DEVELOPMENT REIMAGINED

REIMAGINING THE INTERNATIONAL FINANCE SYSTEM FOR AFRICA

The Borrowers Club.

Background: What is the Borrower's Club and Why is it Needed?

Coordinating African Borrowers Will Support Higher-Quality External Borrowing and Debt Restructuring Terms.

The international finance system is overwhelming creditor-centric and is not considerate of the borrower's needs. Creditors are often organised through "club" or "committees", such as the Paris Club, which exclude the Borrower from negotiations. These creditor coordination arrangements are not new. They were used for the HPIC initiative, and most excluded the borrower from negotiations. After presentation of the case, the borrower exits, and a French representative conducts shuttle diplomacy to inform the borrower of the outcome. It is an antiquated, colonial arrangement.

Subsequently, there is an urgent need to increase Borrower Coordination for countries to share experience and negotiate practices to get more out of the financial system. Such coordination can be achieved through a Borrowers Club – which this brief presents - where African countries club together to both takeout loans and negotiate debt terms.

When borrowers seek to gain access to external financing, they often enter into negotiations where they have a limited bargaining power and are put in a "disadvantaged position". Through a Borrower's Club, countries, African countries can club together. Countries can share information on contract terms of different lenders and can use the club to enhance borrower agency. Borrowers can also use each other's growth prospects as collateral thereby reducing risk.

That is why a Borrower's Club is absolutely necessary to ensure that countries get the most out of the current financial system.

Theory of Change

A Borrower's Club is a proposal which "flips the orthodoxy". The central aim is Borrower Coordination – not Creditor Coordination. The Theory of Change behind the Club has four key points….

1. World is in a situation of too little "cheap" debt for low- and middle-income countries - not too much debt, while internal resources (e.g. DRM) will be insufficient for many years to come.
2. Countries without sufficient access to finance to escape poverty are constrained – they need better/reformed global institutions and interventions to serve them.
3. Too often institutions are designed with creditor/investor perspective in mind - but borrower perspective is critical and can lead to innovation.
4. Currently, it is still possible to avoid a "African debt crisis" and to avoid the mistakes of the 1980s and 1990s.

What is the Borrower's Club?

The Borrower's Club is based on microfinance principles but applied at the macro level. It draws on the concept of the Grameen Bank, which started in Bangladesh with the aim of offering credit to low-income earners. Low-income earners found it difficult to access credit as they did not have formal employment or defined collateral and the Grameen Bank system was particularly beneficial to women as they did not have formal employment.

It is a concept based on microfinance, but implementation is at macro level.

Based on the Grameen Bank concept, African countries would take external loans together and use each other's growth prospects as collateral.

It can enable lower interest rates from creditors, whilst also ensuring important growth projects – especially in countries with no/poor credit ratings - go ahead.

A strong form of coordination – co-benefit that it can also help to exchange experience, ideas (i.e innovation) and increase negotiation skills.

Main focus is on unlocking *new* finance, but here are some potential applications to debt relief negotiations and linkages to other proposals – e.g. LSF.

How would the Club work in practice?

The Club is based on a high degree of trust and collective interest by borrowers, they learn from eachother, build their own knowledge transfer and capacity building. It is the differences in risk profiles that enables risk to be shared and distributed. As the Grameen Bank model suggests, initiating repayment as early as possible, with repayments set as frequent as possible, will improve the borrower's credibility and its long-term ability to repay in full.

The Borrower's Club: Terms

- Borrowers meet regularly to determine priority projects for the members, based on clear eligibility criteria;
- Borrowers appoint a representative(s) to interact with creditors and this can be on a rotational basis;
- Borrowers will appoint an independent trustee based on certain criteria such as its capital or reputation;
- Borrowers as quickly as possible begin to make equal small, low-interest regular payments to an independent trustee;
- The repayments are designed to be small with low-interest rates for ease of payment while also sufficient to build in a "cushion" for temporary collateral;
- Borrowers deliver their projects independently, monitor and evaluate results and meet regularly to keep each other accountable for progress and to agree on new projects;
- If a project is delayed, faces challenges or a borrower faces repayment challenges, the borrower committee must agree for the cushion to be made available to support temporarily;
- Borrowers in arrears do not get more loans.

