Managing Public Debt Under Duress

CABRI Webinar: Managing public debt amidst COVID-19 financing pressures in Africa

25 June 2020

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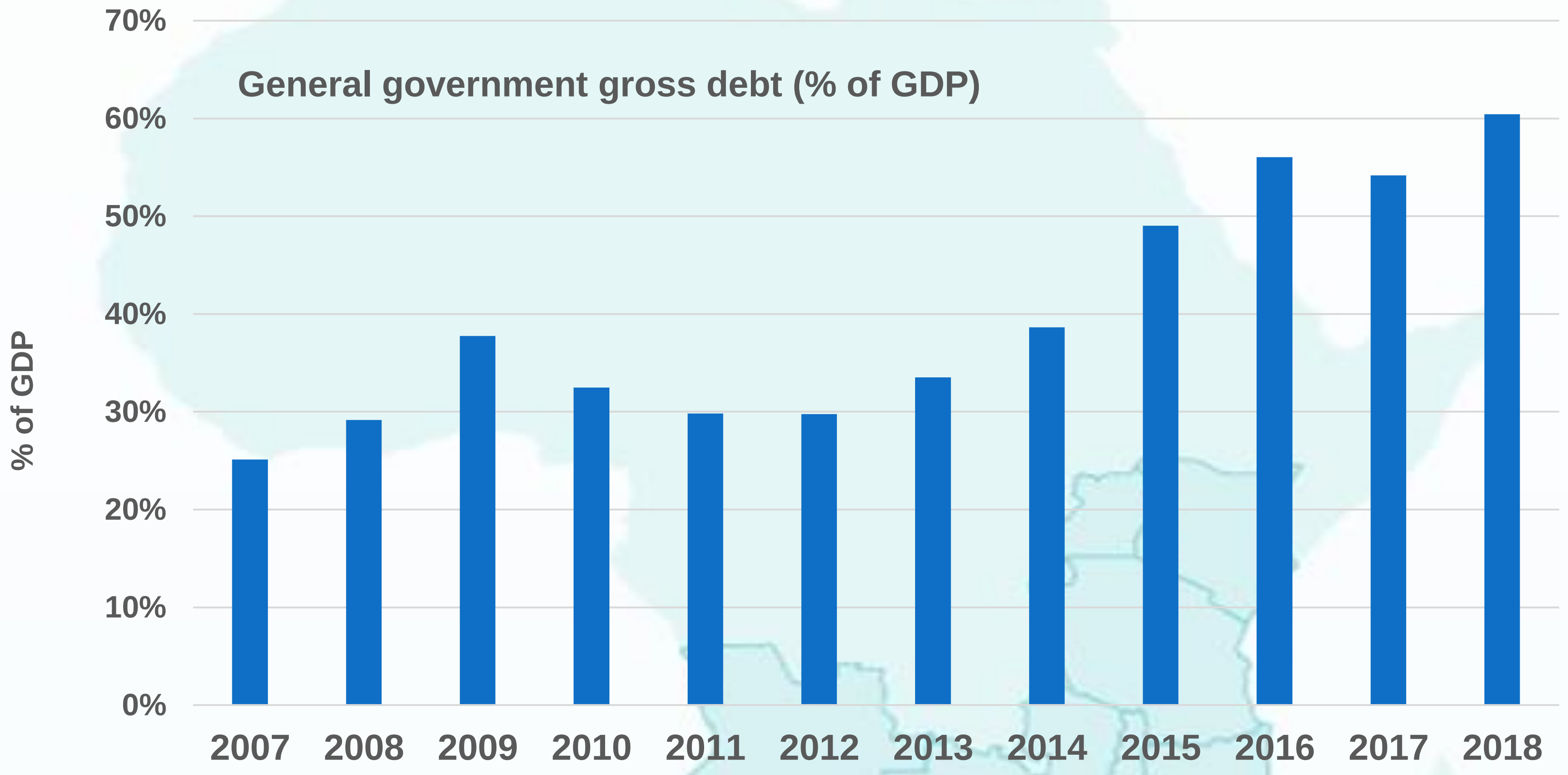
Outline

