SUSTAINABLE DEBT | DETTE SOUTENABLE

DEBT MANAGEMENT ROUNDTABLE
DMR
AN NESG/OSIWA INTERVENTION

DEBT MANAGEMENT, RESTRUCTURING AND SUSTAINABILITY IN ECOWAS

THE NIGERIAN ECONOMIC SUMMIT GROUP | OPEN SOCIETY Initiative for West Africa

DEBT MANAGEMENT ROUNDTABLE

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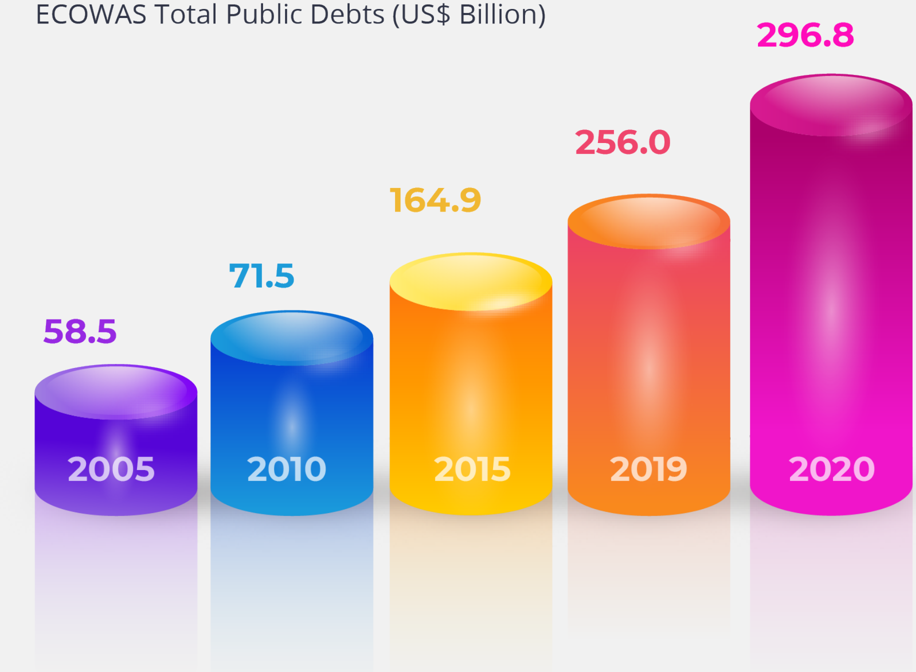
About Sustainable Debt

Sustainable Debt is a multi-channel platform aimed at driving advocacy for sustainable debt management in Nigeria and across West Africa.

1. Understanding the Issue

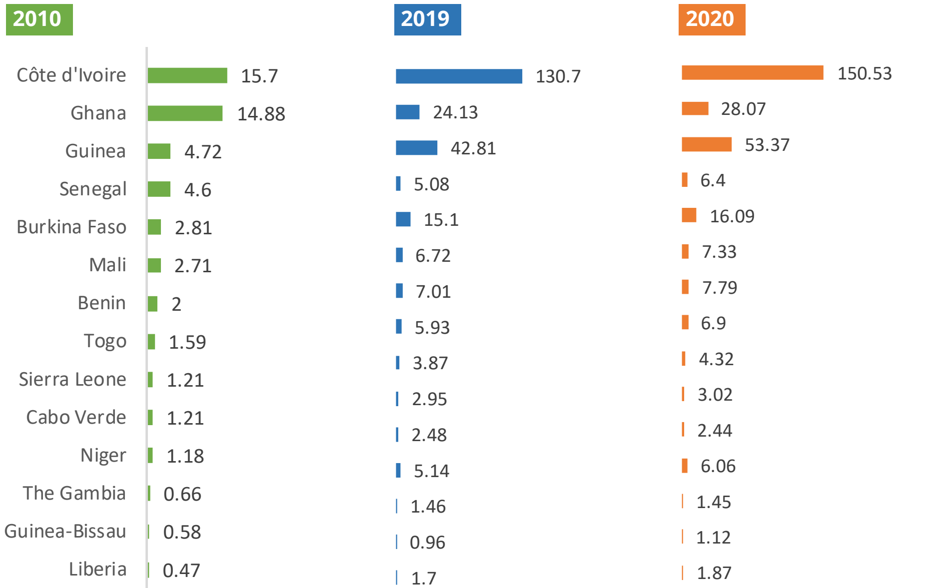
- Beyond limited resources for developmental spending, there are other factors driving debt accumulation.
- Debts are been acquired to support the economy and with the current fragility in economic performance, impact assessment is important.
- Due to the multiplicity of sustainability assessments, there is a need to harmoniously assess the sustainability of the public debt levels in ECOWAS.
- Due to the growing integration among ECOWAS countries and Nigeria's role in the region, a debt crisis in Nigeria could spillover to other ECOWAS countries.
- Some ECOWAS countries are already showing signs of debt distress. Therefore, the situation requires urgent remedial actions.

