Debt Watch - Caribbean

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News

Further calls to immediately cancel Haiti's debt

The Centre for Economic and Policy Research (CEPR) has called for an end to the delay in cancelling Haiti's debt to international agencies.

In its new report, the CEPR has noted that Haiti is currently struggling to meet the requirements for cancellation of most of its total US$1.7billion foreign public debt. However, Haiti has to reach the "completion point" under the World Bank's Heavily Indebted Poor Countries (HIPC) initiative in order to receive debt cancellation. This is not expected until mid-2009 at the earliest.

The CEPR voiced its concern that funds, which could be used for social expenditures in the wake of the devastating hurricane season and rising food prices, are currently being spent on debt service payments.

The CEPR says that Haiti urgently needs debt cancellation in order to address humanitarian needs and help it withstand the effects of the global economic downturn.

Source: Caribbean360.com

IADB doubles grants to Haiti for 2009

The Inter-American Development Bank is to double its grants to Haiti to US$100 million for 2009. The increased funding is to help the Haitian government make vital investments in social and economic programmes.

The IADB has been providing Haiti with US$50 million in grants annually, since 2007, under an agreement to reduce the debts of the poorest member countries in Latin America and the Caribbean. The increase in grant funding was facilitated by a recent agreement among IADB members to shift administrative costs from the IADB's concessional window, the Fund for Special Operations, to the Bank's Ordinary Capital, the source for most of its loans.

The IADB president, Luis Alberto Moreno, also indicated that the IADB Board of Governors has approved US$14.15 million in interim debt relief for Haiti for the first half of 2009.

Source: Inter-American Development Bank

US$5 mn IADB loan to Barbados to improve public procurement system

Barbados is to improve its public procurement system to make it more efficient, transparent and accountable with a US$5 million loan from the Inter-American Development Bank (IADB).

The IADB funds will support the modernisation of the Barbados National Procurement System, a plan being implemented by the Ministry of Finance in order to get more competitive prices and reduce processing time while ensuring the integrity of the mechanism.

The IADB loan is to be repaid over 20 years with a 5-year grace period. It attracts a variable interest rate based on LIBOR.

Source: Inter-American Development Bank

Barbados government to raise Bds$1 billion to pay bills

The prime minister of Barbados, David Thompson, has announced that he will seek a resolution in the House of Assembly to raise BDS$1 billion (US$500 million) to pay a number of the government's outstanding bills. The money will be raised through the issuing of treasury bills, tax reserve and tax refund certificates.

Source: Caribbean Net News

CDB funds road works and sea defences in Dominica

The government of Dominica is to receive a soft loan of US$9.16 million from the Caribbean Development Bank (CDB). The loan is to help finance the rehabilitation of sea defences and road works in the village of Point Michel which was damaged by the passage of Hurricane Omar earlier in 2008.

Source: Caribbean Net News

Guyana benefits from CDB loan and grant financing

The Government of Guyana is to receive a loan equivalent to US$7.5 million from the Caribbean Development Bank (CDB) to assist in enhancing access to technical and vocational education and training (TVET).

The CDB is also to provide a grant equivalent to US$149,940 to the Iwokrama International Centre for Rain Forest Conservation and Development to help the centre improve its revenue-generating capacity through tourism and training of business enterprises.

Source: Caribbean Net News

Guyana gets US$27.9 million IADB loan for low-income housing

The Inter-American Development Bank (IADB) is to provide the government of Guyana with US$27.9 million in loan financing to help improve low-income families' access to housing.

The funding will finance the government's Second Low Income Settlement Programme which is expected to benefit about 12,000 households, or 8% of the country's households.

The IADB loan comprises US$13.95 million from the Bank's Ordinary Capital for a 30-year term including a six year grace period at a variable interest rate, and US$13.95 million from the Fund for Special Operations (FSO) for a 40-year term at a 0.25% fixed interest rate.

Source: Inter-American Development Bank

Jamaica receives US$90 million from the IADB

The government of Jamaica has received US$90 million of a recently agreed US$101 million loan package from the Inter-American Development Bank.