1. Introduction
2. Evolution of public debt during 2007 – 2018, including the main drivers.
3. Vulnerabilities of countries to COVID-19 and how these affect public debt sustainability
4. Short term measures to manage debt vulnerabilities

Introduction

- Public debt has increased substantially in the MEFMI member countries, from 25% of GDP in 2007 to 60% of GDP in 2018:
  - MEFMI member countries are Angola, Botswana, Burundi, Eswatini, Kenya, Lesotho, Malawi, Mozambique, Namibia, Rwanda, Tanzania, Uganda, Zambia and Zimbabwe.
- The increase has been particularly rapid in the post HIPCs such as Malawi, Mozambique, Rwanda, Tanzania, Uganda and Zambia.
  - Zimbabwe remains in debt distress
  - Significant debt accumulation in Angola

Public debt evolution: 2007 - 2018



Source: IMF WEO January 2020

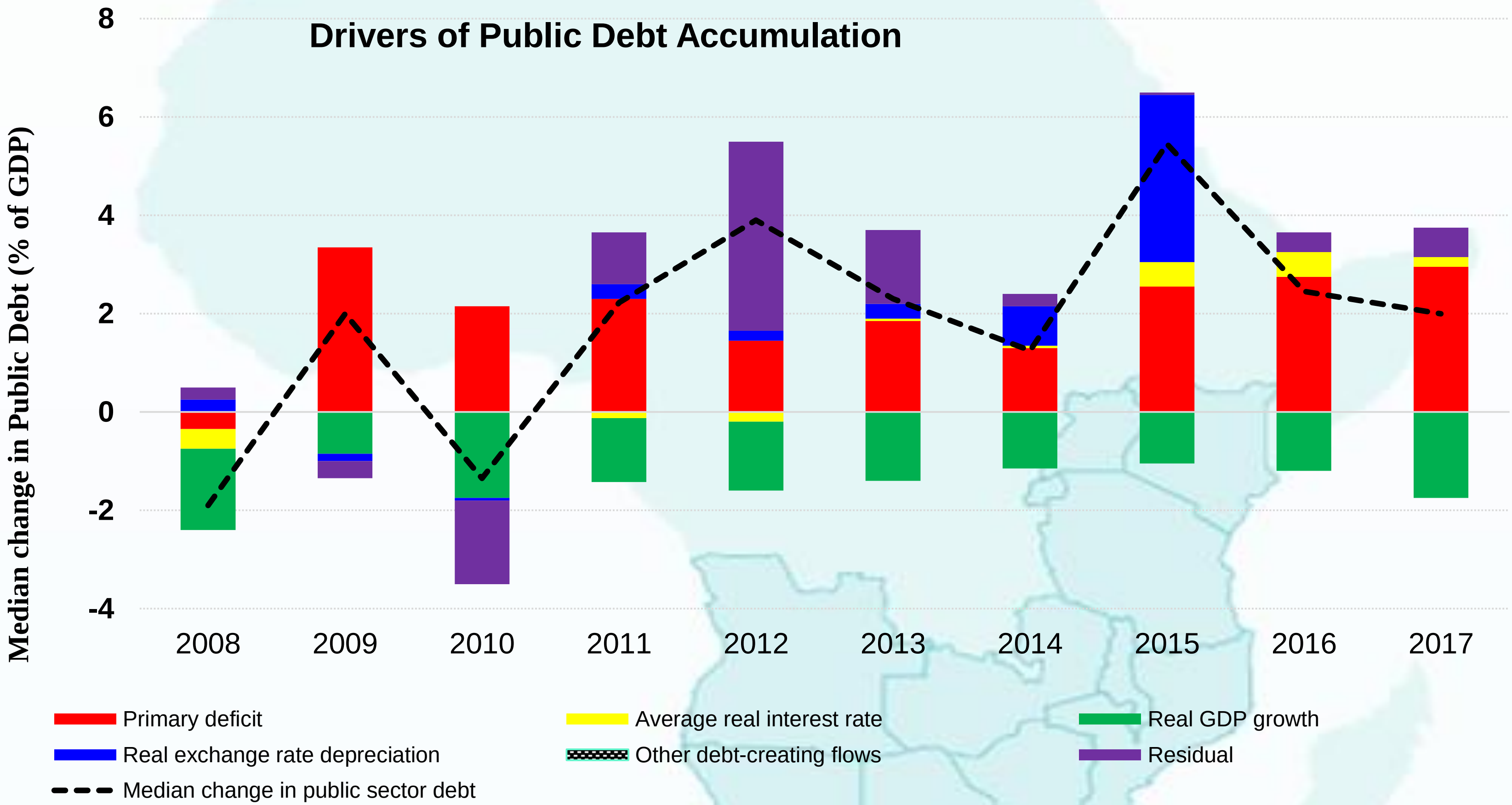
What were the main drivers of debt accumulation?

