

From Debt Collection to Relief Provision:

60 Years of Official Debt Restructurings through the Paris Club

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Abstract*

Despite the frequency of official debt restructurings, little systematic evidence has been produced on their characteristics and implications. Using a dataset covering more than 400 Paris Club agreements, this paper fills that gap. It provides a comprehensive description of the evolving characteristics of these operations and studies the economic dynamics surrounding them. The progressive introduction of new terms of treatment gradually turned the Paris Club from a mere debt collector into a sequenced provider of debt relief. Our study finds that more generous restructuring conditions involving nominal relief are associated with higher economic growth. In contrast, agreements including only NPV relief have no positive impact on growth but encourage the countries receiving these restructuring conditions to pursue a more prudent fiscal policy. This finding is consistent for both EMEs and HIPCs. This paper offers interesting policy messages. When deciding upon the type of relief to be granted through debt restructuring, official sector creditors face a trade-off between stimulating growth and fostering fiscal sustainability. The paper also provides important insights regarding a number of research areas. We argue that research on sovereign debt restructurings needs to incorporate the interaction between private sector and official sector creditors.

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Highlights

- The paper provides a comprehensive description of the evolving characteristics of the Paris Club: from a debt collector to a debt relief provider.
- The paper discusses both the factors affecting the changing role of the official sector and how official sector actions affected outcomes.
- The macroeconomic effect of debt restructuring depends on the form of the debt relief provided.
- Guided by the evolution of the Paris Club, we compare nominal haircut against non-nominal haircut, and agreements based on the NPV relief provided.
- Policy makers providing debt relief face a trade-off between economic growth and fiscal sustainability.

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I. Introduction

An environment of heightened sovereign risk worldwide following the global financial crisis has reignited the interest of academics and policymakers in the resolution of debt overhangs.⁴ Although there is an extensive literature on sovereign debt restructurings, most attention has been paid to restructurings involving only private creditors.⁵ By contrast, little systematic evidence has been produced on the characteristics and implications of debt restructurings involving official creditors despite their fundamental role in the resolution of several crises (IMF, 2013).⁶ This paper helps fill this gap using data from the Paris Club, an informal group of official creditors with 21 permanent members, which provides useful information to deepen our knowledge about the sovereign debt restructurings that have been concluded from 1956 to the present.⁷ Our work makes three main contributions. First, we analyze the evolution of the norms and procedures of the Paris Club to shed light on the role that this forum has played historically in the international financial architecture. Second, we compile and present a comprehensive database covering 422 debt restructuring agreements with 86 sovereign debtors. Third, we use event analysis techniques to examine the macroeconomic dynamics surrounding these episodes and provide econometric evidence on the impact of official sector debt relief using local projection methods.

Our research contributes to a strand of still narrow but growing literature aimed at understanding official sector debt relief and its effects on countries' economic performance. Easterly (2002) focuses on heavily indebted poor countries (HIPCs) and finds that, paradoxically, the debt relief efforts of the 1980s and 1990s resulted in increased indebtedness for these countries. His paper uses dynamic averages to analyze the evolution of per capita incomes in HIPCs and the net present value (NPV) of their debt throughout the implementation of these initiatives, and runs cross-country regressions of several variables capturing countries' policy stance against a HIPC dummy and debtors' initial level of income. He reaches two interesting (though untested) conclusions. First, debt relief may harm

⁴ The fact that, under the on-going Chinese presidency of the Group of Twenty (G20), a working group on the International Financial Architecture has been reactivated, speaks of the relevance of the issue for policy makers. One of the working group's priorities is to improve debt sustainability and restructuring processes. In this regard, the G20 considers the Paris Club as the major platform for restructuring official bilateral debt.

⁵ For one thing, data availability is undeniably better for sovereign loans extended by big banking groups and bonds issued in international financial markets. See Reinhart and Rogoff (2010), Das, Papaioannou, and Trebesch (2012), and Cruces and Trebesch (2014).

⁶ A country's public debt with official creditors is the credits that a government obtains from other governments – bilaterally or in syndication – or from multilateral organisations, such as the International Monetary Fund or the European Stability Mechanism.

⁷ They are Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, South Korea (since 2016), Ireland, Israel, Italy, Japan, Netherlands, Norway, Russia, Spain, Sweden, Switzerland, United Kingdom and United States. As of November 2016, it was announced that Brazil was to join the Paris Club, becoming the 22nd permanent member and the first large developing economy to enter the group for two decades.

growth if it allows countries to delay necessary reforms. Second, a once-and-for-all program is superior to one with gradual relief. Rose (2004) documents a significant negative effect of official debt restructurings on trade, which he interprets as one of the reasons why countries pay their debts. Using a gravity model and a sample of Paris Club restructurings, he finds that following debt restructurings trade falls by 8 percent of GDP and remains depressed for 15 years. Arteta and Hale (2008) focus on the effect of defaults on the private sector's access to capital markets, finding that in that respect official debt restructurings are more damaging than restructurings involving only private creditors.⁸

Barkbu, Eichengreen and Mody (2012) provide a 30-year overview of official sector debt relief. Although they mention that the involvement of the Paris Club was important during the debt restructurings of the 1980s and 1990s, their analysis focuses on official financing and not on the debt relief operations conducted through the Paris Club. Das, Papaioannou, and Trebesch (2012) review a number of issues related to sovereign risk and debt restructurings and present a dataset including debt workouts of external privately held public debt (PSI) and Paris Club agreements (OSI). While they do not carry on any econometric analysis, they present a set of interesting stylized facts. First, OSI is more prevalent than PSI, with evidence of "serial defaulting." Second, there are clusters of restructuring events, for instance in the 1980s. Third, the number of episodes with face-value reductions increased over time both for OSI and for PSI. Fourth, restructurings are conducted both pre- and post-default. Finally, restructurings have become quicker to complete over time.

More recently, Reinhart and Trebesch (2016) focus on the effects of debt relief by comparing episodes during the 1930s (official relief for European nations) and the 1990s (private relief for Latin American countries via the Brady Plan). In many respects, their paper is the closest to our effort.⁹ They show that debt restructurings are more beneficial for growth when they provide nominal haircuts than when relief is provided only in NPV terms (through maturity extensions or interest rate reductions). Finally, Forni et al. (2016) specifically study the impact of Paris Club agreements on growth. According to these authors, if growth generally decreases after a sovereign debt restructuring, the exit strategy from a restructuring agreement matters. Debt relief has the largest growth impact for countries that exit restructurings with relatively low debt levels. However, their paper does

⁸ They argue that this is the case because Official Sector Involvement (OSI), as a rule, comes before Private Sector Involvement (PSI). Diaz-Cassou Erce, and Vázquez (2008) argue along similar lines.

⁹ To make these two sets of events "comparable", they select only emerging economies on their 1990s subsamples. Most relevant for our effort, they disregard that on the 1930s debt was official while in the 90s it was privately-held.

not focus on Paris Club events per se, but on the interaction between restructuring events with PSI and OSI. Moreover, in Forni et al. (2016), Paris Club agreements are represented by a dummy variable only. Our characterization of Paris Club treatments is richer, allowing us to go further in the analysis of the effects of official debt restructurings.

The historical account presented in this paper describes how the objectives pursued by the Paris Club were gradually broadened over time, turning it from a debt collector to a sequenced provider of debt relief, a move that was aimed at overcoming some of the structural development bottlenecks facing the worlds' poorest nations. In fact, we find that official debt relief helps stimulate growth in the short- to medium-term when it comes in the form of nominal haircuts, which vindicates the reform process embraced by the members of the Paris Club since the late 1980s. However, this success might be a mixed blessing from a debt sustainability perspective, as countries receiving nominal debt relief tend to subsequently run significantly larger deficits. When the debt restructuring comes only through maturity extensions and interest rate reductions, larger NPV relief does not provide better growth prospects, but does result in a looser fiscal stance, potentially perpetuating the debt sustainability problem. Our results, therefore, suggest that if the main goal of an official debt restructuring is to reignite growth, creditors should provide nominal haircuts. Instead, if the main objective is fiscal sustainability, agreements carrying no nominal haircut and limited NPV relief may be a better option.

In addition to the empirical evidence on the macroeconomic impact of official debt restructurings, our paper identifies a number of missing links in the existing literature of sovereign debt restructurings, opening up new directions for research. Because of the relevance of the Paris Club as a focal point for private sector debt relief, through its comparability of treatment clause, one overlooked element in the literature we emphasise is the interaction between PSI and OSI, which is essential for understanding the form, timing and macroeconomic effects of sovereign debt restructurings.¹⁰ Our dataset shows that joint intervention and/or successive debt relief provided by both official and private sector

¹⁰ For instance, official sector restructuring deals are not used as an explanatory variable regarding the outcome of PSI, but simply as a robustness check (see Asonuma, Chamon and Sasahara 2016). An exception is the work by Forni et al. (2016), which allow the effect of PSI to differ depending on whether it is preceded by a Paris Club agreement. Still, their characterisation of Paris Club deals through a dummy indicator prevents them from any more elaborate exercise.

creditors is the rule more than the exception. Therefore, omitting these joint forces is likely to be overestimating the effects of PSI.¹¹

The rest of the paper is structured as follows. Section II introduces the key features of debt restructuring events involving Paris Club creditors, emphasising the historical evolution of Paris Club's terms of treatment and the role that this forum has played in the international financial architecture. Section III uses an event study approach to describe the macroeconomic dynamics that surround Paris Club agreements. In Section IV, we go a step further and use local projection methods to unveil the causal impact of Paris Club restructurings on the economic performance of debtors. Finally, Section V concludes and discusses the implications of our results both from a policy and a research perspective.

II. Debt Relief with the Paris Club: A Historical Account

The Paris Club can be described as an informal forum created by a number of like-minded creditor governments to conduct debt-rescheduling negotiations with their official debtors in a coordinated manner. This section presents the evolution of the Paris Club, emphasizing the changes that shaped the role that it has come to play in the sovereign debt regime. Spanning six decades of history (1956-2016), the Paris Club initially functioned primarily as a debt collector. Over the years, however, it began to pursue broader objectives as the need arose, and it is precisely at these times that the most significant changes to the role and proceedings of the group were adopted.

To carry out our analysis, we construct a dataset on bilateral debt restructurings conducted through the Paris Club with information about 422 treatments with 86 debtors. This database was hand-collected from the Paris Club website agreement by agreement.¹² For each treatment, the following information was extracted: the signing country, the date of the agreement, the categories of debt treated,¹³ the total amount treated,¹⁴ the nominal relief provided (if any), the status of the agreement (if active or repaid), the terms of treatment, whether the comparability of treatment clause was applied, participating creditors, and

¹¹ Third party institutions (e.g. the IMF) also often provided fresh cash in parallel to debt restructuring events.

¹² Figure A1 in Appendix 1 presents a typical Agreed Minutes as reported on the Paris Club website for each signed Agreement.

¹³ Among the different types of debt, the Paris Club agreements generally concern only medium- and long-term debt. Short-terms debt (that with a maturity of one year or less) is usually excluded from the treatments, as its restructuring can significantly undermine the debtor country's capacity to participate in international trade.

¹⁴ One shortcoming of this data source is the non-distinction between Official Development Assistance (ODA) and non-ODA claims in the total amount treated. We will assume that the amount treated is all ODA debt. Given that non-ODA claims are treated in less favourable terms than ODA claims, our analysis will overestimate the generosity of the Paris Club terms agreed over time with its debtor countries.

whether the Evian Approach was applied. Additional information about episodes associated with the HIPC initiative was collected from the IMF's completion point and decision point reports, while data from the Evian Approach was retrieved from the Paris Club annual reports. Our dataset also incorporates information on restructurings that involved private creditors, for which we use data from Cruces and Trebesch (2014). Finally, we complemented our dataset with information on the income level, the lending category and a number of macroeconomic and fiscal variables of each of the countries included in our sample. These variables were extracted from the World Bank's *World Development Indicators*.

The Paris Club in its Early Stages: From 1956 to 1980

The origin of the Paris Club is often traced back to the meetings that were held in the French capital in 1956 to reschedule Argentina's debt obligations with the export credit agencies of various OECD countries. However, this was an ad hoc meeting, and the intention of the governments that attended it was not to create a new international organization to conduct debt restructurings. In fact, the governments that became the members of the Paris Club did not agree on a charter (a fact that remains true to this day), and no staff was appointed to perform new tasks. Furthermore, for some time it was not even clear that the Paris Club was to become a permanent fixture of the international financial architecture. During the 1960s and 1970s, there were even discussions about whether the IMF or the World Bank should take over its duties and house bilateral debt rescheduling talks in a 'Washington Club' of sorts (Callaghy, 2002). Eventually, the French government prevailed in these negotiations and the Paris Club was never moved to Washington. On the contrary, a permanent secretariat housed in the French Treasury was created in the late 1970s, which somewhat institutionalized the Paris Club (Rieffel, 1985).

During the first two decades of its existence, the Paris Club was a relatively obscure forum with limited activities. Between 1956 and 1978, it conducted only 26 negotiations with 12 countries, little more than one debt rescheduling negotiation per year on average. Despite this limited relevance, some of the norms and procedures that have shaped the functioning of the Paris Club and the commitments accepted by its members were developed during this period. The Club operates according to the following principles (see Annex 1 for more details): (i) *solidarity*, implying that members agree to act as a group and to avoid taking actions with their debtors that may adversely affect the claims of the other members of the

group; (ii) *consensus*, implying that Paris Club rescheduling deals must be accepted by all of its members; (iii) *conditionality*, implying that the debtors that approach the Paris Club for a debt rescheduling are expected to have previously concluded an agreement with the IMF and to be implementing a macroeconomic adjustment program; (iv) *a case-by-case approach* in the definition of the terms of each rescheduling granted by the members of the group; and (v) *comparability of treatment*, implying that sovereign debtors that reach a rescheduling agreement with the Paris Club are required to seek similar terms from other creditors, with the exception of multilateral organizations, to preserve their preferred creditor status.¹⁵

An important early characteristic of the Paris Club was that it functioned merely as a debt collector. Its members did not contemplate the possibility of pursuing other economic goals through the rescheduling agreements that it reached with distressed countries. Indeed, until the late 1980s one of the foundations of the Paris Club was that the reschedulings it granted should not weaken debtors' moral and legal obligation to repay their debts in full. The binding constraint for Paris Club rescheduling agreements, therefore, was debtors' capacity to service their obligations, and other considerations were rarely taken into consideration (Rieffel, 1985). Reflecting this initial interpretation of the role of the Paris Club, during the first decades of its existence, participating creditors adhered to an "imminent default rule," according to which only countries on the verge of missing their debt service payments would be considered for a treatment (Josselin, 2009). In addition, until the 1976 debt restructuring in Democratic Republic of Congo (then Zaire), another Paris Club norm was that previously rescheduled financial obligations could not be included in a subsequent restructuring (Callaghy, 2002). The Paris Club, therefore, was designed to function as a last-resort option for countries to avoid defaulting rather than as a tool to restore debt sustainability or to improve the economic prospects of heavily indebted nations.

The narrowness of the debt collection objective that initially guided the Paris Club helps explain why until 1987 all agreements were modelled along the lines of the so-called Classic terms. These are non-concessional reschedulings, and hence do not contemplate the possibility of debt relief in NPV terms. Accordingly, Paris Club deals could not include nominal reductions in the debt stock to be treated, and were structured at market interest rates. In Paris Club jargon, the Classic terms provided for "flow treatments," rescheduling maturities as they fell due in the so-called consolidation period, the interval during which an

¹⁵ The comparability of treatment principle is aimed at ensuring taxpayers from Paris Club members that their claims on debtors are not subordinate to those of private institutions or other bilateral lenders that do not belong to the group. Although this rule has remained in place throughout the history of the Paris Club, its practical implementation and the complexity of getting other creditors to accept it has evolved in line with the changing composition of sovereign debt and the growing diversity of financial instruments in sovereign lending.

IMF program establishes that a postponement of debt service payments is necessary to close debtors' financing gap (usually between one and three years). Under the Classic terms, the repayment profile is negotiated with debtors on a case-by-case basis, although it has tended to include a three-year grace period and a 10-year repayment period.