ECOWAS Total Public Debts (US$ Billion)



2. Profiling Public Debt Portfolio in ECOWAS

Public Debt Portfolio in ECOWAS (US$ Billion)



> *The overall fiscal balance in ECOWAS has been in an uninterrupted deficit since 2009, further worsened by the COVID-19 outbreak.*

» The overall fiscal balance in ECOWAS has been in an uninterrupted deficit since 2009, further worsened by the COVID-19 outbreak as almost all member countries have exceeded ECOWAS's convergence criterion for a fiscal deficit of 3% of GDP.

» The public debt structure in the region has markedly changed, however, it is still dominated by external borrowing, particularly, for the West African Economic and Monetary Union (WAEMU) bloc.

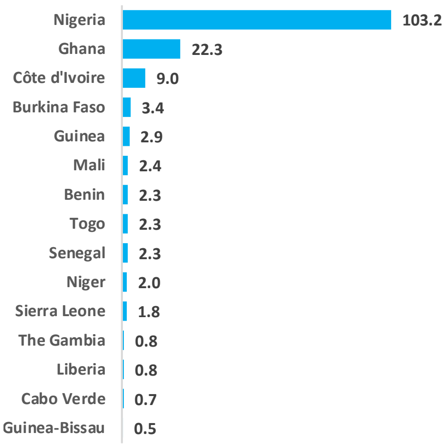
» The domestic debt market is increasingly gaining prominence among ECOWAS countries and is substantial for countries like Nigeria, Togo, Guinea and Sierra Leone.

DID YOU KNOW?

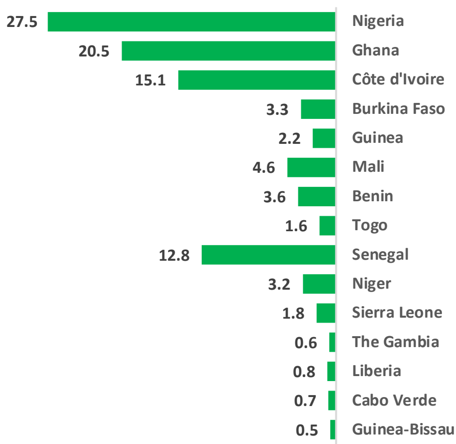
1

All ECOWAS countries except Mali, Guinea and Liberia have exceeded the IMF's **23% threshold** for debt service to revenue

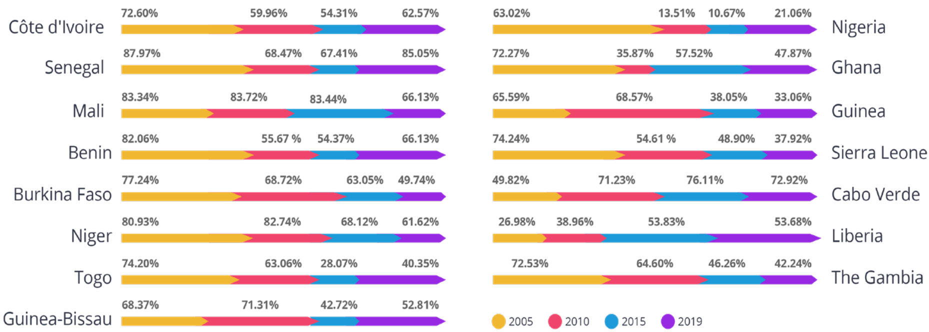
Domestic Debt Stock of ECOWAS Countries in 2019 (US$' Billion)



External Debt Stock of ECOWAS Countries in 2019 (US$' Billion)