Conceptual framework for debt accumulation

- The conceptual framework for debt accumulation is described by the following factors:

Factor	**Impact on debt accumulation (debt-to-GDP ratio)**
Increase in primary deficit	Increases debt-to-GDP ratio
Increase in real interest rates	Increases debt-to-GDP ratio
Real GDP growth	Decreases debt-to-GDP ratio
Currency appreciation/depreciation	Decreases/increases debt-to-GDP ratio
Other debt creating flows	Could increase or decrease debt.

Drivers of debt accumulation during 2007-2018



- Primary deficits have been the main driver of public debt over the past decade; exchange rate effect in 2014-2015; interest rates impact in the past 3 years;
- Real GDP growth has helped reduce the debt accumulation momentum.

Vulnerabilities of Countries to COVID-19 Pandemic Shock

- Global financial conditions.
- Trade linkages with China and Europe
- Changes in the terms of trade.
- Tourism dependency
- Quality of health systems
- Debt sustainability analysis ratings

So, how will these affect public debt accumulation?

Real GDP growth decline/contraction will increase public debt

	2017	2018	2019	2020	2021
Angola	(0.2)	(1.2)	(1.5)	(1.4)	2.6
Botswana	2.9	4.5	3.0	(5.4)	6.8
Burundi	0.5	1.6	1.8	(5.5)	4.2
Eswatini	2.0	2.4	1.0	(0.9)	1.8
Kenya	4.9	6.3	5.6	1.0	6.1
Lesotho	(1.0)	0.4	1.2	(5.2)	5.1
Malawi	4.0	3.2	4.5	1.0	2.5
Mozambique	3.7	3.4	2.2	2.2	4.7
Namibia	(0.1)	0.3	(1.4)	(2.5)	3.2
Rwanda	6.1	8.6	10.1	3.5	6.7
Tanzania	6.8	7.0	6.3	2.0	4.6
Uganda	5.0	6.3	4.9	3.5	4.3
Zambia	3.5	4.0	1.5	(3.5)	2.3
Zimbabwe	4.7	3.5	(8.3)	(7.4)	2.5

Source: IMF WEO April 2020

- The above projections were based on discovery of a cure for Covid-19 in the near term, which is far fetched.
- Consequently, the metrics used to calculate debt sustainability have worsened ie debt/GDP; debt/revenue; debt/exports