The loans reflect the refocused strategy of the Jamaican government to reduce reliance on expensive loans from the international capital markets and to source less expensive loans from multilateral lending agencies to meet its budgetary requirements.

Source: Caribbean Net News

IADB to help region pull through global credit crisis

The Inter-American Development Bank is financing a facility to help countries in the region affected by the global credit crunch.

The Multilateral Investment Fund, which the IADB administers, will provide up to US$20 million in financing to the Emergency Liquidity Facility to help Latin American and Caribbean microfinance institutions weather economic crises and natural disasters.

Source: Caribbean Net News

Feature

The Emergence of MDB Lending in Local Currency – Implications for the Caribbean

In recent years, a number of multilateral development banks (MDBs) have lent to member countries in their local currency. The African Development Bank (AfDB) has done so in respect of the South African Rand (ZAR) since 1997 and, since 2005, has included additional African currencies, beginning with the issuing of a local currency bond in the Botswana pula. In 2003, the Asian Development Bank (ADB) introduced its first lending instrument in selected local currencies, initially limited to private sector borrowers but, subsequently, opened to public sector borrowers in August 2005. The World Bank lent in local currency for the first time in Africa in 2008, making a ZAR 58.2 million loan to the Government of Namibia to support an educational improvement programme.

Closer home, the Inter-American Development Bank (IADB) has also been involved in local currency lending, launching a global bond denominated in Mexican pesos in April 2004. Since its inaugural bond issue, the IADB has issued other bonds in a number of Latin American currencies including Brazilian reais, Chilean pesos, and Columbian pesos.

The impetus for these institutions issuing in local currencies is the recognition that countries issuing debt in foreign currency expose their portfolios to significant currency risk. National governments earn their income predominantly in their domestic currency. Therefore, significant currency mismatches arise when governments contract debt and, as a consequence, service their obligations in foreign currency. Large shares of foreign currency debt leave governments particularly vulnerable to depreciation of the local currency as well as cross-currency volatility.

There is an abundance of empirical evidence that shows that countries with risky debt structures, in effect those with substantial foreign currency debt as well as those with significant short-term local currency debt, are more likely to have lower credit ratings, less exchange rate flexibility and higher volatility of GDP growth and capital flows. What is desirable, therefore, in terms of a safe debt structure is for governments to hold a significant share of long-term domestic currency debt in their portfolio.

For most developing countries, particularly in the Caribbean which largely comprises small-state economies, domestic financial resources are just not sufficient to meet government's financing requirements. Moreover, maturities in the domestic market are often much shorter and interest rates much higher than would be obtained overseas. For many Caribbean economies, therefore, it makes good sense, in the face of underdeveloped domestic markets, to borrow externally in foreign currency and assume the exchange risk in the debt portfolio.

A significant volume of foreign currency debt contracted by Caribbean governments is used to fund projects. There is still extensive demand across the region for project financing to satisfy basic infrastructure needs as well as more sophisticated infrastructure services. With the decline in aid flows from bilateral donors and the limited access of many Caribbean countries to the international capital markets, there is heavy reliance on the MDBs to meet the large financing requirements of infrastructure investment. Yet, at the same time, projects funded with foreign currency debt typically generate their revenues in local currency, creating a currency mismatch between the government's assets and its liabilities. It is this problem that MDB's have faced increasing pressure from their constituents to address.

Within the region, the IADB has in recent years sought to be responsive to member countries by lending in local currency to selected Latin American countries. The benefits have been twofold. Firstly, it has reduced currency mismatches, as both the debt liability and the income generated by the asset are denominated in the same currency. Secondly, it has helped foster domestic capital market development by opening new markets and providing diversification opportunities for local institutional investors such as insurance companies and pension funds.

