Proactive Release

Date: 9 July 2020

The following Cabinet paper and related Cabinet minute have been proactively released by the Minister of Foreign Affairs:

Contribution to the Multilateral Debt Relief Initiative

(CAB-20-MIN-260 refers)

Cabinet

Minute of Decision

Report of the Cabinet External Relations and Security Committee: Period Ended 5 June 2020

On 8 June 2020, Cabinet made the following decisions on the work of the Cabinet External Relations and Security Committee for the period ended 5 June 2020:

ERS-20-MIN-0011	**Contribution to the Multilateral Debt Relief Initiative** Portfolio: Foreign Affairs	CONFIRMED

Michael Webster
Secretary of the Cabinet

Cabinet External Relations and Security Committee

Minute of Decision

Contribution to the Multilateral Debt Relief Initiative

Portfolio **Foreign Affairs**

On 2 June 2020, the Cabinet External Relations and Security Committee:

1 **agreed** that New Zealand continue to support the World Bank's Multilateral Debt Relief Initiative (MDRI) at a total cost of NZ$41.94 million, by providing:

1.1 an unqualified (hard) expenditure commitment for 2021 to 2031, at an estimated aggregate cost of NZ$29.78 million; and

1.2 a qualified (soft) commitment to meeting New Zealand's share of MDRI costs over 2032 to 2044, at an estimated aggregate cost of NZ$12.16 million.

Janine Harvey
Committee Secretary

Present:
Rt Hon Jacinda Ardern
Rt Hon Winston Peters (Chair)
Hon Grant Robertson
Hon Andrew Little
Hon David Parker
Hon Stuart Nash

Officials present from:
Office of the Prime Minister
Officials Committee for ERS

Office of the Minister of Foreign Affairs

Chair, Cabinet External Relations and Security Committee (ERS)

Contribution to the Multilateral Debt Relief Initiative

Proposal

1. To seek Cabinet approval for New Zealand to continue contributing to the World Bank administered Multilateral Debt Relief Initiative (MDRI), at an estimated aggregate cost of NZD$41.94 million from 2021 to 2044.

Relation to Government Priorities

2. The Coalition Government has indicated strong support for multilateralism.

Executive summary

3. The MDRI provides for the cancellation of the debt owed to multilateral development banks (MDBs) by highly indebted poor countries (HIPCs). It is financed by donors, who compensate MDBs for the interest and principal payments on cancelled debt when such payments are otherwise due. This releases fiscal resources for HIPC development and poverty reduction efforts.

4. In 2006 I, as Minister of Foreign Affairs, and the then Minister of Finance approved New Zealand's participation in the MDRI, committing to contribute NZD$68.9 million through to 2044. The cost of the MDRI, which is re-estimated by the World Bank (WB) every three years, has since fallen. New Zealand's total contribution (from inception to 2044) is now estimated as NZD$62.86 million, of which NZD$20.92 million has been paid to date.

5. The WB now seeks refreshed commitments from donors. A formal authorisation of payments to 2031 and provisional commitment to pay for the period 2032 to 2044 is sought. Contributions to the MDRI, made annually, have been provided for in Vote ODA in the current (2018/19 – 2020/21) triennium. For subsequent years, contributions can be readily accommodated from the existing baseline for Vote ODA.

6. Overall, officials are satisfied with the implementation of MDRI and its future risk profile. There is no reason that would justify an exit from this initiative.

7. Accordingly this paper seeks Cabinet approval to recommit NZD$41.94 million for the MDRI, of which NZD$29.78 million is for payments from 2021 to 2031 (averaging NZD$2.71 million annually) and NZD$12.16 million is a provisional commitment over 2032 to 2044 (averaging NZD$1.01 million annually).

Background

8. New Zealand joined the WB and International Monetary Fund (IMF) sponsored MDRI at inception on 1 July 2006, committing to contribute NZD$68.9 million over the years 2007 to 2044.

9. The MDRI was an initiative of the Group of Eight (G8) large developed countries at their Gleneagles Summit in July 2005 in response to the Jubilee Debt Campaign and the Make Poverty History Campaign. The Initiative provides for the cancellation of debt owed to MDBs by HIPCs meeting pre-qualifying conditions in 2003. It was intended to free HIPCs from the financial burden of servicing pre-existing debt, thus releasing fiscal resources to accelerate their development and poverty reduction efforts.

10. In addition to pre-qualifying conditions, countries are required to meet performance criteria, assessed by the IMF and WB, to access the MDRI. These included adopting an IMF poverty reduction and growth programme, satisfactory progress in implementing the programme, and having a public expenditure management system meeting minimum governance and transparency standards.

11. The MDRI is financed by donors, who compensate MDBs for the interest and principal payments foregone on cancelled debt when such payments are otherwise due.[1] This ensures that MDBs are not financially weakened by the MDRI and can thus continue to support the poorest, most vulnerable countries.

Cost of the MDRI

12. At inception the cost of the MDRI was estimated to be USD$37 billion. The cost of the MDRI is revised every three years, and as at October 2019 has fallen to USD$32 billion. This fall reflects slower than expected qualification for the MDRI by some countries[2], exchange rate changes and interest rate reductions.

13. Accordingly, New Zealand's assessed contribution, at a fixed share of 0.13 percent[3], has also declined, from NZD$68.93 million at inception to an estimated NZD$62.86 million in October 2019.