The 1980s Debt Crisis

As can be seen in

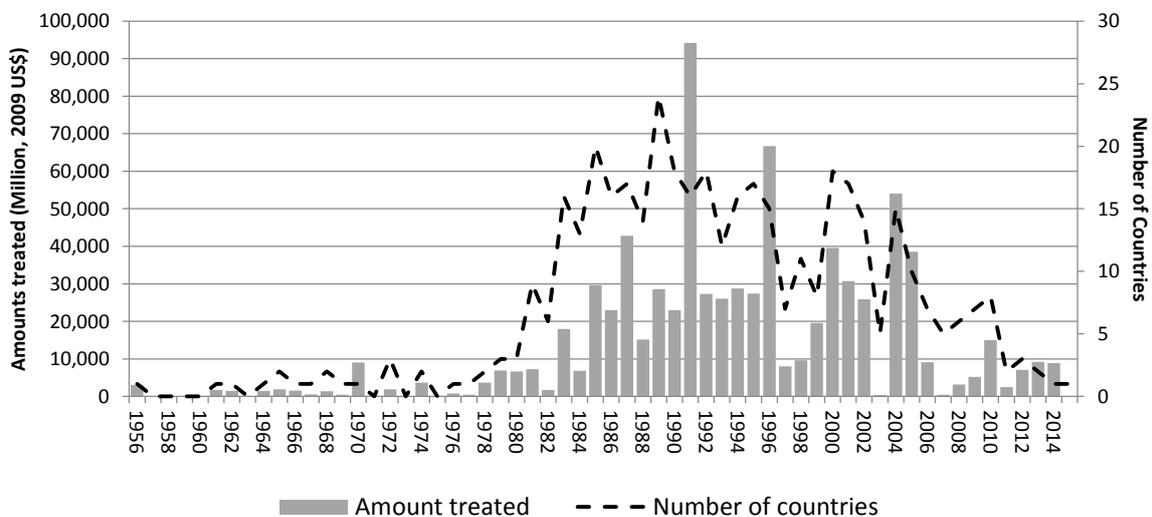
Figure 1, the activity of the Paris Club only really picked up in the 1980s, due to the wave of financial distress that swept through much of the developing world as the surge in sovereign credit that resulted from the recycling of petrodollars during the 1970s abruptly dried up.¹⁶ Illustrating this increasing relevance of the Paris Club, 134 agreements were signed with 49 countries between 1980 and 1989, whereas in the 1950s, 1960s, and 1970s there were only 25 agreements with 10 different debtors. Furthermore, total debt treated during the 1980s amounted to more than \$180 billion, against \$40 billion between 1956 and 1979, both figures in constant 2009 U.S. dollars.

It is important to mention that during the 1980s, the Paris Club worked in tandem with the London Club, which was created by commercial banks in the context of Zaire's debt crisis of the late 1970s. The parallel negotiations that took place in these two forums of public and private creditors was instrumental in ensuring the observance of the comparability of treatment principle, since the bulk of developing countries' debt was in the form of syndicated bank loans (Josselin, 2009). A different picture would emerge in the 1990s

¹⁶ As can be appreciated in Figure 1, the volume of Paris Club treatments also spiked in 1970. However, this can be attributed to one single rescheduling with Indonesia, which concluded a series of four treatments (the previous three were signed in 1966, 1967, and 1968) following the fall of the Sukarno regime. The 1970 deal with Indonesia tried to provide a more durable solution to that country's debt problem, involving obligations for an amount that surpassed US\$2 billion, which became the largest Paris Club deal in history, a condition it retained until the 1980 agreement with Turkey.

because of the securitization of sovereign debt kick-started by the Brady Plan, which made it more difficult to coordinate debt-rescheduling negotiations with private creditors (Díaz-Cassou, Erce, and Vázquez, 2008).

Figure 1: Evolution of Paris Club Treatments

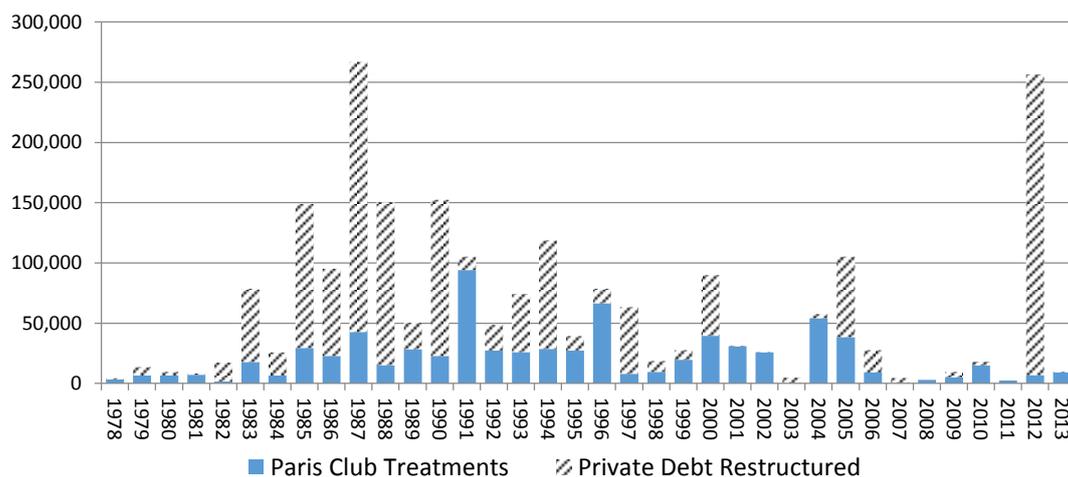


Source: Paris Club.

Notwithstanding the increasing amounts of bilateral debt rescheduled through the Paris Club during the 1980s, its direct role in the management of the 1980s debt crisis should not be overplayed. For a start, the stock of debt treated by the Paris Club between 1980 and 1989 represented on average only 1.3 percent of developing countries' total external obligations. In fact, the weight of the debt treated by the Paris Club as a proportion of the external obligations of the countries that participated in these rescheduling events was lower

during the debt crisis than in other periods: 8.3 percent in the 1980s against 15.7 percent in the 1970s, 11.2 percent in the 1990s, or 19.7 percent in the 2000s.¹⁷ Furthermore, as can be seen in Figure 2, during the 1980s the volume of sovereign debt treated through the Paris Club amounted to about 25 percent of that restructured with private creditors, illustrating the fact that the bulk of the obligations that were at the origin of the debt crisis were held by banks rather than by governments.

Figure 2: Paris Club Treatments vs. Private Sector Involvement (Million, 2009 US\$)



Source: Paris Club, Cruces and Trebesch (2014).

Another indication of the limited role played by the Paris Club in the management of the debt crisis is the fact that only 22 percent of the treatments agreed upon during the 1980s were signed with Latin American countries, even though this region was at the epicenter of the crisis (see Table 1). However, the debt treatments with Latin American countries amounted to 44 percent of total debt treated during the 1980s. This implies that, on average, debt treatments with Latin American countries were about twice as large as other treatments. In any case, between 1980 and 1995 the total value of bilateral debt rescheduled with Latin

¹⁷ Data on external debt are drawn from the World Bank's International Debt Statistics database. Some relevant Paris Club treatments could not be included in these calculations because the World Bank's database has missing observations, such as Russia's debt during the 1990s and Iraq's debt in the 2000s, some of the largest debt restructurings in the history of the Paris Club.

America through the Paris Club amounted to US\$69.5 billion, whereas the amount of debt restructured with private creditors surpassed US\$420 billion. Again, this suggests that the London Club was much more relevant for this group of countries at that juncture.

Table 1: Agreements per Region and Period (Million, 2009 US\$)

	Africa		Asia		Europe		Latin America		Total	
	Amount Treated	Number of Treatments								
1956-1979	5,318	4	15,107	7	6,221	2	13,528	12	40,174	25
1980-1989	71,096	92	7,496	5	46,014	7	48,856	30	173,462	134
1990-1999	98,966	76	18,886	12	161,355	15	51,512	36	330,719	139
2000-Present	140,067	86	89,531	15	1,266	7	15,026	16	245,890	124
Total	315,447	258	131,020	39	214,856	31	128,922	94	790,245	422

Source: Authors' Calculations.

From Debt Collector to Relief Provider

Toward the end of the 1980s, the Paris Club underwent some significant changes as a new restructuring model was adopted under the so-called Venice terms (1987) and the Toronto terms (1988). The introduction of these new rescheduling modalities was aimed at dealing with the challenges facing poorer countries in new ways, and not at addressing the problems of middle-income economies, which arguably were still at the forefront of the 1980s debt crisis. In any case, the inclusion of the Toronto terms to complement the Classic terms was a crucial turning point in the history of the Paris Club. It gave way to a period of 15 years during which several new terms of treatment were added to the Paris Club toolkit, all of them going in the direction of providing increasingly concessional conditions to a targeted group of distressed debtors.

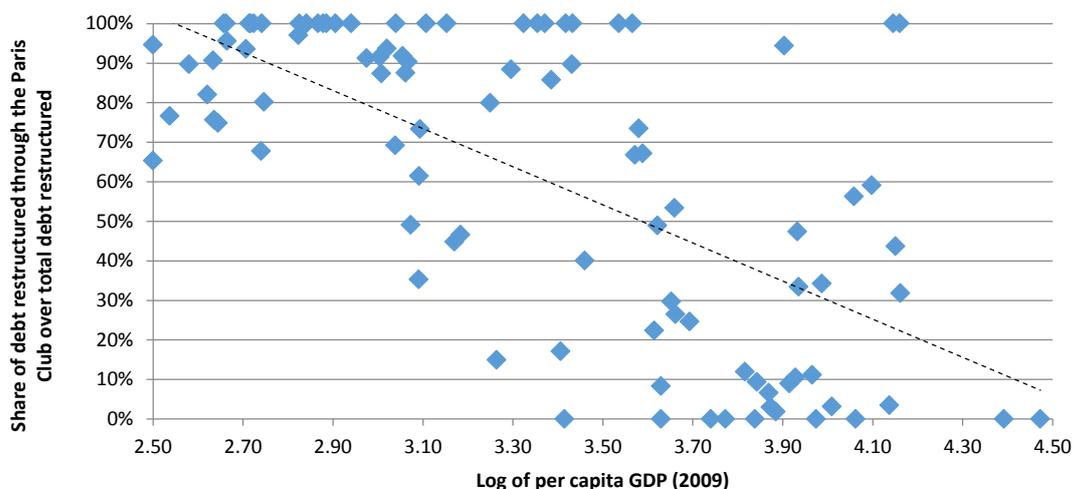
Three of the innovations adopted during this period are particularly noteworthy: (i) the adoption of the Naples terms in 1994, which for the first time allowed the Paris Club to treat the entire debt stocks of certain countries in order to facilitate their exit from the restructuring process;¹⁸ (ii) the introduction of the HIPC Initiative in 1996, which included multilateral claims in the pool of sovereign obligations that could be subject to debt relief; (iii) the adoption of the Evian approach in 2003, which extended the possibility of providing debt relief to non-HIPC countries in order to restore the sustainability of their debt stock.

¹⁸ In Paris Club jargon, these are referred to as stock treatments.

How to explain that after three decades of quasi immobility the members of the Paris Club became willing to undertake such a far-reaching change in the restructuring conditions offered to their official debtors? The main reason behind the progressive adoption of increasingly concessionary terms was the recognition that the combination of flow rescheduling and IMF-supported structural adjustment programs was not slowing down poor creditors' accumulation of debt, and that the heavy burden posed by their financial obligations was central to explaining the dismal economic performance of these countries. Throughout the 1980s and 1990s, this issue gained prominence in advanced economies' public debate when a network of transnational NGOs placed it at the center of their advocacy activity and an epistemic community of economists and academics began to push for a more aggressive debt agenda in favor of developing nations (Callaghy, 2002; Easterly, 2002).

Thus, the moral imperative of debt repayment that the Paris Club had originally emphasized progressively mutated into a moral obligation on the part of creditors to provide relief for HIPC. In other words, the exclusivity of the debt collection objective was dropped to incorporate a development assistance aspiration among the functions of the Paris Club. This fundamentally altered the logic of its rescheduling exercises. It also explains the negative association between the share of debt restructured through the Paris Club over total debt restructured and countries' level of economic development, which is evidenced in Figure 3.

Figure 3: Relative Importance of the Paris Club vs. per capita GDP, by Country



Sources: Authors' Calculations

The gradualism with which these concessional restructuring conditions were introduced reflects the compromises that had to be reached among G7 countries in the debt negotiations that took place in the 1980s and 1990s. Soon after the introduction of the Toronto terms, some important creditors (most notably, the United Kingdom) were already arguing that much more concessional restructuring conditions would be needed to overcome the structural problems facing HIPCs. However, there were budgetary and accounting issues that had to be dealt with to write off these loans, which prevented the Paris Club from progressing faster than it did (Daseking and Powell, 1999). In any case, and irrespective of the pace of the reform, the fundamental transition that took place during this period was the consolidation of the view that an exit from the rescheduling process had to be sought, and that restoring debt sustainability for at least the most distressed poor countries was crucial.

Importantly, with the progressive introduction of increasingly concessional terms of treatment, the Paris Club adopted the practice of topping up previous agreements, a practice that was particularly relevant for the HIPC initiative described below. Topping up implies that the amount of debt relief granted at each step of a phased program is determined by the difference between the total relief that the program targets at that stage and the amount of relief already granted in previous phases of the debt-restructuring process. Under this approach, therefore, debt relief is provided incrementally. The following formula summarizes the topping-up practice:

$$T = (X - Y) / (100 - Y)$$

where T is the top-up percentage of a given debt treatment, X is the targeted debt relief and Y is the debt relief obtained in previous agreements.

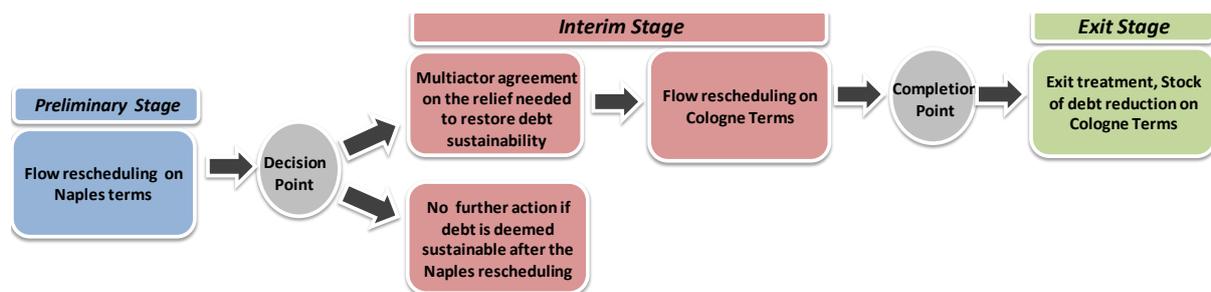
Multi-staged Debt Relief under the HIPC Initiative

The adoption of the HIPC Initiative in 1996 implicitly recognized that to restore poor countries' debt sustainability, multilateral obligations should be included in the restructuring process. To some extent, therefore, the HIPC Initiative eroded international financial institutions' preferred creditor status, although the losses associated with the cancellation of multilateral credit were partially covered by the contributions of a number of donors to a trust fund administered by the World Bank. As had happened with the terms of treatment of the Paris Club, the HIPC Initiative was gradually augmented in terms of the share of multilateral

debt that it was to cover. With the Multilateral Debt Relief Initiative (MDRI) announced in 2005, the World Bank, the African Development Bank, and the IMF went as far as accepting the complete cancellation of poorer countries' debt. Eventually, the total cost of the HIPC and MDRI initiatives, both of which are close to completion, is estimated at US\$75 billion in 2013 NPV terms (IMF, 2014).

The HIPC and MDRI initiatives constituted a further broadening of the objectives pursued by the international sovereign debt-restructuring regime because they conditioned relief on the implementation of an economic reform program and a poverty reduction strategy that went way beyond the usual template of IMF programs. This was instrumented through a multi-stage approach that incorporated two key milestones: a decision point and a completion point. At decision point, countries' economic situation was assessed, the required debt relief computed, and their eligibility to participate in the HIPC Initiative declared depending on their having produced a participatory poverty reduction strategy and on their track record with the IMF and the World Bank.¹⁹ At completion point, HIPC countries' debt was to be written off depending on their track record with the implementation of the policies and the poverty reduction strategy agreed upon at the decision point. A somewhat similar multi-stage methodology was later replicated for middle-income countries in the context of the Paris Club's Evian approach.