Nonetheless, MDBs such as the IADB face constraints in local currency lending. Foremost among these, is the availability of local currency. Certainly, for the IADB, its ability to lend is determined by its ability to raised funds in local currency. This may be constrained by the size of the market. A second constraint is the cost competitiveness of the MDBs local currency lending. Ideally, the MDBs should finance borrowers at a cost lower than that which they themselves could obtain by accessing the local market. This may not be the case for a country's central government. It is likely that the central government would be able to borrow at a cost similar or lower than that of the MDB. Much of MDB lending in local currency has been to the private sector or public sector entities for this reason.

Can Caribbean governments benefit from MDB lending in local currency? Certainly Caribbean countries with high currency risks exposures due to either a high share of foreign currency debt or a high volume of foreign currency debt in nominal terms would benefit, particularly if such debts were contracted with multilateral lending agencies. Countries such as Jamaica, Belize and Grenada could be ideal candidates. Take Jamaica, for example. Given the large size of its external debt (US$6.1 billion, 2007) virtually all of which is foreign currency debt, and the sizeable share of its domestic debt (15%) which is denominated in, or indexed to, a foreign currency, Jamaica faces substantial currency risk exposure in its debt portfolio. The recent slide in the Jamaica dollar vis-à-vis the US dollar by more than 10% over the past 4 months underscores the vulnerability of the portfolio to exchange rate movements. Borrowing in local currency lending would insulate the portfolio from such currency movements.

The Jamaican government has been aggressive in re-engaging the multilateral lending agencies as an alternative source of funding to the international capital markets. The IADB, the leading lender to Jamaica among MDBs, has committed to lending the country between US$200 –US$300 million over the next three years. Given Jamaica's vulnerability to currency depreciation, receiving IADB financing in local currency would help significantly in mitigating such risk. The challenge is for the IADB to lend to the Jamaican government at cost competitive interest rates. Raising funds in the local market at rates less than the government would obtain may be difficult but not impossible especially if the IADB uses its leverage as a triple A rated issuer and pulls in new investors.

Innovative ways need to be found to reduce the riskiness of Jamaica's and many other Caribbean debt portfolios. Offering local currency financing to these countries is one such option. With the annual meeting of the MDBs are not far away, this may be one item for the agenda. *Michele Robinson*

Debt Statistics

Regional

For many Caribbean countries, external debt accounts for the bulk of the public debt portfolio. The predominance of external debt, almost all of which is denominated in foreign currency, embeds significant currency risk in government debt portfolios both in terms of cross-currency movements in the major international currencies and in terms of local currency depreciation.

The table below shows selected Caribbean countries whose public external debt portfolios exceed 50% to the total share of public debt.

Country	Share of external debt to total public debt (%) (2007)
1. Belize	89.9
2. Dominica	71.4
3. Grenada	74.9
4. Guyana	72.8
5. Montserrat	86.2
6. St. Lucia	58.8
7. St. Vincent	56.2

Source: ECCB, IMF

National

Barbados 

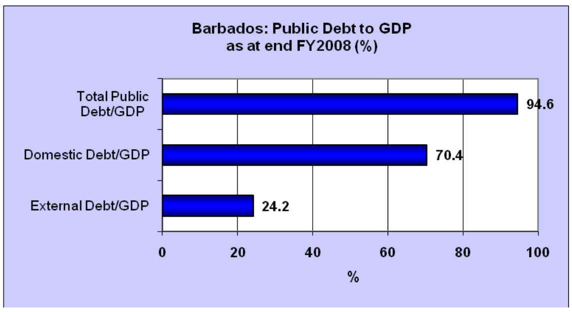
The table below provides data on key indicators in relation to the total public debt of Barbados.

Barbados: Public Debt Indicators

in percent of GDP (%)

	FY2006	FY2007	FY2008
Public and Public Guaranteed Debt	91.6	92.8	94.6
External Debt	28.9	27.6	24.2
Domestic Debt	62.8	65.2	70.4

Source: International Monetary Fund



Barbados has one of the highest per capita incomes and social development indicators in the Caribbean. With a per capita income of US$13,605 in 2007, Barbados enjoys a strong economy, based largely on high-end tourism and offshore financial services. It also benefits from strong political and governance indicators. It is this relatively high standard of living, strong economic fundamentals and political stability that accounts for Barbados investment grade ratings in the international capital markets.

