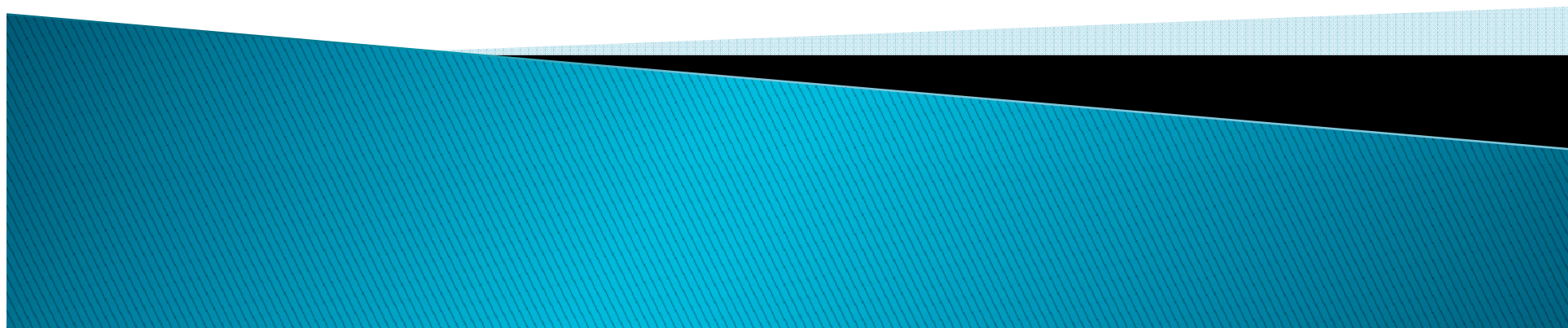


The Challenges of High Debt, Addressing the Debt Overhang: The Cases of Jamaica and Antigua

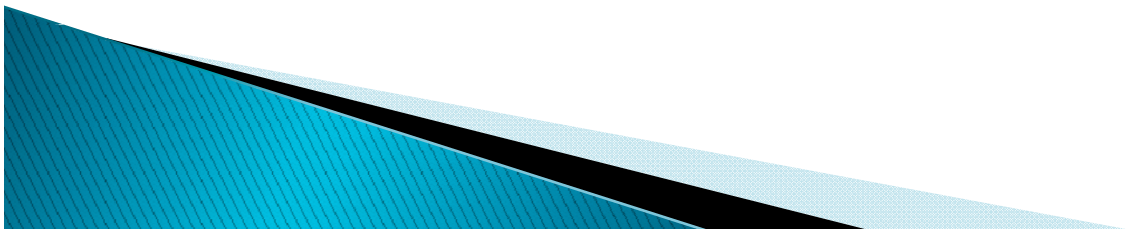
Trevor Alleyne

Western Hemisphere Department
International Monetary Fund

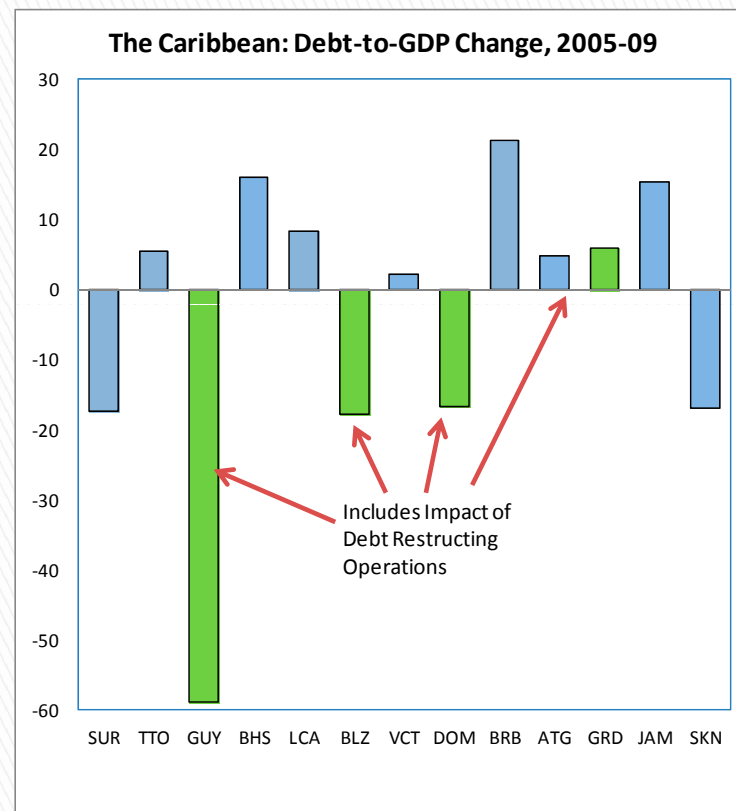
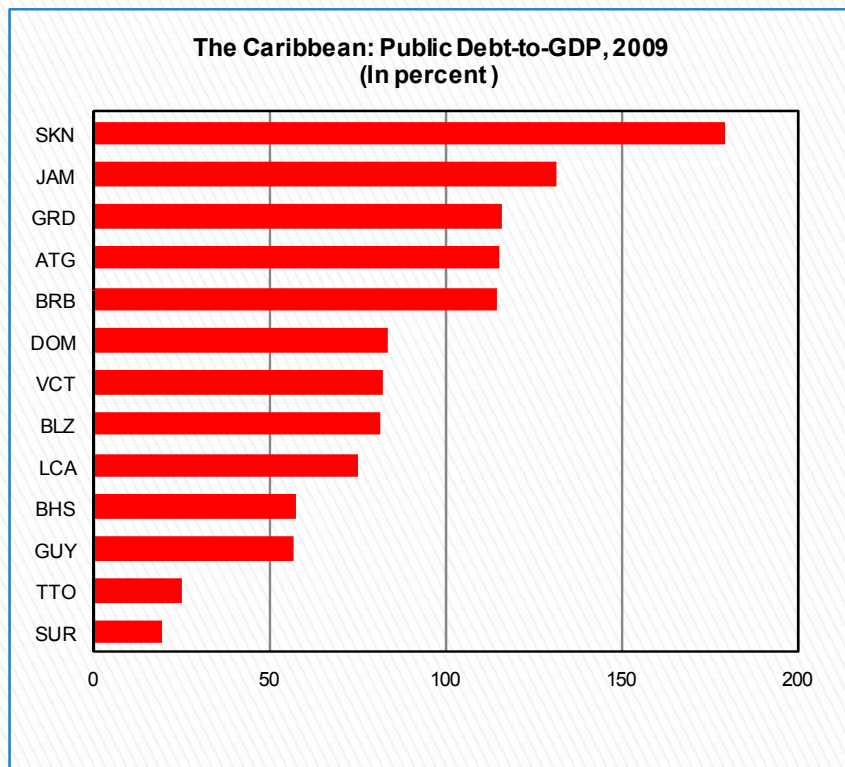


Outline

- ▶ **Why debt is bad?**
- ▶ **The impact of debt on growth**
- ▶ **Two Caribbean cases:**
 - **The case of Jamaica**
 - **The case of Antigua and Barbuda**



