CARIBBEAN: Debt initiatives highlight disaster impact

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Abstract

Multilateral debt relief options.

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Full Text

SUBJECT:Multilateral debt relief options.

SIGNIFICANCE:At the Third International Conference on Financing for Development, the UN Economic Commission for Latin America and the Caribbean (ECLAC) presented a proposal for multilateral debt relief for Caribbean island states. Barbados's finance minister, Chris Sinckler, has since called for the region to be granted no less favourable debt relief than that made available under the Heavily Indebted Poor Countries (HIPC) Initiative in the 1990s.

ANALYSIS: Impacts.

Caribbean countries cite debt reduction as indispensable to tackle both socioeconomic stability and global risks such as climate change.

However, securing broad support for debt reduction will be difficult.

The question of conditionality will be a vexed one.

Multilateral debt relief is not new:

Under the Multilateral Debt Relief Initiative (MDRI) launched in 2005, G8 countries called on the IMF, World Bank, and the African Development Fund (AfDF) to cancel all debt claims on low-income countries that had reached, or would eventually reach, the completion point under HIPC.

In 2007, the Inter-American Development Bank (IDB) also agreed to provide similar debt relief to five HIPC-eligible countries in the Western Hemisphere.

Countries seeking debt relief under the MDRI were required to maintain satisfactory macroeconomic policies, and to implement poverty reduction strategies and sound public-expenditure management.

Debt burden.

In 2000, the Caribbean's average gross public debt was equivalent to 68% of GDP, ranging from 24% in The Bahamas to 120% in Guyana. Ten years later, the average was 82%; excluding oil and gas rich Trinidad and Tobago, the average was close to 90%.

Recent World Economic Outlook estimates for 2015 show that the average has crept up to 85%, ranging from 62% in The Bahamas to 133% in Jamaica. Guyana's debt fell sharply in the mid-2000s due to debt relief received under HIPC, but the ratio rose from 60% of GDP in 2012-13 to an estimated 71% in 2015. According to ECLAC, debt service payments absorb between 30% and 60% of government revenue in Antigua and Barbuda, Barbados, Grenada, Jamaica and Saint Lucia.

Climate and debt.

The shift into unsustainable debt reflects domestic factors including an expansion of the public sector and government bailouts of failed financial institutions. However, it also reflects external factors, including natural disasters, the removal of trade preferences on sugar and banana exports, and the effects of the global recession on tourism (see CARIBBEAN: OECS struggles with economic challenges - October 30, 2013).

The region is one of the world's most disaster-prone, measured by disasters per capita and per square kilometre. The effects on growth and debt are significant (see CARIBBEAN: Hurricane season preparations underway - April 1, 2015).

According to research done at the IMF, output typically falls by about 1% in response to an average hurricane or severe storm. In Eastern Caribbean Currency Union countries, the debt-to-GDP ratio typically rises by almost 5 percentage points in the year of a hurricane occurrence. Moreover, recovery and reconstruction costs are largely financed by borrowing on commercial terms. Caribbean countries are ineligible for concessional borrowing from multilateral financial institutions.

ECLAC estimates that the cost of natural disasters in the region amounted to 30 billion dollars between 2000 and 2014. World Bank estimates indicate that average annual natural disaster losses in the Caribbean total 850 million dollars, compared to 200 million in the Pacific islands.

Adjustment efforts.

Calls for debt reduction have occurred against a background of considerable adjustment and debt restructuring efforts. Since 2002, six countries have entered into adjustment programmes with the IMF: Antigua and Barbuda, Dominica, Grenada, Guyana, Jamaica, and Saint Kitts and Nevis.

Jamaica .

The Jamaica fiscal programme requires annual primary surpluses of 7% of GDP -- among the highest across IMF member countries (see JAMAICA: Budget offers stability, but risks persist - March 26, 2015).

Saint Kitts and Nevis.

Saint Kitts and Nevis reduced its gross public debt from 160% of GDP in 2010 to 80% in 2014, largely because of inflows from its Citizenship by Investment (CBI) programme. CBI-related revenues were equivalent to 14.0% of GDP in 2014, contributing to an overall government surplus of 9.5% of GDP.

Grenada.

Grenada's adjustment included a public-sector wage freeze and workforce reduction, the introduction of a CBI programme and fiscal responsibility legislation to cap expenditure in line with trend growth in real GDP.

Its efforts to restructure its debt have been the most comprehensive in the Caribbean in recent years, encompassing private bondholders, the Exim-Bank of Taiwan, and bilateral debt. On bonds, the agreement reached in principle covers instruments that account for close to one-third of total public debt. Terms include a phased 50% principal haircut, with half of the reduction taking effect up front and the remainder upon completion of the sixth review of the IMF programme.

Grenada's bond restructuring is expected to reduce public debt by 13% of GDP in 2017 compared to the projected trajectory without the restructuring. Moreover, the Paris Club is tentatively scheduled to discuss the treatment of its loans to Grenada in September. As a result, Grenada's public debt is expected to fall to 68.0% of GDP by 2020 from 107.5% in 2013.

ECLAC proposal.

The ECLAC proposal includes the following elements:

Multilateral institutions would gradually write off 100% of their loans to small states, with bilateral donors also asked to participate.

Countries benefitting from debt relief would be required to make annual payments of scheduled multilateral concessional debt service in local currency into a Caribbean Resilience and Stabilisation Fund over ten years, to be managed by an institution such as the Caribbean Development Bank (see CARIBBEAN: Development Bank seeks expanded role - July 5, 2010).

Small Caribbean states would access the Fund to finance projects that promote growth, reduce poverty or protect the environment.

The resilience window of the Fund would provide financial resources for social development, disaster relief and projects to reduce disaster risk and mitigate climate change.

The stabilisation component would provide countercyclical resources for addressing external shocks.

Outlook.

ECLAC's analysis of the Caribbean's vulnerability to natural disasters and their debt impact helps clarify and place in a climate-related context the current crisis of large debts, sluggish growth and increasing anxiety.

This has helped to correct the notion that current debt levels are uniformly the result of overspending, inefficiency and weak fiscal adjustment.

However, progress in bringing the proposal onto the global development agenda will be slow. It will require the support of the multilaterals' shareholders, including countries in other regions facing slow growth and high debt burdens.

Debt relief under HIPC and MDRI was available to all countries meeting HIPC or low-income criteria, and they were obliged to undertake adjustment and reform measures in exchange for debt relief. The ECLAC proposal has left unclear issues of eligibility, conditionality and the tricky matter of how to ensure equal treatment across the membership of the multilateral financial institutions.

CONCLUSION: The ECLAC proposal reflects growing sentiment that IMF-led fiscal adjustment alone cannot resolve the Caribbean's difficulties, and that only debt reduction can break the cycle of crisis, adjustment, sluggish growth and social ills. Caribbean leaders hope that the proposal for multilateral debt relief will be placed on the global development and climate change agenda.

Details

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