# Debt Watch - Caribbean

## Issue No. 13: July/August 2009

## News

### ECLAC projects 1.2% fall in Caribbean GDP in 2009

The Economic Commission for Latin America and the Caribbean (ECLAC) projects that the GDP of English and Dutch-speaking Caribbean nations will fall by 1.2% in 2009. ECLAC notes that the economic slowdown in the sub-region will be less pronounced that in Latin America as a whole (3.1%) but also notes that economic growth in 2010 will only reach 0.5%. The low growth projections are largely predicated on the week performance of countries that depend on tourism and financial services (Bahamas, Barbados, Jamaica, and the member countries of the Eastern Caribbean Currency Union).

*Source: Caribbean Net News*

### IADB undertakes US$26 billion loan conversion

On August 1, 2009, the Inter-American Development Bank (IADB) closed the largest liability management operations it has ever executed with its clients. The exercise allowed borrowers to take advantage of historically low interest rates in United States dollars by locking fixed rates.

In total, 41 borrowing shareholders and government guaranteed institutions accepted the offer and converted US$26 million of outstanding debt – more than half of IADB's total loan portfolio – to new interest rates and/or dollars.

The total participation rate was 76% of the US$34.8 million of loans eligible for the offer. The IADB amended 518 loan contacts in its loan portfolio in order to change the interest rates and currencies, where applicable.

The offer allows countries and entities with sovereign guaranteed loans to convert "adjustable rate" loans to fixed rate or debt tied to the three-month dollar London Interbank Offered Rate (LIBOR), or a combination of both. Adjustable interest rates, introduced by the IADB more than a decade ago, were difficult for clients to forecast and hedge because they reflected the cost of the pool of IADB borrowings. Adjustable rates used in the IADB's Currency Pooling System and Single Currency Facility Loans.

*Source: Inter-American Development Bank*

### Jamaica takes advantage of IADB conversion offer

Jamaica is among the borrowers that have taken advantage of the offer by the Inter-American Development Bank (IADB) to convert "adjustable rate" loans in its portfolio to fixed rate or debt tied to the three-month dollar London Interbank Offered Rate (LIBOR), or a combination of both.

The Head of the Debt Management Unit in Jamaica's Ministry of Finance, Pamela McLaren, said that after a detailed and prudent assessment of the eligible IADB loans in the Government's portfolio, the decision was taken to convert 100% of Jamaica's pooled-currency IADB loans and over 50% of its single-currency IADB loans. At the end of June 2009, Jamaica's total pooled-currency IADB debt amounted to US$93 million and single currency debt to US$444.6 million.

*Source: Jamaica Gleaner Online*

### Standard and Poor's downgrades Jamaica

The international rating agency, Standard and Poor's(S&P), has downgraded Jamaica's long term sovereign credit rating from B- to CCC+ and assigned the country a negative outlook.

S&P stated that Jamaica's fiscal accounts, which were already under pressure before the international financial crisis started last September, have deteriorated even further this year. S&P projects that Jamaica's government borrowing requirement for the fiscal year 2009/10 (ending March 31) to be 20% of GDP. They also project that gross general government debt will rise to 120% of GDP.

In March 2009, S&P lowered both Jamaica's long-term foreign and local currency sovereign credit ratings by one notch to B- from B and lowered the country's short-term ratings to C from B.

*Source: Jamaica Observer*

### Moody's maintain stable outlook on Jamaica

Moody's Investor Services has maintained its stable outlook on Jamaica's B2 government bond ratings. Moody's said that its outlook reflected its expectation that the government of Jamaica will sign off on the pending US$1.2 billion stand-by arrangement with the International Monetary Fund and address financing shortfalls exacerbated by the global economic crisis.

*Source: Jamaica Observer*

## IMF approves US$1.2 bn in debt relief to Haiti

In an announcement on June 30, 2009, the International Monetary Fund (IMF) has granted Haiti US$1.2 billion in debt relief. The relief frees up money for the government to spend on health, education and fighting poverty, the IMF further stated.

