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## A case study on debt conversion, Spain and Argentina

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# Debt conversion for education. The case of Spain and Argentina

Carlos Aggio

## Introduction

This paper analyses the rationale behind the recent agreement between Spain and Argentina on debt conversion for education. Firstly, it shows the impact of the last economic crisis on debt services and public expenditures to education. Secondly, it describes how the debt conversion for education proposal has been shaped through i) Argentinean and other Latin American countries advocacy work and ii) Spanish political will to support the initiative. Thirdly, it presents the characteristics of the actual project that will be implemented in Argentina.

## Economic crisis and its impact on education expenditures

In 2001-02, Argentina experienced one of the worst economic crises in its history. Income per capita, which had begun to contract in 1999, fell by about 20 percent in the three years ending December 2002, inflation reignited, the banking system became largely paralyzed, and the Argentine peso, which was then pegged at par to the U.S. dollar, reached lows of Arg\$3.90 per U.S. dollar (in mid-2002). At that time, debt services represented 8% of GDP and the government defaulted on its debt.

The crisis had an obvious negative impact in Government's revenues and its capacity to respond to the increasing social demands. In particular, the education sector showed worrying signals of under investment both in relation to the levels of expenditures registered in the mid 1990s and in relation to the GDP (MECyT, 2004). Public expenditures to education dropped dramatically in 2002 at all levels of Government. In 2003, total public expenditures to education were two-third of the 1998 level (Figure 1). Moreover, public expenditures to education as percentage of GDP were 3.7%. More than 2 percentage points below the 6% target set by Law in 1993<sup>1</sup>. In the course of 2003, the economy began to recover and so did resources allocated to education. However, educational investment remained insufficient for the dimension of the educational challenges ahead (MECyT, 2004).

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<sup>1</sup> The Federal Education Law (N. 24195) Art. 61 sets the target of 6% of public expenditures on education as percentage of GDP.

Figure 1 Public expenditures to education by level of government in constant prices 1998=100



(\*) Estimations

Source: MECyT (2004)

### Debt conversion as a strategy for increasing resources for education

The interest payments on central government debt which in 2001 reached 8% (MECON, 2005) compared with the necessary resources to attend the educational challenges, made attractive the idea of swapping part of that debt for education investments. Accordingly, Argentina with other countries in the region started advocating for debt conversion for education in various international forums. Although most of the Argentinean debt is with the private sector (more than 80% of total), most of the advocacy work so far has been focused on debt with official donors. The debt conversion for education is defined as the cancellation of debt in exchange for a commitment to mobilize domestic resources for education. The economic rationale is based on the willingness of a creditor, in this case a creditor government, to cancel debt owed by a debtor government in exchange for the debtor setting aside an agreed amount of funds (Norris, 2000). Doing so is a way of reducing Government debt burden and at the same time increasing resources to the squeezed education budget.

Originally, the proposal was discussed in two international meetings among Education Ministers across Latin America<sup>2</sup>. In those reunions, Ministers agreed to explore the possibility to convert part of the external debt payment of countries into education programs. Immediately after, the proposal was officially formulated by the Argentinean Education Minister, Daniel Filmus, in his speech at the 32nd UNESCO General

<sup>2</sup> Third Meeting of Ministers of Education in the framework of the Inter-American Council on Integral Development (CIDI) of the Organization of American States (OAS) held on August 2003 in Mexico City and the XIII Conferencia Iberoamericana de Educación, held on September 2003 in Tarija, Bolivia.

Conference (Paris, October, 2003), where he requested UNESCO to assume leadership in this subject. At the same time, civil society organizations were also lobbying in favor of the idea both in Argentina and Spain (Ingelmo, 2005). The OEI (Organización de Estados Iberoamericanos para la Educación, la Ciencia y la Cultura) a multilateral institution which fosters cooperation among Ibero-American countries in the fields of education, science, culture and technology have also played an important advocacy work and dissemination ([www.oei.es/deuda](http://www.oei.es/deuda)).