Figure 4: Paris Club Involvement in the HIPC Process



The Paris Club has been an important participant in the HIPC Initiative, and according to the Fund's estimates, has borne 36 percent of its overall cost (IMF, 2014). In most cases, the Paris Club granted three treatments sequentially, topping up at each of them the debt relief previously provided. As can be seen in Figure , during the preliminary period that preceded decision point, HIPC countries were granted a rescheduling under Naples terms of

¹⁹ Countries had to be eligible for concessional lending from the IMF and the World Bank to take part in the HIPC Initiative.

treatment. In turn, during the interim period (between decision and completion point), countries were eligible for an additional rescheduling under the more generous Cologne terms of treatment. At completion point, the process was completed with an additional restructuring of bilateral debt up to the level required to reach the target agreed upon at decision point. In addition, it was common for Paris Club creditors to provide additional debt forgiveness beyond that required by the HIPC Initiative.

Nominal Relief for Emerging Economies: Evian Terms

Up until the early 2000s, most of the innovations adopted by the Paris Club focused on poorer countries. A different picture would emerge after the G8 Summit held in Evian-les-Bains in 2003, where a new methodology was introduced to deal with non-HIPC cases. The reason behind the G8's decision to go in that direction was largely geopolitical: following the Second Gulf War, the international community needed a mechanism to write off part of the debt that had been accumulated by Saddam Hussein's regime even though Iraq was a country that did not qualify for any of the Paris Club's concessional terms of treatment. The Evian Approach was a solution devised to meet that need, further distancing the Paris Club from its initial debt collection role.

The Evian Approach introduced a new protocol applicable to middle-income economies that incorporated debt sustainability considerations and explicitly pursued the objective of providing a long-lasting exit strategy from the rescheduling exercise also for non-HIPC countries. Furthermore, with the adoption of this new protocol, the G8 claimed to contribute to the reform of the international financial architecture that was being discussed at the time, whose aim was to facilitate the resolution of the financial crises that had swept through emerging markets since the mid-1990s.²⁰

A similarity between the Evian approach and the HIPC Initiative is that both are articulated through a multi-staged framework for the delivery of debt relief. The first step contemplated by the Evian approach is the elaboration of a standard IMF debt-sustainability assessment to determine whether the country requesting a Paris Club rescheduling faces a liquidity or a solvency problem. Should it be deemed to have a liquidity problem but a sustainable stock of debt, the debtor is eligible for a traditional flow treatment under Houston terms if it is a lower-middle-income country, or under the Classic terms of treatment if it is

²⁰ See G8 Finance Ministers' Statement, May 2003: http://www.g8.utoronto.ca/finance/fm030517_communique.htm

not. Instead, if the debtor is deemed to be facing a solvency problem, the process by which a definitive debt restructuring will be granted is initiated.²¹ During the first stage of this process, the debtor's compliance with the conditionality of an IMF-supported program is assessed and, in the meanwhile, a flow treatment is granted to ensure that its financing gap is covered as required by the Fund. As a second stage, the country is required to successfully undergo another IMF-supported program, upon the satisfactory completion of which the Paris Club delivers a final exit treatment expected to bring the country's debt back to a sustainable path.

As opposed to the various restructuring modalities that were introduced for poorer countries during the 1990s, the Evian Approach did not standardize the terms of treatment granted to the countries that would qualify for it. In the case of middle-income economies, therefore, the Paris Club strictly adhered to the case-by-case principle, tailoring each debt restructuring to the financial situation of the debtor as assessed by the debt sustainability analysis conducted in conjunction with the Fund. To provide the Paris Club with the flexibility required to adapt its response to the specific situation of each debtor, the Evian Approach also allowed for the provision of net present value debt relief in exceptional cases, and for the inclusion of short-term debt in the deal. In addition, as is the case of more traditional terms of treatments, the scope of the debt restructurings agreed between the Paris Club and the middle-income debtors that benefit from the Evian Approach is determined by the type of treatment granted (flow treatment, stock re-profiling, stock reduction), the categories of debt included in the deal, and the cut-off date.

Table 2: Bilateral Debt Restructurings under the Evian Approach

²¹ It is important to note that no absolute criteria have been established to discriminate between liquidity and sustainability issues, and that the Paris Club reserves the right to develop its independent judgment about the debtor's situation.

Country	Date	WB Classification	Terms	Amount treated (million US\$)	Nominal debt relief (million)	Nominal debt relief %
SUSTAINABLE CASES						
Kenya	1/15/2004	Lower-middle income	Houston	353	0	0%
Dominican Republic	4/16/2004	Upper-middle income	Classic	193	0	0%
Gabon	6/11/2004	Upper-middle income	Classic	716	0	0%
Georgia	7/21/2004	Lower-middle income	Houston	161	0	0%
Dominican Republic	10/21/2005	Upper-middle income	Classic	137	0	0%
Moldova	5/12/2006	Lower-middle income	Houston	151	0	0%
Djibouti	10/16/2008	Lower-middle income	Houston	76	0	0%
Antigua and Barbuda	9/16/2010	High-income	Classic	110	0	0%
Saint Kitts and Navis	5/24/2012	High-income	Classic	5	0	0%
Total				1,902	0	0%
UNSUSTAINABLE CASES						
Iraq	11/21/2004	Upper-middle income	Ad Hoc	37,158	29,727	80%
Kyrgyz Republic	3/11/2005	Lower-middle income	Ad hoc	555	124	22%
Nigeria	10/20/2005	Lower-middle income	Ad Hoc	30,066	18,000	60%
Seychelles	4/16/2009	High-income	Ad Hoc	163	73	45%
Myanmar	1/25/2013	Lower-middle income	Ad Hoc	9,868	5,556	56%
Total				77,810	53,480	69%

Sources: Authors' Calculations

Table 2 provides a summary of all the agreements that have been concluded under the Evian Approach. So far, nine countries out of the 14 that have been treated under the Evian Approach were facing a liquidity problem and, therefore, received either the Houston or the Classic terms depending on their income level. In turn, five countries were considered to have an unsustainable debt stock, and therefore received debt relief ranging from 22 percent in the case of the Kyrgyz Republic to 80 percent in the case of Iraq. Three of these restructurings (Iraq, Nigeria, and Myanmar) backed a political regime change, and account for close to 99 percent of the debt relief granted under the Evian Approach since its inception.²² This suggests that the involvement of the Paris Club with middle-income countries was partially guided by the political objectives of creditor governments. The Evian Approach, therefore, may be interpreted as another broadening of the functions of the Paris Club that moved it closer to becoming a diplomatic tool for its members.

In sum, this section has reviewed the history of the Paris Club, emphasizing the gradual process through which it mutated from being a mere debt collector to becoming a provider of debt relief. The remainder of the paper analyzes the macroeconomic implications of this increasing willingness and ability of the Paris Club to deliver net present value and nominal relief to its debtors.

²² Iraq's 2004 Evian debt treatment was approved one year after the Second Gulf War and the appointment of a transitional government in Baghdad. The nominal debt reduction associated with that deal amounted to almost US\$30 billion (about 80 percent of the debt owed to the Paris Club), the biggest debt relief ever granted by the Paris Club. In turn, Nigeria's restructuring in 2005 was the second-largest Paris Club deal. It was signed by newly elected president Obasanjo, who successfully managed to lobby in favor of a "democratic dividend" after 30 years of military regime (Callaghy, 2009). The deal granted the country US\$18 billion debt forgiveness in nominal terms (about 60 percent of the total debt owed to the Paris Club). Myanmar is the last country to have received a debt treatment under the Evian Approach (2013), which included US\$5.6 billion or 60 percent of the debt owed to the Club. At the time, Myanmar was undergoing a transition to democracy after a military dictatorship that lasted for close to 50 years.

III. Macroeconomic Dynamics Before and After Paris Club Agreements

Methodology and Design

To analyze the economic dynamics surrounding official debt restructurings, in this section we adopt a regression-based event approach and compare the evolution of selected macroeconomic and fiscal variables eight quarters before and after Paris Club agreements are reached (see Broner et al., 2013).²³ Our generic regression equation reads as follows:

$$Y_{i,t} = \alpha_i + \gamma_i t + \sum_{s=-8}^{s=8} \beta_{t+s} event_PC_{i,t+s} + \epsilon_{i,t}$$

The dependent variable $Y_{i,t}$ is a vector of macroeconomic and fiscal variables. It includes real GDP growth, government debt, fiscal expenditure, revenues and deficits, and principal and interest payments on public debt. Except for real GDP growth, all these variables are scaled by the level of nominal GDP. Given that our dataset on Paris Club events is quarterly while the macroeconomic and fiscal variables that we use are only available yearly, we resort to a linear interpolation to transform them into a quarterly frequency. $event_PC_{i,t+s}$ is a dummy variable indicating whether a Paris Club restructuring event takes place at time t .

In addition to this generic specification, we explore different features of Paris Club restructurings by comparing the agreements that involved a nominal haircut from those that did not. In the latter category, we further distinguish between the restructurings that carried a high NPV relief and those that had a lower NPV relief. β_{t+s} is the vector of coefficients of our interest. We examine whether β_{t+s} vary significantly before and after Paris Club restructurings and whether they are significantly different across our various subsamples. For this, we apply one-sided Wald tests.

In general, we test the following null and alternative hypotheses to compare the coefficients of a given type of event i , s quarters before and after a restructuring:

$$H_0: \beta_{t-s}^i \leq \beta_{t+s}^i, s = 1, 2, 3, \dots, 8$$

$$H_a: \beta_{t-s}^i > \beta_{t+s}^i, s = 1, 2, 3, \dots, 8$$

²³ We run robustness checks using different windows (i.e., 6, 10, and 12 quarters before and after a Paris Club restructuring event) and the results do not change (to be verified).

We test the following null and alternative hypotheses to compare the coefficients of two subsamples i and j (e.g., with or without nominal haircut) at a given time point:

$$H_0: \beta_{t+s}^i \leq \beta_{t+s}^j, s = -8, -7, \dots, 7, 8$$

$$H_a: \beta_{t+s}^i > \beta_{t+s}^j, s = -8, -7, \dots, 7, 8$$

We report the p value of the one-sided Wald test in the regression table. When $p < 0.1$, we strongly reject the null hypothesis and accept the alternative hypothesis. Vice versa, when $p > 0.1$, we fail to reject the null hypothesis but can alternatively strongly reject the alternative hypothesis. To keep the paper tractable, we present the main results from our event analysis in a visual way.²⁴

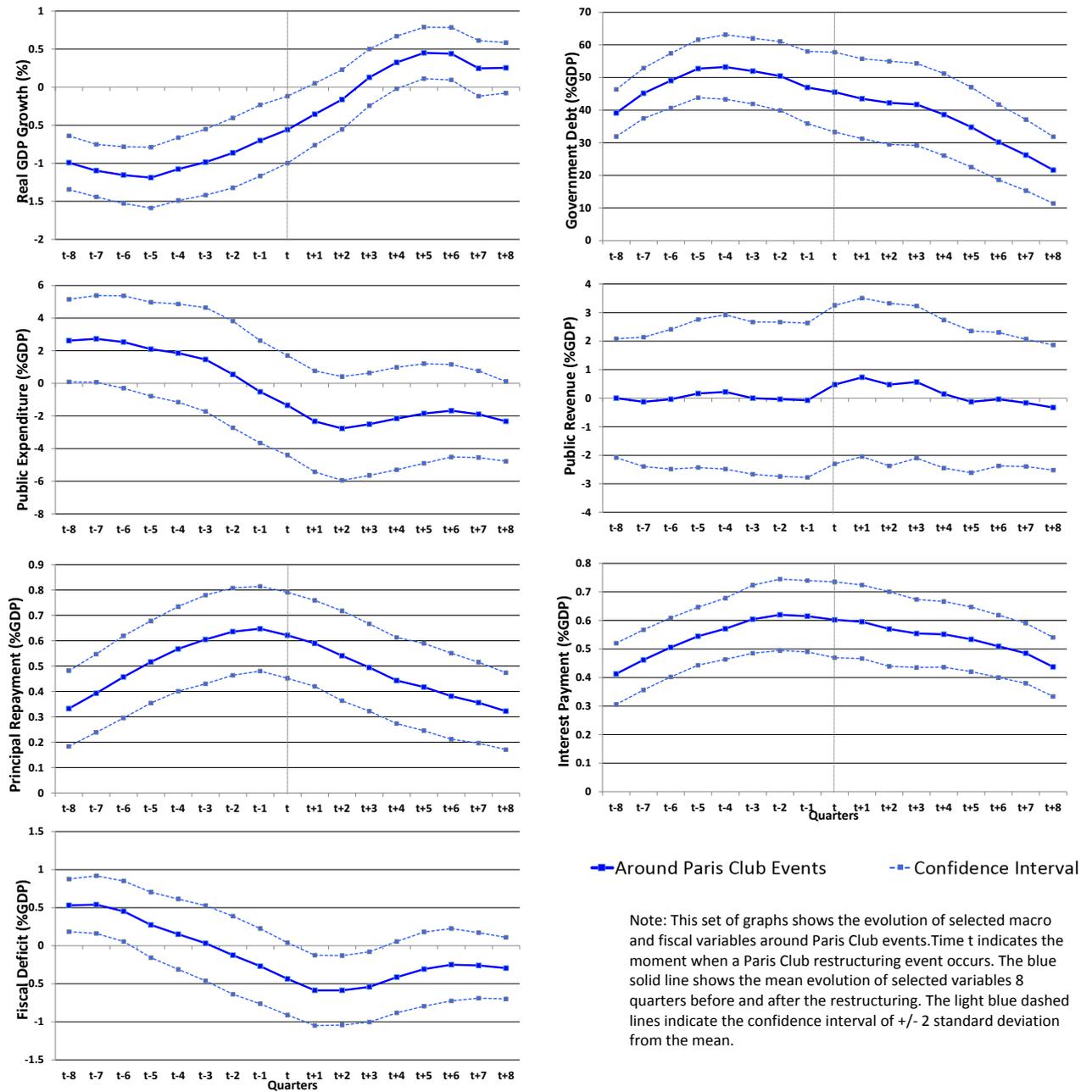
Stylized fact 1: Economic growth accelerates in the aftermath of Paris Club agreements.

When examining our full sample of events, we observe that real economic growth rates are negative before and in the immediate aftermath of Paris Club restructurings, but go into positive territory after four quarters with a strong statistical significance (see Figure 5). The one-sided Wald test confirms that the coefficients after the restructuring are unambiguously higher than before.

In turn, public debt starts to decline five quarters before the Paris Club treatment, and remains on a downward sloping path throughout the window considered. However, the one-sided Wald test fails to reject the null hypothesis (with a type I error of 0.002) that debt levels are higher before than after the restructuring. Public expenditure and the fiscal balance follow a similar path, both starting to fall eight quarters before the debt restructuring takes place, and increasing again one quarter after the restructuring. However, statistically speaking post-restructuring expenditure and deficits are both below their pre-restructuring level at a significance level of 99 percent. The debt service burden, both principal and interest payments, present a bell shape, with payments peaking one or two quarters before the restructuring event.

²⁴ Regression and Wald test results are available upon request.

