AFRICAN DEVELOPMENT BANK GROUP

DIVERSIFYING THE BANK'S PRODUCTS TO PROVIDE ELIGIBLE ADF-ONLY COUNTRIES ACCESS TO THE ADB SOVEREIGN WINDOW

COSP DEPARTMENT

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SCCD: F.S.

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ACRONYMS

ADB	African Development Bank
ADF	African Development Fund
CPIA	Country Policy and Institutional Assessment
DSA	Debt Sustainability Assessment
DSF	Debt Sustainability Framework
FY	Financial Year
GDP	Gross Domestic Product
GNI	Gross National Income
HIPC	Highly-Indebted Poor Countries
IDA	International Development Association
IMF	International Monetary Fund
KPI	Key Performance Indicator
LIC	Low Income Country
MDB	Multilateral Development Bank
MDRI	Multilateral Debt Relief Initiative
NCB	Non-concessional Borrowing
NPV	Net Present Value
RMC	Regional Member Country
WB	World Bank

STRATEGY AND OPERATIONAL POLICIES DEPARTMENT

DIVERSIFYING THE BANK'S PRODUCTS BY PROVIDING ADF-ONLY COUNTRIES ACCESS TO THE ADB SOVEREIGN WINDOW

EXECUTIVE SUMMARY

Since the 1998 review of the Bank Group's Credit Policy, the macroeconomic performance of most low-income African countries has improved significantly. In particular, many African economies are now characterized by high economic growth, a stable macroeconomic environment and low or moderate risk of debt distress. This turnaround is the result of improved policies, a decade of impressive economic growth, reforms in public financial and debt management and the HIPC/MDRI initiatives. However, Africa needs to invest substantial resources in order to accelerate and sustain high rates of growth and transform the structure of its economies to generate much needed employment. These investments cannot be met by scarce concessional resources. As a result, several countries in Africa have started borrowing significant amounts of money on commercial terms during the past 5-6 years, at rates significantly higher than what the Bank could provide. The Bank Group's 2013-22 Strategy calls for additional financing and innovative instruments tailored to meet the needs of low-income African countries

In order to allow the Bank to respond proactively to the economic developments in RMCs over the past decade, it is proposed that eligible ADF countries be granted access to the ADB sovereign window, for financing viable projects. The private sector in ADF countries already has access to ADB financing and this proposal will allow governments to also access ADB resources, subject to a stringent set of criteria. The criteria, which will ensure that ADB resources do not contribute to an increase in debt distress, include: (i) the country must have a sustainable debt profile and be classified as having low or moderate risk of debt distress**,** as defined by an IMF Debt Sustainability Assessment (DSA), (ii) the country must have headroom for non-concessional borrowing, as determined by the IMF DSA, and in compliance with the IMF external debt limit policy for countries under fund-supported programs and the Bank Group Policy on Non-Concessional Debt Accumulation, (iii) the country must have a sustainable macroeconomic position, as determined by a Special Risk Assessment conducted by Management, and (iv) the country must receive a positive recommendation by the Bank's Credit Risk Committee, based on the Bank's elaborate risk management framework. Moreover, as is the case with all Bank financed projects, economic and social rates of return will be used, among other factors, to ensure that the projects maximize development impact. In partnership with other organizations, especially the IMF, the Bank intends to undertake additional analytical work on debt sustainability analysis and to scale up support to RMCs for project preparation as well as debt management, to ensure optimal implementation of this proposal.

This proposal will make the ADB sovereign window more responsive to the growing needs of ADF countries, which have seen their ADF allocations decline during the most recent replenishment, while at the same time helping the Bank diversify its client base and mitigate high concentration risk.