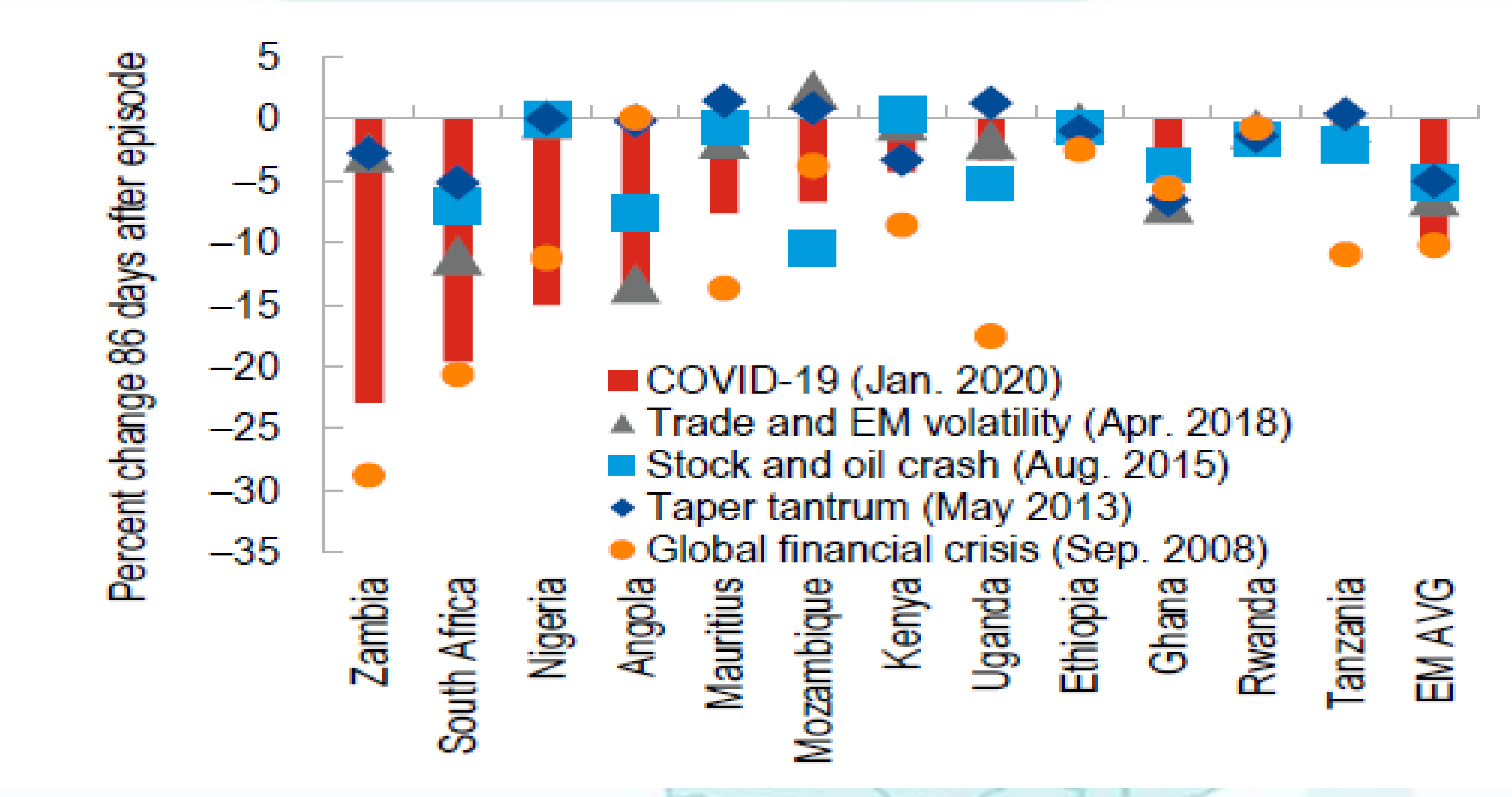
Public debt to increase due to higher fiscal deficits

- Decline in real GDP growth or economic contraction, will reduce revenues available to governments.
- In addition, all countries have announced fiscal measures that will increase fiscal deficits
  - Temporary tax breaks will reduce revenues
  - Increased health and social-economic spending will increase public expenditure
  - Potentially direct bailouts of enterprises, though mostly this has been done via loans, taxes and other policies
- Budget deficits are expected to increase compared to earlier forecasts
  - Malawi: fiscal deficit to increase from about 3% of GDP in 2019/20 to 9% of GDP in 2021
- Public debt will undoubtedly increase because of higher fiscal deficits financed through borrowing.