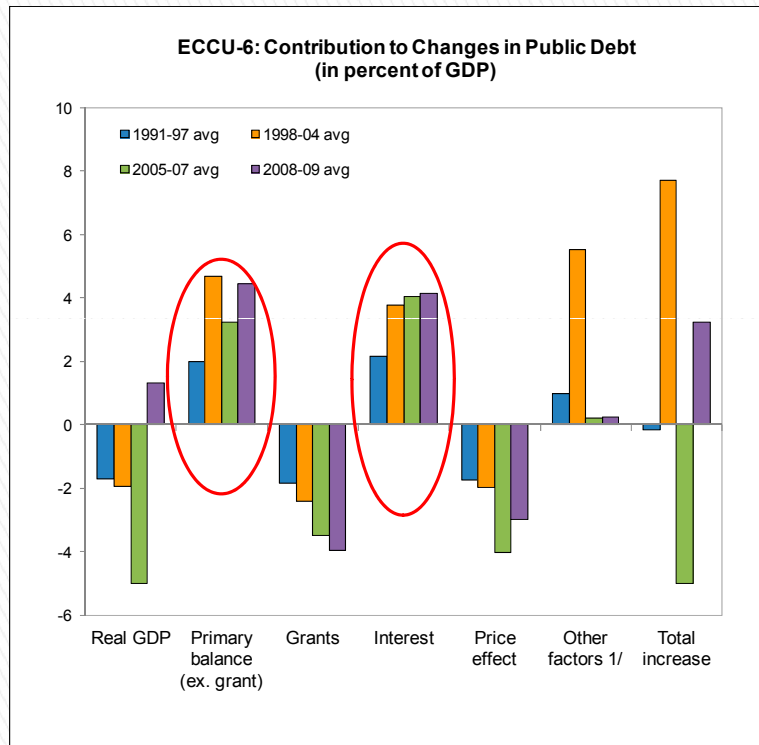
The “Debt Picture” in the Caribbean



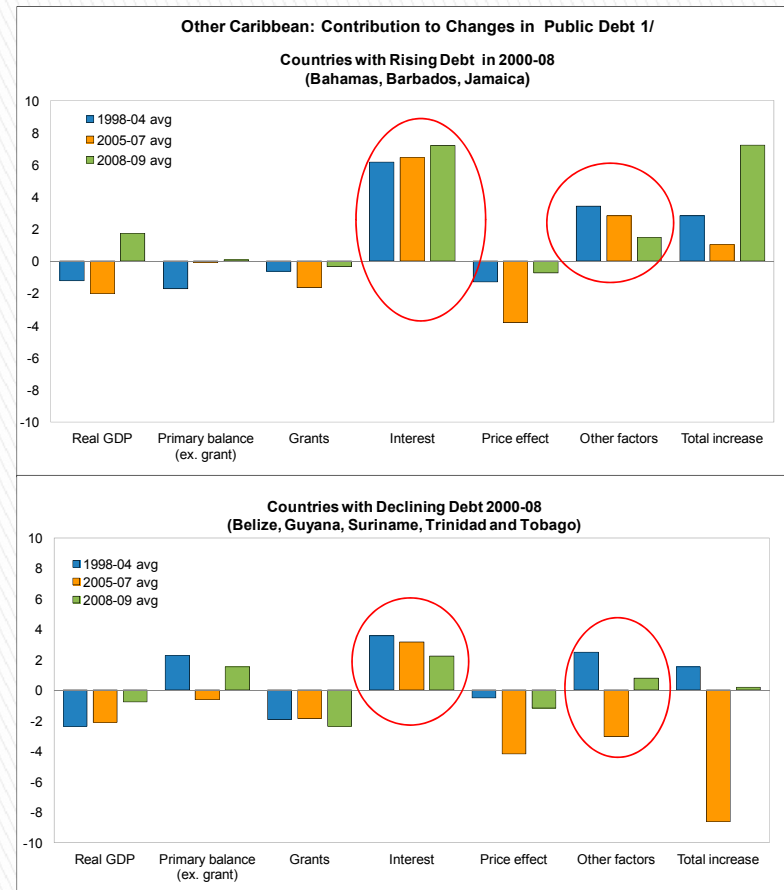
Debt in some Caribbean countries is among the highest in the world...

And has been sustained at high levels for several years...

Why has Debt accumulated?



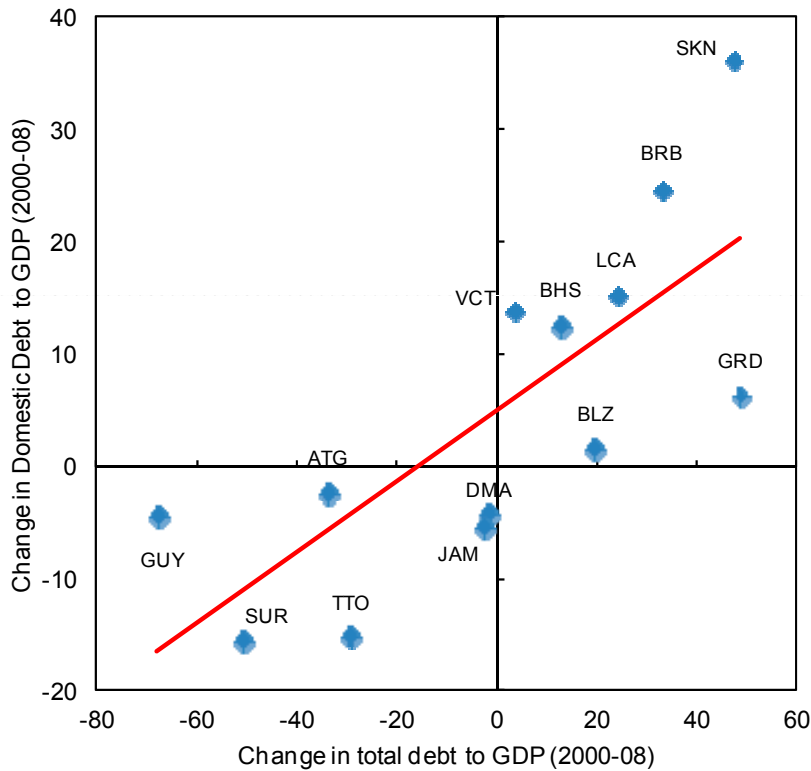
1/ Includes the effect of debt restructurings, privatization, recognition of off-balance sheet liabilities and increases in debt by public enterprises.



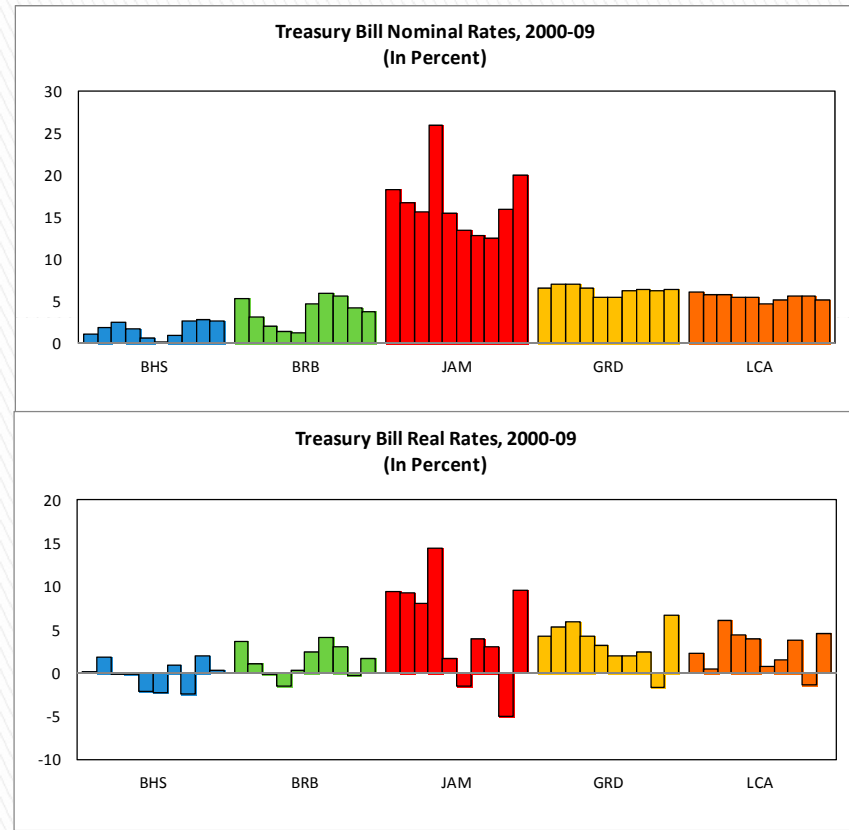
In the ECCU, large fiscal deficits and interest bills have contributed to debt accumulation, magnified by off-balance sheet events.

In the rest of the Caribbean, the impact of heavy interest bills dominates as a key contributor, followed by that of ad-hoc events...

How has Debt been sustained?