I. INTRODUCTION

1. The late 1980s and early 1990s were characterized by a debt crisis in many African countries. In April 1995, as a result of growing concerns regarding mounting loan arrears and poor creditworthiness in some countries, the Joint Steering Committee of the Bank Group's Board of Governors decided that "the Bank should, until further notice, apply the same credit eligibility criteria as the World Bank" (see Annex 1). Subsequently, in 1998, some member countries, concerned about the limited availability of development finance available to ADF-only countries requested the Bank Group to reconsider its credit eligibility criteria and develop its own Credit Policy as envisaged in Resolution B/BD/94/07/Rev.1. The Bank accordingly undertook a review, of its Credit Policy (see documents ADB/BD/WP/98/40 & ADF/BD/WP/98/33), but Management observed that a large number of RMCs were still carrying unsustainable external debt burdens and therefore were not good candidates to borrow on non-concessional terms. The review recommended that the Bank should maintain its existing credit policy, and periodically review it and amend it only when economic conditions and creditworthiness of RMCs improve in response to on-going structural economic reforms.

2. During the past decade, there has been a substantial improvement in the macroeconomic outlook and debt profile of a majority of African economies, as evidenced by higher growth rates, lower fiscal and balance of payments deficits, significantly improved debt indicators and growing accumulation of reserves. At the same time, the Bank Group's robust risk management framework has successfully lowered the Bank's portfolio risk profile and contributed to the Bank's financial strength. As a result, and together with shareholders' strong level of support through callable capital commitments, this has helped the Bank regain and maintain its AAA rating since 2003. However, at the same time as the continent's economic fundamentals have improved, there has emerged a growing mismatch between the Bank's financing capacity and its ability to respond to the needs of its low-income regional member countries. ADF-only countries, which face significant domestic political pressures to reduce their development deficit in order to create an economic environment that is able to absorb large pools of young school leavers, have to share a very limited pool of concessional resources to finance development expenditures and only 16 regional member countries can presently access the ADB non-concessional window for sovereign loans. Of the 16 countries, five countries dominate the Bank's ADB portfolio, resulting in a high concentration risk for the Bank. Some of these countries have also experienced rating downgrades in recent years due to their domestic economic and political environment. To provide low income regional members countries with increased access to financial resources as well as enable the Bank to diversify its client base, it is important for the Bank to review its instruments and ensure that they respond to the continent's evolving needs.

3. Management therefore proposes to grant ADF-only countries access to the ADB sovereign window under a specific set of criteria, discussed in Section III. This proposal is distinct from the normal "graduation" process, which is explained in Annex 2.

4. In line with the Bank Group's Strategy for 2013-22, the proposal will partially address the needs of eligible ADF countries for additional development funds, in addition to other sources of finance and will make the non-concessional window more relevant to eligible countries, without compromising the financial stability of the Bank[1]. It will also have a signaling and catalytic effect, while increasing the number of clients eligible for the Bank's non-concessional window and will improve the diversification of the Bank's portfolio, thereby mitigating the high concentration risk currently inherent in the Bank's portfolio.

5. The remainder of the document is organized as follows. Section II discusses the rationale for the proposal. Section III presents details of the proposal while issues relating to the smooth implementation of the proposal are outlined in Section IV. Section V concludes the document.

II. RATIONALE FOR THE PROPOSAL

6. Since the last review of the Bank Group's Credit Policy in 1998, the economic situation of most sub-Saharan African countries has changed fundamentally. Over the past decade, Africa's GDP grew on average by 4.7 percent a year. Excluding North Africa, part of which is in transition following the events in 2011, South Africa and other sub-Saharan middle income countries, the average growth rate in LICs increased to 7 percent over this period. This solid growth record has been supported by several factors, especially the improved macro and microeconomic policies adopted by African Governments, the favorable commodity prices which have benefited Africa's resource rich countries, and the debt relief initiatives provided to most highly-indebted poor countries.

7. The combination of strong growth, good macroeconomic management and debt relief have resulted in a sharp decline in the debt burdens for most sub-Saharan African economies during the last decade. As a result, the debt profile of ADF countries has changed profoundly. The external debt of ADF countries which averaged 90% of GDP in 1995 and 45% in 2005 fell to around 19% in 2012. Debt sustainability projections suggest that the medium-term debt outlook for sub-Saharan Africa is generally favorable. These projections indicate that average debt-to-GDP ratios are expected to edge up only marginally in the next five years relative to end-2012 levels[2].