Fiscal deficits as % of GDP

	2017	2018	2019	2020	2021
Angola	(6.3)	2.2	0.1	(6.0)	(2.5)
Botswana	(1.1)	(4.6)	(6.2)	(5.9)	(3.1)
Burundi	(7.2)	(5.3)	(6.0)	(9.0)	(6.8)
Eswatini	(7.0)	(11.2)	(8.0)	(8.9)	(7.6)
Kenya	(7.9)	(7.4)	(7.8)	(7.7)	(6.9)
Lesotho	(4.0)	(4.4)	(3.8)	(2.0)	(7.0)
Malawi	(7.3)	(5.5)	(6.4)	(6.3)	(5.2)
Mozambique	(2.9)	(6.9)	(0.2)	(7.7)	(6.1)
Namibia	(5.0)	(5.3)	(4.7)	(7.0)	(6.1)
Rwanda	(2.5)	(2.6)	(5.2)	(8.1)	(4.6)
Tanzania	(1.2)	(1.9)	(2.9)	(3.8)	(4.4)
Uganda	(3.2)	(3.8)	(6.7)	(6.8)	(6.6)
Zambia	(7.7)	(8.2)	(7.6)	(5.7)	(6.9)
Zimbabwe	(8.1)	(4.5)	(2.6)	(4.9)	(1.5)

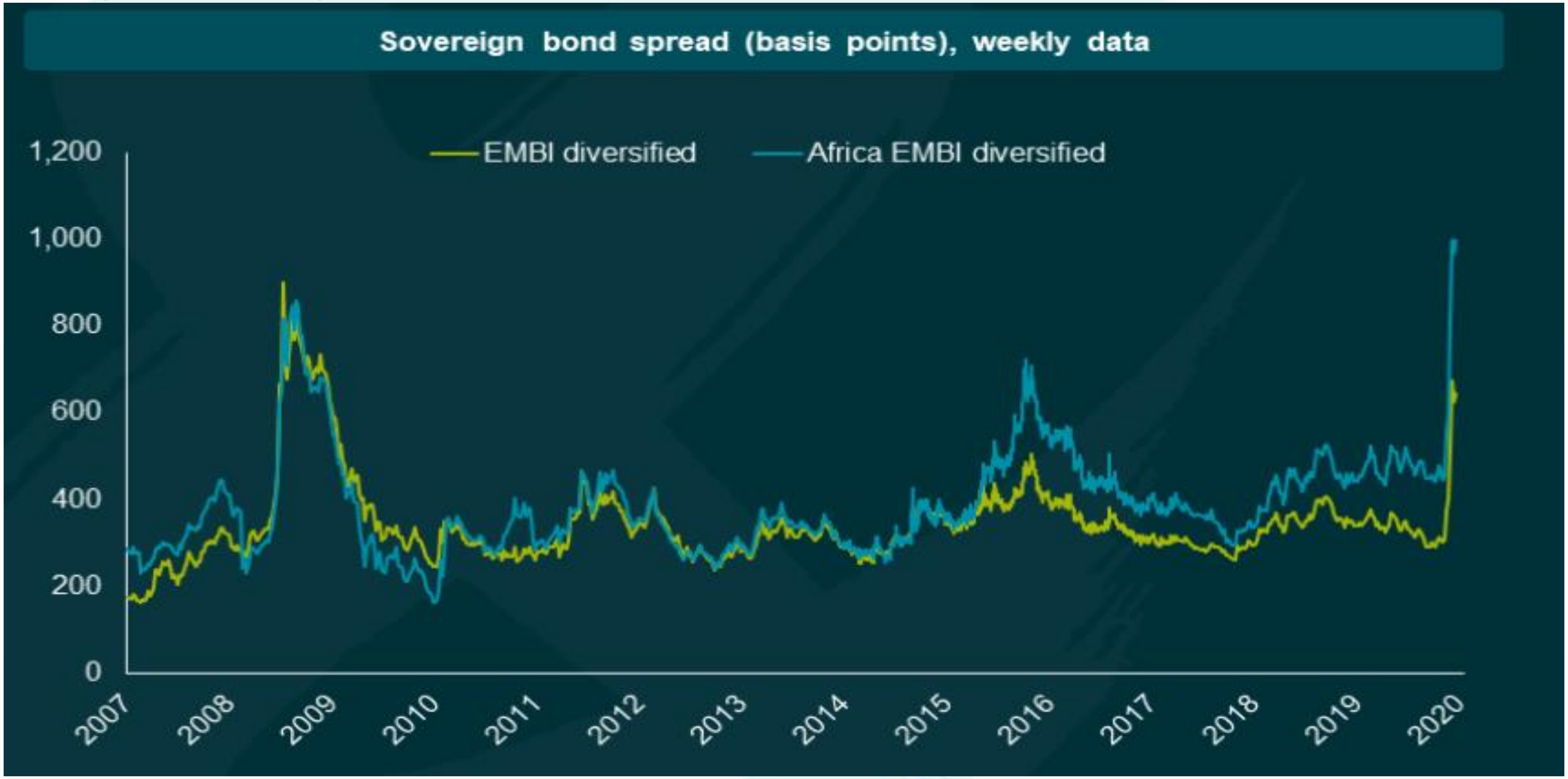
Exchange rates have also depreciated during the pandemic



