

WHAT DETERMINES A SUCCESSFUL DEBT OFFICE¹



By Jason Kamweru

The recent evolution of debt office

Since the recent debt crisis started more than twenty years ago, debt management has undergone transformation to become a critical input in the financial management of most of the developing countries. Prior to the debt crisis, debt management was confined to resource mobilization and debt servicing. In most cases, even the two functions were not co-coordinated. One or more department would be responsible for mobilizing funds by raising loans and grants. Once agreements were signed, there was no follow-up to ensure that disbursements are received on time. Demand notes from creditors were never verified and would be paid on sight. At that stage, the concept of a debt office was strange to most of the developing countries.

The next stage is what may be considered as the primary steps towards the evolution of debt offices in developing countries. During this phase, the debt crisis caught countries completely unaware. The causes of the debt crisis in the 80's are well documented. Poor debt management, oil shock and poor commodity prices are some of the reasons for the crisis. There was knee-jerk reaction from the countries stung by the crisis. First there was an urgent need to come up with computerized debt management systems. Debt units were quickly formed with little or no institutional support. These units mostly had one mandate- to compile debt figures. With no institutional support, it was left to these units to use their own talents to gather loan documents and other information needed to compile debt statistics.

It is around this time that I joined the Debt Management Unit in the Ministry of Finance in Kenya and would beg to share my experience. First, apart from a few officials working in the department where we were located, nobody else in the Ministry was sure what our role was. Loan documents were kept under lock and key by the Accountant General. It was not easy to access these documents which were, as a rule marked "Secret and Confidential". Many are the times we were turned away when we went to collect loan agreements, because we were not "security vetted"! When it came to loan interpretation, we were as bewildered as the next man in the street! We would huddle around one loan agreement and argue over the meaning of statements and words. Different opinions would fly around the room and the opinion aired by the loudest person would carry the day! My interpretation rarely saw the light of the day mainly because I was not loud enough!

¹ The views expressed in this paper are those of the authors and should not be attributed to or reported as reflecting the position of the Commonwealth Secretariat.

When it came to collecting historical transactions, our only source of data were the accounting ledgers maintained by the Accountant General's department. As would be expected, most of the data was maintained in local currency and we had to convert these transactions back into foreign currencies. Multicurrency loans were a different story. No one had a clue how to handle them.

It was around this time that the Commonwealth Finance Ministers Meeting mandated the Commonwealth Secretariat to come up with a debt management system and soon after the CS-DRMS software was born. With the entry of the Commonwealth Secretariat in the field, most of the countries, for the first time, initiated a structured approach to debt management. As part of the CS-DRMS package, countries had to first consent to an institutional review to come up with structures to support the software and debt management in general. This marked the birth of the initial debt offices with a defined structure. The relationship between the debt unit and other departments in the government, including Central Bank was defined. This was a turnaround point for debt management. In many countries, the real work of building debt databases started in earnest. Formal training in debt management kicked in. Various institutions including World Bank and regional Development Banks started offering debt management courses. The transformation from the earlier phase was dramatic. Debt management skills became an integral part of economic management. Institutions mandated to manage economic affairs had now to consult the debt units if they were dealing with issues that would impact on the debt position of the country. In almost all countries contracting of new loans was now restricted to only one government department, and even then, had to consult the debt management office before undertaking any new borrowing. Some countries went ahead and created debt management committees, but at that point they were not very effective and in many cases, ceased functioning. This is the time debt management was embraced as a specialized skill.

From the late 80's there were several initiatives by the international community to deal with the debt burden that was weighing down on developing countries. There was also intense pressure on developed countries, including international development institutions to reduce and cancel debt owed by developing countries. This campaign had two unintended consequences. First, it created the impression that debt management is a priority for the debt distressed countries. Countries that did not have a debt problem but had initially embraced debt management now seemed to change their minds and paid little attention to it. The same applied to countries that would not directly benefit from the debt relief initiatives. Second, among the beneficiary countries, debt management was reduced to debt relief. There was over-emphasis on debt relief initiatives. Other debt issues were relegated to the periphery.

Debt management is now in what may be considered as the third phase. In this phase, countries are adopting what is being considered as modern debt management practice. There are at least two options that countries can choose from. The first option entails creation of an independent Debt Management Office (DMO). In this option, an independent body is created and all debt management activities transferred to this body.

The DMO is answerable to Parliament and is independent of the Central Bank and the Ministry of Finance. Nigeria, for example, has chosen this model.

The second option is to have the DMO as a department within Ministry of Finance. All debt management activities are brought under one roof, including debt servicing. Ideally, there should be one consolidated database with data being entered at source. For example, exchange rates are entered at the Central Bank, debt service by the staff who make the payments and loan documents interpreted by those tasked with negotiations. This model is new and in the East and Southern Africa region, Kenya has adopted it. Currently the Macroeconomic and Financial Management Institute (MEFMI), the World Bank and ComSec are working very closely with the Kenya Government to ensure the successful implementation of the project.

One thread that runs across the different options is the organization of DMO's into Front, Middle and Back Office. There is new emphasis to have each office play its role, unlike in the past when the distinction between the three was less clear.

Other countries are reforming the existing debt offices to make them more effective. A number of countries are re-looking at the concept of debt committees and have or are in the process of reviving them. In the area of domestic debt there is renewed initiative to bring it on-board in debt management. The same applies to the management of grants and private sector debt.