8. However, in order to further accelerate and sustain growth and enhance the structural transformation of its economies, the continent needs to address a number of binding constraints, in particular infrastructure bottlenecks in low-income African countries. By addressing the infrastructure deficit alone, it is estimated that Africa's growth can increase by 2 percentage points per annum[3]. The vast financing needs, however, cannot be met only by scarce concessional resources. Hence, Africa must mobilize and leverage additional financing.

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[1] The timeliness of the proposal is also underscored by a call made by the African Governors of the World Bank Group and the International Monetary Fund during the 2013 African Caucus for the World Bank Group to 'Exercise flexibility by exploring modalities for expanding IBRD lending to IDA countries, for the purpose of structuring large-scale transformational projects with regional impact'.

[2] IMF : Regional Economic Outlook : Sub-Saharan Africa, May 2013

[3] AfDB Group & World Economic Forum : "Strategic Infrastructure in Africa: A business approach to project acceleration" May 2013

9. Many RMCs have already taken steps to access a menu of financing options. Some countries are proactively securing creditworthiness ratings from independent rating agencies, thereby signaling their economic strength. Consequently, at a time of quantitative easing by some OECD countries, this has facilitated their access to international markets for long term finance. Indeed, sub-Saharan African countries have borrowed in excess of US$11 billion on commercial terms since 2006. While these non-concessional resources have supplemented the concessional funding provided by the Bank and other development partners, they have been an expensive source of development finance in support of Africa's transformation agenda.

10. Recognizing these developments, the International Monetary Fund (IMF) introduced a Policy on External Debt Limits in 2009. The IMF Policy seeks to ensure that Fund-supported programs continue to help such countries strike the appropriate balance between debt sustainability and borrowing for productive investments that will support growth. The Policy aims to provide LICs with enhanced flexibility to tap non-concessional resources within a well-specified debt sustainability and macroeconomic framework. Annex 3 provides information on ADF countries that have recently accessed non-concessional financing under the IMF framework and the non-concessional borrowing limits that have been agreed with the IMF.

11. In 2011, the Bank Group amended its non-concessional debt accumulation policy to provide a more flexible and streamlined approach for ADF countries to contract and manage debt in a sustainable manner. The amendments were aligned with the changes in the IMF external debt limit policy and concessionality framework. The amendments aligned the Bank's policy with current practices in supporting LICs financing needs. For ADF-only countries with low risk of debt distress (green light countries, as per the Debt Sustainability Framework, see Annex 4), flexibility was applied to accommodate their non-concessional borrowing needs consistent with the assessment of their debt management capacity.

12. However, the Bank Group's Credit Policy, which was approved in the aftermath of the African debt crisis of the 1990s, has not been amended to reflect recent developments and the changes in LIC's financing patterns. Greater flexibility needs to be introduced in the Credit Policy to assist those ADF countries that are at low or moderate risk of debt distress to meet their development objectives while maintaining a sustainable debt position. At the same time, such access should not jeopardize the financial stability of the Bank. Non-concessional borrowing that is transparently contracted by RMCs with low or moderate-risk of debt distress and within the sustainable commercial debt limits agreed with the IMF, together with strong policies and institutions can complement – but not substitute – for limited concessional resources to finance projects with high development outcomes, in particular those which contribute to the structural transformation of their economies.

III. PROPOSAL TO GRANT ELIGIBLE ADF COUNTRIES ACCESS TO THE ADB SOVEREIGN WINDOW

13. All ADF countries will potentially be eligible for loans from the ADB sovereign window. However, eligibility does not guarantee access. ADF countries access to ADB sovereign resources, to finance viable projects, will be on a case by case basis. It will be granted subject to the fulfillment of the following criteria:

    i. **The country must be at low or moderate risk of debt distress,** as determined by a debt sustainability assessment (DSA) of the IMF. When such an assessment is not available for a particular country, the Bank will undertake a DSA using the agreed methodology of the IMF and discuss the outcome with the Government, the IMF and other relevant agencies.

    ii. **The country must have headroom for non-concessional borrowing,** as determined by a Debt Sustainability Assessment carried out by the IMF, and in compliance with the IMF external debt limit policy for countries under Fund-supported programs and the Bank Group's Policy on Non-Concessional Debt Accumulation. For eligible countries, the level of financing will be determined on the basis of this headroom analysis as well as the country's envelope for non-concessional borrowing as determined by the Bank's Sustainable Lending Limit (SLL). Under no circumstances will the financing exceed the country's SLL or its headroom for non-concessional borrowing, whichever is less.

    iii. **The country must have a sustainable macroeconomic position**. Only those ADF countries that have achieved and maintained a stable and sustainable macroeconomic stance, consistent with positive growth prospects, will be eligible to access financing. This will be determined on the basis on a Special Risk Assessment, as outlined in Annex 5.

    iv. **The country's request for financing must be approved by the Bank's Credit Risk Committee,** based on the country's risk assessment.