- Consequently, external debt servicing has increased in local currency terms

Interest rates have risen during crisis

- Africa's sovereign bonds spreads have increased by about 700 basis points since February 2020, reaching all-time highs for countries such as Zambia, Gabon, Angola and Nigeria, and ratings downgrades for South Africa.



Source: M&G Securities Limited

Impact of interest rates on debt

- While the region's spike in Eurobond redemptions is not due until 2022, coupons have to be paid in the interim period.
  - Zambia
  - Namibia
  - Rwanda
  - Kenya

- The conditions for refinancing might worsen at maturity of the bonds.

Public debt during/after COVID-19 crisis (% of GDP)

	2017	2018	2019	2020	2021
Angola	69.7	89	109.8	132.2	124.4
Botswana	39.6	41	39.4	39.8	38.8
Burundi	48.6	53.4	59.4	67.7	68
Eswatini	25.1	33.4	38.4	46.8	49.5
Kenya	55.2	60.1	60.8	64.5	66.8
Lesotho	38	47.1	48.5	51	50.5
Malawi	61.1	63.1	63.4	68	69.1
Mozambique	102.4	107.2	109	125.4	124.9
Namibia	43.9	50.2	53.2	66.6	67.7
Rwanda	32.3	34.8	38.6	55.1	57.1
Tanzania	37.7	38.6	38.1	40	41.8
Uganda	33.7	35.6	40	46.3	50.7
Zambia	33.7	35.6	40	46.3	50.7
Zimbabwe	52.9	37.3			

Debt vulnerabilities will increase……

- Debt burden indicators to worsen arising from:
  - Increased debt stocks.
  - Higher interest rates.
  - Exchange rate depreciation.
  - Matrices used to calculate debt sustainability have worsened.
  - Bail outs by governments..
- Elevated debt vulnerabilities in most countries, especially those which had:
  - high debt distress prior to the pandemic
  - moderate risk of debt distress
- Countries which had narrow margins of debt sustainability could be reclassified to moderate risks

What should countries do to minimise the risks?

- Take advantage of the debt relief initiatives offered by IMF, G20;
  - Seek debt relief from China, which is the main creditor to many developing countries
- Integrate debt management into the country's economic management processes, including conducting debt sustainability analysis and medium term debt management strategies; and improving internal coordination.
- Enhance communication with investors, both external and domestic
- Adopting frameworks to manage contingent liabilities
- Use market borrowing mechanisms (avoid central bank advances)

Thank You