Determinants of success

While discussing debt management, one inescapable fact is that some debt offices are more successful than others. What is defined as successful? To answer this question we need to look at the main functions of a debt office. The External Debt Statistics: Guide for Compilers and Users –commonly referred to as The Guide lists seven functions of a debt office. These are; policy, regulatory, resourcing, recording, analytical, controlling and operating (see Guide for details on what each of these functions entails). If these are the functions, then the success of a DMO can be measured by how well it has performed in each/some of these functions. Some of these functions may not be applicable to some of the countries for now. For example, most of the countries in East and Southern Africa are weak in risk management. However, there are those common functions that each DMO must perform and these can be used as a measure of effectiveness. If this statement is true, then we can rate DMO's according to how they are able to effectively undertake the above functions.

What factors then influence the effectiveness of a DMO? My answer to this question is based on my experience and observations, mostly in the East and Southern Africa region. Needless to say, my experience may not necessarily apply to all regions.

First, institutional set-up is a crucial ingredient in a debt office. In my region, DMO's are either fully fledged departments or units within departments. Where they are fully fledged departments, they tend to have better institutional support. Their relationship with other government departments and agencies are clearly defined. They tend to interact with these other institutions and as a result they are expected to produce output and in return get inputs. The outputs could be in the form of weekly, monthly and annual reports. Inputs could be in the form of data/documents that the DMO's need so as to maintain the database. This process means that they are well integrated within the institutions where they are located.

Where the DMO's are departments, there is clear division of labour. The internal structures of the organization tend to be well defined. In general such DMO's are well resourced in terms of personnel. On the other hand, where they (DMO's) are units, there is no clear division of labour and they tend to have very few staff. Experience has also shown that in most cases, the staff in such units will in addition to debt management also have other primary responsibilities. Debt management therefore takes second priority. On interaction with other institutions with inputs or requiring outputs from debt units, typically they (units) score poorly. The units tend to be isolated and are "lost" within the departments they are located in.

Second is the issue of caliber of personnel manning the DMO's. In the pecking order of debt management, the Back office is perceived as less prestigious than, say, the Front and Middle office. The latter two offices generally do not have a problem attracting officers with the right qualifications. On the other hand, the Back offices in some countries are manned by personnel without the needed qualifications. The Back office is the backbone of the debt office and the effectiveness of the DMO is directly related to the quality of staff there-in. Inputs from the Back office are required by both Middle and Front offices in their operations.

Closely related to the above is the issue of staff motivation. Poorly motivated staff will end up performing poorly in their jobs. Cases are known where staff are transferred to debt offices as a punishment. This does not augur well for debt management. There is a very high element of personal initiative in debt management work. Where officers feel alienated, it inevitably leads to poor performance by DMO's.

Leadership and support by senior management are crucial ingredients in a debt office. The effectiveness of a debt office is related to the type of leadership it has and the support it receives from senior management. Without being specific, cases are known in the region where the fortunes of a DMO change with leadership. This has been a major contributor to situations where today a debt office is very vibrant and tomorrow it becomes almost moribund and vice versa. Support by the top management is related to leadership. A debt office has to compete for recognition in the institution where it is located. Ministries of Finance and Central Banks, where DMO's are typically located, are large bureaucratic organizations. Each department tries to compete for the attention of the top management. A DMO that fails to find its niche in this competitive environment will

find itself being overshadowed and even risk being perceived as irrelevant. Once this happens, it will find it difficult to compete for resources.

Availability of resources and infrastructure is another important determinant of an effective debt office. Infrastructure may include right computers, printers, IT support, network etc. A modern debt office must take advantage of current technology to improve its performance. For example, it is no longer necessary to have the server containing the database sitting in the debt office. Technology now allows the server to be located even outside the building hosting the debt office and allow all parties access. Disaster recovery strategy is today an integral part of any IT environment. Unfortunately most of the debt offices do not comply with international standards for disaster recovery. This is a real threat to these offices and in the event of a disaster striking, all that has been achieved could be instantly lost. Comfortable offices, staff development programme, good interpersonal relationships etc are other factors that could impact on productivity of debt office staff.

Last, but certainly not the least, are those factors that operate outside the debt office. First, there is the issue of a Computer Based Debt Management System (CBDMS). Modern debt offices cannot operate without a CBDMS, whether locally developed or acquired off the shelf. All the countries I cover use CS-DRMS. This software plays a critical role in the effectiveness of a debt office. To illustrate this point, we only have to compare the debt offices before and after introduction of CS-DRMS 2000+. Before the current system was developed, very few countries were putting emphasis on domestic debt management. Today, nearly all the countries in the region are using the CS-DRMS domestic debt module and laying emphasis on domestic debt management. Why this development? The simple answer is that the technology available is friendlier, meets the needs of the countries and has gone a long way in encouraging countries to manage their domestic debt portfolio. This amply demonstrates that CBDMS can act as the engine of effectiveness of debt offices. Related to the issue of CBDMS is availability of technical support. Efficient technical support is crucial for smooth operation of CBDMS. The nature of work done by debt offices is such that in most cases, output is required at very short notice. This means the debt systems must be operational at all times. If technical support fails to respond on timely basis and in an efficient manner, it could negatively impact on the integrity of the whole system. DMS has identified this as a priority area and we have seen big improvement in terms of technical support. Other initiatives are underway, including the use of the web, to improve the support offered to clients.

The Regional Advisers project is another initiative to bring support closer to the clients. In addition, DMS is working closely with regional organizations and countries to support debt management activities. These include training, seminars, retreats – all geared towards making debt offices more effective. Those debt offices that are taking advantage of these initiatives will continue to be more effective than those that take a back seat.

To recap, the article begins by summarising the evolution of the modern debt office since the emergence of the recent debt crisis back in the mid 1980s. It then reviews factors that influence the effectiveness of a debt office. Readers may have divergent views on the factors based on their own experiences. It would therefore benefit our client base if you shared them by contributing article for posting on this website

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