Initially the idea gained consensus only among debtor countries, but in 2004 Spain expressed publicly its support. Thus, Spain was the first official support from the Donor community. Rodríguez Zapatero, Spanish Prime Minister in his first speech before the UN in September 2004 made public his intentions of doubling official development assistance over the next four years, until it totals 0.5% of GDP, so as to reach 0.7% of GDP as soon as possible. He also announced that beyond their commitment towards the High Indebted and Poor Countries Initiative (HIPC), they will actively get involved in debt exchange operations in favor of social development initiatives, especially in primary education (Rodríguez-Zapatero, 2004).

The Spanish position hinted by its Prime Minister, was then confirmed in the XIV Ibero-American Summits held in San José de Costa Rica. In that occasion, both Education Ministers and Heads of States of more than 20 countries in the region expressed again their high interest in the initiative their final communiqués. At that time, Spain made the commitment to get involved actively in debt conversion for social development projects giving high priority to basic education (Declaración de San José<sup>3</sup>). In 2005, the initiative became part of the international cooperation strategy for the period 2005-2008 (MAEyC, 2005).

### **Debt Conversion for education (Programa de Conversión de Deuda por Educación, CDxE)**

Last January, while Argentina was negotiating the restructuring of its external debt with private creditors, Spain agreed to make allowances for US\$ 100 M of debt under the condition that it will be invested in education. This first announcement was followed by another one where Spain agreed to swap US\$ 50 M of the Ecuadorian debt for social investments in that country<sup>4</sup> (education and health). There are signs of undergoing negotiations between Spain and other Latin American countries such as Brazil, Cuba, Peru and Venezuela<sup>5</sup>.

The Argentinean Finance Ministry has already guaranteed the funds availability. Instead of repaying the Spanish Government for US\$ 100 millions, it will transfer it to a special protected account for the use of the Education Ministry. These funds will be allocated to education on top of what is already budgeted and therefore it will represent a truly increase in resources.

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<sup>3</sup> [http://www.cumbresiberoamericanas.com/declaraciones\\_finales/san\\_jose.htm](http://www.cumbresiberoamericanas.com/declaraciones_finales/san_jose.htm)

<sup>4</sup> <http://www.presidencia.gov.ec/noticias.asp?noide=4549>

<sup>5</sup> <http://www.rree.gob.pe/portal/boletinInf.nsf/0/0db49de64ac1897b05256fc800702865?OpenDocument>,  
<http://www.la-moncloa.es/web/asp/muestraDocImp.asp?Codigo=p2009040>  
[http://www.venezuela-avanza.de/archiv/archiv04/html/palacio\\_de\\_la\\_moncloa.html](http://www.venezuela-avanza.de/archiv/archiv04/html/palacio_de_la_moncloa.html)

The funds will be disbursed over a period of 4 years in two existing scholarship programmes for poor students in basic education: Programa Nacional de Becas Estudiantiles (PNBE) and Programa Nacional de Inclusión Escolar) (PNIE). These programmes, which receive external funds from the IADB, have contributed to diminish drop-outs in secondary school over and after the economic crisis by giving scholarship to 350.000 disadvantaged students<sup>6</sup>. The current project will provide additional resources. Although these programmes operate across the country, the Spanish funds will be entirely focus on helping poor students who live in the relatively poorer regions of the country (North-East, North-West and Buenos Aires suburbs), to complete lower secondary education (Enseñanza General Básica EGB III). Despite lower secondary education is compulsory, net enrolment ratio was below 80%. This ratio is lower in all the provinces of the North East and West. The suburbs of Buenos Aires show a higher NER but is the region that concentrates the larger number of poor people in the country.