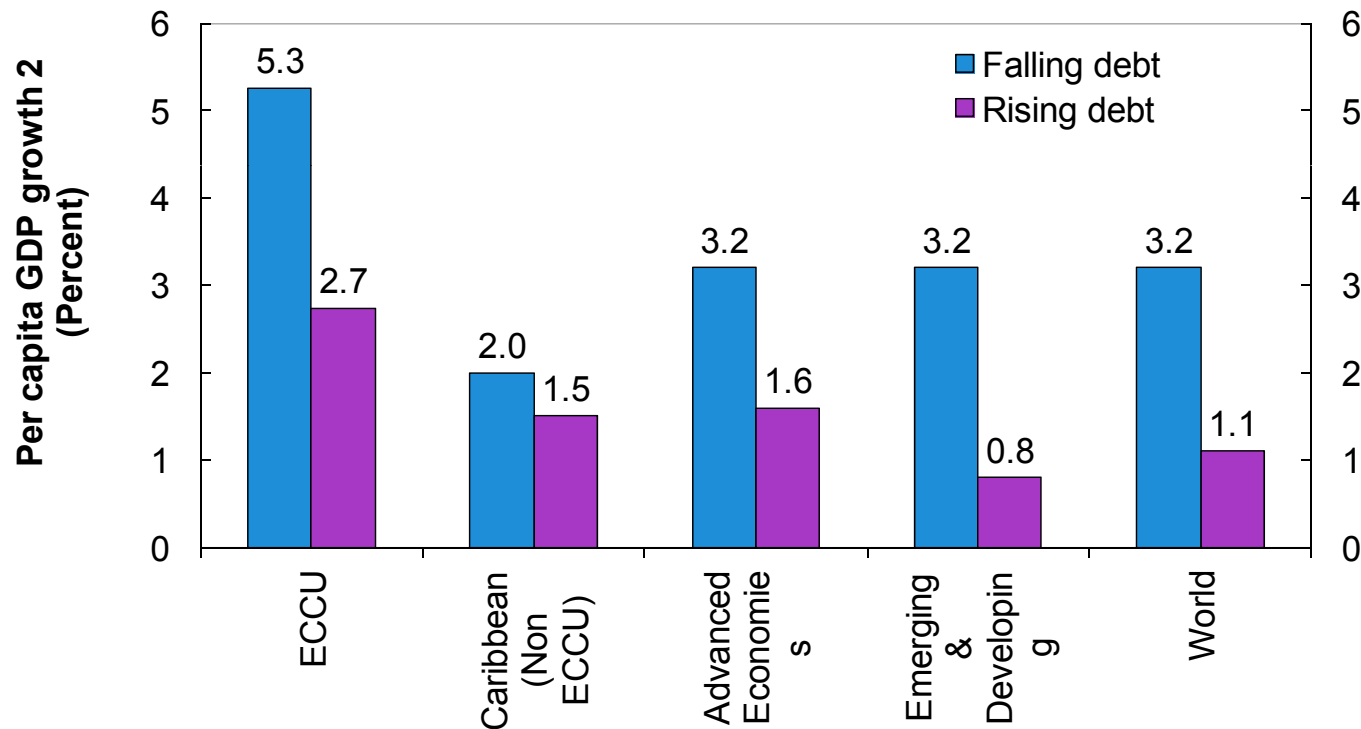
Rising total debt has relied heavily on access to domestic creditors...



But the response of traditional market indicators is still limited in most cases...

Reducing debt from high levels helps growth

World: Real per Capita GDP Growth During Periods of Rising and Falling Debt, 1970–2007¹



Sources: Heston, Summers, and Aten (2009); and IMF staff calculations. Based on the *Fiscal Monitor* (IMF 2010b), p. 63.

¹ Initial debt > 60 percent of GDP.

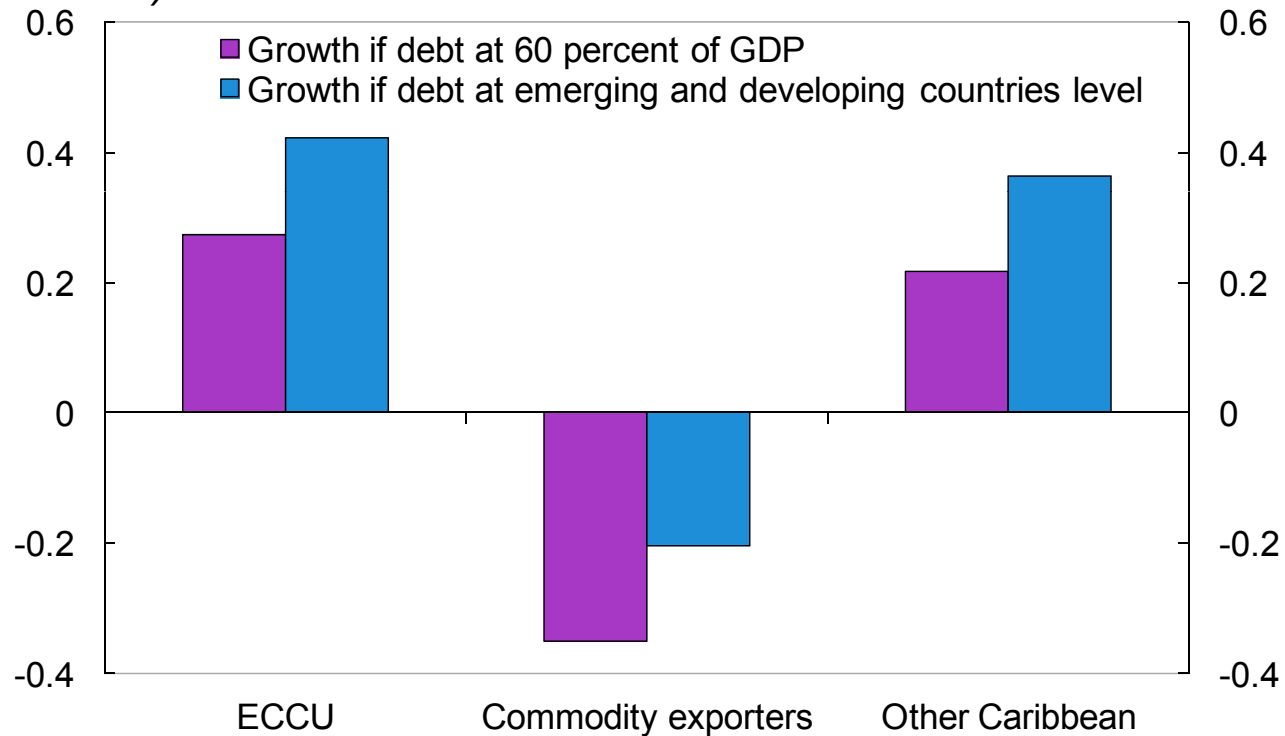
² Average for subsequent 5 years.

ECCU includes Antigua & Barbuda, Dominica, Grenada, St. Kitts & Nevis, St. Lucia, and St. Vincent & the Grenadines.

Non-ECCU Caribbean includes the Bahamas, Barbados, Belize, Guyana, Jamaica, Suriname, and Trinidad & Tobago.

Reducing debt has a positive impact on growth, and the inverse is also true

Caribbean: Effect of Debt on Growth ¹
(Percent)



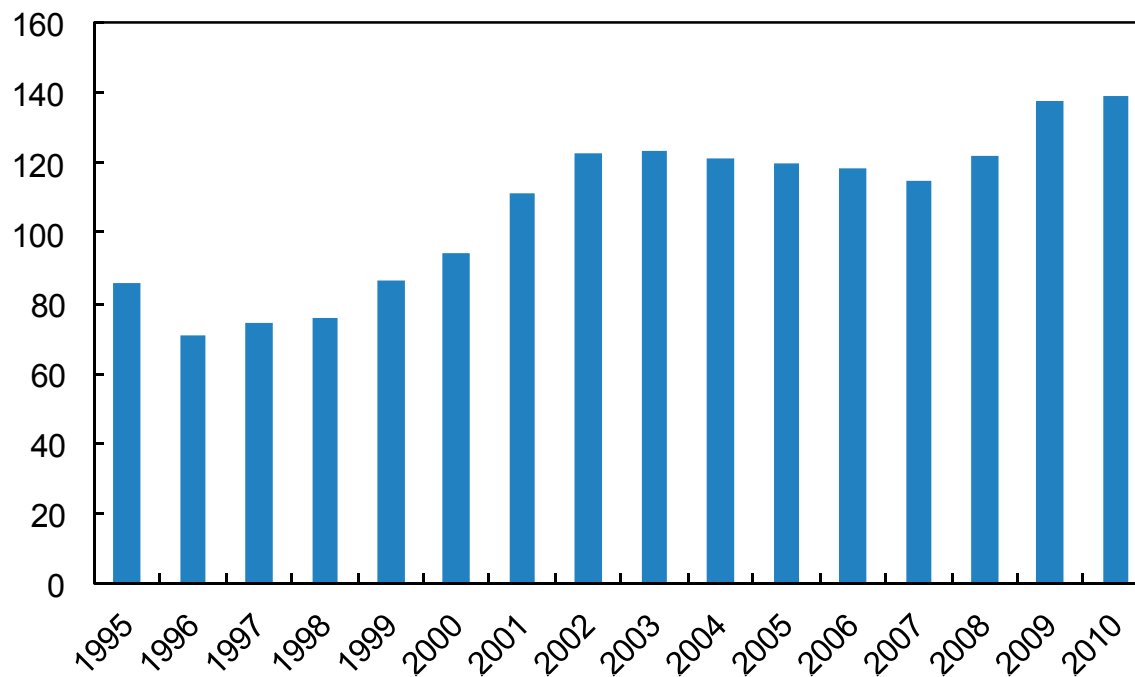
Source: IMF staff calculations.