How would the Club work from a Creditor or Investor Perspective?

First, the Club removes the potential for arbitrary and unforgiving financial lenders to breath down on the borrowers' necks. Second, lenders in this system end up taking lower risks with lower interest rates being required but the returns are guaranteed – meaning there is less need for relief in future.

Creditors asked to invest into an instrument with lower "pooled" risk due to borrower coordination, and significant returns

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Creditors provided with an understanding of results and returns of collective projects by the borrower's representative(s) and trustee - not individual projects (NB: this is just like typical commercial investors)

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Creditors provide finance at highly concessional rates, each can determine the regular but small repayments required, in discussion with independent trustee. Ideally trustee-creditor repayments schedule is LONGER than borrower to trustee schedule.

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Creditor receives regular repayment and evaluation reports from independent trustees - not borrowers directly - avoids both foul play and pressuring.

Experience and Challenges

Why hasn't the Borrower's Club existed already? There are some relevant examples at the macro level. For example, the Europe has €800 billion NextGenerationEU recovery instrument which operates on "pooling" principles and has saved interest rate payments. While more of an "open call" for project ideas, such that creditors can see country volumes, backed by voluntary guarantees and possible further contributions from MS and THEN bond issuance - it provides useful lessons.

For example, unanimous voting to limit the influence of more powerful BC member countries in the decision-making process, and also shows it makes a difference – the use of joint lending through the EU for the €100 billion used to mitigate unemployment risks during the pandemic has saved almost €6 bn in interest payments to individual member countries, with no extra costs for the EU as a whole.

One reason we have not seen it for low middle income countries – its partly design – a colonial mindset. For example, the Club may present a challenge to certain creditors (esp. sovereign) to provide credit without being able to condition/leverage borrowing countries, etc. But it will be beneficial to other lenders who do not require conditionality and do not require/prefer creditor coordination.

In addition, there are lessons that can be learnt from the Grameen Bank. For example, the Bank did not offer more loans to those that had arrears - those that did not repay their loans looked for methods to earn high income so as to repay loans leaving them in a vicious debt cycle. This is encapsulated in our design by keeping project caps so that it is not necessary to do this.

The Borrower's Club can operate across a spectrum of coordination activities…

There is an urgent need to increase Borrower Coordination for countries to share key information. Such coordination can be achieved through a Borrowers Club, which can exist across a spectrum of different forms of coordination to enhance Borrower agency in the IFS. For example, the Club could negotiate and share information on contract terms by different lenders and discuss how to enhance Borrower agency into such terms. Another example is that borrowers could use the Club to secure new lending, by using each other's growth prospects as collateral thereby reducing risk.

Taking out new loans

Countries club together to take out new loans - sharing their growth prospects as collateral. This can fund bilateral and/or regional projects to accelerate growth.

Sharing Experiences and Lessons Learnt

Countries can use the Club to share experiences on dealing with creditors, the terms they secured, best practices for negotiating and much more

Restructuring Debt

Countries can use the Club to restructure debt amongst them - that means that debt repayments can be spread across multiple borrowers to ease fiscal space.

Next Steps…

1. **African (and other) borrowers should as a priority work together (and receive support) to convene and coordinate** together on their own, share experience and negotiation practices to get more out of the financial system, including the IFIs, emerging economies such as China, the Paris Club and private sector lenders.

2. **International Organisations should consider how to reorient to introduce or become "borrowers clubs"** to enable the poorest countries to access much needed finance to meet the SDGs. This includes MDBs such as the IMF or World Bank, International Institutions such as UNECA, or Groups such as the G20, supporting Borrower Coordination efforts through leveraging their coordination capacity and platforms.

3. **African Finance Ministers must come together to discuss how the Club can benefit their economies going forward and identify any challenges.** This will provide a good foundation on additional terms and conditions to take the Club into the Pilot phase.

4. **Pilot phase of the Club.** Once the details have been worked out and members have confirmed, a Pilot run of the Club should be initiated, before being launched on a larger, regional scale.

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