The relief was granted as part of the Enhanced Heavily Indebted Poor Countries (EHIPC) Initiative, a joint programme between the IMF and the World Bank's International Development Association (IDA).

Haiti is the 26th country to receive debt relief under the IMF and World Bank initiative and the final eligible country in the America's to reach this milestone.

*Source: International Monetary Fund*

## CDB to provide US$10 mn policy-based grant to Haiti

The Caribbean Development Bank (CDB) is to provide a policy-based grant equivalent to US$10 million to the government of Haiti. The grant is part of a broader programme of support by other multilateral financial institutions that seeks to enhance fiscal and debt management in Haiti through a series of technical assistance projects. The International Monetary Fund, the World Bank and the Inter-American Development Bank are the other institutions involved.

*Source: Caribbean Development Bank*

## IADB approves US$25 mn grant to Haiti

The Inter-American Development Bank (CDB) has approved a US$25 million policy-based grant to Haiti to support priority public expenditures and fiscal reforms.

The grant, which will be disbursed in a single trance, will support the Haitian government's reforms to increase tax and customs revenues, improve the efficiency of public spending and strengthen the management of the public debt.

*Source: Inter-American Development Bank*

## Antigua and Barbuda receive US$50 million in assistance from Venezuela

The government of Antigua and Barbuda has received US$50 million in financial assistance from the government of Venezuela. The financial assistance comes in the aftermath of the collapse of the Allen Stanford business empire which has badly hurt the economy of the small state, causing losses and layoffs and damaging the nation's image as an offshore destination.

Antigua and Barbuda is the third member of the 15 nation most English-speaking Caribbean Community (CARICOM) to join ALBA, an alliance established by Venezuela to counter US influence in Latin America.

*Source: Caribbean Net News*

## Barbados secures US$120 mn from Scotiatrust and Merchant Bank

The government of Barbados has secured US$120 million through a Scotiatrust and Merchant Bank bond issue. The funds are intended to boost the government's foreign exchange reserves and help finance major capital works.

The Barbadian Prime Minister, David Thompson, in singing the agreement emphasised that the arrangement was not a signal of further private borrowing by his administration. He further stated that the loan was consistent with Barbados' medium term debt strategy.

The bond is divided into two tranches, with US$80 million for five years with 14 quarterly payments, and the remaining US$40 million for ten years with 14 semi-annual repayments.

*Source: The Barbados Advocate*

## Dominica receives US$5.1 mn under the IMF Exogenous Shocks Facility

The Executive Board of the International Monetary Fund has approved a disbursement in the amount of SDR 3.28 million (US$5.1 million) under the rapid-access component of the Exogenous Shocks Facility (ESF).

The Exogenous Shocks Facility comes with minimal conditions and quick disbursements. It is intended to assist small-island developing states respond to adverse external economic conditions.

Dominica has experienced extensive damage to crops and infrastructure from two hurricane strikes in 2007-08. In addition, the economy has been badly affected by sharp fall in tourism earnings, FDI inflows and remittances all a consequence of the global turndown. The IMF financing will help limit the decline in Dominica's external reserves and help catalyze support from the international donor community.

*Source: International Monetary Fund*

## Grenada seeks IMF assistance

The government of Grenada has announced plans to ask the International Monetary Fund for financial assistance to help pull though the global economic crisis.

Grenada's Finance minister, Nazim Burke, said that the island wants a financial package that will help out debt on a sustainable trajectory, undertake reforms to improve the business environment and strengthen the government's capacity for economic and fiscal adjustment.

Grenada has written a letter of intent to the IMF requesting the completion of the third review under the Poverty Reduction and Growth Facility (PRGF) - the IMF's low-interest lending facility for low-income countries – and the release of the associated disbursement in an amount equivalent to some US$6 million.

