DEBT MANAGEMENT IN JAMAICA

Michele Robinson

Bank of Jamaica
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1. Introduction and Overview

At the end of 1970 Jamaica's stock of debt amounted to US$154.mn or 12 per cent of GDP, and 29 per cent of exports of goods and services. By 1975 the debt had more than quadrupled. By 1980 the debt had almost tripled again. Rapid debt accumulation also took place in the first half of the 1980s, the stock growing two-fold from the 1980 position to US$3.6bn., or to a peak of 160 per cent of GDP and almost 280 per cent of exports of goods and services. Since 1985 substantial growth has occurred in only one year, 1987. Thereafter, the level of debt outstanding has remained virtually constant.

Jamaica, with a small, highly open economy, has the undesirable distinction of having been classified throughout the decade of the 1980s as one of the most heavily indebted countries in the world. With debt per capita amounting to just under US$2,000 for the latter half of the 1980s and the debt service ratio, prior to rescheduling, in excess of 50 per cent on average for the period, the classification is only partially indicative of the severity of the problem of debt. Not reflected in the debt indicators is the social cost associated with debt. Successive administrations have become increasingly constrained in providing the investment in social services and amenities consistent with improved living standards. For Jamaica, the debt has halted the process of development.

The rapid increases in the debt in the 1970s and 1980s and the phenomenal transformation from a low and manageable debt service, even up to 1980, to a crisis of illiquidity in the 1980s begs the questions as to the role and effectiveness of debt management during this period.

If Debt Management is simply defined as ensuring the efficient use and control of borrowed funds then, by implication, it suggests two broad activities. Firstly, that ability to repay must be ensured through 'efficient use' of the funds.

Secondly, that by effective ‘control’ the decisions regarding the role and/or level of debt accumulation must form an integral part of macro-economic policy.

With that framework, four time periods have been distinguished as coinciding with different phases of debt management, and are as follows:-

1970-76:	rapid debt accumulation; no debt management;
1977-80:	rapid debt accumulation; forced debt management;
1981-85:	rapid debt accumulation; reactive debt management;
1986-present:	high but stable debt stock; active debt management.

It is argued that in the first phase of rapid increase in the debt there was a complete absence of debt management. With debt and, particularly, debt service appearing within containable levels at that time, and with imbalances in the external accounts perceived as temporary, the issue of the capacity of the country to repay did not appear to have been critical. The growth of debt went unchecked.

In the subsequent two periods, 1977-80 and 1980-85, debt management did take place. In the first instance it was passive or involuntary, imposed by the conditionalities of a Fund Programme and the inability to meet commitments falling due on commercial obligations. In the next phase debt management evolved to be ‘reactive’, responding to the increased inability to service debt by a series of reschedulings of not only commercial debt, but also of bilateral obligations. This reaction of rescheduling continues to the present.

In the final phase, 1986 to the present, debt management has become increasingly pro-active but focus still remains limited to the existing debt portfolio and not beyond to the terms under which new debt is to be contracted.

Active debt management in this period has been confined to the following:

a) establishment of a centralized debt database essential to effective monitoring of debt;

b) concerted efforts at external debt diplomacy, whereby Jamaica has taken an active role in proposing new debt initiatives to the international community;

c) creating an institutional framework for increased co-ordination among public institutions involved in debt.

Debt management is steadily assuming a more important role as an element Jamaica's overall debt policy. Nonetheless, the scope of debt management remains limited. With an expanded role of the possibility does exist for debt to return to manageable proportions.

2. 1970-1976: Not Debt Management

Jamaica has historically had a deficit on the current account of the balance of payments. For the two decades up to the early 1970's, this deficit was financed primarily by private capital flows, much of it direct investment in the mining sector. However, by 1973, a number of developments, chief of which was t he first oil price shock, combined to result in a dramatic widening in the current account deficit. Also significant among these developments was the declining rate of growth and subsequent decline of private capital inflows as international developments in the alumina market and soaring energy cost predisposed foreign investment to alternative mining sites.

