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Improving transparency of lending to sovereign governments

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Key messages

- Transparency of debt terms and conditions is a prerequisite to responsible borrowing and lending, and crucial to effective policy decision-making and risk management.
- While sovereign borrowers bear primary responsibility for reporting public debt data, creditors must also contribute to ensure that lending is transparent. This is recognised in two creditor-driven initiatives: the 'G20 operational guidelines for sustainable financing' (2017) and the Institute for International Finance 'Voluntary principles for debt transparency' (2019).
- The effectiveness of the Guidelines and Principles is undermined, however, by a lack of practical guidance for implementing them and monitoring compliance by debtors and creditors.
- Crucial to putting the Guidelines and Principles into practice will be the inclusion of exceptions to non-disclosure provisions in debt contracts, allowing the parties to comply with them by disclosing key terms and conditions irrespective of confidentiality clauses. This could be enhanced by the addition of a disclosure annex.
- Because of the voluntary nature of the Guidelines and Principles, incentivising compliance is crucial. This can be done by actively monitoring and publicising those lenders that comply with them.

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Acronyms

DSA debt sustainability analysis
EITI Extractive Industries Transparency Initiative
EMBI Emerging Market Bond Index
G20 Group of 20 most industrialised nations
IATI International Aid Transparency Initiative
IBRD International Bank for Reconstruction and Development
IDA International Development Association
IFI international financial institution
IIF Institute of International Finance
IMF International Monetary Fund
LPN loan participation note
MAM Mozambique Asset Management Company
MDB multilateral development bank
OECD Organisation for Economic Co-operation and Development
PRGT Poverty Reduction and Growth Trust
SOE state-owned enterprise
UNCTAD United Nations Conference on Trade and Development

1 Introduction

Transparency of the debts owed by governments and the guarantees they have given is an important issue for the international community. The increasing risk of debt distress in many of the world's poorest countries, coupled with several recent cases of inadequate disclosure that put macroeconomic stability at risk, have highlighted the urgent need to make lending to governments more open, particularly the terms and conditions.

The underlying assumption is that more disaggregated information on public debt will enable borrowers and lenders to make more responsible borrowing and lending decisions, ultimately making a debt crisis less likely. Better-quality data can also directly impact sovereign ratings and, by extension, lower borrowing costs. Furthermore, civil society and parliaments require access to the right information in a timely manner to hold governments to account, thus facilitating good governance and aiding the fight against corruption and mismanagement. When debts are hidden, the discovery of the potential misuse of borrowed funds can lead to a country losing market access and/or being cut off from donor funding. This can trigger an economic crisis and bring about a sovereign default – an event that is generally painful for all stakeholders.

Debt transparency is also critical for sound policy decision-making and effective risk management in the context of the Covid-19 pandemic. The risk of debt distress needs to be closely monitored during these uncertain times, given the considerable pressures on governments to spend more and the various shocks to countries' capacity to service their debts. The international community, therefore, requires a firm grasp of the debt numbers, as well as the characteristics of that debt, if it is to provide timely and appropriate support and avoid a debt crisis in some of the poorest, most vulnerable countries. In addition, countries seeking to access debt-relief initiatives, such as the G20 time-bound suspension of debt service payments, must commit to disclose all public sector financial commitments (debt). This is primarily to ensure that creditors are sharing the burden fairly and to prevent the over-accumulation of new non-concessional debt (with some exceptions) during the suspension period.

The international financial community has actively sought to build the capacity of sovereign borrowers to record, monitor and report debt data. While some countries have improved their debt-recording, monitoring and reporting capacity over the last decade, recent cases of hidden public debt highlight that much more needs to be done (World Bank and IMF, 2018).

- In the Republic of the Congo, the state-owned oil company entered pre-financing contracts with oil traders on behalf of the government, but these were not reported in official debt statistics.
- In Ecuador, liabilities including advance oil sales and short-term treasury certificates, worth about 9% of gross domestic product, also went unreported in official debt data.
- In Mozambique, loans to two state-owned enterprises (SOEs) were fully guaranteed by the state, but not included in estimates of the public debt stock.

However, while the sovereign borrower bears primary responsibility for reporting public debt data, international financial institutions (IFIs) and creditors can also play an important role in supporting transparency. Several public-sector initiatives have promoted transparency in sovereign debt markets, including the Organisation for Economic Co-operation and Development's (OECD) sustainable lending principles for official export credits (2008; 2018) and the United Nations Conference on Trade and Development (UNCTAD) 'Principles on

promoting responsible sovereign lending and borrowing' (2012). The G20 countries endorsed the 'G20 operational guidelines for sustainable financing' in 2017 (G20, 2017), which include enhanced information sharing and transparency of official bilateral lending to lower-income countries. More recently, the Institute of International Finance (IIF), a global industry association for the world's largest financial institutions, proposed the 'Voluntary principles for debt transparency' (IIF, 2019). This is intended to improve the transparency of private-sector transactions with lower-income countries. These voluntary initiatives, though a step in the right direction, will not lead to fully transparent accounting of public-sector borrowing for reasons we explain in this paper.