14. The proposal will:
    - Have a signaling and catalytic effect by acknowledging the good economic performance and growth prospects of eligible ADF-only countries. In particular, by providing these countries with access to ADB financing, the Bank will be able to crowd in additional private sector financing, thereby reducing their need to borrow on commercial terms, having a positive impact on their debt sustainability;
    - Respond to the findings of the African Development Bank Client Assessment and the Bank's Ten Year Strategy (2013-22) for more financing to be channeled to ADF countries and more relevant instruments to be tailored to their needs;
    - Enable the Bank to broaden its base of potential clients;

- Enhance the Bank's delivery capacity by improving the role of its non-concessional envelope in supporting the development agenda of the continent through sovereign instruments; and
- Help diversify the Bank's sovereign portfolio, minimize concentration risk within the portfolio and increase the Bank's footprint on the continent.

15. In meeting this objective, the Bank Group, its Management and staff will be guided by two principles:

- **Principle 1**: **Selectivity**. Under this proposal, only RMCs exclusively classified as category A by the Bank Group Credit Policy and at low to moderate risk of debt distress will have access to the non-concessional loans from the ADB sovereign window. The proposal does not impact the Bank's graduation process and nor does it imply a change of category status. Regular access of blend countries to the ADB window will continue to be governed by the existing Credit Policy[4].

- **Principle 2: Financial integrity.** The Bank will preserve the highest possible international credit rating in its class of Multinational Development Banks (MDBs). To this end, the Bank will maintain high standards of operational performance and financial prudence in line with the policies and processes of its Risk Management Framework.

IV. POLICY IMPLEMENTATION

16. In order to ensure smooth implementation of the proposal, the Bank will undertake to do the following:

17. **Special Risk Assessment.** The Risk Management Framework of the Bank Group will be the paramount screening tool to guide Management's decisions with regard to eligibility and loan amounts under the proposed financing. The Bank Group will conduct regular special risk assessments of potential beneficiary ADF countries. The risk assessment will cover, among other aspects, the country's macroeconomic performance and growth prospects, its absorptive capacity for additional financial resources over the medium term, its fiscal performance and outlook, and the country's debt sustainability profile. The capital adequacy framework and exposure management as well as the risk assessment will inform the Bank's Credit Risk Committee (CRC), in its central role in establishing country borrowing limits. The country exposure limits will continue to be used as a risk-based benchmark to plan the Bank's assistance. A Special Risk Note analyzing the fulfillment of the criteria spelled out in Paragraph 13 and presenting the outcome of the special risk assessment, will be submitted to the Board of Directors, along with the Project Appraisal Report, as part of the approval process for the project. Annex 5 presents the draft table of contents for the Special Risk Note on an eligible country.

[4] See annex 2 for a description of the graduation process framework

18. **Project selection.** In addition to the Special Risk Assessment, for each proposed transaction, the Bank will conduct an ex-ante evaluation of the project and/or program's viability and expected development outcomes, highlighting the economic rationale for the project/program and its contribution to inclusive and sustainable growth, while not jeopardizing the country's debt sustainability. In particular, the appraisal of such projects or programs will establish the economic viability of the proposed project/program, through the calculation of economic and social rates of return, in line with the Bank's established methodologies.

19. **Partnership.** In addition to the collaboration mentioned above on the determination of the countries' eligibility, the Bank will ascertain, as appropriate, whether its development partners, in particular the IMF and World Bank, as well as rating agencies, have any concerns about the adequacy of the country's economic policies and prospects.