¹ Assumes 2009 debt-to-GDP levels drop (or increase) to 60 percent or 44.9 percent of GDP.

JAMAICA

Public debt doubled as a percent of GDP as a result of the bailout of the financial system following the 1990s crisis

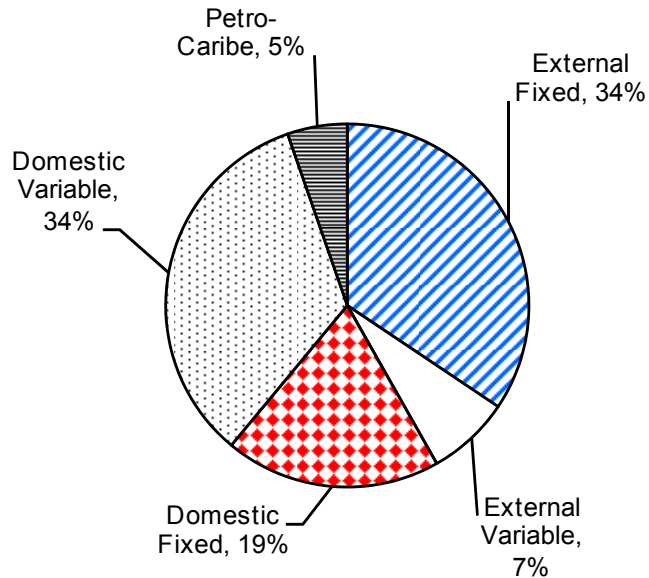
Jamaica: Gross Debt to GDP Ratio
(percent)



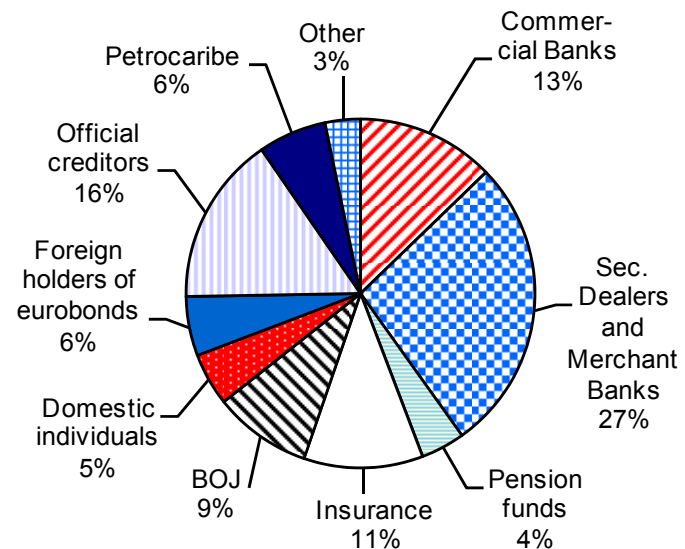
Jamaica - Public Debt 2009

- By type of instrument and holder

Public Debt by Instrument and Variability 1/
(percent of total public debt)



Holdings of Government Direct Debt 2/
(percent of total government direct debt)



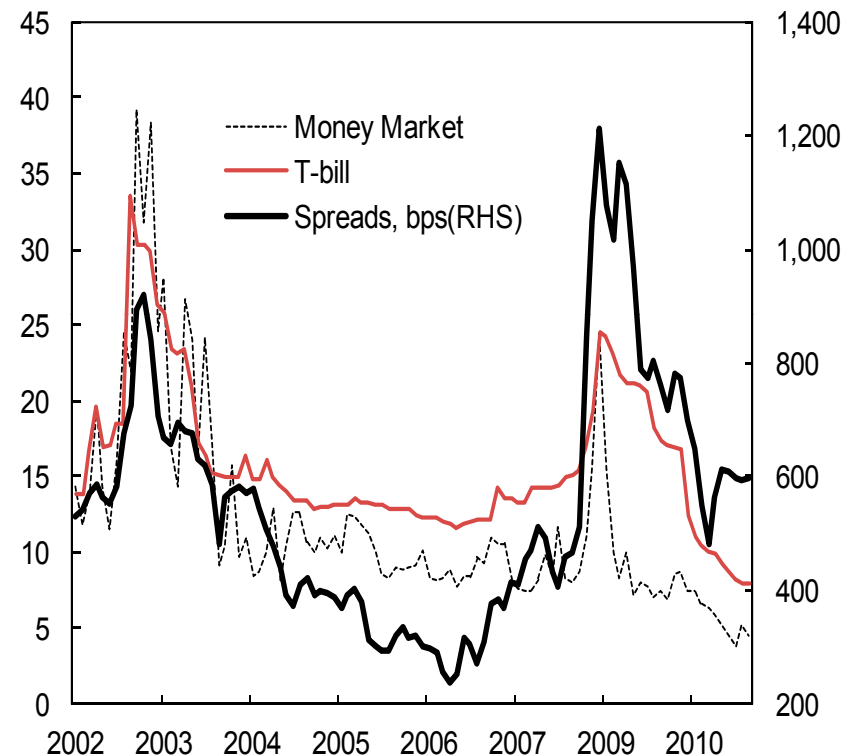
Sources: IMF staff calculations based on data from MoFP, Petrocaribe Fund and Banking sector balance sheets.

1/ Includes government guaranteed debt.

2/ Assumes 80 percent of eurobonds are held domestically. Does not include government guaranteed debt.

The global crisis created serious problems for debt management

- ▶ International capital market effectively closed.
- ▶ Domestic creditors demanded large increase in interest rates to rollover maturing debt, while also shortening maturities. Interest bill jumped to over 16 percent of GDP in FY2009/10.
- ▶ Rating agencies downgrade debt



Source: JP Morgan, Jamaican authorities and Fund staff calculations.
1/ Jamaican interest premium is estimated as the sum of risk free rate (proxied by the U.S. Federal Funds rate), emerging market premium (proxied by the EMBI+ index), Jamaica sovereign premium (proxied by the blended yields on Jamaica Eurobonds) and Jamaica currency premium (the difference between Jamaica 6 month T-bill yields and other identified risk premiums).

Policy Response – Fiscal adjustment is crucial more is needed.

- ▶ Fiscal measures to increase primary surplus: tax rate increases, wage freeze.
- ▶ Structural reforms in the fiscal area, especially those aimed at strengthening PFM.
- ▶ Focus of adjustment expanded to the public entities, which had been responsible for a significant part of public sector expenditure and debt generation.
- ▶ Address debt overhang: responsible for weak economic growth and periodic bouts of financial market volatility, impeding sustainability of past fiscal adjustment efforts.



Debt Exchange: Design and Pre-launch Considerations

- ▶ **Protect stability of financial system.**

- Detailed (institution-by-institution) stress testing carried out.
- No principal haircut.
- Financial sector support fund.

- ▶ **Legal clarity.**

- Legal aspects of the debt exchange (including constitutionality) were thoroughly analyzed to minimize potential sources of contention.
Debt exchange was voluntary.

- ▶ **Creditor buy-in.**

- Numerous consultations with bond holders about their balance sheet needs in order to maximize the demand for the new instruments.
- Strategic communication with rating agencies to influence their assessment of the debt exchange and the post-exchange outlook.