The objective of the paper is to provide readers with an understanding of how existing creditor-driven initiatives to improve the transparency of official bilateral and private-sector lending can be strengthened and effectively put into practice. We focus on the Guidelines and Principles of the G20 and IIF because of the significant disclosure gaps involved in the two types of lending.

The rest of the paper is structured around the following four questions. Chapter 2 answers what are the potential benefits of debt transparency to various stakeholders. Chapter 3 examines how transparent are different types of debt financing. Chapter 4 looks at what creditors are doing to improve transparency. Chapter 5 recommends how these creditor-driven initiatives can be improved so that the benefits of transparency are realised. While more transparent debt data will not, in and of itself, prevent the build-up of an unsustainable debt burden, it can help to minimise the risk of debt crises and to take timely remedial action when they occur. Section 6 concludes with our key take-away messages and recommendations.

2 Transparency for what?

Debt transparency plays a critical role in ensuring good lending and borrowing practices. Transparency can be understood as making information publicly available, so that it is accessible to interested stakeholders and the wider public. However, the type of information matters. Reporting aggregate numbers without a detailed breakdown means that users will be unable to ascertain whether specific loans are included in the total debt figures reported by the government in question. In addition to potentially 'hidden' debt, insufficient information on the terms and conditions of borrowing can also undermine responsible borrowing and lending practices (IMF and World Bank, 2018). In the rest of this section, we focus on the importance of disclosing the specific terms and conditions of government financing, including the use of government guarantees. This includes, but is not limited to, the amount of the financing, fees, charges and interest, the intended use of proceeds, the payment schedule and collateral requirements.

First, transparency benefits citizens by giving them the information they need to hold their government accountable. However, more information in the public domain does not automatically lead to citizen engagement and accountability. It requires civic interest and institutions or groups with the capacity and space to scrutinise what the government does. The type of information provided and the level of complexity are also important. Meaningful civic engagement requires access to information of far greater granularity than what is typically published in the national budget or in consolidated debt reports. For instance, what is a specific loan intended to finance? What are the costs of the loan (interest rate and any other fees)? How quickly does it have to be repaid and are there any triggers for early repayment? What is the penalty for not repaying the loan? The more the public can answer such questions from publicly available data, the more likely it will be that debt transparency can serve its purpose of allowing independent analysis and enabling greater public participation in policy processes. This type of public scrutiny may also help deter corrupt and fraudulent deals among government officials and lenders by increasing the likelihood of detection.

While this type of transparency does not exist in the world of corporate finance, a strong case can be made for public debt. This is because governments have a fiduciary duty to taxpayers, who bear the ultimate burden of repaying the sovereign's debt. Moreover, non-transparent borrowing can adversely impact the lives of citizens, as illustrated by the aforementioned Mozambican debt scandal, which involved commercial bank lending to three SOEs. As described in Box 1, two of the loans were undisclosed, while the guarantee of the third was a controversial matter. The discovery of this 'hidden debt' caused the country's economic growth to plummet and donors to freeze funding, forcing the government to make deep cuts in public spending.

Second, creditors and donors also require accurate and comprehensive information on a borrower's debt profile to make informed decisions when extending financial support. Several creditors use the IMF's formal framework for conducting public and external debt sustainability analyses (DSAs) to assess a country's capacity to repay its debts and to flag any potential fiscal issues (e.g. debt sustainability, defaults) the borrowing country may face in future. One of the key data inputs into this analysis are financing terms (namely, principal, interest rate, currency and maturity). Making informed lending decisions are challenging if creditors are unaware of large parts of a country's debt and the financial terms of that debt.

Third, from a private-investor perspective, transparency is crucial for properly pricing

Box 1 Mozambique's hidden debt

Mozambique's debt scandal stemmed from three loans incurred by different state-owned enterprises (SOEs), guaranteed by the central government. The loans were arranged by the banks, VTB and Credit Suisse, and included the following financing arrangements:

- a $622 million loan to Proindicus to perform coastal surveillance
- a $535 million loan to the Mozambique Asset Management Company (MAM) to build and maintain shipyards
- a $850 million loan to Ematum to build a tuna fishing fleet.

Of the three loans, only that granted to Ematum was publicly disclosed. It was later converted into loan participation notes (LPNs), which were traded on the open market. These Ematum LPNs were, in turn, legally extinguished in April 2016 through an exchange of the notes for $727 million of sovereign Eurobonds issued by the Government of Mozambique, which resulted in an entirely new legal obligation (novation). The Ematum LPNs had been discussed in various IMF country reports, been included in Mozambique's public debt statistics, and were publicly traded and included in JP Morgan's Emerging Market Bond Index (EMBI). Moreover, the subsequent Eurobonds (which extinguished and replaced the LPNs), were a legally distinct obligation, fully disclosed to the Mozambique citizenry and approved by the National Assembly, in accordance with the country's constitution and budgetary law.