Figure 5: The Effect of Paris Club Treatments



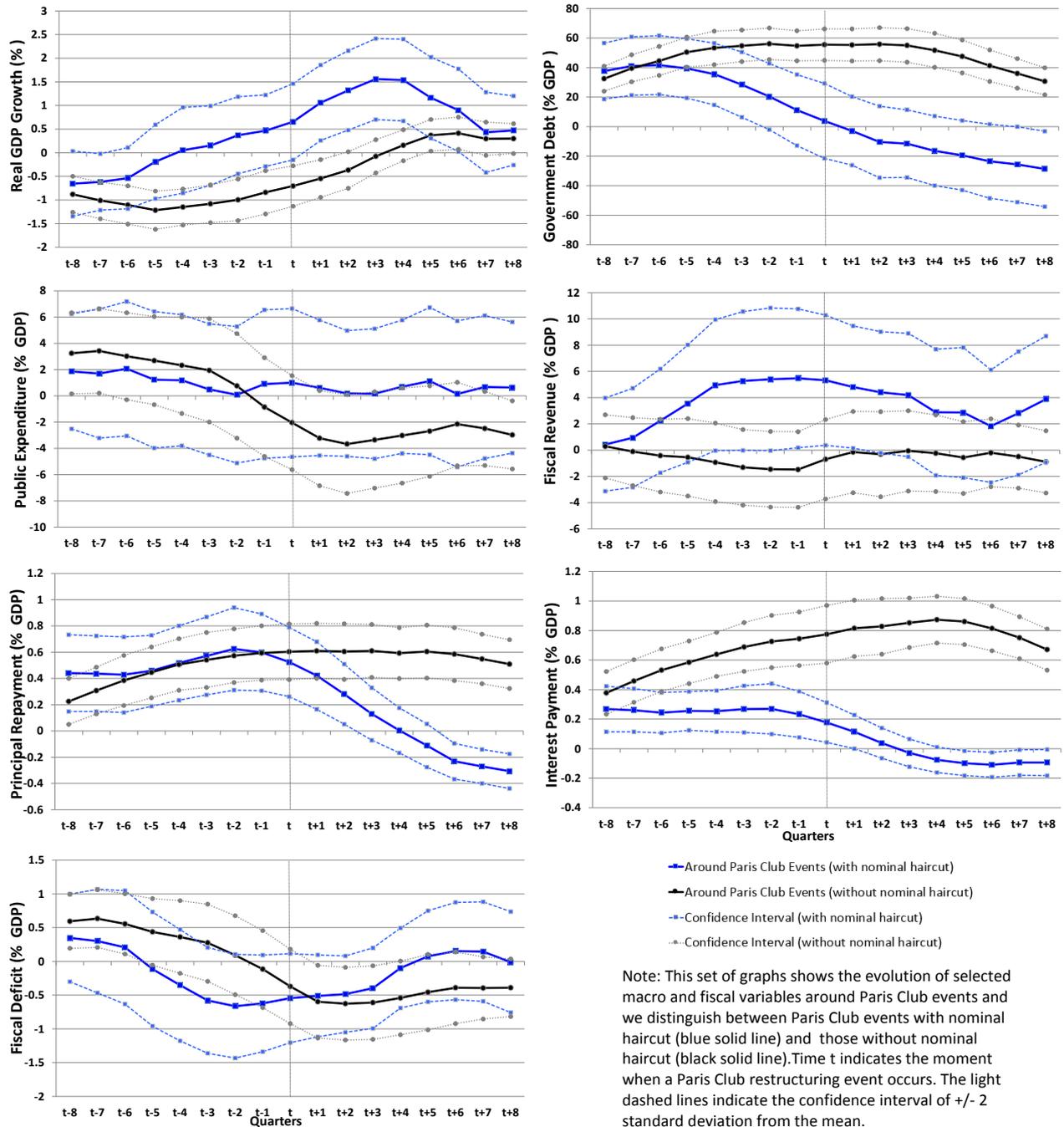
Sources: Authors' Calculations

Stylized fact 2: Restructurings carrying nominal and high NPV relief deliver the strongest impact on economic activity.

What are the economic implications of the increasing ability and willingness of the Paris Club to provide debt relief both in NPV and in nominal terms? Our data suggests that the restructurings that granted nominal debt relief are correlated with better economic dynamics: as shown in Figure 6, post-restructuring real GDP growth rates are on average significantly

higher in these events than in those that did not carry a nominal haircut. Moreover, nominal debt relief episodes are also associated with lower public debt ratios and with a lower debt service burden in terms of principal and interest payments.

Figure 6: Event Analysis - Nominal Haircut vs. Non-nominal Haircut



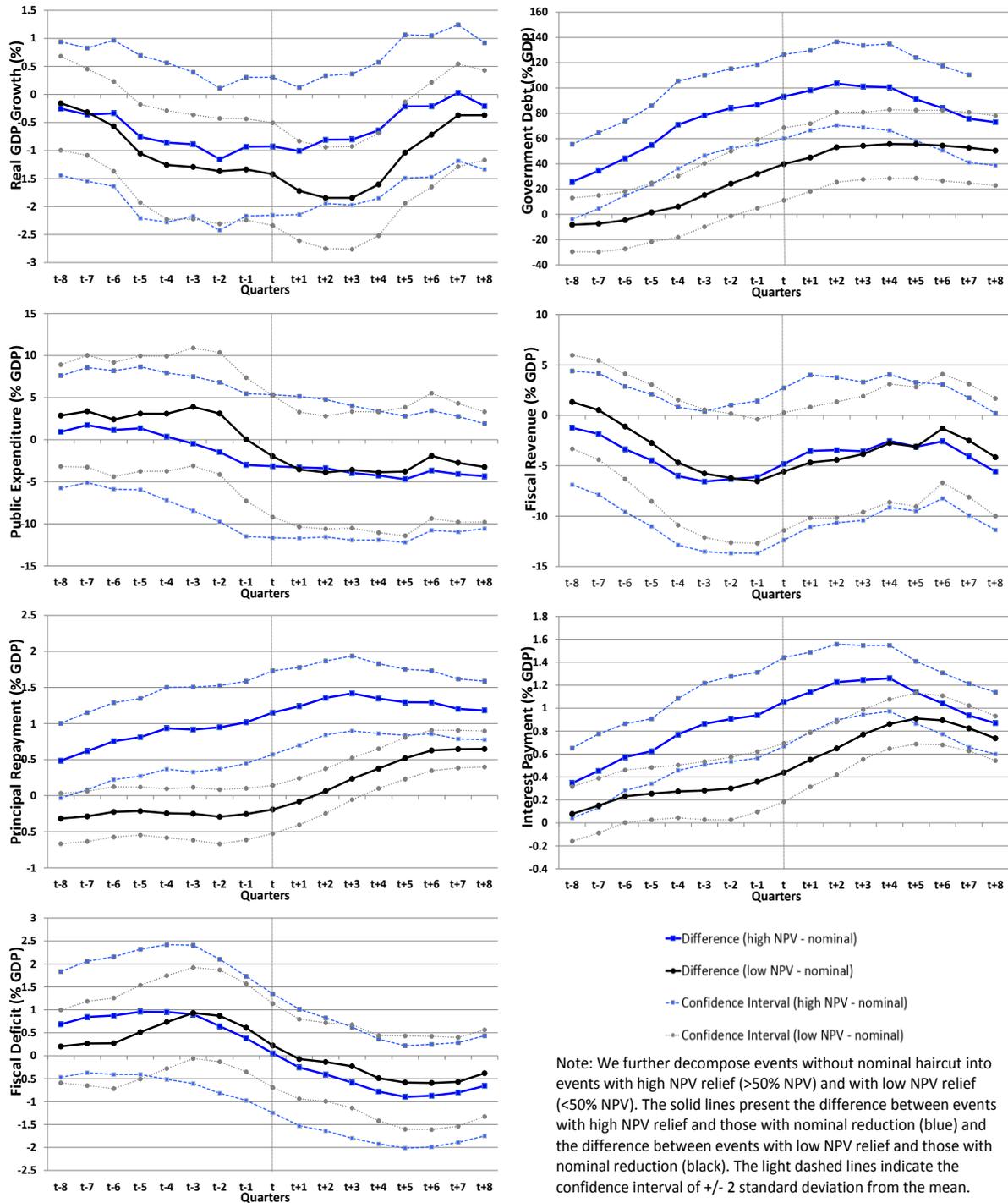
Sources: Authors' Calculations

To dig deeper into Paris Club restructurings without nominal haircuts, we distinguish between events that delivered high NPV relief (above 50 percent of the debt treated) and

events with low NPV relief (less than 50 percent of the debt treated). We then run an augmented version of the generic regression equation as follows:

$$\begin{aligned}
 Y_{i,t} = & \alpha_i + \gamma_i t + \sum_{s=-8}^{s=8} \beta_{t+s}^{nominal} eventPC_{i,t+s}^{nominal} + \sum_{s=-8}^{s=8} \beta_{t+s}^{highNPV} eventPC_{i,t+s}^{highNPV} \\
 & + \sum_{s=-8}^{s=8} \beta_{t+s}^{lowNPV} eventPC_{i,t+s}^{lowNPV} + \epsilon_{i,t}
 \end{aligned}$$

Figure 7: Event Analysis - High vs. Low NPV Relief (relative to nominal haircut)



Sources: Authors' Calculations

Based on the regression results and the one-sided Wald test, we observe that regardless of the degree of NPV relief, real economic growth is higher after the restructuring while the fiscal deficit is lower. However, we only find a statistically sufficient improvement

(with a significance level of 94.7 percent) of the government debt-to-GDP ratio in events with high NPV relief.

To what extent do NPV relief operations differ from restructurings carrying a nominal haircut? This question has important policy implications given that nominal debt reductions are sometimes forbidden by law, as is the case of the European Union. Figure 7 presents the results comparing the events with high and low NPV relief relative to a benchmark scenario with a nominal haircut. The first salient result that we observe is that there is no statistically significant difference in growth rates between the cases in which official debt restructurings carried a nominal haircut and those that did not but carried high NPV relief. In contrast, events with low NPV relief are associated with significantly worse growth dynamics after the restructuring than events with nominal debt reduction.²⁵

Stylized fact 3: Debt restructuring modalities matter.

Another historical trend emphasized in Section II is the gradual proliferation of new terms of treatment in the toolkit of the Paris Club. Table 3 summarizes the main descriptive statistics on the various types of agreements (except for Evian terms).

Table 3: Evolution of Paris Club Terms of Treatment

	Number of Agreements	Countries	Amount Treated (billion US\$)	Nominal Relief (billion US\$)	Nominal relief % Amount Treated	NPV Relief	Agreements per Country
Ad Hoc	33	25	238.9	53.5	22.4	-	1.3
Classic	165	58	153.9	0.0	0.0	0%	2.8
Toronto	28	20	6.1	0.0	0.0	33%	1.4
Houston	35	21	72.0	0.0	0.0	0%	1.7
London	26	23	8.6	0.0	0.0	50%	1.1
Naples	47	33	31.6	8.4	26.7	67%	1.4
Naples 50%	6	4	3.1	0.2	5.7	50%	1.5
Lyon	7	5	6.0	0.9	15.1	80%	1.4
Cologne	39	32	24.2	6.0	24.9	90%	1.2
HIPC Exit	36	36	36.8	24.0	65.3	-	1.0
Total	422	86	581.2	93.1	16.0		4.9

Sources: Authors' Calculations

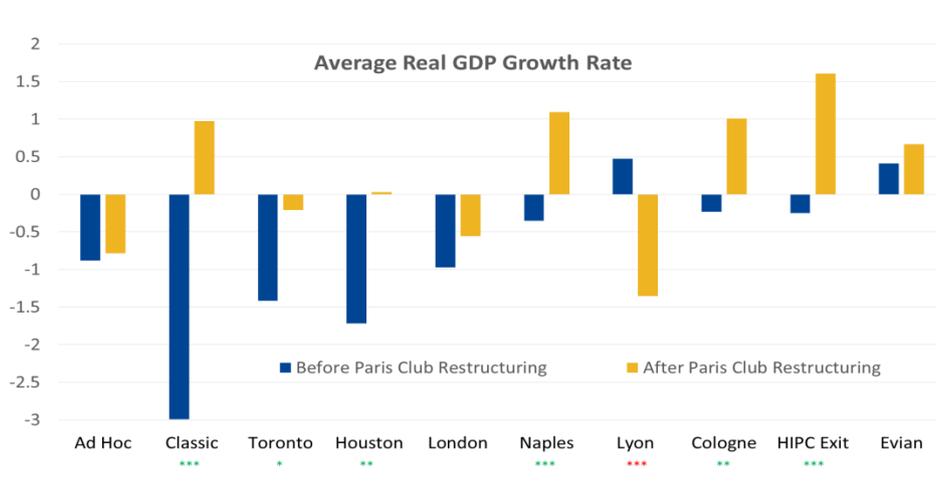
To assess the differential impact of these restructuring modalities, we now repeat our event analysis using all subsamples of Paris Club terms of treatment. The new regression specification is stated as follows:

²⁵ Figure A2 in Appendix 2 further presents the differences between events with higher or lower NPV relief. Growth rate is unambiguously higher with events having benefitted from higher NPV relief. Events with high NPV relief are also significantly associated with higher government debt throughout the window considered.

$$Y_{i,t} = \alpha_i + \gamma_i t + \sum_{terms} \sum_{s=-8}^{s=8} \beta_{t+s}^{terms} eventPC_{i,t+s}^{terms} + \epsilon_{i,t} \text{ where terms} \\ \in \{Ad\ hoc, Classic, \dots Evian\}$$

We focus primarily on whether growth rates are significantly higher after official debt restructurings under the different terms of treatment, and on whether this improvement depends on the terms of treatment applied. As before, we run the one-sided Wald test to compare real GDP growth before and after a Paris Club restructuring event under a given term of treatment. Figure 8 graphically shows the test results: the blue bars indicate the average growth rate before the restructuring agreement is reached, while the yellow bars show the situation afterward. We observe that after the introduction of the Naples terms in 1995, Paris Club treatments seem to have become better able to turn negative growth rates into economic expansion. Although this analysis does not imply causality, our result suggests that the debt relief initiatives conducted by the Paris Club in past decades may have been a success to the extent that they were aimed at stimulating economic growth. Interestingly, however, the Classic terms of treatment also seem to be associated with an improvement in growth, which raises doubts about the previous assessment given that these terms of treatment are the mildest in terms of debt relief.

Figure 8: One-sided Wald Test - Real GDP Growth Before and After Restructuring



Note: Stars indicate the different significance level. While the green stars indicate that post-restructuring growth is higher than pre-restructuring, the red stars indicate the opposite. *** p<0.01, ** p<0.05, * p<0.1.

Sources: Authors' Calculations

In addition, we test whether growth rates are statistically different between any two pairs of terms, before and after a restructuring event. Namely, we test the following null hypothesis:

$$H_0: \sum_{t=-8}^{-1} \beta_t^{term,i} \leq \sum_{t=-8}^{-1} \beta_t^{term,j}, \text{ or } H_0: \sum_{t=1}^8 \beta_t^{term,i} \leq \sum_{t=1}^8 \beta_t^{term,j}$$

The p-values of this statistical exercise are summarized in the matrices below. Table 4 confirms that Classic terms are associated with significantly higher post-restructuring growth rates than Toronto, Houston, London, and Lyon terms after the restructuring (yellow cells), although pre-restructuring we do not find statistically significant differences in growth (white cells). We also find that, in terms of growth, the Lyon terms are clearly inferior to the Classic, Houston and Naples terms and to all the post-Lyon terms, a result that is even clearer when we narrow down our focus to HIPC and IDA countries only. Indeed, Table 5 shows that the Lyon terms are strictly inferior to the Naples term, but also to all the other terms of treatment for which HIPC countries are eligible, that is, Cologne and HIPC Exit terms.