*Source: International Monetary Fund*

## Barbados signs agreement with EU

The Barbados government has signed a EURO 10.13 million financing agreement with the European Union (EU) to help modernise the country's International Business and Financial Services Sector. The financing is part of the EU's annual development assistance following of the reform of the EU's sugar regime.

*Source: Caribbean Net News*

## IADB to fund Guyana disaster risk management plan

The Inter-American Development Bank (CDB) is to approve a US$1 million dollar grant to support the design and implementation of an integrated disaster risk management plan for Guyana. The grant will fund the development of a national integrated disaster risk management plan and the design of an investment programme in flood prevention and mitigation among others.

The Bank said that the grant is in keeping with IADB's country strategy with Guyana for 2008-2012

*Source: Inter-American Development Bank*

## IMF approves US$10.7 mn for St Lucia under the Exogenous Shocks Facility

St Lucia will receive SDR 6.89 million (US$10.7 million) from the International Monetary Fund under the rapid-access component of the Exogenous Shocks Facility (ESF).

The IMF noted that the global economic slowdown has strongly affected tourism activity in the Caribbean. The impact on St Lucia has been considerably as government tax revenues, foreign exchange reserves and employment are closely linked to tourism. Real GDP growth is projected to contract by as much as 2.5% and unemployment to increase substantially in 2009.

The IMF arrangement is expected to help mitigate the impact of the global crisis on St. Lucia's economy.

*Source: International Monetary Fund*

## Trinidad state oil company sells US$850 million bonds

The Petroleum Company of Trinidad and Tobago Limited (Petrotrin) sold US$850 million of 10 year bonds in its first dollar denominated debt sale in two years.

Petrotrin sold the 9.75% bonds to yield 9.875 or a spread of 618.4 basis points over similar-maturity Treasuries. Credit Suisse Group AG and JP Morgan Chase & Company underwrote the sale.

*Source: Caribbean Net News*

## Feature

## To Restructure or Not To Restructure – The Case of Jamaica

Currently, there is an ongoing debate in Jamaica as to whether the public debt should be restructured. The underpinnings of this debate are obvious - Jamaica's debt is enormous.

Jamaica's outstanding debt (domestic and external) amounted to US$13.5 billion or 116% of GDP at the end of the 2008/09 financial year. Domestic debt accounts for more than half of this total with a share of 54%. The huge debt imposes a crippling burden on the country. Debt service payments absorb virtually all of central government revenues (99.2% for 2008/09). The provision of public goods and social services is severely impaired as a result. Debt service accounts for almost 60% of the government budget. With public sector wages accounting for another substantial share of the government budget (22.4% in 2008/09), precious little is left for public investment.

What is the Jamaican government to do? Consider Jamaica's position against some widely accepted international benchmarks for public debt. Debt-to-GDP of 60% is considered the threshold beyond which debt is unsustainable. In other words it is the point beyond which governments typically face difficulties meeting their debt service obligations. Jamaica's debt-to-GDP is almost double this total. Other international benchmarks paint an even grimmer picture of Jamaica's debt situation. Total debt service (domestic and external) as a share of government revenue should not exceed 15%. In 2008/09, Jamaica had a corresponding ratio of over 6 times that amount, at 99%.

Only one benchmark meets the threshold requirement for debt and that is the ratio of external debt service to exports of goods and services, commonly referred to among debt management practioners as the debt service ratio. The international benchmark is 20%. Jamaica has a debt service ratio of 14.6%. Arguably it is this ratio that has over the years allowed Jamaica continued access to the international capital markets because from an external perspective, Jamaica earns sufficient revenues from its exports to adequately service its external debt. It is a partial view – one that in recent years is being replaced by a more holistic perspective that takes into consideration the effects of a large and growing domestic debt.

But what options are available to Jamaica to reduce its debt and debt burden and get its debt ratios to internationally acceptable levels. There are two options.

One is to grow out of the problem. In other words, generate the necessary fiscal revenues out of increased productive activity to narrow the fiscal deficit and reduce the appetite for debt.