In contrast, the Proindicus and MAM loans to acquire military equipment for the security services and the Ministry of Defence were not publicly disclosed or agreed by the Mozambique parliament. These loans were revealed to IMF staff in April–June 2016, triggering an economic crisis which brought about a default on all external commercial debt. An independent external audit of the loans highlighted inadequacies in the process for incurring the loans and particularly in granting of the government guarantees as well as a lack of transparency regarding the use of the loan proceeds.

Source: Olivares-Caminal (2019); IMF and World Bank (2018)

sovereign finance and the associated default risk. If investors are uncertain about the terms and conditions of a substantial portion of a country's total debt, they are likely to adopt a prudent approach by increasing risk premia, thereby raising the sovereign's borrowing costs. In this regard, numerous studies provide evidence of the measurable financial benefits of fiscal transparency. Kemoe and Zhan (2018) show that fiscal transparency lowers the costs of borrowing to the sovereign and increases foreign demand for sovereign debt in emerging-market and developing countries. Choi and Hashimoto (2017) find that data transparency leads to a 15% decline in the EMBI spread a year after such reforms are carried out. Arbatli and Escolano (2012) find that fiscal transparency has positive and significant effects on countries' credit ratings. Gelos and Wei (2005) provide evidence that emerging-market funds systematically invest less in less transparent countries. While these studies use broad measures of fiscal transparency, they suggest that a sovereign borrower that willingly discloses the terms and conditions of its borrowing is likely to enjoy a higher level of trust and confidence among investors, leading to lower borrowing costs.

Fourth, the IMF requires reliable and comprehensive debt data to detect, prevent and resolve debt crises. An important part of IMF surveillance involves conducting the aforementioned DSA to assess a country's risk of debt distress (in other words, the likelihood that a country will experience difficulties in repaying its debt) and recommend actions for mitigating vulnerabilities. When it comes to the latter, the results of the DSA inform the design of adjustment programmes, including limits on accumulating new debt. Moreover, the recently revised debt sustainability framework (IMF, 2018) highlights

the importance of knowing the purpose of borrowing in order to assess whether borrowing is being used for productive investments and whether it will potentially lead to lower debt ratios over time via higher growth, revenue and exports. Given that a DSA is only as good as the underlying data used, insufficient or inaccurate information on the terms and conditions of a country's debt portfolio is likely to impair the quality of the IMF's analysis and advice.

Lastly, insufficient information on the terms and conditions is a problem when it comes to crisis resolution. In case of default, comprehensive information on a country's debt portfolio is required to assure fair burden sharing and an orderly process to manage and exit the crisis. Uncertainties about collateralisation arrangements, whereby the provision of finance is secured against either future commodity exports or specific project revenues, can complicate the overall resolution process. This is because it grants a specific creditor preferential rights over specific assets or future flows of funds, undermining the positions of other creditors and limiting a debtor's ability to defer paying creditors with collateral in a restructuring event. This complexity was demonstrated in the recent crisis in Chad and the Republic of the Congo (Bredenkamp et al., 2020). None of the international debt databases collects information on the collateralisation features of loans.

While debt transparency is important as a public good, economic actors may have legitimate reasons to preserve the confidentiality of market-sensitive information. Confidentiality may even be in the public interest in some cases. Examples of sensitive material information include contracts entered into for the purposes of hedging risks or those involving national security issues. Premature disclosure of information may adversely affect market sentiment as well as the economy. At the same time, the UNCTAD (2019) recommends that any delay in disclosing potentially sensitive information should be only for the amount of time necessary to further the underlying policy objective and should be clearly authorised, with the reason for the delay stated. Ultimately, demands for greater transparency need to be carefully balanced against the need to protect sensitive information.

3 How transparent are different types of debt financing?

Public debt is an important source of financing for sovereign governments. The rapidly evolving financing landscape means sovereign borrowers have more choice than they did two decades ago. In light of the benefits of transparency highlighted in the previous section, this section assesses the transparency of the terms and conditions of the three main categories of debt financing currently available to sovereigns:

1. multilateral lending is financing provided by international institutions, such as the IMF and World Bank, including regional development banks
2. bilateral sovereign lending is financing provided by governments (or governmental agencies) to other governments (or governmental agencies)
3. private-sector lending is financing mainly in the form of commercial bank loans or bonds issued in capital markets.

3.1 Multilateral lending

The transparency of multilateral lending is generally not seen as problematic due to the high degree of accountability and scrutiny imposed on multilateral lenders by their own internal policies and procedures. In a 2018 survey of 25 multilateral development banks (MDBs), 16 had policies on public communication or disclosure (Engen and Prizzon, 2018). Many of the traditional global and regional MDBs are also registered with the International Aid Transparency Initiative (IATI) and provide detailed financial and non-financial information on projects. Multilateral lenders (specifically, the Asian Development Bank, the African Development Bank, the World Bank International Development Association (IDA) and the Inter-American Development Bank) also tend to top the Aid Transparency Index, outperforming bilateral sovereign lenders (Publish What You Fund, 2018). One of the indicators of aid transparency assessed in this index relates to the publication of loan repayment conditions or special terms and conditions.