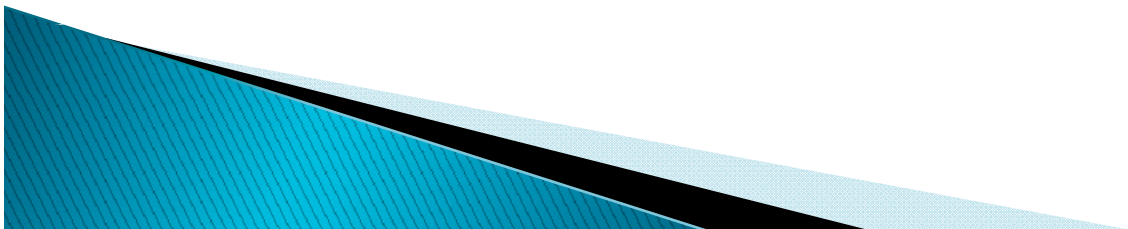
Debt Exchange: Design and Pre-launch Considerations (continued)

▶ Allocation rules

- Targeted reduction in the share of variable rate and US\$-denominated debt to lower exchange rate and interest rate risk.
- Increase maturity of the debt stock

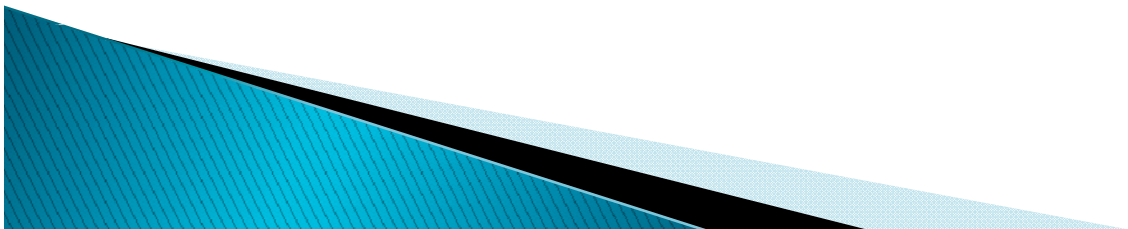
▶ Simplify functioning of debt market

- The new (benchmark) bonds—25 in total, comprised of 11 fixed, 9 variable, 3 US\$-denominated, and 2 CPI-index bonds—replaced over 350 different securities in circulation.



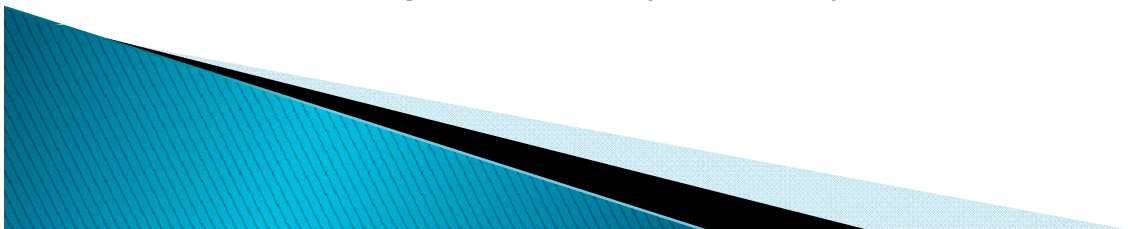
Carrots and Sticks

- ▶ **Call option to be exercised; use of tax surcharges.**
 - Although participation was voluntary, no holdout would be allowed to obtain a competitive advantage by opting out of the operation.
- ▶ **IMF Stand-By Arrangement.**
 - By late 2009, strong market sentiment that, without an agreement soon, Jamaica would quickly tumble into an economic and financial crisis. Government announced “No debt exchange, no IMF”.
- ▶ **Financial Sector Support Fund.**
 - Financed by the multilateral institutions to provide liquidity support (at non-punitive rates) in the event of negative effects of debt exchange. Access to the fund open only to institutions that exchanged over 90 percent of the old bonds in their portfolios.



Jamaica Debt Exchange (JDX)

- ▶ Par-neutral exchange of domestically-issued GOJ bonds for new bonds with reduced coupons and extended maturities.
- ▶ Eligible bonds (J\$701.6 billion)
 - Average interest rate
 - J\$-denominated – 19 percent
 - US\$-denominated - 9 percent
 - Average maturity – 4.7 years
- ▶ New bonds (J\$695.6 billion) – 99.5 percent participation
 - Average interest rate
 - J\$-denominated – 12.5 percent
 - US\$-denominated - 7 percent
 - Average maturity – 8.3 years



Net present value reduction

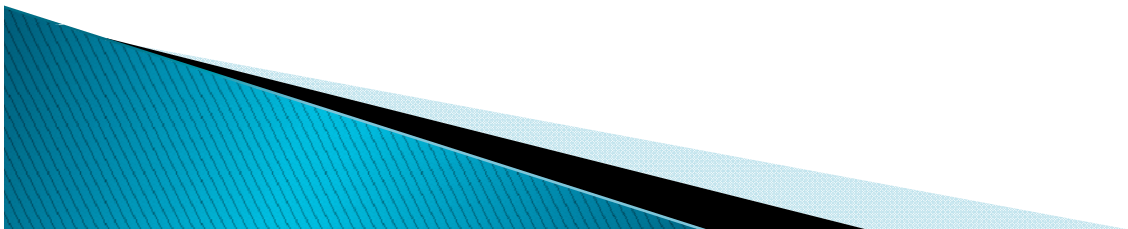
Flat ER, 3 percent inflation

Discount factor (%)	12	15	18	20
NPV (J\$ million) 1/	698,418	612,393	543,416	504,635
Haircut (%)	-0.4	12	21.9	27.5

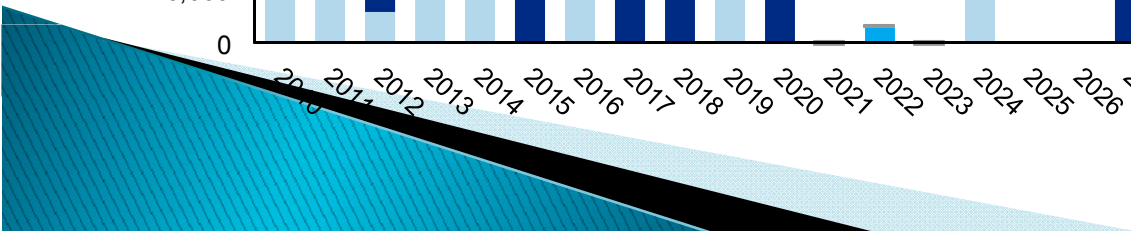
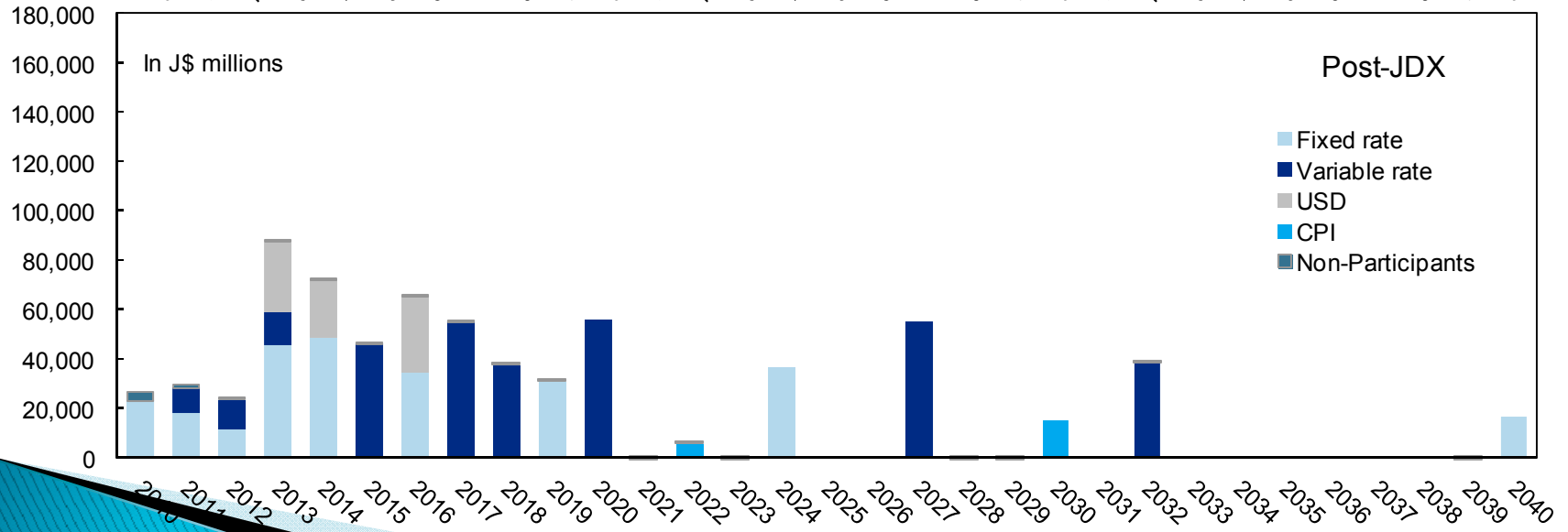
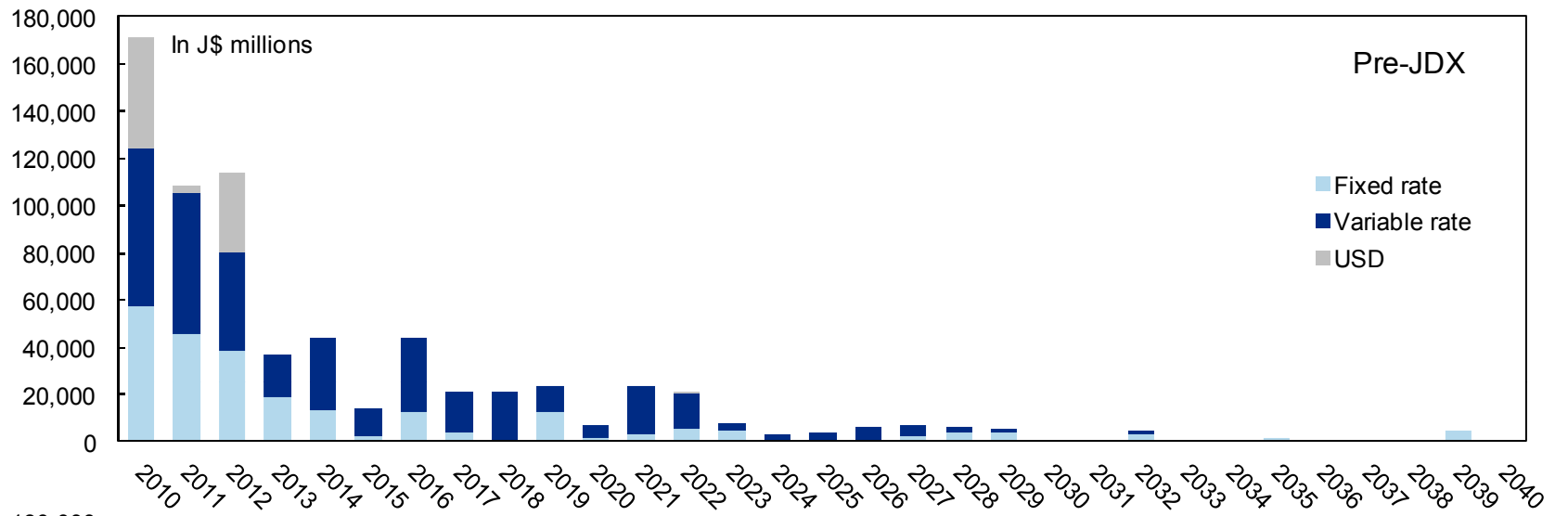
ER depreciates 3 percent, 6 percent inflation

