

Debt Relief and Education in HIPC Jesus Crespo Cuaresma and Gallina A. Vincelette*

With the launch of the Heavily Indebted Poor Countries (HIPC) Initiative in 1996, debt relief efforts by a wide range of creditors (multilateral, bilateral, and commercial) were directed specifically towards poor countries struggling to cope with external debt that heavily burdened export earnings or fiscal revenues. Modifications approved in 1999 provided faster, broader and deeper debt relief, and further linked the debt relief effort to the Initiative's goal of releasing resources for poverty-reduction and social policies. The Initiative was supplemented in 2005 by the Multilateral Debt Relief Initiative (MDRI) to accelerate countries' progress toward the United Nations Millennium Development Goals (MDGs). Debt relief assistance of US\$117 billion has been committed to the 33 countries that have reached the decision point under the two Initiatives. These two major international efforts have helped reduce significantly the debt burden of HIPCs.

Debt relief might be expected to have an effect on human capital accumulation, particularly educational outcomes, but no convincing empirical evidence exists for such effects. To fill this gap, we assess empirically the effect on educational variables within HIPCs of debt relief provided at the HIPC Initiative decision and completion points. In particular, we test for statistical differences in changes in educational expenditures, pupil-to-teacher ratios, and drop-out and repetition rates between countries that reached the HIPC Initiative decision and completion points and other eligible HIPCs.

Descriptive statistics suggest that, on average, countries that have reached the HIPC Initiative decision point have significantly increased educational expenditure in comparison with pre-decision-point countries. Albeit from low levels of less than 4 percent, educational expenditure as a percentage of GDP in post-decision-point countries are over one-third of a percentage point higher on average than in pre-decision-point countries, and the ratio of expenditures in primary education to total educational expenditure is 3 percentage points higher. Similarly, significant differences are present in countries that have reached the decision point for the change in the share of educational expenditures over total public expenditure and for the change in the share of educational expenditures in primary education over total educational expenditures.

Post-completion-point countries present on average close to 30 percent (or 1 percentage point of GDP) higher levels of educational expenditure, 27 percent lower drop-out rates (or nearly 10 percentage points), and 54 percent (over 6 percentage points) lower repetition rates when compared with HIPCs receiving interim assistance. There is, however, a large variation across country/year observations, as measured by the standard deviation and the difference between maximum and minimum values of the education variables. Post-completion-point countries have reduced drop-out rates in primary schooling by over 4 percent on average.

For these results to be interpretable in the causal sense, we control for the potential sample selection problem using two estimation procedures: (i) matching estimates based on propensity scores, and (ii) Heckman's (1979) sample selection estimator. We estimate the effects on the change in educational variables of HIPCs reaching the HIPC Initiative decision or completion point, after controlling for other factors such as quality of democratic institutions, inflation, armed conflicts, net aid transfers, income (per capita), GDP growth rate, and country size, among others. The analysis is carried out exclusively on the change in educational expenditures as a percentage of GDP, the change in primary schooling drop-out rates, the change in repetition rates in secondary schooling, and the change in the pupil-to-teacher ratio.

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Overall, we find that reaching the HIPC Initiative decision point does not significantly affect human capital accumulation. But we do find that countries that receive higher levels of net aid, and where armed conflict is not present, are more likely to reach the decision point. As a factor of reaching the decision point, our results suggest that price stability may be marginally significant, but that neither the quality of governance nor civil liberties have played a significant role.

An important finding is that reaching the HIPC Initiative completion point is associated with lower drop-out rates in primary education. The effect is robust across estimation methods: a significant decrease in drop-out rates after the completion point, with estimates of the quantitative effect ranging from around 5 to around 9 percentage points, compared to the average rates of 43 percent for HIPCs in the interim period. Significant decreases in the repetition rates are also observed in some specifications, although this result does not appear robust across methods. The same applies to differences in educational expenditures and pupil-to-teacher ratios.

In sum, the results of the study give evidence that while government educational expenditures do not tend to increase sharply after HIPCs reach their respective decision or completion points, primary schooling drop-out rates nonetheless decrease significantly after the completion point.