Despite these favourable indicators, Barbados has been experiencing high and rising debt in recent years. Barbados' public debt has grown from 74.1% of GDP at the end of 1999/2000 to 94.6% at the end of 2007/08. The surge in public debt comes on the back of the 2001 September 11 attacks in the US and the global slowdown that followed events that exposed Barbados' high vulnerability to the external environment. As a consequence, Barbados suffered a severe recession. The government's policy response was to embark on a major public investment programme accompanied by substantial increases in public sector wages. The outcome was a significant widening of the public sector deficit, a more than six-fold increase from 2% at the end of 2000/01 to almost 13% at the end of 2002/03. With the debt financed primarily by debt, the public debt-to-GDP ratio jumped from 74% to 87% over the two year period to end 2002/03.

While the Barbadian economy rebounded strongly in 2004, continuing to grow at a solid pace until 2007/08, and the central government deficit narrowed by half to 6% of GDP at the end of 20006/07, high levels of debt persisted. Off-budget activities and the deficits of a number of loss-making public enterprises were the main factor behind the growing debt. Also a factor was the sizeable investments in infrastructure for the hosting of the Cricket World Cup (CWC) held in the Caribbean in 2007. By the end of 2007/08, the public sector debt-to-GDP ratio had risen further to 94.6%.

A breakdown of the public sector debt shows that domestic debt, with a share of 75%, accounts for the bulk of public debt. Of the 80% of domestic debt held by the central government, almost 80% is long-term, helping to mitigate the rollover risk associated with short-term debt. Official creditors account for just over 52% of Barbados public and publicly external debt. Flows from official creditors have been on the wane and as a result, private creditors, in particular investors from the international capital markets, account for a considerable share of the debt. Sovereign debt issues from Barbados continue to enjoy investment grade status, with Moody's assigning a Baa2 rating on long-term foreign currency debt and Standard and Poor's, a BBB+ rating.

Barbados wishes to become a top-ranked middle-income country by 2020. Moreover, it aspires to reduce central government debt to 60% of GDP by 2012. These twin objectives face serious obstacles in the present global economic environment. The government has committed to significant expansion in infrastructural development to meet its development objectives. However, the anticipated levels of expenditure are not likely to be met by commensurate increases in revenue, especially since higher revenue growth was predicated on continued strong economic growth particularly in the tourist sector. Tourism receipts are projected to fall significantly as the credit crunch takes hold in the US and the UK, the main markets for Barbadian tourism.

The IMF, in its most recent staff report (July 2008) anticipates that even with a deficit target of 2 ¼%, the overall public debt ratio will continue to rise over the medium-term. It has recommended an additional tightening of the primary fiscal balance by 4 percentage points of GDP in the upcoming fiscal year and greater fiscal prudence over the medium term to generate a public sector balance and reverse the trend in debt.

The Barbadian authorities will be seriously tested in the next one to two years. Rising oil and food prices have eroded consumer purchasing power and the government will be pressed to adjust wages accordingly. Inflation is expected to increase almost two-fold to 8.6% in 2008. At the same time, declines in visitor arrivals have precipitated an economic slowdown in Barbados, likely to slow further as the global credit crunch takes hold. Real GDP is projected to slow to 2% in 2008/09 from 3.3% in 2007/08.

Government will need to temper its development objectives in the short-term if it is to weather the global financial crisis and ensure long-term fiscal sustainability over the medium to long-term. It is only by implementing tough measures fiscal now, that government can progress in reducing its public debt, a key factor in generating strong and sustained economic growth over the long term. *MR*

Upcoming Events/Courses

March 2009

- March 27 - 31: 50th Annual Meetings of the Board of Governors, Inter-American Development Bank and the 24th Annual Meetings of the Inter-American Investment Corporation (IIC), in Medellin, Columbia.

January 2009

- January 19 - 23: Crown Agents hosts *Workshop on Debt Management and Public Finance Management Systems,* in London, 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:

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