The terms and conditions of the largest MDBs tend to be publicly available, with fairly standardised terms for specific groups of countries, based on a transparent set of criteria. The World Bank's lending terms, for example, depend on whether a country is classified as an IDA, International Bank for Reconstruction and Development (IBRD) or 'Blend' country. Similarly, the African Development Bank Group and Asian Development Bank offer differentiated financing terms to specific groups of countries.

3.2 Bilateral sovereign lending

Bilateral sovereign lending presents serious concerns from a transparency standpoint. Bilateral loans are negotiated at governmental level and, in some instances, their purpose may be geopolitical. As a result, they are not always fully disclosed to the public or IFIs, such as the IMF.

In sovereign bilateral lending, it is also important to distinguish who grants the loan, for example, Paris Club or non-Paris Club bilateral lenders. The former is an informal group of 22 permanent sovereign lenders, hosted by the French Treasury, which aims to

coordinate solutions to the payment difficulties experienced by debtor countries. Paris Club renegotiations are based on a number of clearly defined terms and principles, such as solidarity, consensus and information sharing, which are pre-agreed by creditor countries. This facilitates the decision-making process and the conclusion of agreements. Moreover, every year, the Paris Club publishes the amount of its claims on foreign countries (Paris Club, 2019). Most of its countries also report detailed information on the grants and concessional loans given to developing countries for developmental purposes. This is publicly accessible from the Creditor Reporting System managed by the OECD.

In contrast, non-Paris Club bilateral lenders are rarely part of an established creditor coordination and information-sharing group and are not necessarily bound by Paris Club terms, principles and standard disclosure requirements. Consequently, their behaviour is generally considered less predictable should a sovereign borrower face financial distress. These bilateral lenders, particularly China and United Arab Emirates, also score lower than the other lenders when it comes to overall aid transparency (Publish What You Fund, 2018). While there is some information on the size and timing of Chinese loans from a variety of private and academic sources, information on loan terms and conditions from the China Development Bank or the Export-Import Bank of China (China Exim Bank) is scarce to non-existent (Hurley et al., 2018). The lack of transparency of Chinese lending is an issue of concern, as China often lends at market rather than concessional terms (with risk premia), over shorter maturities and, at times, with collateral arrangements that secure repayment through commodity export proceeds, in particular, from oil (Horn et al., 2019).

3.3 Private-sector lending

There are two broad categories of private-sector lending: commercial bank debt and capital market-issued bonds. These two sources of finance can be obtained domestically or internationally.

As bonds allocated to private investors are generally publicly listed securities (unless there is a tightly held private placement), they tend to meet transparency requirements fairly easily due to their listing requirements. The requirements for international issuance, usually governed by English or New York law, are extensive and strict. In other words, the key terms and conditions are already publicly available; it is a matter of collating it. This information is more comprehensive and detailed than that required under the IIF Transparency Principles, but some stakeholders may not know how to find these publicly available documents and/or how to interpret the provisions therein.

In contrast, commercial loans, by definition, are private in nature (despite the fact that the borrower is a sovereign), because they are an agreement that only extends to the parties involved in the loan and involves no market disclosure. Therefore, unless there is a domestic legal requirement in the borrowing country, these tend not to be publicly disclosed. This type of financing is at the heart of the IIF Transparency Principles, which were, to a certain extent, an industry-wide reaction to the Mozambican scandal (see Box 1).

Table 1 summarises this chapter, outlining the level of transparency of the three main external sources of debt financing for sovereigns. We also flag which type of financing falls under the two transparency-related initiatives discussed in the next chapter.

Table 1 Level of transparency of sovereign financing options

Sovereign financing options		Level of transparency	Observations	G20 Guidelines	IIF Principles
Multilateral		High	High degree of transparency due to existing policies in place for most MDBs		
Bilateral	**Paris Club**	Medium*	Limited degree of transparency over the life of the loan Information sharing and IMF involvement at the restructuring level	✓ (G20 countries)	
	Non-Paris Club	Low	Scope for a degree of secrecy	✓ (G20 countries)	
Private	**Loans**	Low	Scope for a degree of secrecy		✓
	Bonds	High	High degree of transparency due to listing requirements (exemptions: private placements, tightly held)		

*Prior to distress, the transparency of Paris Club debt is low, as there is no obligation to disclose bilateral loans. Several countries report these at domestic level due to self-imposed practices. In a distress scenario, however, it becomes high, as all Club members share information concerning their lending to the distressed debtor.