20. **Capacity Building.** In order to help eligible ADF countries improve the management of growing external non-concessional resources, the Bank Group, in close collaboration with the IMF, World Bank and other relevant agencies, will ensure that countries receive appropriate advisory services and support for defining and implementing sound investment programs and mid-term debt strategies. In addition, the Bank will strengthen and leverage its internal skills to step up its engagement in the analysis of the IMF debt sustainability methodology, with a view to significantly contribute to improvements in the DSF over the medium to long term.

21. **Monitoring and Evaluation.** Bank-wide Key Performance Indicators (KPIs) will be reviewed and adjusted on a medium-term basis to provide benchmarks for monitoring and evaluation of the Bank Group's sovereign operations in support of eligible ADF countries.

22. **Policy Review.** Building on the principles that were already defined in the review of the Bank Group Credit Policy in 1998[5], the Bank will regularly revisit the implementation of this proposal to assess its relevance in light of the dynamic changes undergone by African economies. Within this context, a first evaluation of the implementation of this proposal will be conducted 3 years after its approval by the Board. The Bank will also continue to assess the need to align and revise other relevant policies and processes, in light of adjustments and reforms introduced by other international financial institutions that can impact the financing of its RMCs' development programs.

V. CONCLUSION AND RECOMMENDATION

23. **Conclusion:** This proposal reasserts (i) the Bank Group's recognition of the strong economic progress of African countries during the last decade, and (ii) the Bank's mandate to help sustain inclusive growth in its RMCs. The proposal reconciles the need to address the demand for resources to speed up the structural transformation of low-income African countries in a sustainable manner, RMCs' debt sustainability, as well as the Bank's financial stability.

24. **Recommendation:** The Boards of Directors are hereby requested to approve this proposal.

[5] ADB/BD/WP/98/40 – ADF/BD/WP/98/33

ANNEXES

ANNEXE.1 EVOLUTION OF THE BANK GROUP'S CREDIT POLICY

A1.1 In 1992, the Bank adopted the Country Exposure Policy, followed in 1993 with the establishment of the Exposure Monitoring Committee. In 1994, when adopting the Bank's lending program, the Board of Directors directed Management to develop creditworthiness guidelines that would guide the Bank in its lending to RMCs. However, since the Board of Directors were unable to reach consensus on a suitable Credit Policy based on Management's proposals, the matter was escalated to the Board of Governors pursuant to Article 29(1) of the Bank Agreement which, among other matters, empowers the Board of Governors to "issue general directives concerning the credit policy of the Bank". The Board of Governors in turn delegated the matter to the Joint Steering Committee of the Boards of Governors for consideration. At their meeting in Nairobi in May 1994, the Joint Steering Committee was unable to reach consensus on the matter. Accordingly, they met in Madrid in October 1994 and issued a "Joint Statement of Credit Policy" (see Document ADB/BG/SC/WP/94/03 on the meeting held in Madrid, Spain on 7 October 1994).

A1.2 Subsequent to this general directive from the Board of Governors, the Board of Directors could still not reach consensus when they considered the draft Credit Policy submitted to them by Management in Document ADB/BD/WP/94/104/Rev.1 and its corrigenda. Indeed, following their consideration of that proposal from Management, they adopted Resolution B/BD/94/07, but the classification criteria used in that Resolution was still not deemed satisfactory to all. As a result, the Board of Directors again referred the matter to the Board of Governors for their directives, pursuant to Article 29(1) of the Bank Agreement. The Board of Governors then convened a Consultative Committee in Washington, DC on 28 April 1995, which examined the issues impeding the adoption of the Credit Policy, and, notably, the negative impact this was having on the negotiations for the ADF-VII Replenishment. The Consultative Committee then directed that the Board of Directors should amend Resolutions B/BD/94/07, particularly, by inserting a provision requiring the Bank Group to "adopt the existing criteria used by the World Bank for [this purpose], until such a time as the ADB formulates a set of criteria more appropriate to its operations".

A1.3 It was as a result of this directive that the Board of Directors then adopted Resolution B/BD/94/07/Rev.1, the provisions of which, inter alia, resolved that "pending the formulation of its own system of country classification, the Bank adopts the criteria in use by the World Bank, and amends the system of eligibility developed in the annex to Resolution B/BD/94/07 on the Credit Policy of the Bank adopted on 21 November 1994", as well as makes the system effective from the date of adoption of Resolution B/BD/94/07/Rev.1.