Discount factor (%)	12	15	18	20
NPV (J\$ million) 1/	705,557	618,644	548,901	509,667
Haircut (%)	-1.4	11.1	21.1	26.7

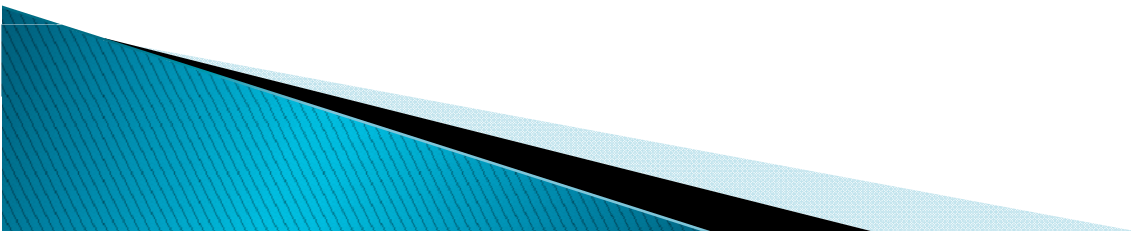
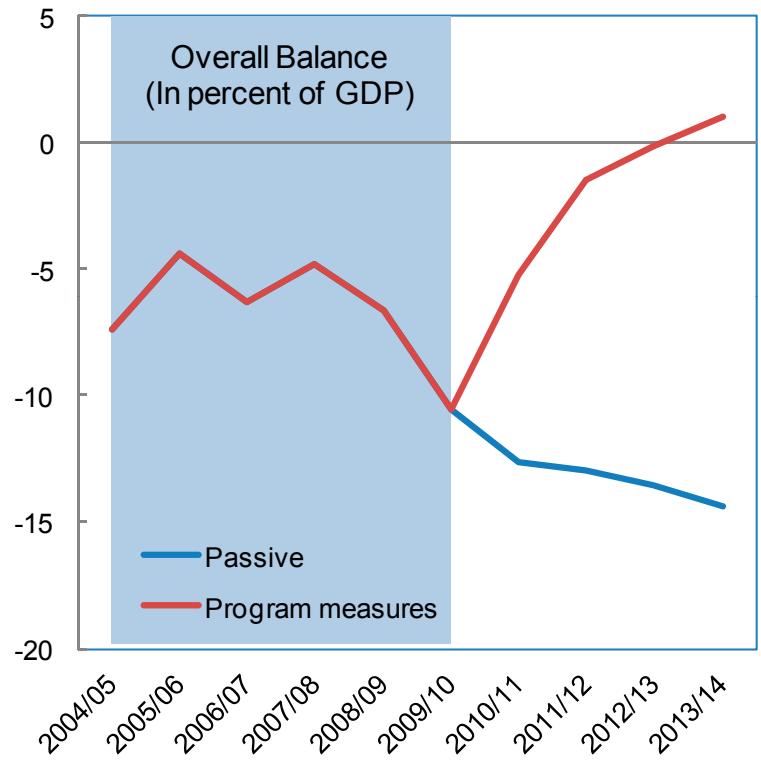
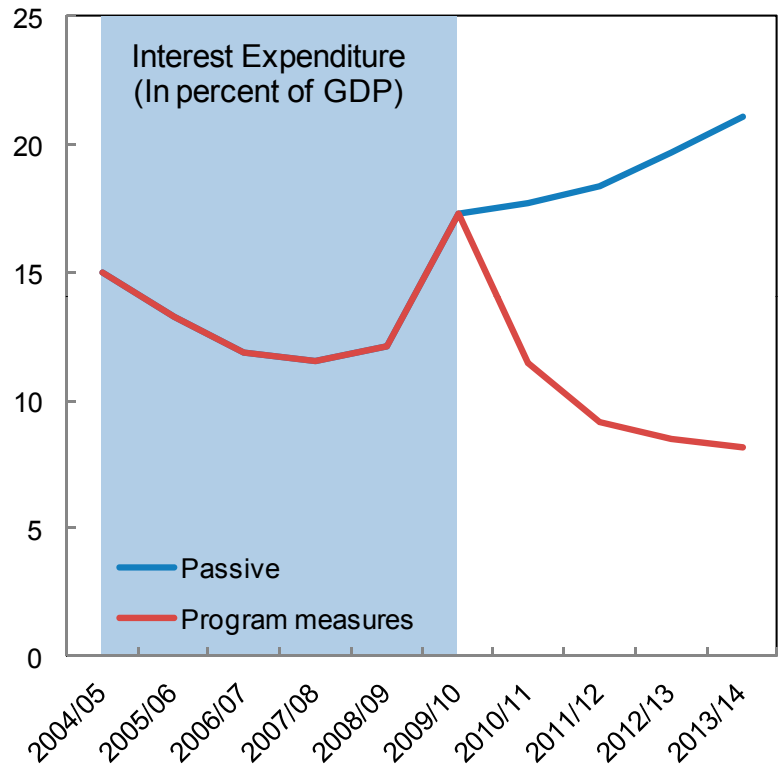
1/ The face value of the bonds exchanged is \$J 695.6 billion, with the amount of eligible bonds at \$J 701.6 billion.