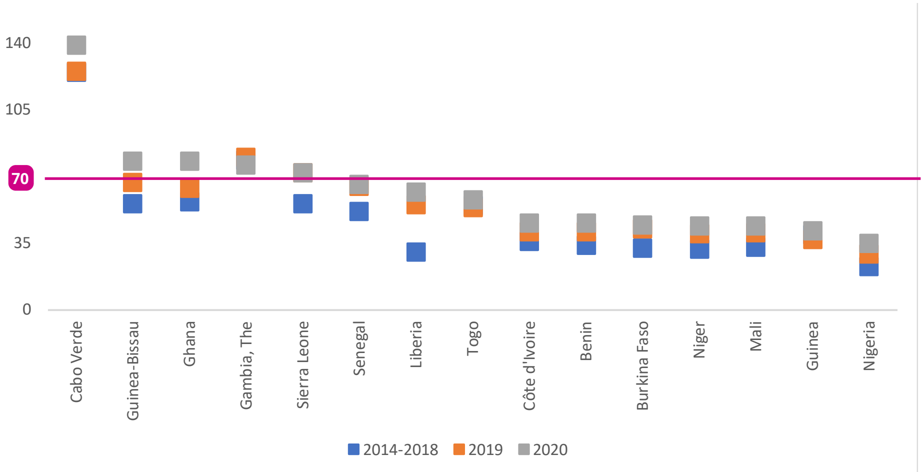


External Debt as a Share of Total Debt in ECOWAS (%)

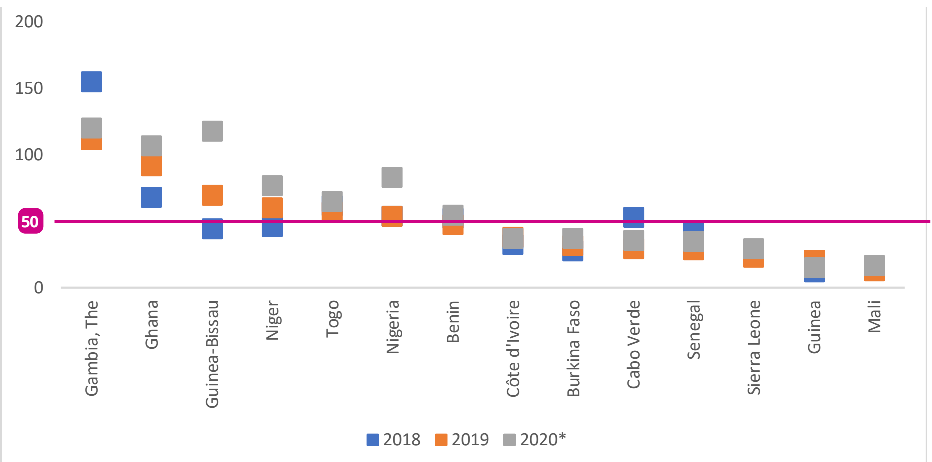


> *Total external public debt for ECOWAS stood at US$98.92 billion in 2019, of which 41.3% (US$40.86 billion) is in multilateral loans...*

Public Debt to GDP Ratio (%)



Debt Service to Government Revenue (%)



> *The debt service burden has become relatively high for most ECOWAS countries, particularly in the aftermath of COVID-19.*

- The recent wave of public debt accumulation in ECOWAS has been accompanied by rising debt ratios which have conveyed a distressing situation for some countries.
- The debt service burden has become relatively high for most ECOWAS countries, particularly, in the aftermath of COVID-19.
- Many countries have debt service-to-revenue ratios between 50-100% which implies that they spend over half, and in some cases around 100%, of government revenue in the payment of interest on debts and barely anything left to finance development.
- This has been the crux of public debt concern for ECOWAS countries, especially Nigeria, Ghana and the Gambia as debt can only be serviced with revenue and not GDP or export.
- The debt service burden in ECOWAS countries is, however, heavy on domestic debt despite the dominance of external debt among most countries.

3. Public Debt in ECOWAS and the Macroeconomy

Drivers of Public Debt Accumulation in ECOWAS

Most ECOWAS countries exceeded or move closer to the IMF's Debt/GDP ratio threshold of 70% in 2020.