A1.4 Accordingly, when the Bank Group reviewed its Credit Policy in Document ADB/BD/WP/98/40 – ADF/BD/WP/98/33 on 9 March 1998, it decided to "maintain its current Credit Policy which is identical to the World Bank's", but also to "continue to review and, if need be, amend the Credit Policy as the economic conditions and creditworthiness of RMCs improve in response to their on-going structural economic reforms".

ANNEX.2: THE GRADUATION PROCESS

A2.1 The Credit Policy determines each country's eligibility for ADF resources only (Category A), ADB resources only (Category C), or a blend of resources from the two windows (Category B, blend countries) on the basis of two criteria: the concept of relative poverty, as measured by GNI per capita below/above an agreed threshold (US$1,205 for FY14) and creditworthiness to sustain non-concessional financing.

A2.2 Graduation refers to the process by which an ADF-only country transitions to blend or to ADB-only status, or a blend country to ADB-only status. Reversal is the process by which an ADB-only or a blend country ceases to be creditworthy for non-concessional financing and/or its per capita income level drops below the threshold and needs readmission to ADF financing.

A2.3 ADF countries whose income per capita level has been above the operational cut-off for more than two consecutive years and who have been deemed creditworthy for non-concessional resources shall be reclassified as ADB-only. Blend countries whose income rises above the operational cut-off and subsequently stays at that level for 2 consecutive years will likewise be reclassified to ADB-only.

A2.4 Graduation from ADF is a flexible process that typically extends over several years.
The ultimate objective of ADF's graduation approach is to help countries make a successful and lasting exit from dependence on concessional resources and to avoid reversals back to ADF. Consequently, graduation is not driven by a mechanistic approach, but relies on careful case-by-case evaluations. The current process begins with a positive assessment of creditworthiness and reclassification of a country from ADF-only to blend ADB/ADF ("blend") status and concludes with a reclassification from blend status to ADB-only borrower with no further access to ADF resources. To smoothen the transition, a phasing-out/phasing-in period of appropriate length is determined on the basis of objective criteria, taking into account countries' needs for concessional funds. In the interim years, ADB and other market based sources of financing are phased in and ADF and other concessional assistance to the country in question are phased out. In line with the practice at other Multilateral Development Banks, phasing out normally takes place over a period of 2 to 5 years or 1 to 2 ADF cycles from the time that the country meets both the income and creditworthiness criteria. Based on the number of years of the transition period, the ADF allocation will be reduced and the access to ADB resources increased in a step-wise manner.

A2.5 For each graduating or reversing country, a tailored transition program is drawn up, defining the modalities of Bank Group support, in particular the financing mix during the transition period. Graduation normally gives a country access to a higher volume of ADB Group resources than it had before. Firstly, an SLL of ADB lending is nearly always a multiple of the country's ADF allocation. Secondly, the phasing-out and phasing-in schedule is designed in such a way that the sum of the percentages of the ADF and ADB resources is greater than 100% of the ADF resources alone.

ANNEX.3: AGREED CEILING WITH THE IMF ON NON-CONCESSIONAL EXTERNAL BORROWING BY RMCs

Country	Ceiling ($million)	Period	Observation
Ghana	3,400	2011	The 2011 ceiling on the contracting or guaranteeing of new non-concessional external debt (US$3,400 million) comprises the following two sub-ceilings: (i) a sub-ceiling for the oil and gas exploration and production projects in Ghana and to acquire equity stakes in companies undertaking oil and gas exploration and production in Ghana (US$1,250 million); and (ii) a sub-ceiling for any sector other than the oil and gas sector (US$2,150 million).
Kenya	1,500	2013-2014	The ceiling has been raised to incorporate possible new requests for guarantees in coming months and the possible issuance of a sovereign bond within the FY 2013/14 if market conditions justify it.
Mozambique	1,600	2009-2013	These loans are intended to finance only public infrastructure projects with a proven ability to generate financial and debt-servicing capacity, as evidenced in the summary description of the project. As of end-September 2012, NCB usage stands at $1,380 million
Rwanda	605	2012-2013	$400M was issued as Eurobond in April 2013. Half of the proceeds to repay unfavorable government-guaranteed loans for Rwandair and the Kigali Convention Center. The other half will be used to finance the completion of the Kigali Convention Center (US$150 million) in FY2013/14 and the Nyaborongo hydro-power plant (US$50 million) to increase electricity supply and reduce the cost of generation in Rwanda.
Senegal	800	2011-2014	A total ceiling of US$800 million applies