Table 4: Cross-term Comparison - All Terms

<u>Pre-restructuring</u>										
	Ad Hoc	Classic	Toronto	Houston	London	Naples	Lyon	Cologne	HIPC Exit	Evian
Ad Hoc										
Classic	0.181									
Toronto	0.444	0.828								
Houston	0.427	0.789	0.474							
London	0.471	0.847	0.538	0.56						
Naples	0.909	0.998	0.9732	0.968	0.977					
Lyon	0.983	1	0.999717	0.998	0.999	0.896				
Cologne	0.932	0.999	0.99317	0.979	0.99045	0.561	0.069			
HIPC Exit	0.933	0.999	0.99476	0.9779	0.9898	0.591	0.121	0.527		
Evian	0.923	0.985	0.945	0.955	0.94	0.702	0.508	0.68	0.669	

<u>Post-restructuring</u>										
	Ad Hoc	Classic	Toronto	Houston	London	Naples	Lyon	Cologne	HIPC Exit	Evian
Ad Hoc										
Classic	0.998									
Toronto	0.91	0.0163								
Houston	0.965	0.0445	0.769							
London	0.688	0.0153	0.266	0.121						
Naples	0.999	0.539	0.99528	0.93	0.994					
Lyon	0.702	0.00422	0.232	0.0774	0.493	0.002				
Cologne	0.997	0.523	0.9753	0.894	0.9837	0.491	0.99257			
HIPC Exit	0.999	0.682	0.99252	0.9652	0.99556	0.662	0.999423	0.629		
Evian	0.99	0.364	0.906	0.765	0.949	0.333	0.966	0.357	0.24	

Sources: Authors' Calculations

Table 5: Cross-term Comparison - for HIPC and IDA Countries Only

<u>Pre-restructuring</u>							
	Ad Hoc	Toronto	London	Naples	Lyon	Cologne	HIPC Exit
Ad Hoc							
Toronto	0.444						
London	0.471	0.538					
Naples	0.909	0.9732	0.977				
Lyon	0.983	0.999717	0.999	0.896			
Cologne	0.932	0.99317	0.99045	0.561	0.069		
HIPC Exit	0.933	0.99476	0.9898	0.591	0.121	0.527	

<u>Post-restructuring</u>							
	Ad Hoc	Toronto	London	Naples	Lyon	Cologne	HIPC Exit
Ad Hoc							
Toronto	0.91						
London	0.688	0.266					
Naples	0.999	0.99528	0.994				
Lyon	0.702	0.232	0.493	0.002			
Cologne	0.997	0.9753	0.9837	0.491	0.99257		
HIPC Exit	0.999	0.99252	0.99556	0.662	0.999423	0.629	

Note: Blue cells correspond to a situation where growth rates associated with a restructuring having the term presented in the column is smaller than that around an agreement using the terms presented in the row. Yellow cells indicate the opposite.

Sources: Authors' Calculations

IV. Estimating the Macroeconomic Effects of Official Debt Restructurings

Methodology and general results

As amply discussed in the literature, understanding the macroeconomic effects of sovereign defaults is not easy. This is because defaults are endogenous to countries' economic circumstances, thus complicating the task of extracting the structural effects that debt-restructuring events may have. One way to overcome this technical difficulty is to look only at default events that can be regarded as exogenously determined. For instance, Reinhart and Trebesch (2015) look at collectively orchestrated restructurings, such as war debt restructurings in the 1930s for advanced economies, or the Brady plan in the 1980s for Latin American countries. Forni et al. (2016) use the same approach and consider private restructurings after a Paris Club event as exogenous. Kuvshinov and Zimmermann (2016) present an alternative approach to measure the effects of sovereign restructurings of privately

held debt by estimating impulse-response functions (IRFs). They argue that this modelling technique is suitable because it explicitly controls for endogenous feedbacks, which are inherent to the dynamic relationship between defaults and the macroeconomic context in which they occur.

In line with Reinhart and Trebesch (2016), we argue that Paris Club treatments, especially changes to the terms of debt relief, are politically motivated and not driven by any country's specific circumstances. This implies our events can be regarded as exogenous. In addition, we also follow Kuvshinov and Zimmermann (2016), and study the impact of Paris Club restructurings on economic outcomes by estimating IRFs that control for dynamic feedback effects. Our IRF estimation strategy uses local projections (LP) methods, as in Jorda (2005) and Stock and Watson (2007). This methodology allows us to directly project the behavioral response of selected macroeconomic variables to the signing of a Paris Club agreement by computing estimates of the h -step ahead cumulative average treatment effect while controlling for a host of factors and lagged terms.²⁶ In practice, local projections are regression-adjusted difference-in-difference estimates that collapse the time series information in a pre- and a post- period for each step ahead. Moreover, as described by Jorda (2005), local projections are robust to misspecification.

In our basic linear specification, the response of our variables of interest to the signing of a Paris Club agreement h periods before is obtained from the following equation:

$$\Delta Y_{i,t+h} = \alpha_{i,h} + \beta_h PC_{it} + \Psi_h(L) \Delta X_{i,t-1} + \sigma_{t,h} + \mu_{i,t,h},$$

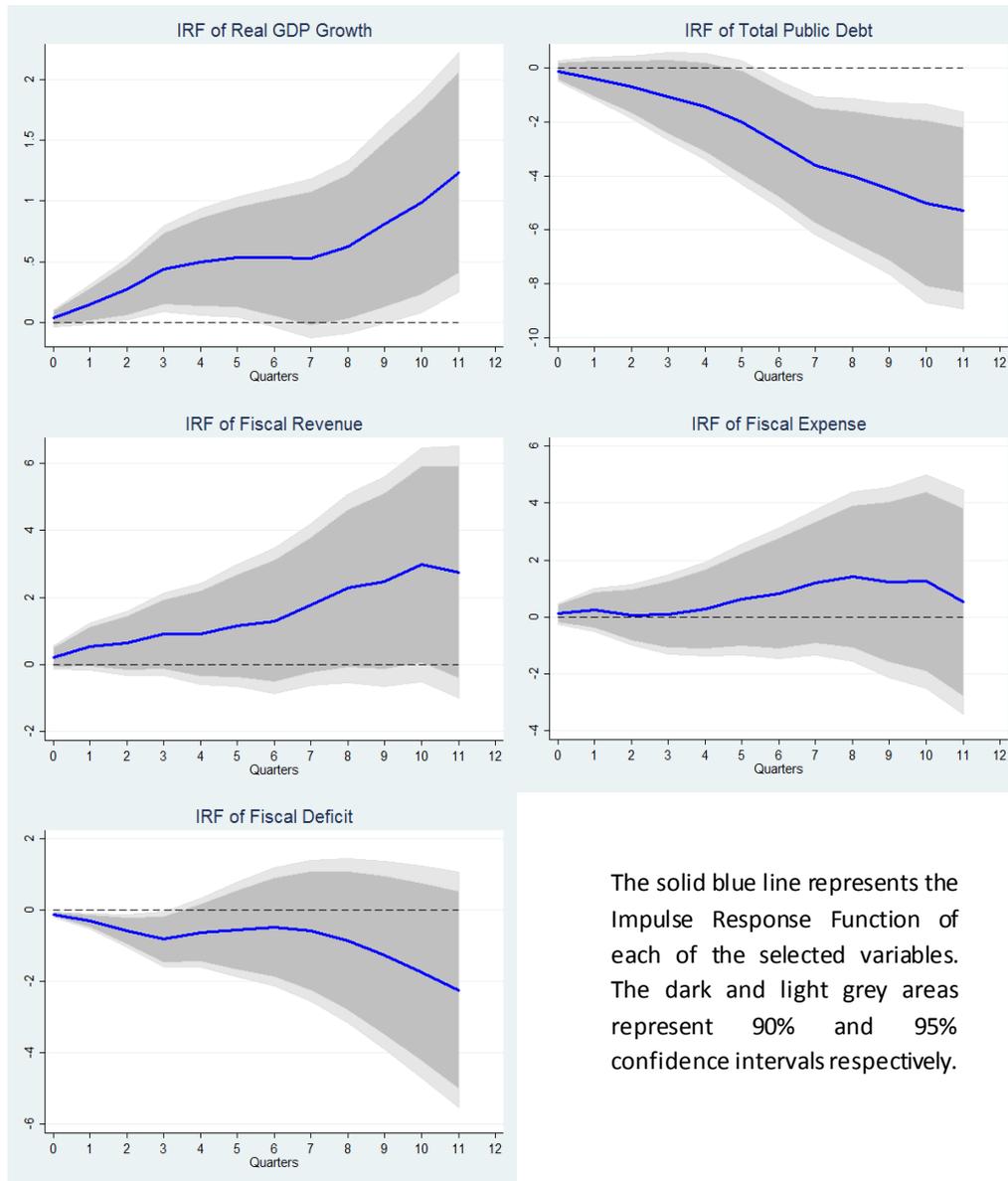
where $\Delta Y_{i,t+h} = Y_{i,t+h} - Y_{i,t}$, represents the accumulated change in our variable of interest at time $t+h$ relative to time t . PC_{it} – as in Section III – refers to the dummy variable capturing the signing of a Paris Club treatment. $X_{i,t-1}$ is a set of lagged control variables including growth, public debt, fiscal deficit, inflation and global factors (U.S. 10-year yields and world real GDP growth). Finally, we include a full set of country and year dummies. Every equation for each h is estimated using robust Driscoll and Kraay (1998) standard errors to correct for potential heteroskedasticity, autocorrelation in the lags, and error correlation across panels. The results of running this analysis are depicted in Figure below.

Our analysis shows that Paris Club restructurings have a clearly positive effect on

²⁶ As explained in Ramey and Zubairy (2014), since local projections do not impose any restrictions linking the impulse responses at h and $h+1$, estimates can display an erratic behaviour due to the loss of efficiency, as the horizon increases. Comparing Jorda (2005) to a standard SVAR, Ramey and Zubairy (2014) finds that the results are qualitatively similar for the first 16 quarters. Since, in this study, we are interested at the short and medium horizon effects we can safely disregard these drawbacks.

growth. Quarterly real GDP growth rate increases steadily after a restructuring event and reaches above 1% two years and half following the restructuring, i.e., an annualized growth rate of more than 4%. In addition, the better economic performance is also associated with a reduction of the stock of total public debt, which becomes statistically significant at the 90% confidence interval five quarters after debt restructuring. Fiscal revenue and expense remain both positive and close to zero but are not statistically significant. Fiscal deficit significantly decreases and enters the negative territory (i.e., fiscal surplus) in the first three quarters following a restructuring. This shows that with the full sample fiscal austerity is observed immediately after a restructuring event and once again two years after the restructuring.

Figure 9: The Effect of Paris Club Agreements



Sources: Authors' Calculations

Nominal and Non-Nominal Debt Relief: How They Differ

As in Section III, we look at the differential impact of various restructuring approaches on the part of the Paris Club. To do so, we expand the equation above by dividing the sample into several mutually exclusive groupings as illustrated below:

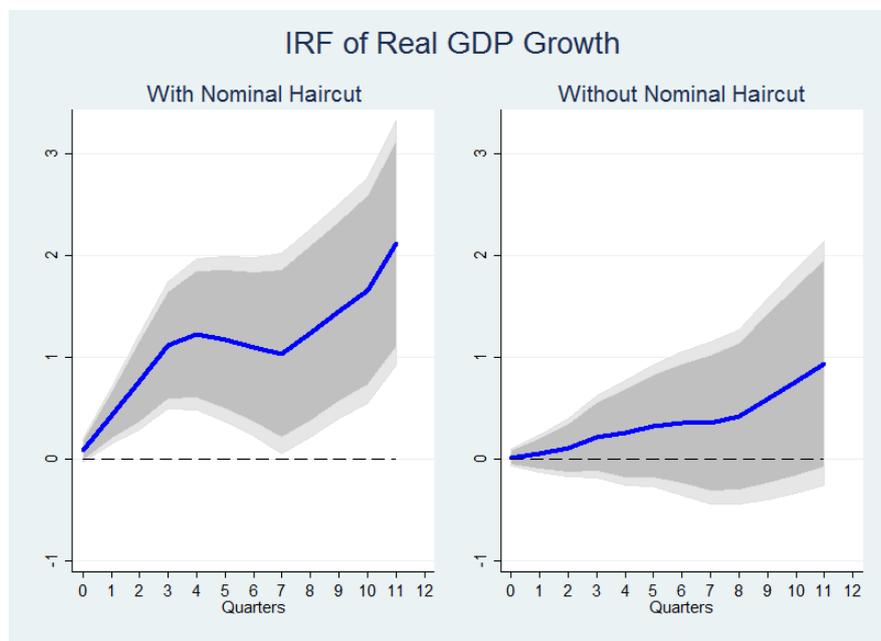
$$\Delta Y_{i,t+h} = \alpha_{i,h} + \beta^A_h PC_A_{it} + \beta^B_h PC_B_{it} + \beta^C_h PC_C_{it} + \Psi_h(L)\Delta X_{i,t-1} + \sigma_{t,h} + \mu_{i,t,h},$$

For instance, $PC_{A_{it}}$ and $PC_{B_{it}}$ can be Paris Club restructurings with or without nominal haircut. $PC_{A_{it}}$, $PC_{B_{it}}$ and $PC_{C_{it}}$ can refer to events with nominal haircut, events without nominal haircut but with high NPV relief, or events without nominal haircut but with low NPV relief.

Again, following our reading of the evolution of the agreements signed by the Paris Club, and in line with the preliminary evidence presented above, we distinguish between PC agreements carrying a nominal haircut from those that did not. Within this latter category, we then compare the impact of more or less lenient restructurings, that is, between agreements with no nominal haircut but with high or low levels of NPV relief. This allows us to assess whether the increasing NPV relief provided by the Paris Club has had a significantly beneficial impact on the countries receiving them.

We focus on three key variables that we believe are fundamental to understand the economic dynamics following the agreements: real GDP growth, public debt, and fiscal deficits. When we present the empirical results on the different size of NPV relief, we will use the events involving nominal haircut as our benchmark, and express the effect of all other events (higher or lower NPV relief) in the difference with respect to the benchmark.

Figure 10: Growth Dynamics



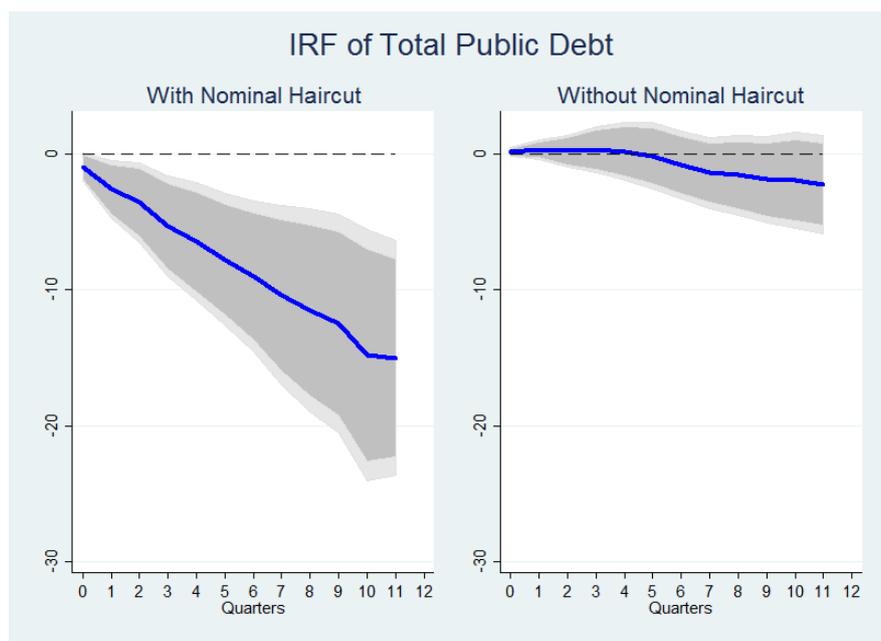
Sources: Authors' Calculations

Figure 10 depicts the IRF of real GDP growth following Paris Club agreements involving a nominal debt reduction (left-hand graph), and those that did not (right-hand

panel). According to our estimates, nominal haircuts are associated with statistically significant and higher growth rates. Remarkably, we find that two years and half after a restructuring agreement, real GDP growth reaches 2% quarter-on-quarter in the countries that were granted a nominal debt reduction. On the contrary, real GDP growth rate is not significantly different from zero in the countries that only received NPV relief.

In turn, according to Figure 11, debt dynamics are more benign following a nominal debt reduction, as one would a priori expect. Indeed, debt falls significantly after Paris Club agreements carrying nominal debt relief, while we do not observe any significant effect on the debt stock following debt reprofiling. In fact, two years and half after the Paris Club agreement, the change in the debt stock is 15% lower with nominal haircut events while it is not significantly different from zero with reprofiling events.