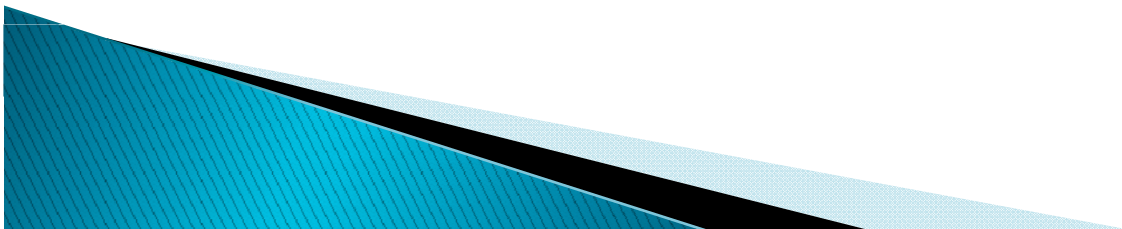
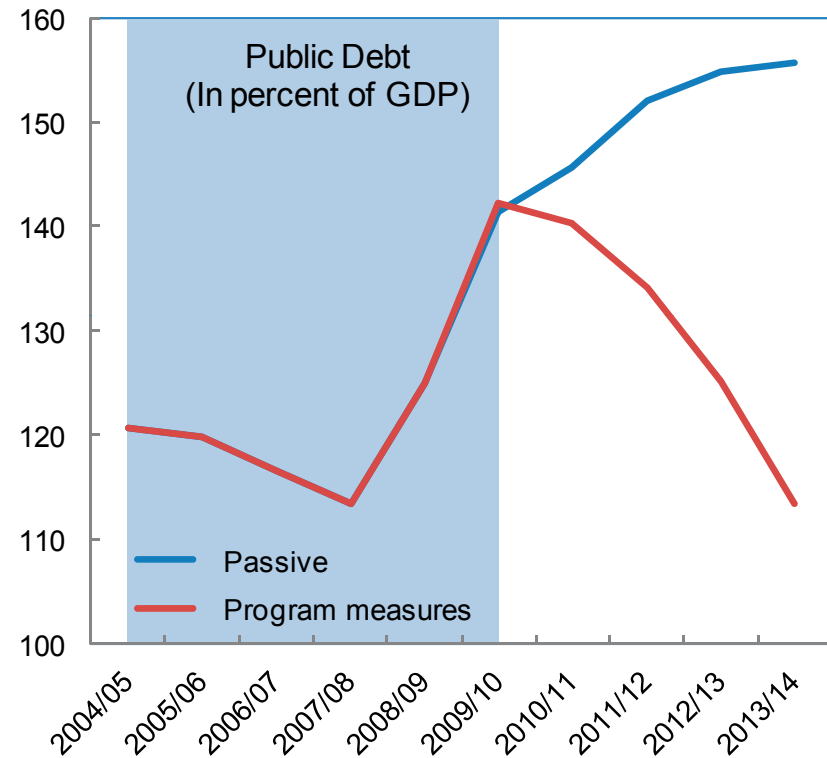
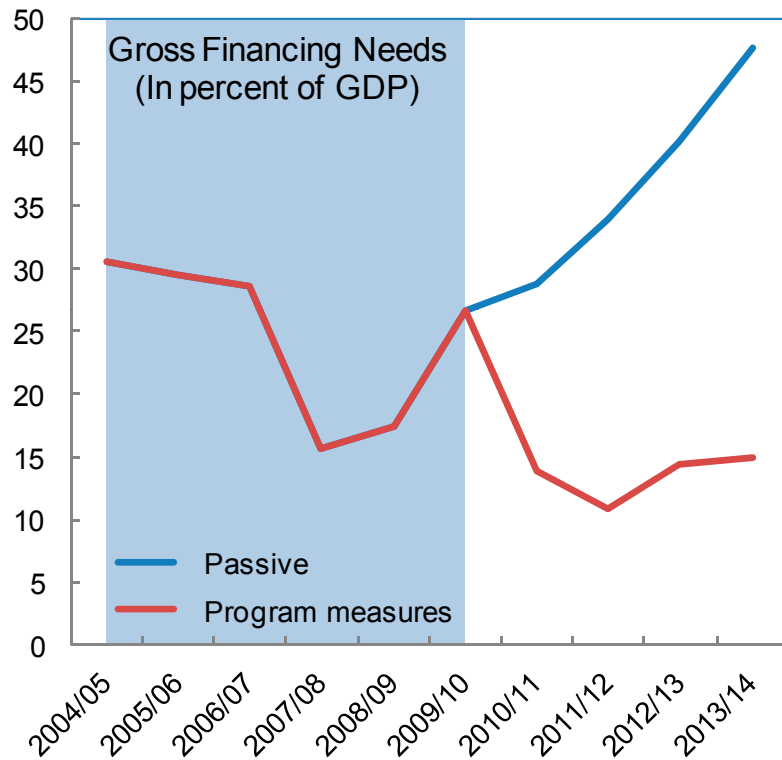
Maturity Profile - Before and After



Fiscal Indicators: Before and After

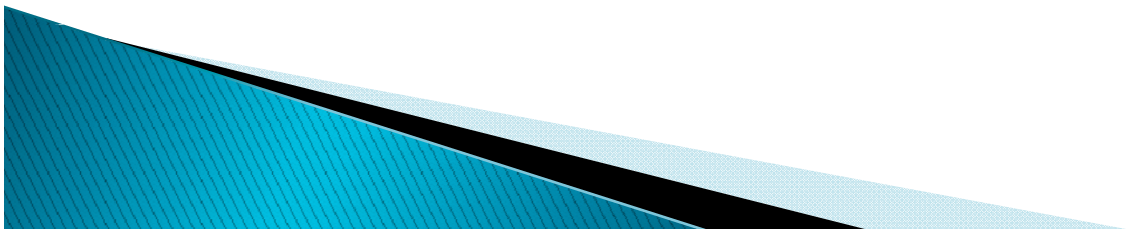


Fiscal Indicators: Before and After (continued)



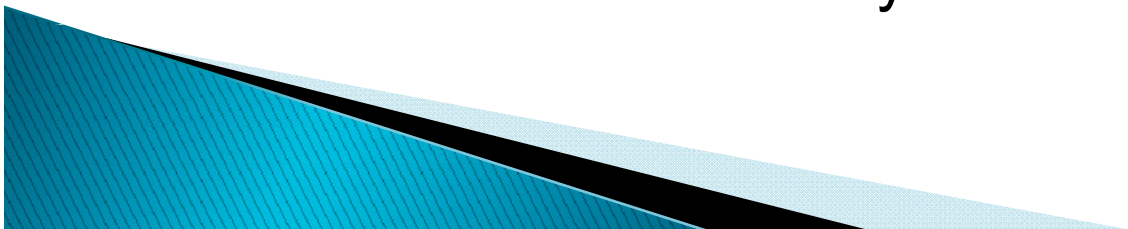
Post-JDX

- ▶ Key sources of risk to capital positions of financial institutions did not materialize.
 - No request to access FSSF
- ▶ Positive reception of program strategy led to market rally:
 - Interest rates on govt. securities have fallen to lowest level in over 30 years.
 - J\$ appreciated strongly during 2010
- ▶ Comprehensive debt management reform still needed.



Summary: Keys to Success

- ▶ Operational design and pre-launch preparation
- ▶ Burden sharing
- ▶ Communication Strategy
- ▶ Strong support from multilateral institutions
- ▶ No principal haircut
- ▶ Social consensus
- ▶ Useful lessons for Euro-area EMEs
 - Financial sector holds bulk of debt, thus safeguarding financial sector stability will be important consideration.



The case of Antigua

- ▶ Between 1998 and 2009, the debt-to-GDP averaged 117%, with a peak of 142% in 2004.
- ▶ Poor track record led to the accumulation of arrears close to half of the total debt.
- ▶ Statutory bodies increasingly important sources of financing (Soc. security fund, Medical benefits scheme).

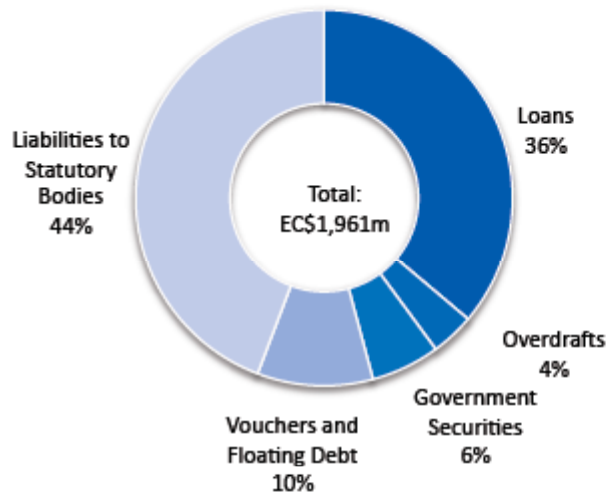
Public Sector Debt Stock by Category, 1998-2009 (% GDP)



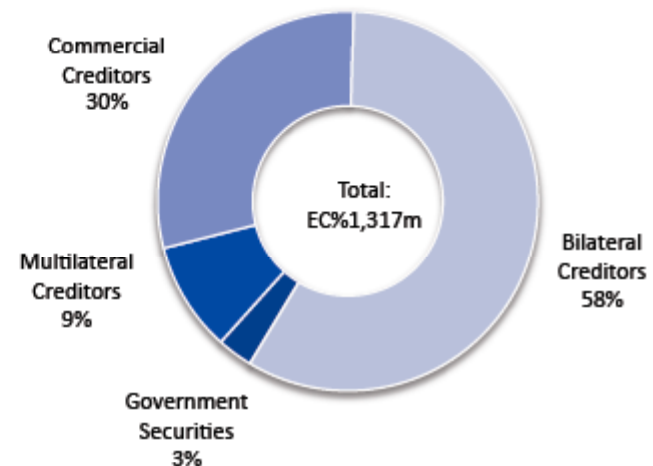
Antigua—Creditors snapshot

- ▶ By end-2009, 2/3 of the total debt owed to domestic creditors, with heavy involvement of indigenous banks.
- ▶ Less than 15% of total debt owed to Paris Club.
- ▶ Currency risk not an immediate issue...