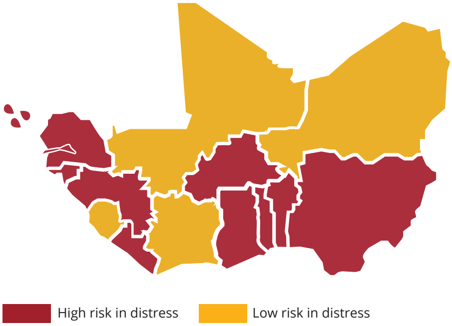
- The drivers of public debt in many countries are often country-specific and could be classified into economic and non-economic factors.
- The Economic drivers include interest rate movements, commodity price volatility, terms of trade shocks, exchange rate volatility and external reserves position.
- Non-economic factors driving public debt include fiscal deficit habit, environmental factors, social factors, political and civil instability, IMF engagements.
- Faced with weak domestic resource mobilization, these countries would require emergency funds to tackle these challenges and have often resorted to borrowing.

Debt-Growth Nexus in ECOWAS

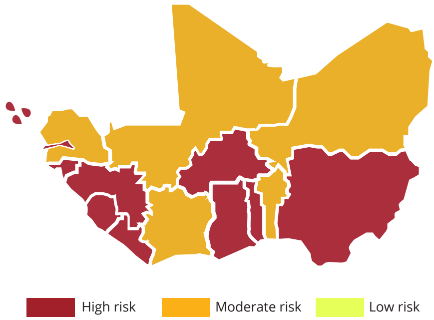
- Debt accumulation constitutes a key driver of economic growth in ECOWAS, however, has a negative impact on the growth of economies in ECOWAS.
- Public debt has the potential to magnify the positive impact of aggregate investment and the negative impact of inflation in the region.
- There is the existence of a debt Laffer curve, an inverted U-shaped relationship between debt accumulation and economic growth among ECOWAS countries with respect to debt-service-to-revenue ratio. This suggests an adverse impact of uncontrolled debt accumulation by member-states on economic growth considering the weak local resource mobilization across countries in the region.
- The findings from this study found that the state fragility with respect to socio-political crises across many countries in ECOWAS imposes huge restrains to the potential positive impact of debt accumulation on economic growth in the region.
- Debt accumulation substantially crowds out private investment in ECOWAS. This suggests that an uncontrolled debt accumulation would lead to a reduction in gross capital formation in ECOWAS as prospective creditors and investors price down the sovereign and investment ratings of, particularly highly leveraged member states.
- This is not to say that debt accumulation is bad because a debtor country benefits partially from a resulting increase in outputs or exports, which helps to service the debts into the future

4. Debt Sustainability Analysis - A Country-Specific Debt Threshold

ECOWAS Countries in Debt Distress



IMF's latest Assessment (2020)

