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Debt for Development: Still an option in the «age of anxiety»?

by

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The views expressed are those of the author and do not necessarily reflect the views of UNCTAD.

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Debt for Development: Still an option in the age of 'anxiety'?

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S. Blankenburg, UNCTAD

Main Messages

- Developing country debt crises or debt vulnerabilities are the result of the global financial cycle being dominated by speculative finance ("long booms in combination with sudden stops")
- Biggest 'surprise' may be that we are not seeing more outright defaults
- Learning how to deal with high risk exposure in international financial markets is necessary, but insufficient not to become a hostage to international financial markets
- Need for regional/international monetary regimes to prevent the existence of sustained imbalances

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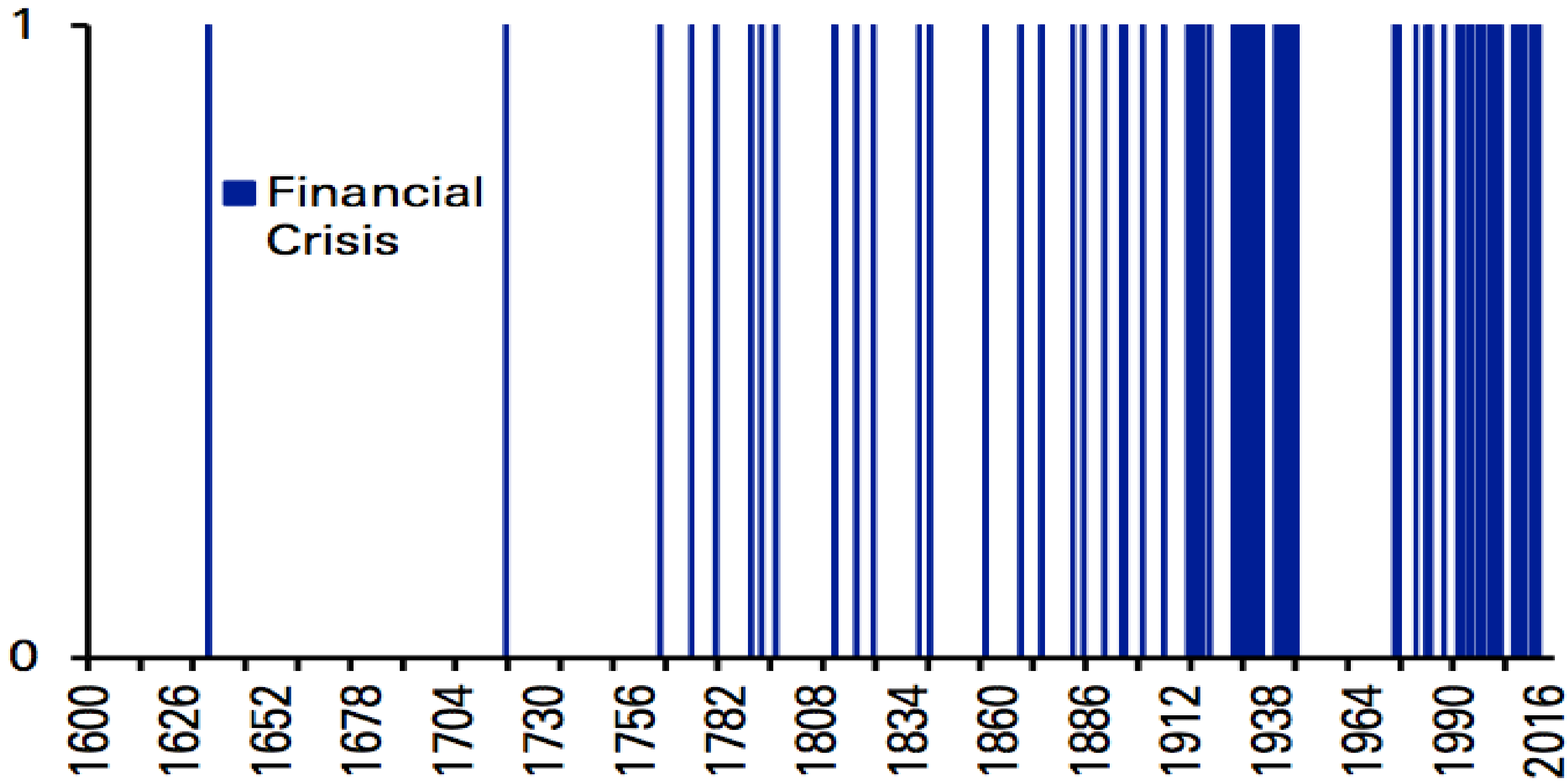
Global Financial Cycles