4 Creditor-driven initiatives for improving transparency

As discussed, there are significant information gaps when it comes to certain types of bilateral sovereign lending and private-sector lending to sovereign borrowers. To address shortcomings in this area, groups or organisations representing the major providers of these types of financing have formulated guidelines and principles to foster greater transparency. This section summarises the salient features and the limitations of the two most recent and significant creditor-driven initiatives in relation to implementation and accountability mechanisms:

- the 'G20 Operational guidelines for sustainable financing' (2017) for bilateral creditors and their agencies
- the IIF 'Voluntary principles for debt transparency' (2019) for private-sector lending.

4.1 The G20 Guidelines: key features and limitations

In March 2017, the G20 countries endorsed the 'G20 operational guidelines for sustainable financing'. These Guidelines cover the conduct of lenders and borrowers in five areas, one of which is information sharing and transparency. The G20 group contains the largest Paris Club creditors and non-Paris Club creditors, the latter including China, India and Saudi Arabia.

With the assistance of the IMF and the World Bank, the group then developed a standardised diagnostic tool (IMF and World Bank, 2019) to allow bilateral creditors and their agencies to evaluate their own performance and their level of compliance with the Guidelines on a voluntary basis. The diagnostic tool classifies their lending practices as 'strong', 'sound' or 'with room for improvement'. 'Strong' is the highest standard, denoting enhanced sustainable lending practices. 'Sound' describes financing practices that are in line with the Guidelines, while 'with room for improvement' reflects financing practices that do not meet the minimum requirements of Guideline implementation.

The key features of the G20 Guidelines on information sharing and transparency are as follows.

1. They apply to the entire public sector of a creditor country, including public agencies, central banks, export credit agencies, national promotional banks, national development banks, SOEs and other entities acting on behalf of the government.
2. The creditor shares information on existing and new lending. A 'strong' practice rating requires a government agency to collect and publish loan-by-loan information for all of its country's official creditor agencies on a single website and update it within three months of new lending. A 'sound' practice rating requires a government's creditor agencies to disclose this detailed information to the IMF and World Bank at least on an annual basis.
3. The type of data to be made available include (but should not be limited to): the amount of the loan, the beneficiary (debtor), the use of proceeds, the interest rate, the maturity and grace period, the structure of any collateral and the amount of collateral provided, if relevant.

4. The creditor reconciles debt data with the borrower at least on an annual basis to prevent any operational errors or misinterpretation of the agreements that could undermine the soundness of the debt data.
5. The creditor refrains from using contractual clauses that limit the disclosure of amount, terms or other conditions in general ('strong') or to IFIs specifically ('sound').
6. The creditor verifies that lending operations are adequately disclosed after the fact in the borrowing country's public debt statistics ('strong').
7. The creditor conducts a post-debt-restructuring data reconciliation (if applicable) with the borrower, ensuring accurate reflection and public availability of any changed terms and conditions in the official debt data.

The Guidelines and corresponding diagnostic tool also have limitations, however.

1. While transparency is one of the key components of the G20 Guidelines, the results of the diagnostic survey for each participating country are not publicly available. Rather, the IMF and World Bank compiled the responses into one report and did not attribute any of the findings to any of the 20 participants (15 members of the G20 and 5 non-members). As the Guidelines are voluntary, one way of promoting compliance would be to make the non-disclosure of survey results less palatable to stakeholders, so that efforts to limit disclosure raises red flags among those involved.
2. The diagnostic tool, as it stands, cannot assess all aspects of the Guidelines when it comes to transparency and information sharing. This includes whether creditors use publicly available templates for financing agreements and refrain from using confidentiality clauses. The absence of a publicly available template may be partly down to the need to tailor contracts to the requirements of each arranging creditor and, indeed, each borrower.
3. The diagnostic survey cannot assess whether the creditor has verified that the loan is soundly accounted for in the borrowing country's debt statistics. This is potentially problematic, as there is a danger that creditors will neglect to improve those areas that are not captured by the tool.
4. Public disclosure of terms and conditions to the wider public is not measured. The distinction between 'strong' and 'sound' practices in the diagnostic tool means the G20 Guidelines can be met even if the creditor only discloses terms and conditions of individual loans to the IMF and the World Bank on an annual basis. It is unclear whether the IMF and World Bank would then make this detailed information available to other stakeholders (although it is likely that this information will be cross-referenced with the data provided during the IMF's Article IV consultations to make sure that the information is captured).
5. The lack of consultation/involvement of non-G20 countries in the formulation of the G20 Guidelines may adversely affect take-up by these countries.

4.2 IIF Principles: key features and limitations

In response to the discovery of several non-transparent loans to developing countries, which contributed to the deterioration of their debt sustainability, the IIF developed the 'Voluntary principles for debt transparency'. This self-policing initiative is intended to enhance transparency in private-sector lending, particularly to the most vulnerable low-income countries. The IIF Principles are subject to annual review of their uptake, implementation and impact.

The key features of the Principles are as follows.