The other is to restructure the debt. In other words, take steps to alter the structure of the debt either through deferring some payments to a later date (debt rescheduling), securing new loans on improved terms to refinance existing loans (refinancing), swapping the debt into some other type of liability (debt conversion) or simply having part or all of the debt extinguished by the creditor (debt write off).

Typically, the driving objective of debt restructuring is to ease the debt burden of a country by obtaining immediate cash relief. Either the debt stock has to be reduced, interest costs have to be reduced, the repayment period for debt service has to be extended or some combination of all three have to take effect. Debt restructuring, in this context, is usually viewed negatively. It signals debt problems.

Many countries, however, restructure their debt not as a response to debt difficulties but in order to actively manage their portfolio and to take advantage of better financing terms in the market. In debt management terms this is commonly referred to as voluntary debt restructuring and is a part of sovereign liability management. An involuntary restructuring occurs when a government's debt is unsustainable and it has little option but to restructure.

But let's go back to Jamaica's two options in resolving its debt difficulties. What are the considerations? Take the growth option. Economic growth creates a virtuous cycle of falling deficits and lower debt, creating conditions for lower interest rates, further growth and further reductions in debt. But growth in Jamaica has been elusive. In 2008, the economy contracted by 0.6%. Since 1991, the country has grown, on average, by a mere 1% per annum. Such growth rates are hardly the trigger for a significant and sustained reduction in the debt. In fact, Jamaica's huge debt is a constraint to growth. Jamaica is in a vicious rather than virtuous cycle of debt and growth.

In 2008, the International Monetary Fund estimated that with a sustained growth rate of about 2.5% per annum and assuming a strong fiscal effort, including a balanced fiscal budget, and no policy deviations or external shocks, at best, Jamaica could achieve a debt-to-GDP ratio of 100% by 2013. Reducing debt-to-GDP to 60%, a target recently adopted by the countries of the Eastern Caribbean Currency Union for 2020, seems a very distant goal for Jamaica.

So what can be done to kick start growth and achieve debt reduction in the near term? The most immediate option for Jamaica is to restructure its debt. But what debt to restructure and what are the implications for the debt and for the economy as a whole?

A look at Jamaica's debt indicates that it is comprised primarily of domestic debt. The domestic portfolio, in turn, is made up primarily of securities issued at market rates. It is the most expensive debt in the portfolio and, from a cost perspective, the most suitable candidate for restructuring.

Ranked second in cost terms are the sovereign bonds issued in the international capital markets. These are classified as part of the external debt although much of it is held by Jamaican residents. These are also debt securities but many enjoy a longer repayment period than their counterparts issued in the domestic capital market.

But, by its very construct, securities are difficult to restructure. Securities, unlike a typical loan, are owed to multiple investors rather than a single creditor. Negotiating with all holders - financial institutions, corporations and individual - to arrive at a consensus is extremely difficult but it is not impossible. Argentina, Ecuador, Moldova, Russia, Uruguay and Ukraine have all undertaken bond restructurings in recent years.

The penalties for restructuring debt from the capital market, whether domestic or international can be severe. Access to further financing is typically closed and for long periods. Jamaica relies heavily on the international capital market and restructuring would likely close these markets for a considerable time. The question is: is it worth the pain to restructure now, suffer the immediate consequences, but benefit from immediate cash relief and more sustainable debt levels in the long term?

For the near future, the international capital markets are closed. Jamaica's debt indicators and debt dynamics have led to downgrades by all the major rating agencies. This may be the opportune time to experience the severe withdrawal symptoms and wean the country of the opiate of international capital market debt. This doesn't address the issue of how to finance the budget in the interim but the answer may be to draw on considerable support from the multilateral financial institutions.