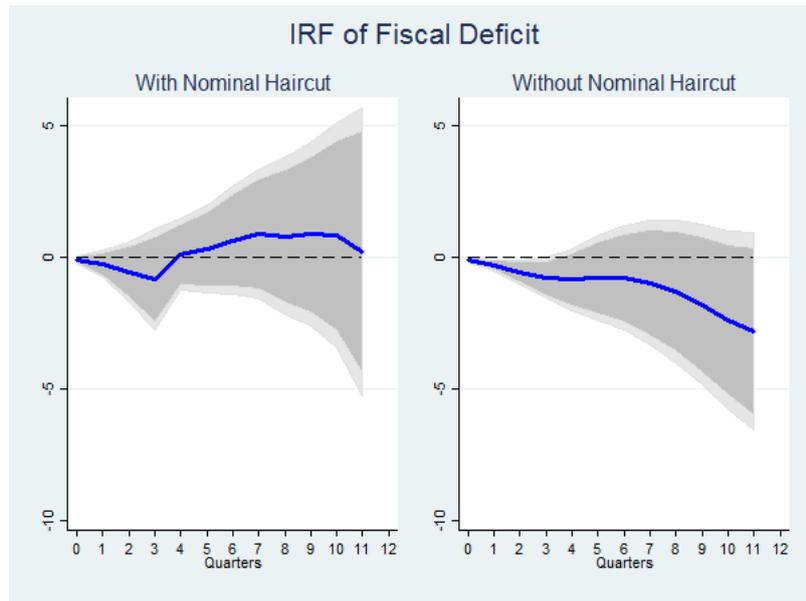
Figure 11: Debt Dynamics



Sources: Authors' Calculations

Next, we study the dynamics of fiscal deficits (in Figure 12, a positive value means a deficit). Quite remarkably, we find that while nominal debt reductions are not accompanied by significant changes in fiscal deficits, debt reprofiling has a significant, albeit short-lived, effect on deficits, which fall during the first three quarters following a restructuring agreement. Our finding shows that countries that only received debt reprofiling generated fiscal surplus immediately after the restructuring.

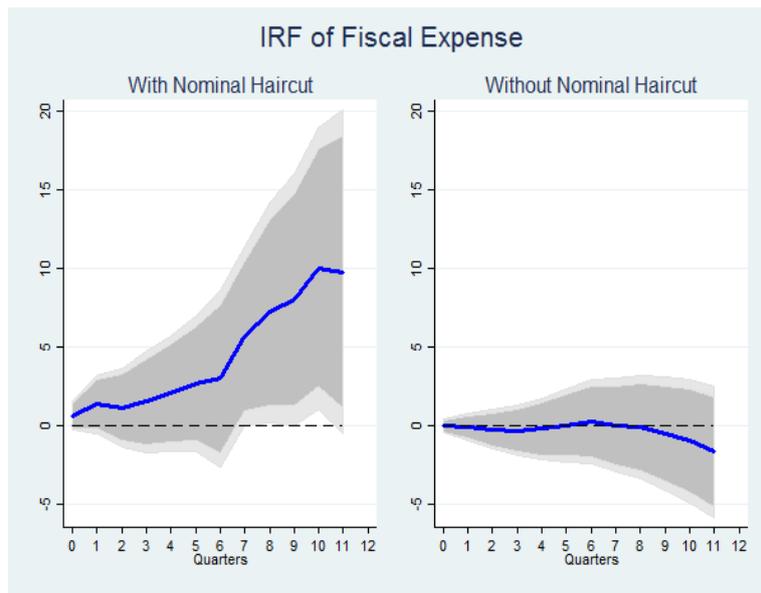
Figure 12: Fiscal Stance



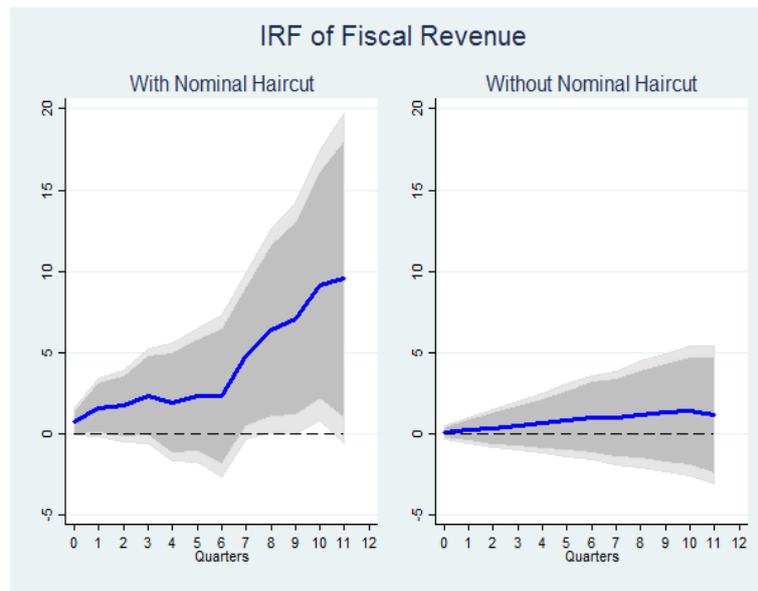
Sources: Authors' Calculations

Finally, we explore the drivers of the different fiscal performance by separately analyzing the dynamics of government expenses and government revenues. The results presented in Figure 13 and 14 show both fiscal expense and revenue are significantly higher seven quarters after a restructuring event.

Figure 13: Dynamics of Public Expenditures



Sources: Authors' Calculations

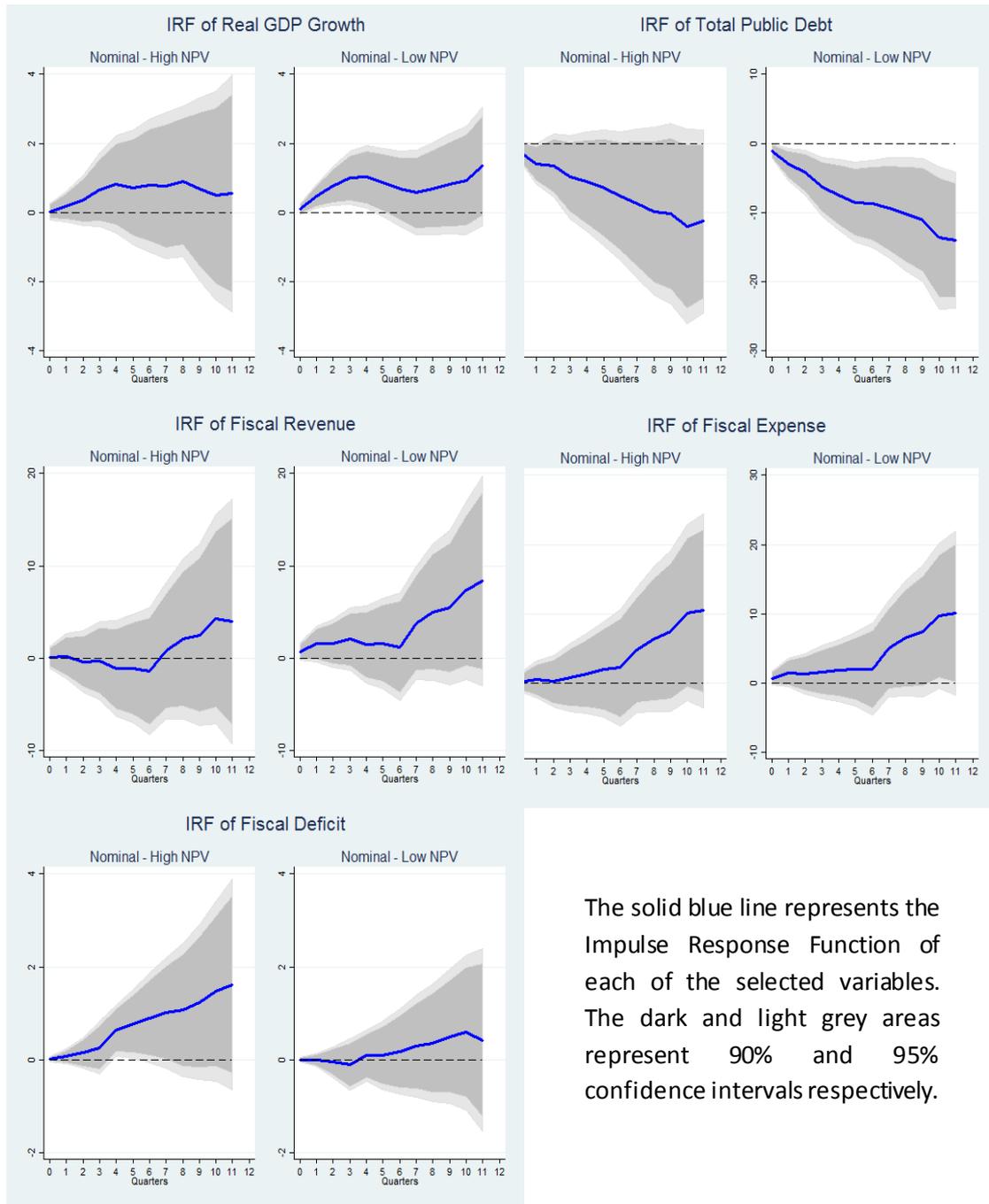
Figure 14: Dynamics of Public Revenues

Sources: Authors' Calculations

Playing with the Terms: Are all Non-nominal Debt Relief Operations the Same?

Our local projections analysis separated Paris Club agreements in three categories, allowing us to assess the extent to which restructurings carrying no nominal haircut have different effects depending on the extent to which they provide high or low NPV relief. Figure 15 presents the difference in dynamics between countries obtaining treatments with NPV relief above the sample average, and countries where the NPV was below the sample average. The results are instructive. First, we observe that there is no statistically significant difference between events with nominal haircut and those with high-NPV debt reprofiling. In comparison, events with nominal haircut seems to generate better growth – at least in the immediate aftermath of a restructuring – than those with only low-NPV debt reprofiling. Second, debt stock is unambiguously lower in countries that received nominal debt reduction than in countries having only received debt reprofiling. This difference is even more statistically persistent when debt reprofiling only provide low-NPV relief. Finally, countries that received nominal debt reduction seem to have significantly higher fiscal deficit than countries that received high-NPV debt treatment. Together with the results shown in Figure 12, our study points to a perverse trade-off that has been long recognized in the theoretical literature: providing nominal relief is good for growth and reduces debt, but seems to incentivize the accumulation of additional debt.

Figure 15: Comparing High and Low NPV Debt Reprofiting Events



Sources: Authors' Calculations

Implications for HIPCs

As a final exercise, we apply our Local Projection methods to a subsample of our dataset: HIPC's. Two factors motivate this exercise. First, 60% of Paris Club events in our sample involve highly indebted poor countries (256 out of total 422 events). This group of countries have always received much attention as they have been long suffering from debt overhang problems. Both nominal haircut and relief in NPV terms were provided to these countries, especially since the creation of the HIPC initiative by the IMF and the World Bank since 1996. Second, from an econometric perspective, using this subsample alleviates the endogeneity problem our empirical study is facing. In fact, the timing of debt relief can be endogenously chosen, since countries often face adverse economic development before debt restructuring and often renegotiate their debt after economic situations start to improve. In line with Reinhart and Trebesch (2016) and Forni (2016), one solution is to adopt the identification strategy of Arslanalp and Henry (2005) and to focus on centrally orchestrated debt relief events, i.e., HIPC's initiative in our sample. This exercise can also serve as a robustness check of the main results presented in previous sections.

We present the main results using the HIPC subsample in Appendix 3. First, if we look at the overall events of Paris Club Agreements involving HIPC's on selected macroeconomic variables (Figure A3.1.), the results are very much similar to that of the whole sample (Figure 9). HIPC's seem to exhibit higher growth rate in the immediate aftermath of Paris Club restructurings. However, the overall debt stock does not seem to decline with statistical significance. Fiscal revenue and expense are both on an increasing path with the 95% of confidence interval, leading to a more ambiguous fiscal deficit.

A more detailed look at the differences between the events providing nominal haircut and non-nominal restructurings with a high or low size of NPV relief also confirms the main results presented in Section IV (Figure A3.2.). There is no significant difference between the whole sample and the HIPC subsample.

V. Conclusion

Although it has been around for nearly 60 years and played a crucial role in the resolution of several debt overhangs, the Paris Club has received relatively little scholarly attention. This paper has attempted to fill that gap, providing three main contributions to the growing literature on official debt restructurings. First, we studied the history of the Paris Club, emphasizing the changes that gradually shaped the role that it has come to play in the

international financial architecture. Second, we constructed a database with over 400 official debt restructurings conducted through the Paris Club, containing detailed information about the characteristics of each agreement. Third, we used this database to study the dynamic response of several macroeconomic variables to the signing of a Paris Club treatment. To do so, we initially applied a regression-based event approach, and then we used local projection techniques, which allowed us to infer causality.

The Paris Club was originally intended to function as a mere debt collector. Accordingly, the debt restructurings that it conducted were considered a last resort option to avoid sovereign defaults, and its financial terms were essentially determined by debtors' short-term capacity to repay. Starting in the late 1980s, this dogma was gradually abandoned as the Paris Club began to be seen as an instrument suitable to pursue broader objectives, such as the restoration of debt sustainability, international development, and even political regime change in strategically important countries. To pursue those objectives, new terms of treatment were progressively added to the toolkit of the Paris Club, all of them going in the direction of sequentially providing more generous conditions to selected groups of debtors. In so doing, we argued that the Paris Club was gradually transformed from a debt collector to a relief provider.

What are the economic implications of this reform process? This paper finds that Paris Club treatments can have a significant impact on economic growth, which somewhat vindicates the official debt relief initiatives that have been conducted since the 1990s to improve the performance of HIPC countries. However, not all agreements have the same effect, and some types of treatment may have no impact on growth at all. In fact, we find that only those restructurings that carry a nominal haircut seem to unambiguously raise the economic prospects of debtors: remarkably, such agreements lead, on average, to 6 percent higher GDP after two years. By contrast, Paris Club treatments carrying only NPV relief have no positive impact on growth. However, the countries that get these restructuring conditions turn out to be more likely to pursue a prudent fiscal policy after the event than those receiving a nominal haircut. Therefore, our results suggest that, when designing a debt restructuring, the official sector faces a trade-off between the objectives of stimulating economic growth and promoting fiscal prudence. Thus, pursuing both objectives simultaneously may prove to be a difficult task.

Our paper has not explored the specific mechanisms through which different types of official debt restructurings may unleash distinct macroeconomic dynamics, which is a topic for future research. However, some hypotheses may be advanced. It might be that nominal

haircuts stimulate economic growth because such restructurings are better able to restore investors' confidence. Instead, investors may view NPV relief operations as temporary fixes that simply kick the problem forward. Thus, such agreements may not raise investment (either domestic or external), thus failing to accelerate growth. The differential response of investors and financiers to the specific features of debt restructurings may also affect countries' ability to finance their deficits, thus contributing to explain the post-restructuring fiscal dynamics that this paper has emphasized. Given the presumed effect of such operations on investor confidence, nominal haircuts may make it easier to fund larger deficits, explaining why we observe that the countries that receive these conditions are less likely to pursue prudent fiscal policies subsequently. In turn, if NPV relief operations do not facilitate access to credit, the countries that take part in these restructurings may be forced to be more persistent in their fiscal consolidation effort.

An alternative explanation is that the nominal debt burden that nations reach in the long term is determined by their preferences or by other structural factors that are not fundamentally altered by a Paris Club restructuring. Therefore, after countries obtain a nominal haircut, they tend to re-converge to the level of indebtedness that reflects their preferences or structural characteristics. Instead, NPV relief operations alter maturities and the profile of interest or principal payments, but not the nominal burden of debt itself. Thus, it might be that such restructurings are less likely to motivate countries to accumulate additional debt to re-converge toward the exogenously determined level of indebtedness that reflects their preferences or structural characteristics.

Finally, the paper provides important insights along which further research can help improve our understanding of the determinants and effects of debt restructuring. Because of the relevance of the Paris Club, though its comparability of treatment clause, as a focal point for private sector debt relief, one overlooked element in the literature we emphasise is the interaction between PSI and OSI, which is essential for understanding the form, timing and macroeconomic effects of sovereign debt restructurings. As an example, we note that the profile of the so-called serial defaulters (Reinhart and Rogoff 2004), countries which default repeatedly, changes dramatically when adding the Paris Club events to those involving PSI. Not only the recurrence of restructuring events doubles, but periods during which a country is facing debt restructuring also change markedly.

Research on sovereign debt restructurings needs to incorporate the interaction between private sector and official sector creditor, and our dataset will allow researchers to pursue that route.