1. They are voluntary, so decisions on whether lenders adhere to them, and countries borrow only from adherents (or not) are up to the financial institutions and sovereign borrowers.
2. Although they are relevant to all types of financing arrangement, they initially apply only to foreign-currency transactions with low-income countries that are eligible for concessional loans from the IMF (through the Poverty Reduction and Growth Trust (PRGT)), on the grounds that these countries

are regarded as more vulnerable to debt sustainability issues (see Annex 1 for a list of PRGT countries).
3. The Principles apply to all transactions entered into directly (such as loans) or indirectly (such as guarantees) by government.
4. They are not intended to apply to financial transactions where transparency is already good (to publicly traded bonds, for instance, as described in Section 3.3).
5. They recommend that certain details of the transactions ('relevant information') be reported to a 'reporting host' (to be decided), including the identity of key parties (borrower, lender, guarantor, agent, etc.), financial terms (amount, currency, interest rate, etc.), intended use of proceeds, status (ranking, immunities, the use of collateral or future flow of funds, guarantees, etc.) and dispute resolution options (governing law and jurisdiction or other).
6. The onus to report is on the lending institution (or agent).
7. The Principles recommend that information be made available after a cooling-off period of 60–120 days after the date at which the funds first move.

Although the development of the IIF Principles is widely seen as a step in the right direction towards improving sovereign debt transparency, there are four potential obstacles that could undermine their effectiveness.

1. The Principles explicitly recognise the importance of having the proper guidelines and tools to enable the 'relevant information' to be publicly disclosed to the 'reporting host'. However, there is no recommendation on the contractual clauses and acknowledgements required (from each of the contracting parties, including the relevant public sector entity counterparty). This omission is understandable, due to the variety of forms that the lending can take, plus the negotiable nature of lending arrangements, which can omit (or include) specific clauses. Moreover, the IIF Principles are not intended to be a complete action plan or roadmap for implementation. It is, therefore, crucial that guidelines are included in the subsequent implementation memorandum to increase the likelihood of the Principles being put into practice. In Section 5.1, we recommend that the parties agree and include a disclosure annex with the 'relevant information' when entering into a new financing arrangement.
2. The interest rate on each transaction is to be reported in a range (to be included in a disclosure template). This is likely to make it difficult to estimate the exact financial impact of a loan, especially when it is large. This feature, however, is related to issues of competition law.
3. Initially, the Principles will apply to a group of low-income countries that "are more likely to encounter problems with repayment of market-rate financing and ultimately debt sustainability" (IIF, 2019). Though they may eventually be expanded to more countries, it is unclear whether the IIF's assertion as to the likelihood of debt distress is correct. It is also possible that the existence of principles that apply solely to PRGT-eligible countries may create a bias towards lending to countries that do not require disclosure.
4. The host institution that will collect and disseminate these data is currently unspecified. Although an IFI like the IMF is seen as a natural choice, there is the risk of a possible, or perceived, conflict of interest here, as the IMF, itself, is a major creditor to sovereign states. An alternative would be to establish an independent, non-creditor organisation to monitor and enforce the Principles, such as that of the Extractive Industries Transparency Initiative (EITI).

Ultimately, despite their shortcomings, the guidelines and principles are welcome developments, in particular, for acknowledging that creditors – both bilateral sovereign creditors and private-sector creditors – have a responsibility to disclose the terms and conditions of their lending to sovereign governments. However, there is room for improvement.

5 How to make transparency initiatives more effective?

As currently conceived, the G20 Guidelines and IIF Principles both contain major gaps that must be addressed for them to be implemented effectively. These gaps make it difficult to put them into practice and to hold creditors to account. This chapter proposes how various stakeholders can work together to fill these gaps.

5.1 Carving out an exception to confidentiality clauses and/or including a disclosure annex

Carving out a limitation in the contract can allow the parties to comply with the G20 Guidelines or IIF Principles and disclose specific contractual details, despite the existence of confidentiality clauses.

Legal limitations on the disclosure of information in a contract tend to be in the form of ad hoc contractual provisions negotiated by the borrower and lender(s). Such limitations typically originate from a confidentiality and/or non-disclosure provision in a financing agreement or separate, standalone contract put in place for that purpose (see Box 2 for more detail). A legal limitation is unlikely to emanate from an administrative act, order, decree or law prohibiting the disclosure of information on a loan.

Contractual constraints, however, do not have to be an impediment to transparency. An important aspect of contractual limitations is that these are mutually agreed by the parties. Thus, the parties may equally agree to make an exception to any limitation and/or to include a specific annex on the disclosure of mutually agreed information (the 'relevant information'), to ensure that the interests of the parties are aligned and to overcome any fear of contravening a contractual provision. For avoidance of any doubt, a line can be included in the confidentiality or non-disclosure clause or agreement referring to the G20 Guidelines or IIF Principles. This

Box 2 Contractual provisions for non-disclosure

Contractual provisions limiting the disclosure of information can generally be grouped into two categories:

1. **Material non-public information**, which usually relates to the confidential information held by borrower and lender and obtained in relation to loan documentation during the application and negotiation phase. Such information is typically used in loan applications to better assess the financial condition of the borrower, particularly repayment capacity.
2. **Confidential information**, which can include material non-public information, is typically identified as 'confidential' in the actual loan documentation. This can be broad ('blanket') or specific. In any event, the documentation always includes certain exceptions, for example, should the information become publicly available or be required by a competent authority.

could be further enhanced by the inclusion of a pre-agreed disclosure annex with the 'relevant information', similar to the current practice for public announcements or press releases.