These adverse economic trends coincided with the entry into office in 1972 of a new political administration which actively undertook to have the State assume the dominant role in economic activity. Government expenditures rose at an annual average rate of 35 per cent in the period 1973/74 to 1976/77, and in the absence of commensurate increases in revenues the size of the fiscal deficit expanded markedly. As a percentage of GDP, the fiscal deficit grew from 7 per cent in 1973/74 to 15 per cent in 1976/77.

In a similar trend, the current account deficit grew from 6 per cent to 11 per cent during the four year period.

As the deficit in the fiscal and external accounts widened rapidly, so too did the inability to finance them out of a domestic resources. Increasingly the gap in the current account was financed by external borrowing and by the depletion of foreign exchange reserves. By 1976, Jamaica's foreign exchange reserves had been exhausted. It was an inevitable outcome of the widening imbalances on the current account compounded by the persistent monetization of the fiscal deficit.

Recourse to foreign borrowing was easily facilitated during the 1970-1976 period, as capital markets were flush with petro-dollars. The early structure of Jamaica's debt portfolio reflects the reliance predominantly on commercial bank financing as more than 60 per cent of the debt accumulated over the period came from that source.

The debt stock between 1970 and 1975 grew from US$154.0mn to US$688.0mn., a more than four fold increase. It represents the fastest growth rate of the debt in any five year period in Jamaica's recent economic history. As a percentage of GDP, the debt had risen from 12 per cent to 31 per cent, and in relation to exports of goods and service the debt rose from 29 per cent to 61 per cent.

The debt was not managed during this period. The dictates of crisis management required immediate support for the imbalance in the fiscal and external accounts, and foreign loans at relatively low cost were easily available to fill the gap. The rapid rise in indebtedness runs contrary to one of the basic debt management tenets on control over the rate of debt accumulation.

While at the end of 1975, the debt indicators suggested that the debt and debt service were still within manageable proportions, what was alarming was, firstly the sharp rate of increase in the debt and, secondly, the absence of any indication that the rate of growth would diminish especially as the malaise in the economy deepened.

Within such a scenario, the implications were clear that Jamaica's future capacity to repay was diminishing rapidly.

Particularly worrisome towards the end of the review period was the maturity structure of the debt which was heavily skewed towards the short-end, consistent with the relatively short-term nature of market borrowings. Available information for the period 1974 and 1975 indicates that on average for each year some 60 per cent of the debt had a maturity of over 16 years.

The cost of borrowing was also rising steeply. As debts contracted from commercial banks had attracted variable rates of interest, Jamaica's debt servicing was increasingly sensitive to rising international interest rates.

By the end of 1976, the foreign exchange problem had critical at the same time that payments on commercial banks fell due. In 1977, Jamaica had little option but to seek balance of payments support under a Standby Agreement from the International Monetary Fund. The stage was set for imposed debt management.

3. 1977-1980: Forced Debt Management

In the period 1977-1980, two IMF Standby agreements were negotiated and implemented, both programmes ending prematurely. Stabilisation measures concentrated primarily on demand-management policies designed to relieve the pressure on the balance of payments. Private consumption and government expenditures were to be subordinated in favour of investment, at levels consistent with targeted improvements in the external accounts.

The desired economic improvements failed to materialize. The current account gap widened from 2 per cent of GDP in 1977 to 8 per cent by 1980. Fiscal expenditure grew both in absolute terms and relative to GDP and as a consequence, the fiscal deficit as a percentage of GDP widened to 17 per cent. Overall economic activity continued to decline and between 1974 and 1980 there was a cumulative decline of 21 per cent in real GDP.

Debt servicing which had been manageable in the preceding review period was by 1977 problematic. Considerable bunching of commercial bank payments had occurred, and these payment began falling due. This sent a negative signal to the commercial banks which became increasingly reluctant to provide fresh funding to the country.