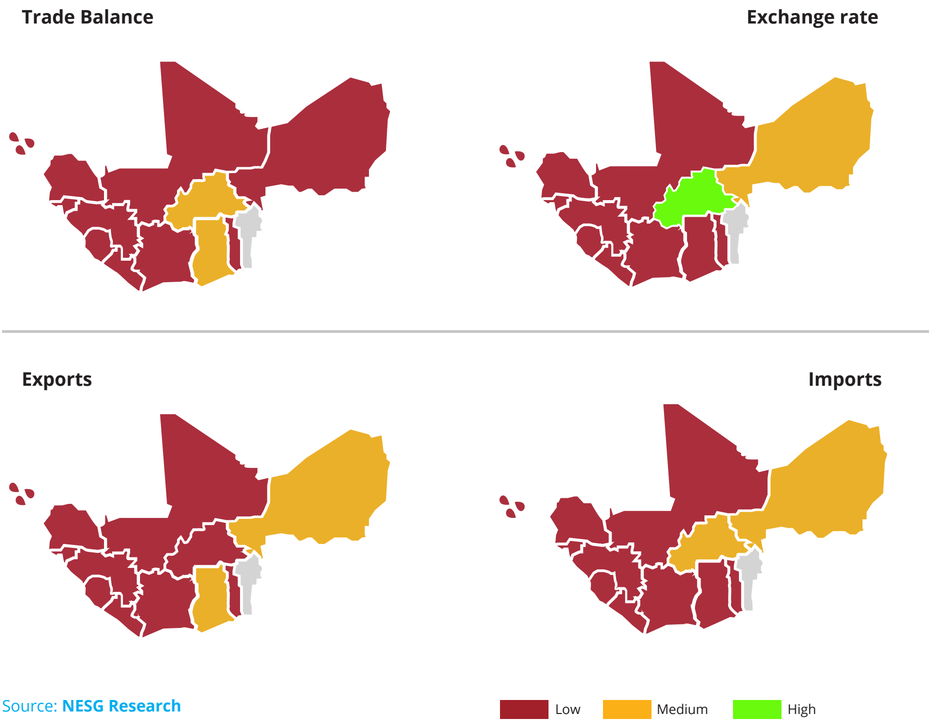


- Based on the IMF's threshold many countries are at varying critical levels across the debt ratios. In essence, many countries have based their debt sustainability decisions on debt ratios that give room for more borrowing.
- Given that debt is serviced with revenue and not the GDP nor the exports, many countries that appear in a safe situation may already be in critical condition as their debt service-to-revenue ratios are close to or over 100%.
- This is, particularly, concerning given that debt is serviced with revenue and not the GDP nor the exports. This oversight puts these countries at high risk of debt distress.
- Hence, this study proposes a Debt Sustainability Index (DSI) that adopts and compressed the five debt ratios into a single weighted time-varying Debt Sustainability Index and then established the solvency threshold (debt distress point) specific for each country.
- As at 2020, eleven ECOWAS countries – Benin, Burkina Faso, Cabo Verde, the Gambia, Ghana, Guinea-Bissau, Liberia, Niger, Nigeria, Senegal and Togo – are in debt distress.
- The remaining four countries – Côte d'Ivoire, Guinea, Mali and Sierra Leone – are at low risk of debt distress.

Source: **NESG Research; IMF/World Bank's Joint Sustainability Analysis**

5. Spillover Effects of Public Debt Crisis among ECOWAS Countries

Whilst accumulation of public debt is not all bad, excessive public debt over and above a certain level as enunciated by earlier findings could lead to a worrisome situation and degenerate into a "Public Debt Crisis". This will be reflected in adverse economic outcomes for the affected country and likely to spillover to other economies in the region.



Source: **NESG Research**

Trade Channel of Transmitting Debt Crisis

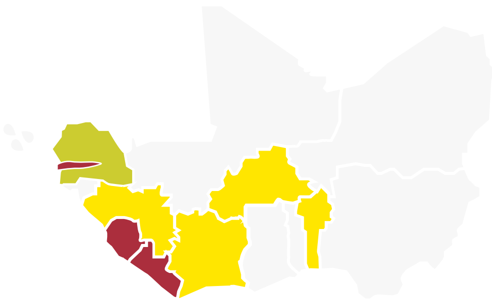
» Trade data show low intra-ECOWAS trade and ECOWAS countries are highly exposed to the rest of the world through trade. Notwithstanding, looking at the Weighted Trade Interdependency Index, Nigeria is a major trading partner of all the countries in the region with over 40% of trade flows within ECOWAS.

» The contagion effects of a public debt crisis in Nigeria will trigger macroeconomic fluctuations in the region except for Guinea and Cabo Verde. This is due to the significant reliance of many ECOWAS countries on Nigeria for imports of crude oil and other petroleum products, manufactured goods and intermediate inputs which top the trade list of most ECOWAS countries' imports.

Financial Channel of Transmitting Debt Crisis

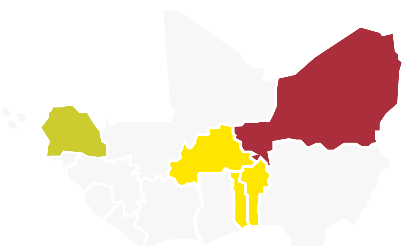
- Financial linkage is another effective transmission channel of a public debt crisis among countries in the same region, however, still small and nascent among ECOWAS countries. Nonetheless, the increasing cross-border expansion among financial institutions in the region has deepened the integration of the financial system in the region.
- Through bank penetration, the impact of a debt crisis in Nigeria on Gambia, Liberia and Sierra Leone is high while it is low for Benin, Burkina Faso, Côte d'Ivoire, Ghana, Guinea, Mali and Senegal.
- Through FDI inflows, the impact of a debt crisis in Nigeria on Benin, Burkina Faso and Togo is low while it is medium for Senegal
- Through remittance, the impact of a debt crisis in Nigeria on Benin, Ghana, Mali, Niger and Togo is high. The impact is low for Burkina Faso, Cabo Verde, Côte d'Ivoire, Guinea, Guinea-Bissau, Senegal and Sierra Leone is low while it is medium for the Gambia.