However, if disclosure is legally feasible, but not politically desirable to the sovereign borrower, these political concerns will probably trump the voluntary nature of the G20 Guidelines and IIF Principles.

5.2 Using public disclosure to incentivise compliance

Incentivising compliance is critical due to the voluntary nature of the G20 Guidelines and the IIF Principles. As currently designed, more responsible lenders may comply with them, while they are ignored by others, so borrowing could be skewed toward the latter in countries where transparency is most needed. For this reason, the non-disclosure of self-assessments that evaluate the adherence of the 15 G20 members (covering 37 lending agencies) and 5 non-members (covering 12 agencies) to the G20 Guidelines is cause for concern.

Actively monitoring and publicising those lenders that are compliant with the Guidelines and Principles, as well as those that are not, could help to incentivise compliance. This is currently the approach of several voluntary transparency-related initiatives, such as the EITI, which aims to improve financial transparency and governance in the extractive sectors. A similar approach is adopted by the IATI, which publishes a list of the organisations, including multilateral and bilateral creditors, that are compliant with its data standard. Making the results of the diagnostic tool for the G20 Guidelines public could be helpful in pressuring bilateral sovereign creditors to improve their lending practices and actively monitor their performance.

Monitoring compliance can be difficult due to information asymmetries, however. As lending arrangements are private, it is difficult to assess whether entities are not reporting, or simply not lending. There can be situations where a lender is assessed as being fully transparent in reporting their transactions, but this may be based only on a subset of transactions (while a 'problematic' loan agreement may be shrouded in a cloak of secrecy).

5.3 Creating a central repository for all loan terms and conditions

While it is commendable that these two groups of creditors are taking responsibility for making their respective lending more transparent, there is a risk that the separate sets of guidelines and principles will lead to multiple databases with fragmented management across several institutions. This could undermine the accessibility and user-friendliness of the databases, while differences in coverage and definitions used, as well as the interface itself, could hamper data comparisons. Ultimately, the end-users of the data may find it challenging to extract and analyse publicly available data on debt terms and conditions.

Similar criticism has been levelled in relation to the different IMF and World Bank debt databases, with one proposed solution being the creation of a centralised webpage summarising debt information from the various databases by country. A possible solution to the terms-and-conditions conundrum, therefore, is the creation of a similar summary page, listing terms and conditions by creditor for each borrowing country.

A more ambitious proposal involves all creditors reporting to a central registry (Eurodad, 2019). The advantage of this approach would be to standardise the data-collection process across the different types of creditor, ultimately improving the comparability of data. At the same time, this raises a new set of risks for the party acting as the repository, as it could trigger a potential liability in the event of a reporting inaccuracy. The responsible organisation would, therefore, need to be properly resourced, with robust protocols in place to mitigate such risk.

5.4 Expanding the IIF Principles to all countries

Although the IIF Principles are intended to apply to all developing countries, as mentioned in Section 4.2, the initial priority is 70 PRGT-eligible countries (see Annex 1). These are the poorest member countries of the IMF, with an income per capita below a certain threshold and no access to the international financial markets on a durable or substantial basis.

Delaying the expansion of the IIF Principles to more countries is problematic for three reasons. First, a significant amount of private-sector lending that falls under the IIF Principles is to countries that are not currently PRGT eligible, such as Angola, Ecuador, South Africa and Viet Nam. On average, between 2016 and 2018, commercial bank lending accounted for roughly 19% of total public external debt in Angola and 11% in Viet Nam (World Bank, 2020). Excluding bonds, commercial bank lending accounted for 34% of total public external debt in South Africa over the same period (ibid.). Second, debt surprises are not confined to PRGT countries. Ecuador, a non-PRGT country, has significantly underreported its public debt, according to a report by the auditor general (IMF, 2019). Third, debt vulnerabilities are on the rise in many emerging markets. Some countries are in outright default and others facing non-trivial financial pressures. If global monetary conditions tighten, the burden of debt will grow and rollover risks will increase. It is, therefore, important to increase the transparency of private-sector lending beyond PRGT countries.

5.5 Building capacity for debt data transparency and reconciliation on the side of sovereign borrower

Although the G20 and IIF initiatives focus on developing norms and procedures for improving transparency on the creditors' side, the international community needs to continue to build the capacity of sovereign borrowers to record and report debt data. Regular data reconciliation by the borrower with creditors and IFIs is also important, as it can flag when the information reported by government authorities is incomplete or inaccurate. In this regard, it would be a beneficial practice for creditors to follow up with the borrower's debt management office to ensure that they have adequately recorded the terms in their debt data.