Table 1. Net Enrolment ratio in lower secondary school. Year 2001

Region	Province	Lower Secondary (EGB III)
Buenos Aires suburbs		85.9
North-East	Corrientes	61.5
	Chaco	63.5
	Formosa	65.5
	Misiones	56.4
North West	Catamarca	74.2
	Jujuy	76.7
	La Rioja	72.7
	Salta	73.7
	Santiago del Estero	58.7
	Tucumán	72.3
<b>Total</b>		<b>78.4</b>

Source: DINIECE [Dirección Nacional de Información y Evaluación de la Calidad Educativa](#) based on INDEC (2001)

Table 2 shows how the funds are planned to be disbursed over the next 4 years. The first year involves students' detection activities and various measures that go associated with the scholarship programme such as textbooks and other teaching material, and institutional projects for the schools which are receiving students with scholarships. From 2006 to 2008, the total amount available will be for cash transfers of Arg \$ 400 per student per year (215.000 additional students per year in those regions). This transfer will go directly to enlarge the students' family income.

Table 2. Disbursements per year

Year	US\$ Millions
2005	5
2006	32
2007	32
2008	32
<b>Total</b>	<b>100</b>

Source: Jefatura de Gabinete del MECyT (2005)

<sup>6</sup> Family income below Arg \$ 500 per month (US\$ 170)

As can be seen from above, the funds will be entirely channelled through the existing management structure that currently administers PNBE and PNIE. However, a special committee for supervision, monitoring and evaluation will be created with representatives of both governments. Local NGOs working in education have already expressed their interest in participating somehow in the initiative (Ingelmo, 2005). But, their inclusion is not yet clear or assured

The amount is negligible in relation to the current Argentinean total debt stock before the restructuring (US\$ 190 Billions) and in relation to what the US\$ 6.8 Billions the country owes to bilateral donors (Spain represents roughly 20% of that debt) which is still defaulted<sup>7</sup>. It is also small compared with the 2003 total public expenditures to basic education US\$ 3.3 Billions (91% Provincial Government 9% Federal Government). However, its relevance is better evaluated when compared with non-salary components as percentage of the total public expenditures on basic education which is roughly 10%.

Despite both creditor and debtor have agreed, to get the actual debt conversion, there is a conditionality associated with the Paris Club. The Paris Club agreements allow creditors to voluntarily undertake debt swaps but the debtor country must have an appropriate program with the IMF that shows the need for Paris Club debt relief. At the moment, IMF - Argentina relations are difficult. The IMF has not approved yet the recent debt restructuring. Despite the relatively small amount of money involved, this may cause delays in the implementation of the debt conversion since Paris Club regulations do not allow country members to forgive debt to countries without an agreement with the IMF.

### **Final comments**

This paper has presented the case of debt conversion for education between Spain and Argentina. The current project to be implemented in Argentina shows that the debt alleviation element is limited. In fact, the total amount of debt converted is a minor percentage of bilateral and total Argentinean debt. Thus the expected impact on debt services reduction will be insignificant. Nevertheless, it could have a non-negligible impact on an education budget which has been affected negatively by the economic crisis. Poor students in relatively poorer provinces will be receiving extra assistance to finish their 10 years of compulsory education. Debt conversion for education should not be seen as 'the' solution to the education financing constraints but is a valid mean to obtain resources for specific education objectives (MECyT, 2004).

So far, there has been only one donor supporting the initiative. It seems that the agreement made by Spain with Argentina (and then with Ecuador) will be followed by others in the region. It is uncertain yet if these projects will motivate other donors to pursue similar initiatives.

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<sup>7</sup> As mentioned, Argentina ended a debt restructuring process on February 24 which did not include bilateral donors. Debt figures are at 31/12/2004 and were taken from <http://www.mecon.gov.ar/download/financiamiento/deudac.xls>.

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	1999	2000	2001	2002	2003	2004*	2005*
National	105	109,6	106,6	57,6	65,5	78,24	82,26
Provincial	110,4	108,8	116,3	73,6	65,1	69,6	68,32
Municipal	119,9	126,2	128,4	78,1	67,5	71,31	70,01
All Levels	109,3	109,5	114,2	69,7	65,3	71,84	71,91