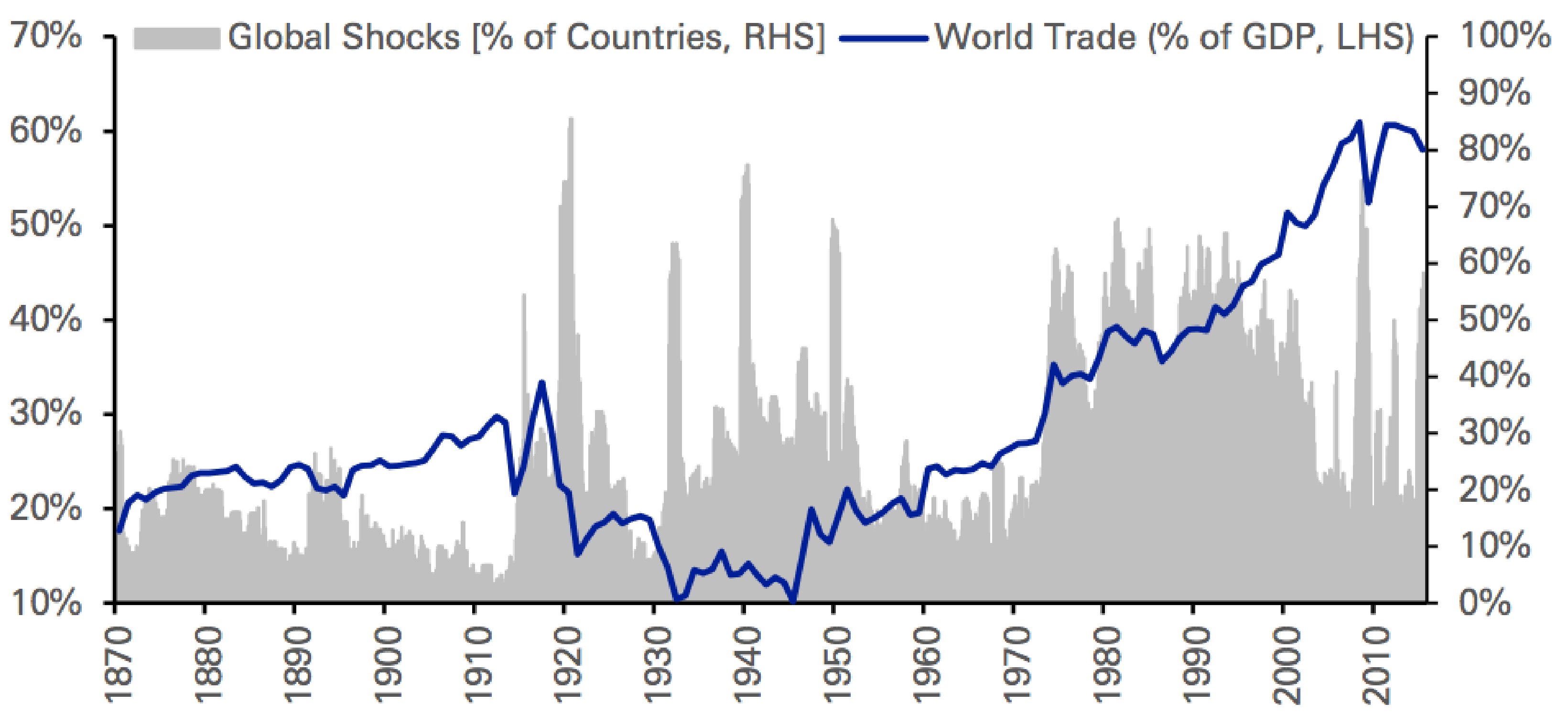
Occurrence of financial crisis through history (Binary variable 1 = Crisis)