			over the period 2011–14 for non-concessional external debt financing to be used for investment projects, including in road infrastructure, the energy sector, and urban water and sanitation, and to reduce the recourse to regional market financing.
Tanzania	3,688	2013-2016	The borrowing plan is as follows: 2012/2013: $1.016 billion 2013/2014: $1.363 billion 2014/2015: $750M 2015/2016: $466M
Uganda	1,500	2013-2017	The envisaged non-concessional borrowing limit of US$1.5 billion is to finance key infrastructure projects—for which feasibility studies are already completed. (Isimba hydro power project, the Kampala-Mpigi highway, and the Kampala-Jinja highway project with non-concessional loans).
Zambia	970	2012-2017	The ceiling include the proceeds of the international sovereign bond ($ 750 million)

Source: ***IMF***

ANNEX.4 THE DEBT SUSTAINABLITY FRAMEWORK AND ADF COUNTRIES CLASSIFICATION

A4.1 1 The DSF analyzes both external and public sector debt. Given that loans to low-income countries vary considerably in their interest rates and length of repayment, the framework focuses on the present value (PV) of debt obligations. This ensures comparability over time and across countries.

A4.2 To assess debt sustainability, debt burden indicators are compared to indicative thresholds over a 20-year projection period. A debt-burden indicator that exceeds its indicative threshold suggests a risk of experiencing some form of debt distress. There are four ratings for the risk of external public debt distress:

- **low risk**, when all the debt burden indicators are well below the thresholds;
- **moderate risk**, when debt burden indicators are below the thresholds in the baseline scenario, but stress tests indicate that thresholds could be breached if there are external shocks or abrupt changes in macroeconomic policies;
- **high risk**, when the baseline scenario and stress tests indicate a protracted breach of debt or debt-service thresholds, but the country does not currently face any repayment difficulties; or
- **in debt distress**, when the country is already having repayment difficulties.

A4.3 Countries with significant vulnerabilities related to public domestic debt or private external debt, or both, are assigned an overall risk of debt distress that flags these risks. This assessment of overall debt vulnerability complements the rating on the risk of external public debt distress.

A4.4 Low-income countries with weaker policies and institutions tend to face repayment problems at lower levels of debt than countries with stronger policies and institutions. The DSF, therefore, classifies countries into one of three policy performance categories (strong, medium, and poor) using the World Bank's Country Policy and Institutional Assessment (CPIA) index, and uses different indicative thresholds for debt burdens depending on the performance category. Thresholds corresponding to strong policy performers are highest, indicating that in countries with good policies debt accumulation is less risky.

Debt Burden Thresholds under the DSF

	NPV of debt in percent of			**Debt service in percent of**	
	Exports	**GDP**	**Revenue**	**Exports**	**Revenue**
Weak Policy	100	30	200	15	18
Medium Policy	150	40	250	20	20
Strong Policy	200	50	300	25	22

ANNEX 5: CONTENTS FOR THE PROPOSED SPECIAL RISK NOTE

The Special Risk Note that will be prepared by management will evaluate the overall macroeconomic stance and risk profile of the country concerned. In order to determine if the overall macroeconomic stance is sustainable, the areas covered by the Special Risk Note will include an assessment of the structure of the economy and its growth prospects; fiscal and balance of payments outlook including vulnerability to shocks; debt sustainability including institutional capacity and track record in managing debt; the country's capacity to absorb additional debt; Bank's exposure to the country and the implications of additional lending to the country for the Bank's utilization of risk capital. A draft outline of the Special Risk Note is presented below.

INTRODUCTION

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