Composition of Domestic Debt



Composition of External Debt

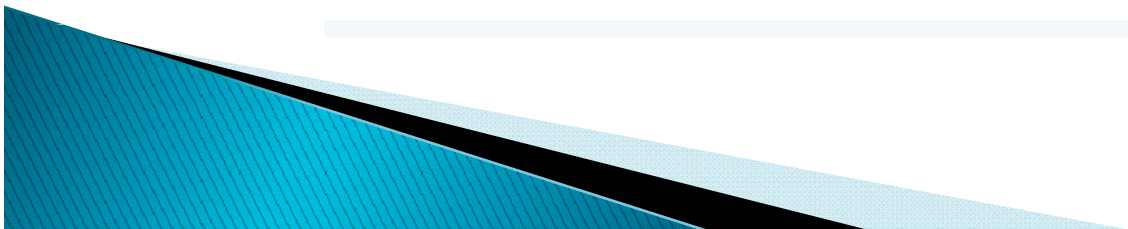


Antigua—Debt sustainability (passive scenario)

- ▶ Debt would have been unsustainable unless restructured.

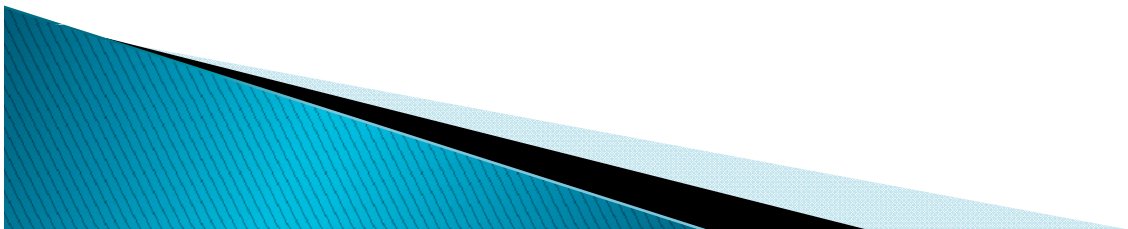
Key Debt Sustainability Ratios

	2005	2007	2010P	2013P
Public Sector Debt Stock	2,762	2,903	3,601	3,832
Of which Arrears	1,500	990	1,837	2,426
Debt-to-GDP	117%	98%	111%	114%
Interest Burden (% of Revenues)	44%	32%	28%	29%
Contractual Interest Burden	15%	12%	13%	9%
Provision for Arrears	29%	20%	15%	20%



Antigua—Road to Restructuring

- ▶ Normalize relations with all creditors;
- ▶ Work bilaterally with indigenous banks to reduce debt service burden
- ▶ Reach agreements with statutory bodies
- ▶ Resolving arrears with domestic suppliers frequently with writedowns
- ▶ Clear arrears with multilaterals
- ▶ Restructuring of bilateral debt (Paris Club).
- ▶ IMF Program—key to regain creditors' confidence.



Antigua—Restructuring principles

▶ Pillars of Restructuring:


- Ring-fence the indigenous banks (safeguard financial system stability);
- Ring-fence RGSM (prevent possible regional spillovers);
- Offer comparability of treatment;
- Be transparent

▶ Goals of Restructuring:

- Complete elimination of arrears;
- Reduction of debt service by 3½% of GDP;
- Shift debt trajectory towards 60% of GDP by 2020 (ECCB target);
- Open up windows to new sources of financing.



Antigua—Achievements so far

- ▶ What has been achieved:
 - Extension of maturity and reduction of interest rates charged by indigenous banks (overdraft accounts → long-term loans);
 - Elimination of arrears with SS and MBS (issuance of long-term bonds, regularization of contributions, and sizeable haircuts);
 - Bilateral agreements with domestic suppliers (mid-size haircuts);
 - Paris Club Agreement (see details);
 - Deal with major commercial external creditor (mid-size haircut).
 - ▶ Still to be done:
 - Payment of arrears to multilaterals (no haircuts);
 - Reaching debt restructuring agreements with non-Paris Club bilaterals (China, Kuwait, VEN).
- 

Antigua—Then versus now

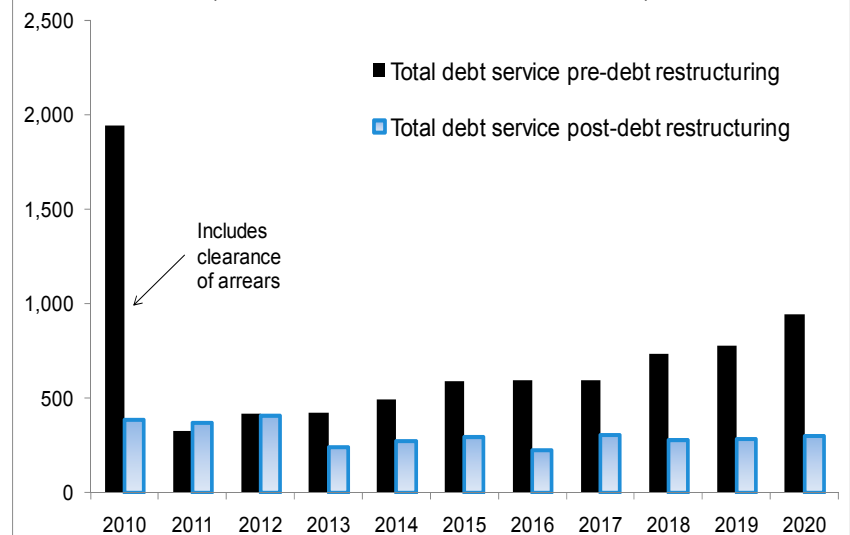
- ▶ Debt service-to-GDP reduced by 3½ percentage points;
- ▶ Debt-to-GDP ratio fell by 26 percentage points—to 94%;

Table 1. Antigua and Barbuda: Summary of Debt Restructuring Terms 1/
(In millions of U.S. dollars as of end-2009, unless noted otherwise)

Creditor	Pre-restructuring debt	Post-restructuring debt
Total public sector debt	1,322.6	1,103.7
Public sector domestic debt	821.9	621.0
ECCB	34.9	34.9
Bank loans (incl. overdraft) 2/	254.6	254.6
Debt to statutory bodies 3/	318.1	166.7
Government securities 4/	32.5	27.8
Supplier credits 4/	181.9	137.0
Public sector external debt	500.7	482.6
Multilateral	45.8	45.8
Bilateral	283.4	283.4
Paris Club	120.6	120.6
Non-Paris Club 5/	162.8	162.8
Commercial 5/	171.5	153.4

Source: Ministry of Finance; Eastern Caribbean Central Bank, and IMF staff calculations.

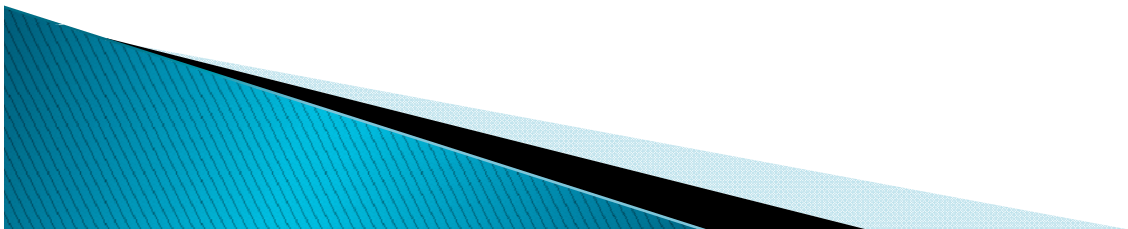
Antigua and Barbuda: Total Debt Service Pre- and Post-Debt Restructuring
(in millions of Eastern Caribbean dollars)



Source: Ministry of Finance; and IMF staff estimates.

Antigua—Vulnerabilities remain

- ▶ Debt ratio still high;
- ▶ Gross external financing requirement (18% of GDP) in 2011-16;
- ▶ Fiscal discipline being maintained under the program;



Thank you!