It became imperative for Jamaica to seek funding from alternative sources. Bilateral funding was not readily available in the required quantities as donor countries viewed the political and economic direction being taken by the then administration, which such caution. Therefore, there was little option but to seek balance of payments from the International Monetary Fund.

With IMF assistance came a network of conditionalities. Among these were restrictions on the level of new short and medium term external borrowing, the underlying rational being to skew the terms to maturity structure more towards its long end. This was to have afforded urgent cash flow relief over the short and medium terms.

Another important facet of the Fund programme was that it facilitated debt rescheduling negotiations between Jamaica and its commercial bank creditors, the Fund's stamp of approval being an essential prerequisite for such a facility.

Because control of the amount of borrowing, with a view to modifying the maturity structure and providing short term debt relief, took place within the framework of a Fund programme, debt management during this period is said to have been 'forced'.

Available data indicate that there was a significant shift in the terms of maturity structure of the debt. From a peak share of 60 per cent of the debt with a maturity of five years or less in 1974, the share of 35 per cent by 1980. The share of debt with maturity of over 15 years rose from 7 per cent to 36.5 per cent.

In addition to the shift in maturity structure, a significant shift in the debt structure by creditor category was also occurring during the period 1975-1980. Most striking was the growth in multilateral debt, which grew by a factor of almost seven to US$543.5mn or 29 per cent of the share of the overall debt. At that time, multilateral debt would no doubt have been very attractive given its long term maturity and relatively lower cost in comparison to market rates.

While there was an evident shift in the maturity and creditor structure of the debt, nonetheless, the overall growth in debt continued at a brisk pace. The absence of restrictions on medium to long term borrowing permitted the growth in the debt to continue unabated, with adverse implications for Jamaica's future ability to service the debt.

In summary, a fundamental principle of debt management continued to be neglected as the capacity of the country to repay its obligations was still diminishing.

4. 1981-1985: Reactive Debt Management

At the end of 1980, a new political administration assumed office. The policy imperative of the new administration was to reverse the negative trends in output, employment and growth which had characterized most of the 1970s. Chief among the objectives was to achieve improvements in the balance of payments, lower inflation, and a greater level of savings and investments. Expansionary demand management policies were accompanies by activities geared at deregulation and diversification of the economy.

The policy initiatives met with moderate success over the period 1981-1983. Inflation moderated to an annual average rate of 7 per cent in this period compared to annual average of 30 per cent in the latter half of the 1970s while real GDP grew on average by 1.5 to 2.0 per cent during this period. The recovery, however, proved short lived.

Associated with the deregulation of the economy, was a massive surge in imports of consumer goods. However, exports contracted sharply during this period as the recession in the US economy deepened. Exacerbating this decline was the significant contraction in Jamaica's principal foreign exchange earning sector, the bauxite and alumina industry. The gap between merchandise imports and exports widen dramatically, the deficit amounting to 9 per cent on average in the years 1981 – 1983. The overall current account deficit deteriorated from 5 per cent to 9 per cent of GDP.

The large imbalances on the external current account were financed by large scale foreign assistance, primarily from the International Monetary Fund, the World Bank and the United States, through its Agency for International Development (USAID). Inflows from the US which amounted to 50 per cent of the share of all bilateral flows in 1981/82 jumped to an annual average of 80 per cent in 1982/83 and 1983/84. World Bank and Fund credit accounted for over 85 per cent of the inflows from multilateral institution.

Between 1980 sand 1985, Jamaica's debt doubled. From a value of 89 per cent in 1980, the debt to GDP ration had reached an alarming peak of 160 per cent in 1985. On an accrual basis, the debt service ratio had risen from 24 per cent in 1980 to 58 per cent in 1985. Also of significance was that the creditor composition of the debt had changed markedly. With 40 per cent share of the total debt, bilateral creditors were the largest source of financing by 1985, followed closely multilateral lending institutions with a share of 38 per cent. Commercial banks accounted for only 11 per cent of the total share of debt outstanding. This compares with shares of 25 per cent and 29 per cent outstanding to commercial banks at the end of 19809 accounted for 21 per cent of the total.

