July 2005 to the country. The mission emphasized the encouraging trend of enhanced transparency in public finance management.

3.6 In view of all these favourable trends and compliance with the eligibility criteria defined by the Boards, Management, after consultations with the Bretton Woods institutions, decided to extend the interim period for Guinea Bissau, following clearance of all its arrears in November 2005. This decision required the mobilization of an additional amount of US\$ 4.73 million from the Trust Fund as HIPC assistance to enable the country to reach the authorized ceiling of 40% approved by the Boards. These resources were effectively mobilized and placed at the disposal of the Bank Group by the HIPC Trust Fund in January 2006. Consequently, the debt relief programme for Guinea Bissau was revised with the assumption that the country will continue to benefit from an exceptional 100% reduction of its debt service to the Bank Group as from January 2006 until exhaustion of the above-mentioned mobilized resources.

3.7 The debt relief will increase total Bank assistance to Guinea Bissau from US\$ 16.78 million to US\$ 20.33 million, in Net Present Value terms, during the new interim period. This relief effort will enable Guinea Bissau to benefit from a 100 per cent reduction of its debt service obligations to the Bank Group from 1 January 2006 to 1 January 2007. Table 1 below gives details on conditions for the use of the mobilized resources in light of the future trend of debt service obligations.

⁶ For more information, see Guinea Bissau: Country Strategy Paper – 2005-2009 (ADB/BD/WP/2005/ 78/Rev.1 - ADF/BD/WP/2005/82/Rev.1) of 10 August 2005.

Table 1: Projections for HIPC Initiative Implementation*(In millions of dollars)*

Maturity Date	Estimate of Amounts Due*	HIPC Allocations	Balance after use of mobilized HIPC resources (4)	Resources to be mobilized by the country for 2007
(1)	(2)	(3)		(5)
1 Jan. 06	2 001 617	2 001 617	4 733 187	-
1 Apr. 06	66 051	66 051	2 731 570	-
1 July 06	1 975 268	1 975 268	2 665 519	-
1 Oct. 06	65 047	65 047	690 251	-
1 Jan. 07	1 977 527	625 204	625 204	1 352 323**
1 Apr. 07	95 118	-	-	95 118
1 July 07	1 964 606	-	-	1 964 606
1 Oct. 07	93 932	-	-	93 932
Total	8 239 166	4 733 187	3 505 979

Source: HIPC and Bank Group Database (16 December 2005).

* Debt service estimates are subject to changes and adjustments due mainly to exchange rate fluctuations.

** In column 5, the balance of 1,352,323 corresponds to the difference between 1 977 527 in column 2 and 625 204 in column 4.

The estimates in column 4 are derived from the series of calculations presented below:

- $2\,731\,570 = 4\,733\,187 - 2\,001\,617$
- $2\,665\,519 = 2\,731\,570 - 66\,051$

3.8 The Bank remains committed with the country's new authorities to ensuring mobilization of other additional resources from development partners to help Guinea Bissau cope with its debt service until achievement of the objectives of the Enhanced HIPC Initiative completion point scheduled for the end of 2007. The total amount of resources to be mobilized to repay all the amounts due in 2007 are estimated at US\$ 3.51 million. The next donor round table on Guinea Bissau, scheduled for 2006, will be decisive in mobilizing these resources which will be vital in preventing any risk of the country being placed under sanction, until exhaustion of the resources already mobilized from the HIPC Trust Fund.

IV. CONCLUSION

4.1 The Boards are invited to take note of the extension of Guinea Bissau's debt relief under the HIPC Initiative. This decision was required to support the quick resumption of critical and vital Bank Group operations in the country, and prevent the return of a cycle of accumulation of huge arrears. To that end, arrangements will be made with the new authorities of the country and with the support of the international community to guarantee sustainability of this approach, and enable the country to reach the completion point under the Initiative in 2007.

4.2 The achievement of this strategic objective would make Guinea Bissau eligible for the international initiative for cancelling the multilateral debt of countries which have reached the completion point under the HIPC Initiative. The deepening of debt relief will thus better help the country to achieve the Millennium Development Goals and benefit from additional resources depending on its performance as regards good policies. The donor round table scheduled for 2006 will be therefore be vital to guaranteeing achievement of these goals, implementation of structural reforms and the post-conflict assistance programme being negotiated with the IMF, the World Bank and the Bank Group.