The existing evidence available suggests that there are still significant gaps for low-income and lower-middle-income countries when it comes to debt recording, monitoring and reporting (IMF and World Bank, 2018; Mustapha and Prizzon, 2018). Moreover, several recent cases of 'hidden debt' have seen key government stakeholders, such as debt management offices, being unaware of certain debt obligations. In some cases, 'hidden' debt liabilities may be deliberate to avoid scrutiny and circumvent the approval process, but it can also result from a lack of clarity on the roles and responsibilities of various actors, as well as lack of clarity on what financing constitutes public debt (as in the case of Ecuador) (IMF, 2019).

Consequently, working with countries to develop a strong governance framework, effective organisational structure, adequate staff capacity and a functional debt-recording system is critical. This will require political commitment at the highest levels of government. In the absence of this commitment, sovereign borrowers may be tempted to use different types of financing instrument, such as public-private partnerships or central bank swaps, to underreport their debt liabilities.

6 Conclusion

Transparency of debt terms and conditions is a prerequisite to responsible borrowing and lending. It allows citizens to subject their government's borrowing to greater scrutiny and gives lenders more certainty about the repayment capacity of the borrowing country. Debt transparency has been the subject of particular attention recently – not least because public debt surprises have been a contributing factor to the fiscal messes in which some developing countries have found themselves of late (Mozambique and South Africa, for instance). In an effort to address the limited transparency of certain type of bilateral sovereign lending and private-sector lending, in 2017, the G20 countries endorsed the 'G20 operational guidelines for sustainable financing', while in 2019, the IIF formulated the 'Voluntary principles for debt transparency'.

Although these two creditor-led initiatives are important steps forward, more needs to be done, by various stakeholders, to make these principles operational and to ensure that creditors are accountable. In this paper, we recommend the following.

1. The parties to a debt contract should agree to make a disclosure exception for necessary disclosure requirements and/or to include a disclosure annex in the agreement to mitigate concerns that confidentiality clauses may discourage or circumvent compliance. We recommend a disclosure annex, as this will already include pre-approved information and help facilitate data reconciliation between borrower and creditor.
2. A list of creditors that are compliant with the Guidelines and Principles should be published annually to incentivise compliance with these voluntary codes of conduct. However, we concede that the private nature of lending arrangements makes it difficult to assess whether the reporting is actually taking place or, more importantly, taking place on the required number of transactions.
3. A central registry or database of debt terms and conditions should be created to prevent the development of multiple databases that are not easily comparable.
4. The IIF Principles are currently aimed at a specific set of lower-income countries, but should be expanded to all developing countries and possibly beyond to make transparency the norm.
5. While the G20 Guidelines and IIF Principles focus on developing creditors' procedures for sharing information, a concerted effort is needed to build the debt-recording and reporting capacity on the side of the sovereign borrower. This will also help the borrower and creditor to reconcile their data with each other on a regular basis, to ensure that the publicly available data is complete and accurate.

Debt transparency is complex, requiring many players to work together to make it a reality. Moreover, full compliance with the G20 Guidelines and the IIF Principles alone will not curtail irresponsible borrowing and lending. A well-functioning domestic legal system and strong rule of law in the borrowing country are critical to curbing any criminal activity related to sovereign debt.

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Annex 1 List of PRGT-eligible countries

1. Afghanistan
2. Bangladesh
3. Benin
4. Bhutan
5. Burkina Faso
6. Burundi
7. Cambodia
8. Cameroon
9. Cabo Verde
10. Central African Republic
11. Chad
12. Comoros
13. Republic of the Congo
14. Democratic Republic of the Congo
15. Côte d'Ivoire
16. Djibouti
17. Dominica
18. Eritrea
19. Ethiopia
20. Gambia, The
21. Ghana
22. Grenada
23. Guinea
24. Guinea-Bissau
25. Guyana
26. Haiti
27. Honduras
28. Kenya
29. Kiribati
30. Kyrgyz Republic
31. Lao People's Democratic Republic (the)
32. Lesotho
33. Liberia
34. Madagascar
35. Malawi
36. Maldives
37. Mali
38. Marshall Islands
39. Mauritania
40. Micronesia
41. Moldova
42. Mozambique
43. Myanmar
44. Nepal
45. Nicaragua
46. Niger
47. Papua New Guinea
48. Rwanda
49. Samoa
50. São Tomé and Príncipe
51. Senegal
52. Sierra Leone
53. Solomon Islands
54. Somalia
55. South Sudan
56. St. Lucia
57. St. Vincent and the Grenadines
58. Sudan
59. Tajikistan
60. Tanzania
61. Timor-Leste
62. Togo
63. Tonga
64. Tuvalu
65. Uganda
66. Uzbekistan
67. Vanuatu
68. Yemen
69. Zambia
70. Zimbabwe

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