14. In May 2006 I, as Minister of Foreign Affairs, and the then Minister of Finance approved New Zealand's participation in the MDRI. This involved a hard

[1] By leaving in place the original debt obligation the MDRI continues to remind governments of their prior debt situation. This is the reason for the long duration, to 2044, of the MDRI, corresponding to the longest maturity of the debt eligible for cancellation.

[2] HIPCs (highly indebted poor countries) eligible for MDRI but not yet qualifying are Eritrea, Somalia, South Sudan, Sudan and Zimbabwe. Somalia is expected to become eligible in 2020.

[3] This share is based on New Zealand's contribution as a proportion of the contributions of all donors to the World Bank's concessional assistance arm (IDA) at the time of MDRI inception.

(unqualified) commitment to make annual contributions to a total of NZD$14.6 million from 2007 to 2016 and a commitment in principle, or soft (qualified) commitment, to contribute a further NZD$54.29 million from 2017 to 2044.

15. Since then, New Zealand has periodically updated these commitments to reflect the revised MDRI cost for the upcoming period. Presently New Zealand has a hard commitment to 2022 and a reaffirmed soft commitment to 2044 (refer CAB Min (11) 15/6).

16. With the latest revision of MDRI costs the WB seeks an extension to 2031[4] of donor hard commitments. For New Zealand this means issuing two commitments totalling NZD$41.94 million: a hard commitment of NZD$29.78 million (covering 2021 – 2031); and a soft commitment of NZD$12.16 million (covering 2032 – 2044). To date New Zealand has paid NZD$20.92 million.

Comment

Impact and Risk

17. When it was established, the perceived risks associated with the MDRI and subsequent grant financing were that countries receiving grants might use the fiscal space created to borrow excessively from other financiers on expensive terms (thus threatening their debt sustainability). Or, perhaps, that they might deliberately borrow excessively in order to qualify for grant financing.

18. To counter such risks, the WB and other MDBs operating concessional funds put in place incentives discouraging such behaviour and to provide technical and policy assistance to improve debt management. These debt management policies align well with New Zealand views on managing debt sustainably.

19. Economic analysts have largely attributed faster growth rates among African developing countries (the main MDRI beneficiaries) since 2002 to debt relief (including the HIPC Initiative which preceded the MDRI). They note that, until recently, MDRI beneficiaries have avoided debt stress. The WB and IMF have also judged that MDRI beneficiaries are in large part making good use of the fiscal space created by the Initiative.

20. The rise in developing country debt in recent years, before the COVID-19 crisis, is not a consequence of the MDRI. Rather this is largely attributable to a combination of the fiscal stress caused by the decline in commodity prices over recent years and the attractiveness of borrowing while interest rates are at unprecedentedly low levels.

4 Setting the donor hard commitment for this period gives the WB and beneficiary countries more certainty over the financial flows associated with both MDB project financing and the MDRI.

21. As a consequence of the publicity surrounding increasing debt levels and pressure from the IMF and WB until recently, some African countries (such as Zambia) had been holding back on raising loans. At the same time the MDBs had been strengthening their policies on developing country debt.

22. More recently these actions have been overshadowed by the fiscal strains of dealing with the COVID-19 pandemic, which threatens debt sustainability. Given the severity of this crisis, it is crucial to maintain support for the MDRI so as not to worsen the position of poor countries through reversing the forgiveness of historical debt. A unilateral decision to do so would damage New Zealand's credibility in the multilateral system and wider global community.

23. New Zealand has been supportive of debt relief initiatives and the objective of freeing resources for development (as enshrined in the UN's Sustainable Development Goals). New Zealand is currently committed to contribute to the MDRI to 2022 and has repeatedly affirmed its soft commitments to support the Initiative through to 2044. Overall my officials assess that the risk environment for MDRI remains satisfactory. There is no major change in the MDRI environment or impact that would justify New Zealand's exit from the Initiative.

Governance

24. New Zealand is satisfied with the implementation of the MDRI to date. Periodic reviews by donors are backed up by implementation oversight by the WB and IMF boards of directors.

Financial Implications

25. Cabinet agreement to contribute to the MDRI will have no impact on the operating balance or on debt. The expenditure on MDRI will be met from within existing baselines of Vote ODA Non-Departmental Other Expense – International Development Cooperation (Multi-Year Appropriation). Contributions to the MDRI, made annually, will be recognised when paid.

Legislative Implications

26. There are no legislative implications.

Impact Analysis

Regulatory Impact Statement

27. Not required.

Climate Implications of Policy Assessment

28. Not required.

Population Implications

29. There are no direct gender or disability implications.

Human Rights

30. There are no Human Rights Act (1993) or New Zealand Bill of Rights Act (1990) implications.

Consultation

31. The Treasury was consulted in the preparation of this paper and agrees with its recommendations.

Communications

32. Media interest on New Zealand's contribution to the MDRI is not anticipated. Officials will work with the Office of the Minister of Foreign Affairs to manage any interest that may arise.

Proactive Release

33. This Cabinet paper will be proactively released.

Recommendations

34. The Minister of Foreign Affairs recommends that the Committee:

- **Agree** that New Zealand continue to support the World Bank's Multilateral Debt Relief Initiative (MDRI) at a total cost of NZD$41.94 million, by providing:

  (a) an unqualified (hard) expenditure commitment for 2021 to 2031, at an estimated aggregate cost of NZ$29.78 million; and

  (b) a qualified (soft) commitment to meeting New Zealand's share of MDRI costs over 2032 to 2044, at an estimated aggregate cost of NZ$12.16 million.

Rt Hon Winston Peters

Minister of Foreign Affairs