Restructuring domestic debt is likely to prove more difficult. Undertaking a restructuring with domestic holders has implications for the domestic financial sector and for the broader economy. Bond issues will not provide the foreign exchange inflows to buoy central bank reserves. This has implications for the exchange rate and in turn, interest rates. The balance sheets of financial institutions will be affected and this may affect their capital adequacy or solvency ratios. These are serious issues and will be of major concern to the central bank. Many small investors will be deprived of investment income. Investors may shun government paper. But what are the alternatives to government paper in Jamaica's thin domestic market? For investors these may be few. Small investors and large financial institutions may likely continue to hold government paper albeit seek to charge a premium for it.

The Jamaican government may find it more manageable and more achievable to target the major holders of government debt – the commercial banks and securities dealers – for restructuring. They are not averse to such a prospect.

However, the position of Jamaica's financial sector is that a restructuring should not make them any worse off. They want any restructuring to be "present value" neutral. What this means is that they want a trade off between the interest rate they receive and the maturity of the instrument. If the government restructures the debt by lowering interest rates, the bankers/dealers will want to hold the securities for a shorter period. On the other hand, if the government seeks to lengthen the term of repayment, a higher interest rate would be demanded.

While such an option is workable it is not likely to provide the government with the magnitude of relief that it needs. The financial sector having enjoyed substantial returns from their securities holdings over the years may have to contemplate sharing some of the burden of a debt restructuring.

So what's Jamaica to do? In 2009/10, it is estimated that Jamaica's debt servicing as a share of the budget will increase, albeit marginally, to 57% and will absorb 96% of total government revenues. Debt to GDP is expected to rise beyond 116%. The immediate option would be to restructure and give the country a fighting chance to grow out of its debt over the long term.

*Michele Robinson*

## Debt Statistics

### National

The table below provides comparative data on Jamaica's debt indicators against selected internationally accepted benchmarks for public debt.

| | **Jamaica 2008/09** | **Internationally Accepted Norms** |
|---|---|---|
| Total Debt to GDP | **115.8** | **60%** |
| Domestic Debt to GDP | **62.9** | **15-20%** |
| Debt Service to Govt. Revenues | **99.2** | **15%** |
| External Debt Service to Exports | **14.8** | **15-25%** |

*Source: Ministry of Finance-Jamaica, IMF, World Bank, Debt Relief International, Commonwealth Secretariat*

## Upcoming Events/Courses

### November 2009

- November 27-29: Commonwealth Secretariat - Commonwealth Heads of Government Meeting (CHOGM); Port-of-Spain, Trinidad and Tobago.
- November 16-20: Centre for Latin American Monetary Studies (CEMLA): Joint CEMLA/IMF/World Bank Training for Trainers Workshop on Debt Sustainability for Low Income Countries; Mexico City, Mexico.
- November 16-20: World Bank Treasury: Implementing Government Debt Strategies; Washington, DC, USA.
- November 9-13: World Bank - Designing Government Debt Management Strategies; Washington, DC, USA. November 9-11: UNCTAD - Debt Management Conference; Geneva, Switzerland.
- November 8-12: Crown Agents - Debt Management and Public Financial Management Systems; Dubai, UAE

### October 2009

- October 19-20: CARTAC/IADB – LAC Debt Management Workshop on Debt Sustainability and Debt Statistics in Washington DC, USA.
- October 10: Eastern Caribbean Central Bank (ECCB) – Meeting of the ECCU Regional Debt Coordinating Committee in Basseterre, St. Kitts.
- October 6-7: IMF/World Bank – Annual Meetings of the World Bank Group and the International Monetary Fund in Istanbul, Turkey.
- October 5-19: Crown Agents – Advanced CS-DRMS User Training Workshop in Worthing, United Kingdom.

### September 2009

- September 17-18: Commonwealth Secretariat - Private Sector External Debt workshop on Capturing Debt Data in London, United Kingdom.
- September 1-4: Central Bank Publications Ltd - Residential Workshop on Government Debt Management: New Trends and Challenges in Cambridge, United Kingdom

If you have information about an important event or development related to public debt management in or relevant to the Caribbean, please email Michele Robinson at:

consult@michelerobinson.net