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Appendix 1: Institutional and Operational Features of the Paris Club

Institutional Features of the Paris Club

The group meets regularly (“Tour d’Horizon” meetings) and upon request by the debtor countries (negotiation meetings). The “Tour d’Horizon” are one-day meetings held monthly in Paris to discuss the situation of debtor countries and methodological issues. Tour d’Horizon sessions may include negotiation meetings. Negotiation meetings occur when, after having concluded an agreement with the IMF on a program that shows that the country is unable to meet its external debt obligations and thus needs a new payment arrangement with its external creditors, a debtor country approaches the Paris Club to negotiate a debt treatment. The debt treatment agreement signed between Paris Club creditors and the debtor country at the end of the negotiation meetings is contained in the so-called *Agreed Minutes*. In accordance with Paris Club principles, decisions are taken by consensus. The Chairman of the Paris Club chairs the meetings.²⁷ A permanent Secretariat, in charge of preparing the negotiating sessions and run by a team of French Treasury officials, was set up at the end of the 1970s when the Paris Club’s activity started to become more intense. To gather the most representative array of creditors, the Paris Club recently redefined the rules governing participation in its negotiations. Besides observers from international financial institutions, the current Paris Club’s association framework distinguishes between permanent members, prospective members, and ad hoc participants.²⁸

The characteristics defining a Paris Club agreement, its conditions, and its coverage are laid down in the *Agreed Minutes*. Key to the understanding of the framework in which the Paris Club operates is the nature of this document. Indeed, as the Paris Club is not an institution and has remained strictly informal, the outcomes of its negotiations are not legally binding. Accordingly, the *Agreed Minutes*, signed by the Chair of the Paris Club, the representatives of the debtor country and the representative of each creditor taking part in the negotiations, is a non-legally binding document establishing the minimum debt relief conditions that will guide the bilateral negotiations required for the bilateral agreements to be effective.²⁹ Only the signature of these bilateral agreements confers a legal effect to the agreement reached during the negotiating meeting. While the *Agreed Minutes* constitute only a recommendation to the governments of Paris Club creditors and of the debtor country to conclude bilateral agreements implementing the provisions of these *Agreed Minutes*, in observance of the Paris

²⁷ The head of the French Treasury has traditionally served as Chair.

²⁸ International Monetary Fund and World Bank representatives attend every Paris Club meeting.

²⁹ The debtor is often represented by the Minister of Finance, who heads a delegation of Ministry of Finance and Central Bank officials.

Club principle of solidarity, all members agree to act as a group in their dealings with a given debtor country and thus commit to implement the recommendations contained in the Agreed Minutes. Moreover, under this principle, they also agree to exercise caution with respect to the impact that the management of their claims may have on other members' claims.

Permanent members abide by all Paris Club principles and participate in all Tour meetings and all negotiation meetings (as observers if they hold no claim on the invited debtor country). Ad hoc participants are granted access to Tours d'Horizon sessions based on a signalled interest for specific countries and/or issues. Ad hoc participants' participation is subject to the agreement of permanent members and of the debtor country.³⁰ Finally, prospective members are ad hoc participants, with temporary membership granted upon expression of serious interest in adhering to the Paris Club. Prospective members are expected to adhere to the Paris Club Principles in their entirety and to take extra steps in terms of adherence to the Paris Club's information sharing and solidarity principles. In case of participation in a debt workout, all creditors, irrespective of their level of association, must act in good faith and conform to the six principles of the Paris Club.

Figure A1. Contents of the Agreed Minutes

TOGO Debt Treatment - June 12, 2008	
Supporting agreements with the international institutions	IMF programme supported by an Arrangement under the Poverty Reduction and Growth Facility (PRGF) approved on April 21, 2008 Download the IMF report - PRGF document
Total external debt of the country	\$2100 million as of December 31, 2007, \$973 million of which being due to the Paris Club as of April 01, 2008
Amounts treated	\$740 million, of which \$347 million being canceled, of which \$393 million being rescheduled
Categories of debts treated	treatment of arrears as of March 31, 2008, treatment of maturities falling due from April 01, 2008 up to March 31, 2011
Repayment profile	treatment under Naples 67% terms (cancellation rate of 67%) <ul style="list-style-type: none"> • repayment of non ODA credits over 23 years, with 6 years of grace, after cancellation to a rate of 67% • repayment of ODA credits over 40 years with 16 years of grace
Specific provisions	<p>possibility to conduct debt swaps</p> <p>On a voluntary and bilateral basis, the Government of each Participating Creditor Country or its appropriate institutions may sell or exchange, in the framework of debt for nature, debt for aid, debt for equity swaps or other local currency debt swaps:</p> <p>(i) the amounts of outstanding loans and consolidations as regards ODA debts, with the exception of those administered by IDA and provided by the European Union member States;</p> <p>(ii) the amounts of other outstanding credits, loans and consolidations with the exception of those administered by IDA and provided by the European Union member States, up to 10% of the amounts of outstanding loans, credits and consolidations as of 30 June 1992 or up to an amount of 20 million of dollars of the United States of America, whichever is higher.</p> <p>good will clause</p> <p>Participating Creditor Countries agree to grant a topping-up of the debt reduction to Cologne terms once the Togolese Republic reaches its Decision Point under the Enhanced Debt Initiative for the Heavily Indebted Poor Countries, provided that the Government of the Togolese Republic maintains satisfactory relations with the Participating Creditor Countries and the IMF.</p> <p>Phases</p> <ul style="list-style-type: none"> • First phase : From April 01, 2008 up to March 31, 2009 implemented at the signature of the agreement • Second phase : From April 01, 2009 up to March 31, 2010 implemented at July 17, 2009 • Third phase : From April 01, 2010 up to March 31, 2011 implemented at July 23, 2010 <p>de minimis threshold of 10 000 USD</p>
Comparability of treatment provision	<p>In order to secure comparable treatment of its debt due to all its external public or private creditors, the Government of the Togolese Republic commits to seek from all its external creditors debt reduction and reorganization arrangements on terms comparable in net present value to those set forth in the Agreed Minutes dated 12 June 2008 for credits of comparable maturity. Comparability of treatment for debt reduction in net present value is assessed not only on the basis of the reduction in the face value of the debt but also on the terms of repayment of the debts not cancelled.</p> <p>Consequently, the Government of the Togolese Republic commits to accord all categories of creditors - and in particular creditor countries not participating in the Agreed Minutes dated 12 June 2008, commercial banks and suppliers - a treatment not more favourable than that accorded to the Participating Creditor Countries.</p> <p>For the purpose of the comparison between the arrangements concluded by the Government of the Togolese Republic with its creditors not listed in the Agreed Minutes dated 12 June 2008 on the one hand, and arrangements with the Participating Creditor Countries on the other hand, all relevant elements will be taken into account, including the exposure of the creditors not listed in the Agreed Minutes dated 12 June 2008, the level of cash payments received by those creditors from the Government of the Togolese Republic as compared to their share in the Togolese Republic's external debt, the nature and characteristics of all treatment applied, including debt buy backs, and all characteristics of the negotiated claims and in particular their repayment terms whatever forms they take, and in general the financial relations between the Government of the Togolese Republic and the creditors not listed in the Agreed Minutes dated 12 June 2008.</p>
Cutoff date	January 01, 1983
Organisation of the session	<p>The meeting was chaired by Mr. Julien RENCKI, Vice Chairman of the Club de Paris The head of the debtor country's delegation was Mr. Adj. Ouh AYASSOR, Minister of Economy and Finance</p> <p>Participating creditors AUSTRIA, BELGIUM, CANADA, DENMARK, FRANCE, GERMANY, ITALY, JAPAN, NETHERLANDS, SPAIN, SWEDEN, SWITZERLAND, UNITED KINGDOM</p> <p>Observers RUSSIAN FEDERATION, UNITED STATES OF AMERICA, African Development Bank, IMF, UNCTAD, World Bank</p> <p>Press release Read the press release Download the press release in PDF</p>

Sources: Paris Club

³⁰ Ad hoc participants cannot block consensus.

Paris Club Principles

Despite the limited relevance of the Paris Club from 1956 to 1980s, some of the norms that have defined its role and the commitments accepted by its members were developed during this period. These principles are: (i) solidarity, implying that members agree to act as a group and to avoid taking actions with their debtors that may impact negatively on the claims of the other members of the group; (ii) consensus, implying that Paris Club rescheduling deals must be accepted by all of its members; (iii) conditionality, implying that the debtors that approach the Paris Club for a debt rescheduling are expected to have previously concluded an agreement with the IMF and to be implementing a macroeconomic adjustment program; (iv) a case-by-case approach in the definition of the terms of each rescheduling granted by the members of the group and information sharing; and (vi) comparability of treatment.

Information sharing and solidarity principles are two of the six principles based on which the Paris Club operates. The six principles, detailed in Table A1, underpin the common discipline that creditors agree to respect at all times to facilitate the decision-making process.

Table A1. The Six Principles

Solidarity
All members of the Paris Club agree to act as a group in their dealings with a given debtor country and be sensitive to the effect that the management of their particular claims may have on the claims of other members.
Consensus
Paris Club decisions cannot be taken without a consensus among the participating creditor countries.
Information sharing
The Paris Club is a unique information-sharing forum. Paris Club members regularly share views and information with each other on the situation of debtor countries, benefit from participation by the IMF and World Bank, and share data on their claims on a reciprocal basis. In order for discussions to remain productive, deliberations are kept confidential.
Case by case
The Paris Club makes decisions on a case-by-case basis in order to tailor its action to each debtor country's individual situation. This principle was consolidated by the Evian Approach.
Conditionality
The Paris Club only negotiates debt restructurings with debtor countries that: <ul style="list-style-type: none"> - need debt relief. Debtor countries are expected to provide a precise description of their economic and financial situation, - have implemented and are committed to implementing reforms to restore their economic and financial situation, and - have a demonstrated track record of implementing reforms under an IMF program. This means in practice that the country must have a current program supported by an appropriate arrangement with the IMF (Stand-By, Extended Fund Facility, Poverty Reduction and Growth Facility, Policy Support Instrument). The level of the debt treatment is based on the financing gap identified in the IMF program. In the case of a flow treatment, the consolidation period coincides with the period when the IMF arrangement shows a need for debt relief. When the flow treatment extends over a long period of time (generally more than one year), the Paris Club agreement is divided into phases. The amounts falling due during the first phase are treated as soon as the agreement enters into force. Subsequent phases are implemented following completion of conditions mentioned in the Agreed Minutes, including non-accumulation of arrears and approval of the reviews of the IMF program.
Comparability of treatment
A debtor country that signs an agreement with its Paris Club creditors should not accept from its non-Paris Club commercial and bilateral creditors terms of treatment of its debt less favorable to the debtor than those agreed with the Paris Club.

Source: Paris Club website <http://www.clubdeparis.org/sections/composition/principes/six-principes>

According to the *information sharing principle*, introduced in 2004, permanent members must respond to all data-sharing requests.³¹ This principle highlights the nature of the Paris Club as a unique information-sharing forum. Next, while earlier Paris Club agreements were signed under standardized terms, the Paris Club has evolved to support tailor-made solutions. This belief is embedded in the *case-by-case* principle, which was consolidated in 2004 with the introduction of the Evian Approach. Two other Paris Club principles were strengthened by the introduction of this approach: the *conditionality principle* and the *comparability of treatment* principle.

The conditionality principle requires debtor countries approaching the Paris Club in search of a debt treatment to be under an IMF program and to remain on track in its implementation.³² Indeed, often Paris Club agreements, especially the ones that extend the debt treatment over a long period, are phased and the approval of IMF program reviews are set as preconditions (together with other conditions that might have been established in the Paris Club agreement) to access successive phases of debt treatments.³³

The conditionality principle is also important in that the level of the debt treatment itself is informed by the financing needs identified in the IMF program. Paris Club agreements granting flow treatments aim to close the debtor country's financing gap identified by the IMF in the framework of its program. Flow treatments usually coincide with the period covered by the IMF program, the so called "consolidation period." Only maturities falling due during this period (and, in some cases, also arrears accumulated since its start) are treated. This flow treatment is in opposition to stock treatments. Paris Club stock treatments apply not only to the payments due over a given period (as flows treatments do), but to the entire stock of debt. The aim of stock agreements is to provide a country with the so-called exit treatment.³⁴

Another crucial norm adopted early on by the Paris Club was the comparability of treatment principle. According to this principle, sovereign debtors that reach a rescheduling agreement with the Paris Club are required to seek similar terms from other creditors. Only multilateral organizations have traditionally been excluded from this principle to preserve their preferred

³¹ Beyond workouts, ad hoc and prospective members share data based on reciprocity, although they are encouraged to provide data on claims (see Paris Club 2014 Annual Report).

³² The only exception to this rule has been the 2005 Paris Club Agreement with Nigeria. The country was not under an IMF financial assistance program but was the first country to use the Fund's Policy Support Instrument, a non-financial instrument that enables low-income countries to receive Fund advice and support without a borrowing arrangement.

³³ Underlying this principle is the assumption that the inability to service existing debt reflects poor economic management.

³⁴ Such agreements are used in two cases. Under the HIPC initiative, actions by the Paris Club creditors take the form of a stock treatment granted at *completion point*. For other cases, stock treatments may be granted, on a case-by-case basis, to countries with a satisfactory track record with both the Paris Club and the IMF, and where there is sufficient confidence in the debtor's ability to meet its obligations under the debt agreement.

creditor status. The comparability of treatment principle is aimed at ensuring taxpayers from Paris Club member countries that their claims on debtors are not subordinate to those of private institutions or other bilateral lenders that do not belong to the group. Although this rule has remained in place throughout the history of the Paris Club, its practical implementation and the complexity of getting other creditors to accept it has evolved in line with the changing composition of sovereign debt and the growing diversity of financial instruments in sovereign lending.

What does comparability of treatment mean for different creditor groups?

To ensure balanced treatment of the debtor country's debt by all external creditors, the Paris Club Agreed Minutes include a comparability of treatment clause (CTC). Insistence on fulfilment of the CTC is designed to ensure that Paris Club countries' taxpayers' claims are not subordinated to those of other creditors. Moreover, applying such a clause helps ensure that the agreed debt treatment achieves its intended goal of putting debtor countries' debt burdens on a sustainable path.

Paris Club creditors do not expect the debtor's agreements with other creditors to exactly match the terms of the Paris Club's own agreement. Instead, given the diversity of other possible creditors, they require that the debtor seek terms comparable to the Paris Club's agreement. They also require the debtor to share with the Paris Club the results of its negotiations with other creditors. In practice, Paris Club creditors take a broad-based approach in their assessment of whether a debtor has met the comparability of treatment requirement. Factors for assessing comparability include, for each type of creditor, changes in nominal debt service, net present value (NPV), and duration of the restructured debt. While no kind of debt instrument is inherently protected from treatment, Paris Club creditors do consider on a case-by-case basis whether mitigating factors argue against demanding comparable treatment from a particular creditor or debt instrument. They can make exceptions, for example, when the debt only represents a small proportion of the country's debt burden and when restructuring would unduly interfere with the smooth running of trade. Short-term trade finance is generally excluded from Paris Club rescheduling.

Non-Paris Club official bilateral creditors grant medium- or long-term loans generally similar to those provided by Paris Club creditors. Consequently, non-Paris Club official bilateral creditors often restructure on terms very similar to those agreed within the Paris Club. These creditors may also participate in Paris Club treatments and, under these circumstances, apply the same treatment as the Paris Club.

In contrast, debtors' relations with external private creditors are more complex. There is a long track record of international banks rescheduling their exposures to sovereign borrowers, often through the London Club. The Paris Club's experience is that it can be more difficult to make a direct comparison between the efforts of creditors that choose to reschedule flows and those that restructure their stocks of debt. For example, in recent cases where debtors have sought financial relief from bondholders, the debtors have offered new bonds in exchange for the existing instruments. As a rule, comparability of treatment is assessed based on the effect of private treatments in terms of duration, NPV, and flow relief.

Source: Paris Club website.

<http://www.clubdeparis.org/sections/composition/principes/comparabilite-traitement>

The conditionality principle plays a key role in the multi-staged delivery of debt relief under the Evian Approach. This has affirmed its role as a key prior requirement for debtor countries to receive a *comprehensive debt treatment*. Similarly, with the inception of the Evian Approach, the *comparability-of-treatment* principle switched from being a principle to be observed ex-post to a principle to which debtor countries actively commit ex ante.³⁵ *Comparability of treatment* is embedded in a clause, the comparability of treatment clause (CTC), included in the debt treatment agreement signed in the Agreed Minutes. In accordance with this clause, the debtor country undertakes to seek from other official bilateral creditor countries that are not members of the Paris Club and private creditors (mainly banks, bondholders and suppliers) a treatment on *comparable terms* to those granted by the Paris Club members. The rationales behind this principle are the preservation of the financial interests of the Paris Club creditors (and thus of their taxpayers), the guarantee that the Paris

³⁵ The Evian shift to an ex-ante application of the principle aims to mitigate one of the limit of the clause: its reliance on debtors' responsibility.