Bank Penetration (% of Banking Assets)



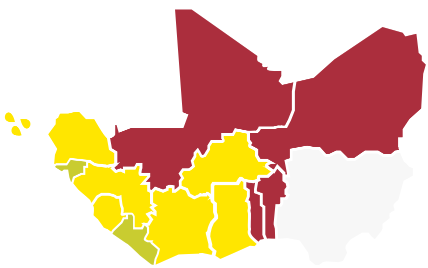
Low Medium High

Foreign Direct Investment (FDI)



Low Medium High

Remittance



Low Medium High

6. Implications for Policy Intervention

The data and analysis conducted in this study have so far affirmed the concerns of stakeholders on the sustainability of public debt in the region. Findings from this study revealed that public debt in ECOWAS is driven by varying factors across member countries but the habit of always spending more than they can make in revenue has been prevalent across board. In Nigeria, Economic factors such as the interest rate environment, exchange rate volatility, slow growth, and dependence on the earnings from oil export have been major drivers of debt. Meanwhile, military spending to tackle insurgency and insecurity has been a major non-economic factor driving up public debt in Nigeria. This study found that debt accumulation has not been supportive of economic growth in the region due to the issues around crowding-out effect on investment, state fragility, leakages and weak resource mobilization. Based on the debt sustainability analysis, eleven ECOWAS countries are already in debt distress and there is the potential for the transfer of risk of a debt crisis in one country to the other particularly from Nigeria to others.

In terms of policy interventions, it stands out that public debt accumulation needs to be curtailed in the region. This is important for ECOWAS countries to avoid a lost decade of getting to the point where debt settlement will be the only agenda of the government for years to come. In essence, there is a need to identify alternatives to borrowing: expanding the revenue base, adoption of Public-Private Partnership and some other social financing strategies. Also, public debt in ECOWAS has reached a level where these countries need support and some innovative debt restructuring to placate the burden on these countries to free up resources for development. Debt forgiveness, though not sufficient in the management of the debt situation, will go a long way to ease the debt burden on these countries.

The Nigerian Economic Summit Group (NESG) and the Open Society Initiative for West Africa (OSIWA) have established the Debt Management Roundtable to engage core stakeholders in the fashioning of policy recommendations on these policy areas to solve public debt problems in Nigeria and ECOWAS at large.

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Benin

Republic of Benin is one of the most debt-distressed countries in ECOWAS, with a debt index higher than 50% of its solvency threshold.

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Burkina Faso

The World Bank projects Burkina Faso is at moderate risk of debt distress, with a total public debt portfolio of US$6.4 billion in 2019

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Cape Verde

Cape Verde's public debt to GDP ratio is projected to hit 137.6% this year, almost double the IMF's 70% benchmark.

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Côte d'Ivoire

Côte d'Ivoire is the only West African country that did not join ECOWAS as a founding member in 1975. Its fiscal balance stands at –4.6%

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The Gambia

Gambia is the smallest country in ECOWAS, with a fiscal deficit currently pegged at – 3.9%

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Ghana

The current ECOWAS Chairman, President Nana Addo Akufo-Addo, hails from Ghana. Its fiscal balance is pegged at –12.6%

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Guinea

Guinea practised a system of government called '*communocracy*' for 20 years. Its public debt to GDP ratio for 2020 was 41.4%

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Guinea-Bissau

Guinea-Bissau's debt to GDP ratio is projected to hit 78.1% in 2021, exceeding the IMF's 70% benchmark.

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Liberia

Liberia is regarded as Africa's oldest republic. Its public debt service to revenue ratio for 2020 was 9.6%

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Mali

Mali used to be one of the world's richest nations and was home to great emperors. Its public debt portfolio for 2019 was US$7.7 billion

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Niger

Niger is one of the world's hottest countries, tagged 'the frying pan of the world'. Its public debt portfolio for 2019 was US$5.4 billion

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Nigeria

Nigeria's fiscal deficit is currently pegged at – 4.2%, exceeding the ECOWAS 3% fiscal benchmark by 1.2%

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Senegal

Senegal once played host to the Paris-Dakar Rally, regarded as the toughest car race on the planet. Its public debt portfolio for 2019 was US$18.2 billion

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Sierra Leone

Sierra Leone is regarded as the 8th least developed country in the world. Its fiscal balance exceeds the ECOWAS benchmark at –3.3%

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Togo

Togo's capital Lome was once considered the most beautiful city in West Africa. The country's fiscal balance exceeds the ECOWAS benchmark at –3.3%

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