Speaking Notes for
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Debt Sustainability Panel

CGD Conference on Financing Low-Income Countries: Towards Realistic Aspirations and Concrete Actions in a Post-Covid 19 World

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Introduction

1. **The COVID pandemic is still evolving with considerable uncertainty.** The magnitude of the shock has prompted extraordinary responses — first to secure lives, and, second, to reduce the social and economic burden from the pandemic on the vulnerable segments of the population.

2. **Massive fiscal response packages and supportive monetary policy measures have been implemented in many countries to deal with the fallouts from the crisis**. However, in most low-income countries (LICs), the situation has been complicated as most LICs are confronting the crisis under conditions of elevated debt profiles and high debt service payments. Initial IMF and World Bank Debt Sustainability Analyses (DSA) from the onset of the crisis show that external government debt service payments in LICs will be much higher in 2020 and remain elevated in the medium term. This has constrained policy responses to the crisis and amplified vulnerabilities across most LICs.

3. **The Fund and other multilateral institutions as well as some bilateral partners have responded with some financial support.** Although the scale of the crisis requires massive additional financial support to safeguard progress towards the SDGs, elevated debt levels and the accompanying high debt service payments means that much of the support will rather fund debt obligations and limit the ability of LICs to respond to the crisis. This has necessitated calls for suspension of debt obligations and debt forgiveness in some instances and there are major risks inherent in this approach.

4. **The Debt Service Suspension Initiative (DSSI), launched by the G20, for instance provides scope for additional resources for the world's poorest countries to mitigate the impact of pandemic.** By freezing external debt service payments until the end of 2020 from all official bilateral creditors, it is estimated that a debt 'standstill' of roughly $11.5 billion in emergency liquidity support could be available to eligible countries in 2020, equivalent to about 40 percent of total projected public external debt service (World Bank, 2020).

5. **As one would naturally conclude, the DSSI is a step in the right direction, and designed to help countries respond to the crisis.** For example, some analysts have argued that the emergency support by the

IMF/World Bank and the announcement of the DSSI programme have contributed to the significant reductions in the sovereign bond spread for most of the emerging market economies, including even those that did not participate in the programme. However, risk perception levels remain high and above the pre-COVID levels. It thus appears that the pandemic would leave behind some medium to long-term shocks to fiscal and financial settings of these economies such that their fading would require more than what the DSSI would seek to solve. Several limitations of the programme have been identified:

a. Adverse impact on market access countries since it may send the wrong signal about the country's credit worthiness.
b. Potential unintended legal ramifications from possible contravention of some of the legal clauses/agreement.
c. Heterogeneity of debt composition potentially implies that countries with low official multilateral and bilateral debt under consideration may not benefit much from the initiative; and other creditor participation remains largely uncertain.
d. Restrictive conditionality may hurt more — especially for countries with sizable access to international capital market funding – since countries accessing the DSSI will have to comply with IMF /World Bank ceilings on non-concessional borrowing.

Debt Management in Ghana: A Historical Perspective

6. After a relatively long period of economic challenges, **Ghana benefited from debt forgiveness in 2005** as part of efforts by development partners to assist the country recalibrate the economy towards reducing the huge developmental gaps identified under the millennium development goals.

7. **However, the magnitude of the estimated infrastructure deficit** in almost all segments of society— economic, environmental, health, education etc —was such that the small tax base, largely composed of a relatively small formal economy, and limited income from the traditional raw material exports, could not finance the required capital investments.

8. **The need for other sources of financing became crucial**. Following years of successful macroeconomic stabilisation, partly helped by debt relief, the country began the process of accessing foreign private capital. First, the domestic primary market for government securities was opened

to non-resident investor participation; and, in 2007, the first sovereign bond was successfully issued in the Eurobond market, one of the first in SSA. This step was important since:

a. the domestic financial system was shallow and could not generate enough resources to support the development agenda to reduce poverty;
b. although concessional loan facilities, such as by IDA and ADF, were largely attached to specific mutual interest of Ghana and the DPs, certain required strategic set of infrastructures to meet the strong desire to transform the economy into a market based could not be financed through those means.

9. **In the process, the composition of external debt shifted significantly** towards the private financial markets while a sizable proportion of domestic debt is now held by non-residents.
   a. share of sovereign bonds 42% in external debt stock in July 2020;
   b. Non-resident holding of domestic debt as share of domestic debt stock was 20.4% in July 2020 from 38.5% in 2017.

10. **While access to external financing has facilitated the execution of critical infrastructural projects**, helping to expand the frontiers of growth, it has also complicated macroeconomic management and increased vulnerabilities.

Way forward over the next couple of years

11. **The relatively complex structure of the Ghanaian debt stock requires that debt management should include** regular access to domestic market (with an eye on non-resident investors), regular access to the international capital market, maintaining a stable exchange rate and inflation, sustaining real sector growth at the rate enough to pay down existing debt, and minimizing the interest cost on the various components of the public debt stock.

12. **For frontier economies like Ghana, debt sustainability and growth have become the most critical policy anchor underpinning macroeconomic management**. Ghana has opted for the clear path that requires maintenance of sound macroeconomic fundamentals that will

ensure market access at least cost and while at the same time engaging the attention of non-residents at the longer end of the domestic market.

How the international community can work together to help countries get through the current debt

13. The DSSI or even calls for debt cancelation can provide enormous relief to countries to deal with the current debt challenges. Nonetheless, there are major risks including:
    a. The signal it sends to the market about credit worthiness
    b. Potential loss of market access in the medium to long term
    c. May raise the cost of external financial
    d. Risk of moral hazard

14. **Importantly, while efforts at mobilizing subsidised funds to support emerging economies is a welcome one**, as these will help meet present critical social spending needs at reasonable cost, a **more enduring support** should include:
    a. correcting the narratives of our economies in the international discourse space.
    b. Highlighting the opportunities for growth above the global average is critical.
    c. Also, encouraging investor interest in impactful infrastructural projects that would enable our economies to expand the capacity to generate higher sustainable and equitable growth is another channel through which the international community can support fiscal sustainability in the economies of developing countries like Ghana.

15. **Finally**, **perhaps crucially, it is important for these economies to be supported to:**

    a. Strengthen and implement reforms aimed at dismantling bottlenecks in domestic revenue mobilization and administration,
    b. Define a feasible fiscal adjustment plan to stabilise debt in the medium term.
    c. Support transparency in debt statistics
    d. Ensure sustainable lending/borrowing
    Improve the capacity of domestic financial institutions to support domestic productive capacity.