The future capacity of the country to repay the massive accumulation of debt which occurred during this period was largely predicated on the assumption by the authorities that the country was on a sustainable economic growth path and that future export earnings would be sufficient to adequately service the debt. In the light of experience these assumptions proved to be unrealistic.

With the assumption that the country, could, in the medium term, grow its way out of the debt, attention was focused primarily on the means by which cash flow relief from debt service could be obtained in the interim. Hence, rescheduling of commercial bank and bilateral debts became the centerpiece of Jamaica’s debt management programme.

In the five year period, 1981-1985, three commercial bank rescheduling took place (1981, 1984, 1985). In 1985, the first multi-year rescheduling was negotiated and commercial bank obligations falling due for the period 1985 through 1990 were rescheduled. It was envisaged that with a multi-year arrangement in place sufficient time would elapse for Jamaica to carry through its economic adjustment and enable it to service its obligations relatively comfortably. Formal bilateral negotiations under the aegis of the Paris Club were first conducted in 1984. Subsequent reschedulings have taken place in 1985, 1987, 1988 and 1990.

As reschedulings became the norm, it became increasingly evident that the debt problem had become intractable. Reschedulings, although proving short term debt relief, would eventually have to be repaid. With the contractual cut-off date fixed by the Paris Club, the amount of relief available in successive reschedulings was diminishing. In addition, the capitalization of interest arising from bilateral reschedulings was increasing the overall level of indebtedness. Interest payments on rescheduled commercial bank debts were also becoming onerous.

In addition to these factors, the structure of the debt itself had begun to constrain the amount of debt which was reschedulable. Some 40 per cent of the debt was owed to multilateral financial institutions and therefore was not eligible for rescheduling.

With the full utilization (in terms of amounts rescheduled) of the debt rescheduling facility, it was apparent that other elements of debt management would have to be employed if any progress in tackling the problem of the debt and its servicing was to be made. In effect, debt management would have to become increasingly pro-active.

5. 1986 to the Present: Pro-Active Debt Management

Since 1986, the performance of the economy has been mixed. Macro-economic policies have centered around high demand management as efforts were concentrated on correcting the large imbalances which still persisted in the fiscal and external accounts.

Most favourable international conditions, in particular declining international oil prices and higher prices for bauxite and alumina exports did however allow for some revitalization of the economy in the period 1987/88 and early 1988/89. Earnings from tourism also rose markedly, and in fact surpassed those from bauxite and alumina exports.

The deficit in the current account fell from 12 per cent of GDP in 1985/86 to 4.5 in 1987/88 and the overall public sector deficit from 10.3 per cent to 5.8 per cent.

For fiscal years 1986/87 and 1987/88, the economy grew in real terms at an annual average rate of 5 per cent. However, the passage of Hurricane Gilbert caused severe dislocations to the economy, and the growth rate slowed to 1.5 per cent, far less than anticipated.

Fiscal expenditures in the aftermath of Gilbert increased outside of programmed ceilings, as reconstruction efforts got underway. Improvements on the current account deficit were also less than expected.

The level of indebtedness stabilized after 1985, but for a jump in 1987 due primarily to the depreciation of the US dollar. Multilateral and bilateral lending continued but the level of inflows was far less than that in the period 1980-1985. While inflows were diminishing, at the same time repayments not subject to rescheduling continued apace. Hence, by 1987 Jamaica began to make net transfers to its major creditors, in particular the World Bank and IMF. Over the two year period 1988/89 to 1989/90 total net transfers to multilateral institutions have amounted to in excess of US$450mn., or on average 12 per cent of GDP.