Club efforts to restore debt sustainability in the debtor country is effective and is not diverted to repay other creditors on better terms, and the promotion of capital market efficiency with an eye to avoiding moral hazard. The implementation of the clause is needed to fulfill the financing gap. The negotiation procedures that became the standard for Paris Club rescheduling events were also established early on. As a first step, debtors are expected to request a meeting once they comply with the prerequisites of being under an IMF-supported program, of providing evidence about their problems to meet debt-servicing obligations, and of having a preliminary restructuring proposal (Vilanova and Martin, 2001). Meetings themselves also begin with a presentation by the concerned country to the various participants in the negotiations, which include the permanent and non-permanent members of the Paris Club as well as several outside observers. Subsequently, debtors' delegates leave the room, and the proper negotiations take place between the members of the Paris Club to define the terms of the agreement. These include the categories and amount of debt that will be treated, the relief (if any) to be granted, the maturity and grace period associated with the rescheduling, the consolidation period, and the cut-off date. It is important to note that these deals are preliminary steps to initiate conversations between the debtor and its various creditors, both the members of the Paris Club and other bilateral and private financiers. It is only after these bilateral negotiations are concluded that their financial obligations will be restructured and, therefore, that debt relief will materialize.

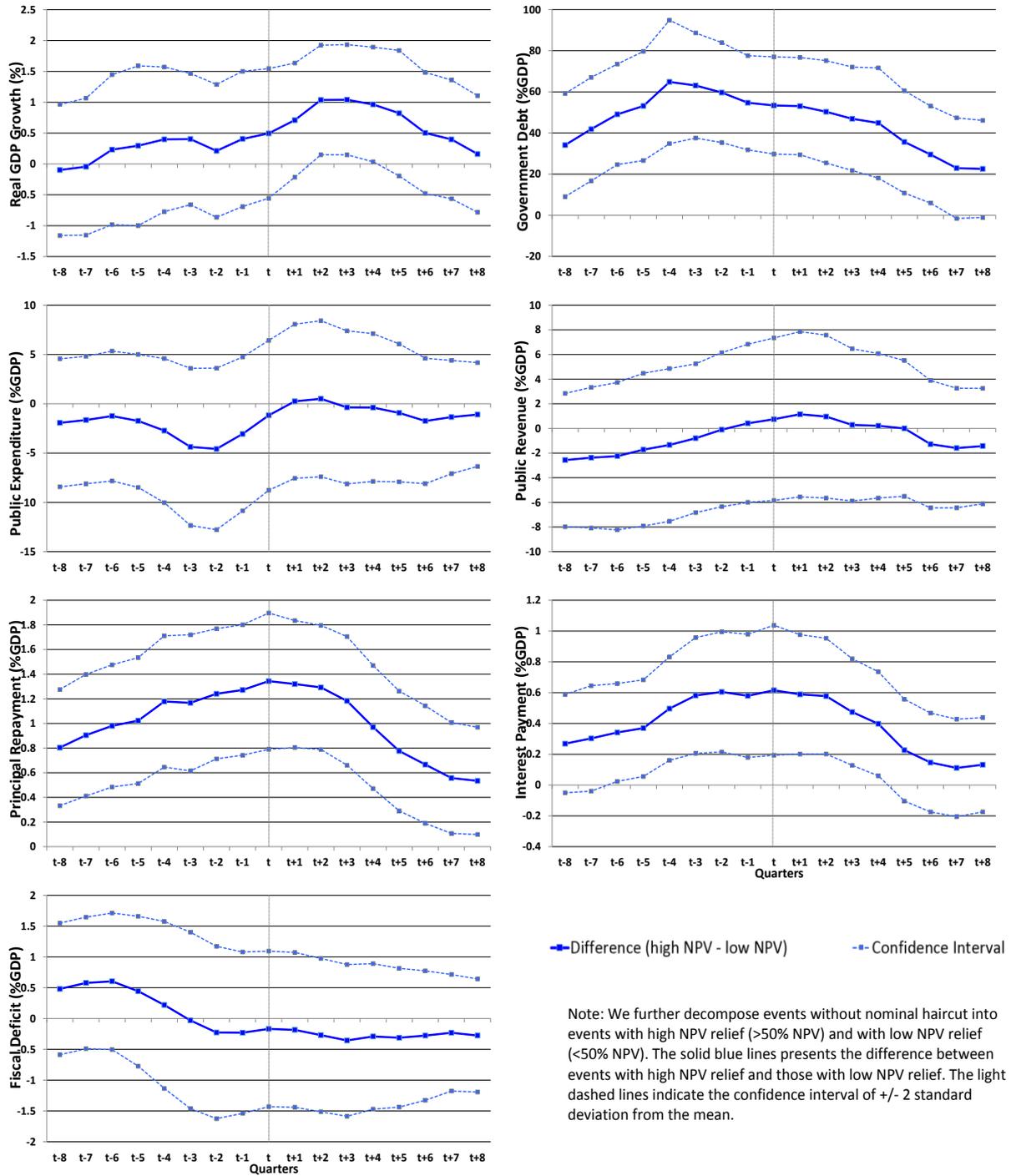
Table A2: Summary of the Terms of Treatment

	Year of introduction	Debt Relief in NPV terms (up to)	Eligible Countries	Other Considerations
Standard or Classic Terms	1956	Non-concessional	All countries	Terms defined on a case by case basis, although usually 10 year repayment period and 3 year grace period.
Venice Terms	1987	Non-concessional	Poorest countries of Sub-Saharan Africa	Extended repayment terms up to 20 years and grace periods up to 10 years for poorer countries.
Toronto Terms	1988	33% of consolidated non-ODA debt	Highly indebted poor countries	Non ODA debt restructured through partial write-offs, concessional interest rates or longer repayment periods. ODA debt rescheduled in non concessional terms with 25 years maturity and 14 years grace periods.
Houston Terms	1990	Non-concessional	Highly indebted lower middle income countries	Reschedulings with maturities of 20 years for ODA debt and up to 15 years for non ODA debt. 10 years grace period for ODA debt, 8 years for non-ODA debt. Allowed for debt conversion mechanisms.
London Terms	1991	50% of consolidated non-ODA debt	Highly indebted poor countries	Instrumented through partial write-offs, concessional interest rates or interest payment capitalization (only non-ODA debt). ODA debt rescheduled with 30 years maturity and 12 years grace periods. Extended the debt conversion mechanisms for low income countries.
Naples Terms	1995	67% of consolidated non-ODA debt	IDA countries	Allowed for stock treatments for the first time for countries with a good record with the IMF. Instrumented through partial write-off or through debt service reductions. ODA debt refinanced with 40 year repayment period and 16 years grace period.
HIPC Initiative	1996	As required to restore long-lasting debt sustainability	HIPC countries that would reach completion point	Explicit objective of providing an exit from the rescheduling process to the most heavily indebted countries that could commit to a credible reform process.
Lyon Terms	1998	80% of consolidated non-ODA debt	HIPC countries	Instrumented through a partial write off or through a debt service reduction option. ODA debt refinanced with 40 year repayment period and 16 years' grace period.
Cologne Terms	1999	90% of consolidated non-ODA debt, and 100% of ODA debt	HIPC countries	Instrumented through a partial write off or through a debt service reduction option. Creditor countries encouraged to cancel 100% of ODA debt.
Enhanced HIPC	1999	As required to restore long-lasting debt sustainability	HIPC countries that would reach completion point	Multilateral debt relief became tied to the adoption and implementation of poverty reduction strategies
Evian Approach	2003	As required to restore long-lasting debt sustainability	Non-HIPC countries	For the first time, debt sustainability taken into consideration in the restructuring of middle income countries' debt. Only to be considered in case of imminent default. Treatments tailored to debtors' specific circumstances.

Sources: Paris Club

Appendix 2: Event Analyses

Figure A2. Comparing High and Low NPV Relief in the Absence of Nominal Haircuts



Sources: Authors' Calculations

Appendix 3: Using the HIPC subsample

Figure A3.1. The effect of Paris Club Agreements (HIPC subsample)

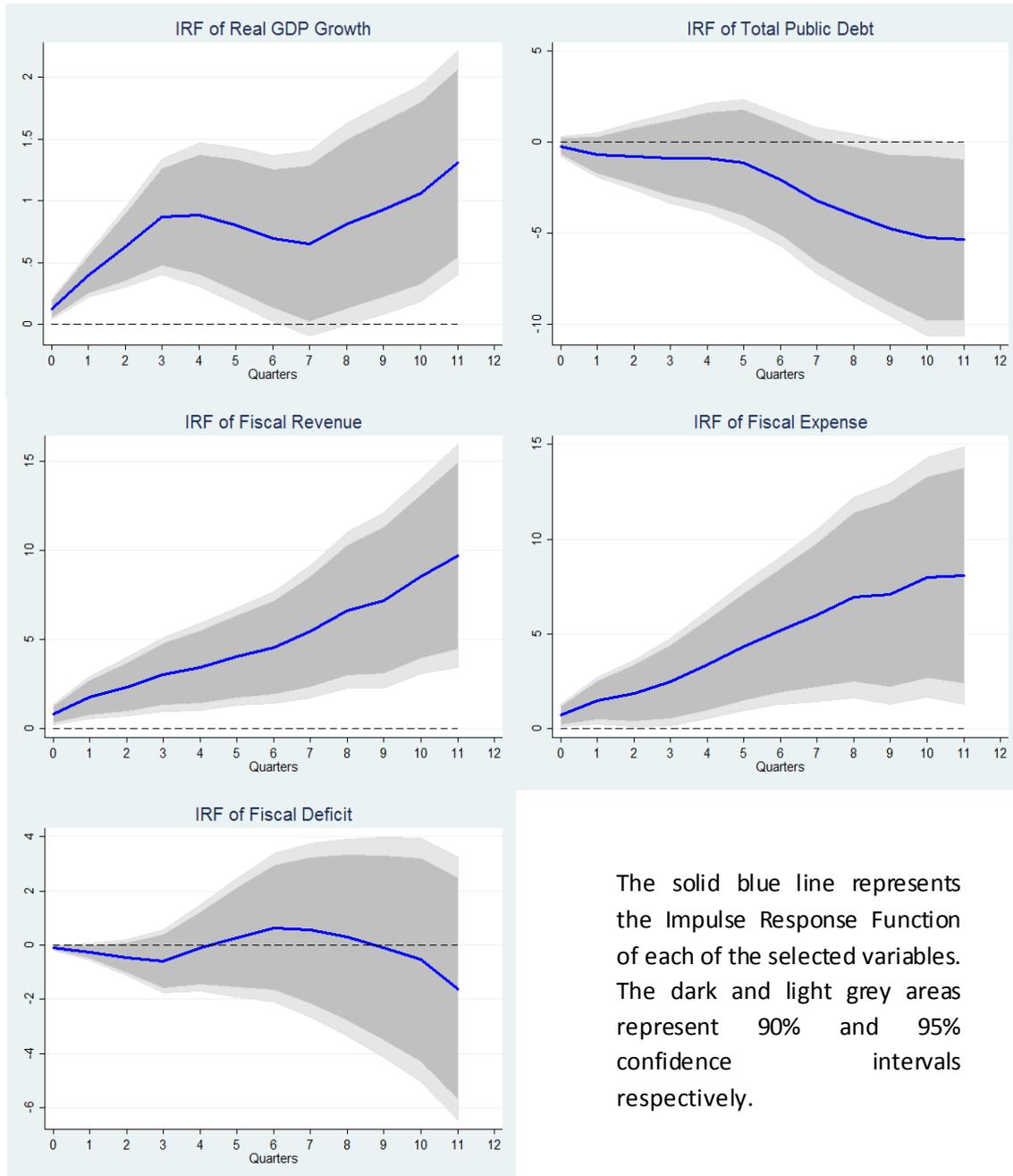
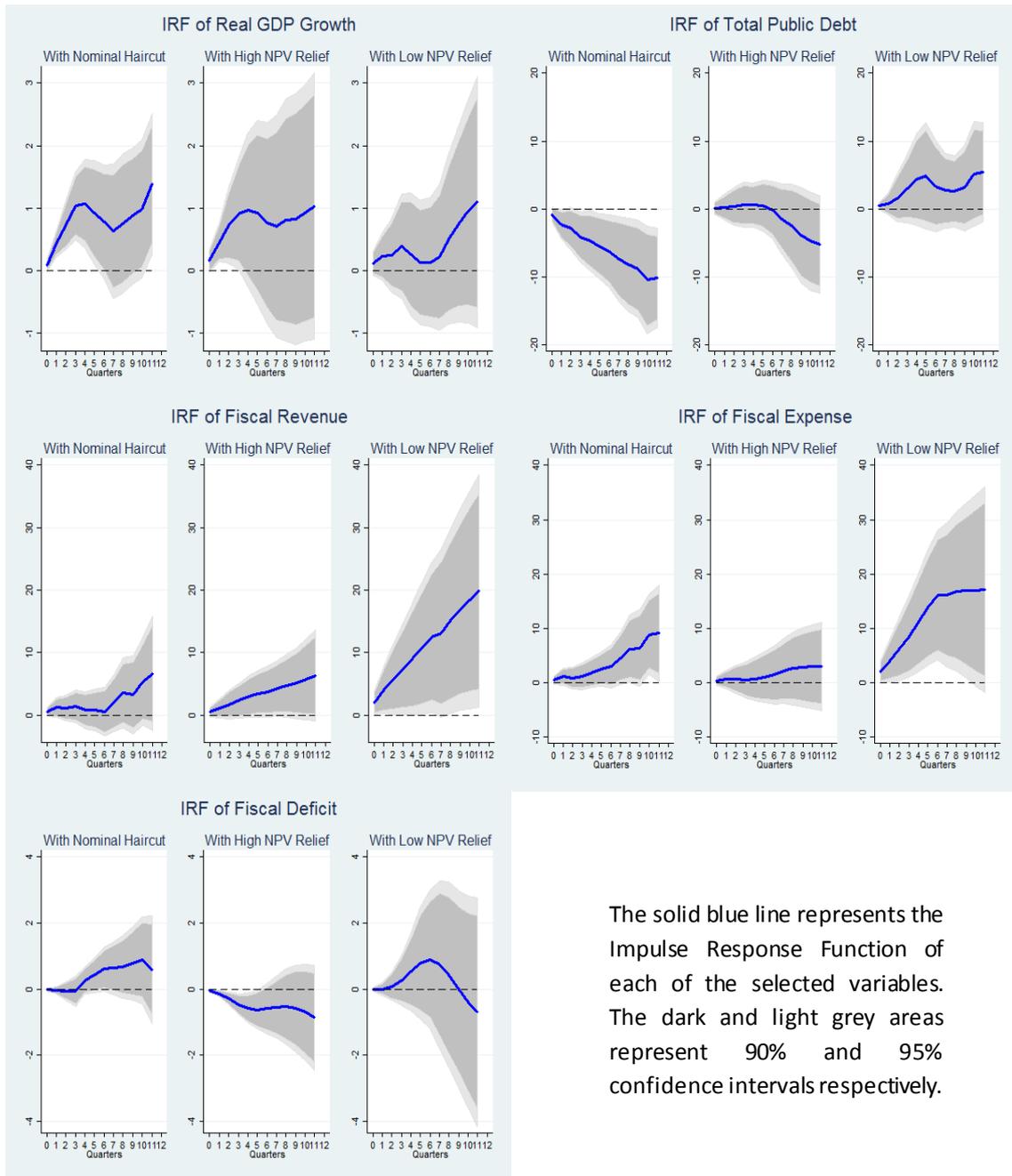


Figure A3.2. Between nominal relief and non-nominal relief (High NPV vs. Low NPV)



The solid blue line represents the Impulse Response Function of each of the selected variables. The dark and light grey areas represent 90% and 95% confidence intervals respectively.