Within the context of a high level of indebtedness, the authorities undertook a number of initiatives. First among these was the effort to centralize the debt database in order to facilitate more effective monitoring of the debt and greater accuracy of the numbers. The catalyst for seeking to establish a comprehensive database was the rescheduling exercises, which required that projections on debt and debt servicing in the medium term were available and reliable. With the assistance of the Commonwealth Secretariat, a packaged debt recording and management system was installed at the Bank of Jamaica in 1986. The rationale for housing the centralized system at the Bank was primarily because the Bank had the responsibility for managing the country's foreign exchange and for implementing the adjustment programmes agreed to with the Fund. A department within the Central Bank, the External Debt Management Department was established in early 1986, with one of its core functions being to ensure the 'accurate and timely recording and retrieval of data concerning the total external debt'.

Institutional arrangements also extended to the establishment of two Committees; a Debt Policy Committee, chaired by the Governor of the Central Bank and reporting to the Financial Minister, and a Working Committee which reported to the Policy Committee. The view was that these Committees would facilitate consultation on the formulation of debt strategies, and would also ensure a smooth flow of information between the relevant public agencies and into the centralized database.

The launching of a debt conversion programme in 1987 was also a feature of active debt management. The primary objective of Jamaica's debt conversion programme was to reduce Jamaica's debt to the commercial banks by US$200mn or 50 per cent of the total debt owed these institutions. The programme was also intended to facilitate and encourage new investment in designated priority sectors of the economy. While the programme to date has only been moderately successful, its implementation is indicative of the willingness of the authorities to seek new options to ease the debt burden.

Jamaica also began to take a more active role in joining with the international community to seek solutions to the debt. In 1987, Jamaica put for consideration at various regional and international fora its first official proposal on the debt. The initiative, subsequently adopted by the Caricom group of nations, proposed the establishment of a new facility by the multilateral financial institutions to overcome the constraint of not being able to reschedule debts due to them. This facility would enable countries such as Jamaica, highly indebted to the multilateral institutions, to refinance these obligations at longer maturity tantamount, therefore, to a rescheduling of these debts.

The proposal which was circulated to the international community and presented at the 1987 IMF/World Bank annual meetings, failed to garner substantial support from creditor governments. Debt initiatives at that time were addressed primarily to middle income countries, highly indebted to the commercial banks and the low-income debt-distressed Sub-Saharan countries. Nonetheless, the proposal was significant for its pioneering role at the time. Of interest, is that more recent debt proposals (The Craxi Report 1990) in recognition of the problems faced by countries heavily indebted to official sources, contained in essence the basic elements of Jamaica's early proposal.

The efforts started in 1987 continue today, as Jamaica adds its voice to these pressing for meaningful ways to address the problem of the debt.

The debt at the end of 1989 amounted to US$4.0 billion or 105 per cent of GDP. Debt service at 32 per cent of exports of goods and services remains unacceptably high. Nonetheless, the debt while high has remained at virtually the same level since 1987. With debt management becoming increasingly active, if the growth in the overall level of the debt is contained it is conceivable that, in the medium term, the debt can return to manageable proportions.

6. For the Future

Debt management has evolved to become increasingly pro-active. However, there still remain elements to overall debt management which need to be pursued.

Foremost among these is the need to agree on a set of guidelines for providing consultations on the contracting of new debts and to regularize the flow of information. In the absence of a formalized set of arrangements, it has not been possible to systematically and comprehensively evaluate the terms under which new loans are contracted, and actively ensure improved terms. New techniques related to liability management such as interest and currency swaps are as yet unexplored. Using these tools could provide additional foreign exchange savings to the country.

With the level of debt presently stable, if the growth of debt is rigidly controlled and the terms on which new loans are contracted improved (45 per cent of debt is contracted on concessional terms the debt indictors which are already improving should recover even further. The challenge for the future is for debt management to assume a more active role in bringing the debt to more sustainable levels. With effort, it can be done.

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