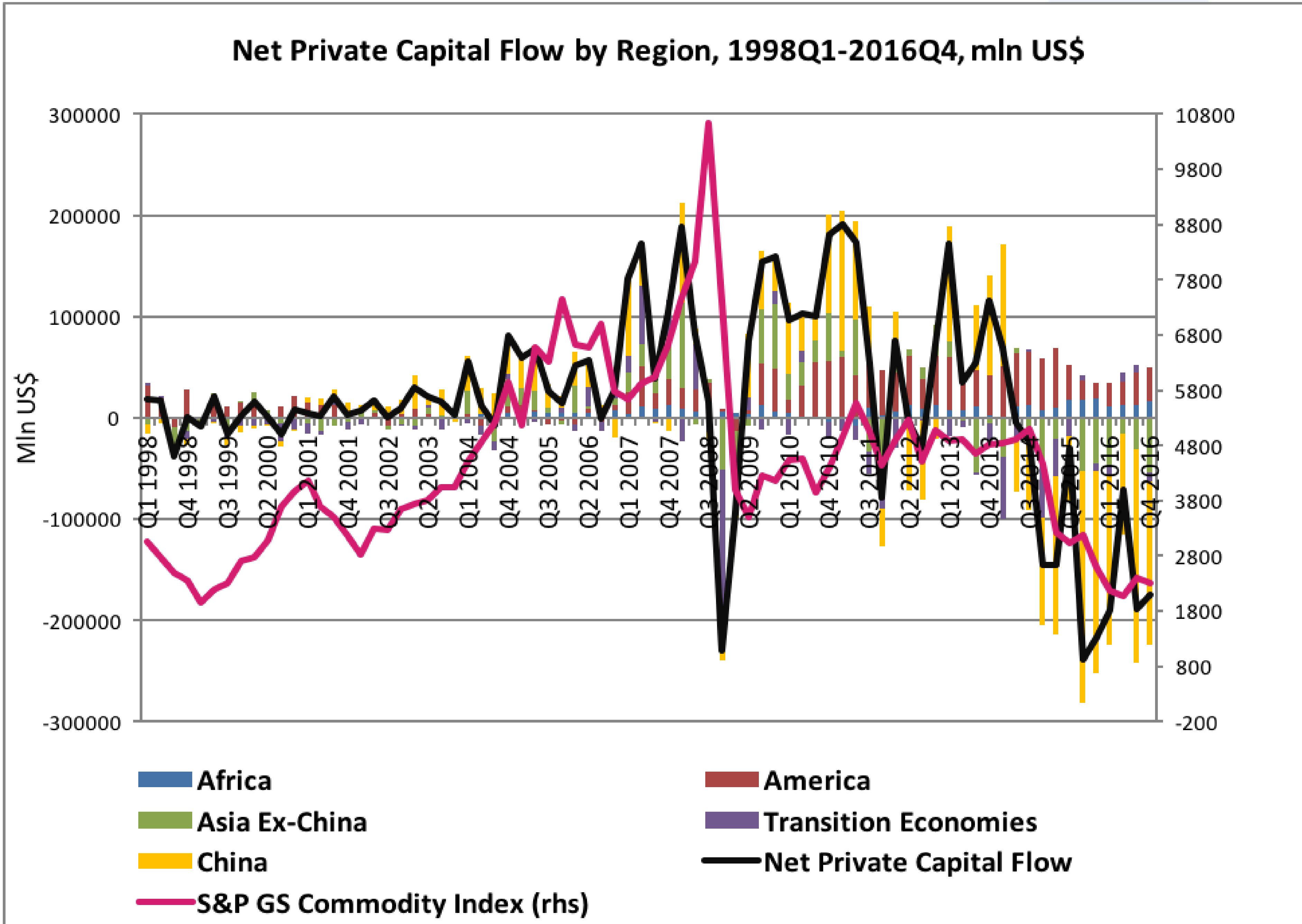
Source: Deutsche Bank

Global Financial Cycles

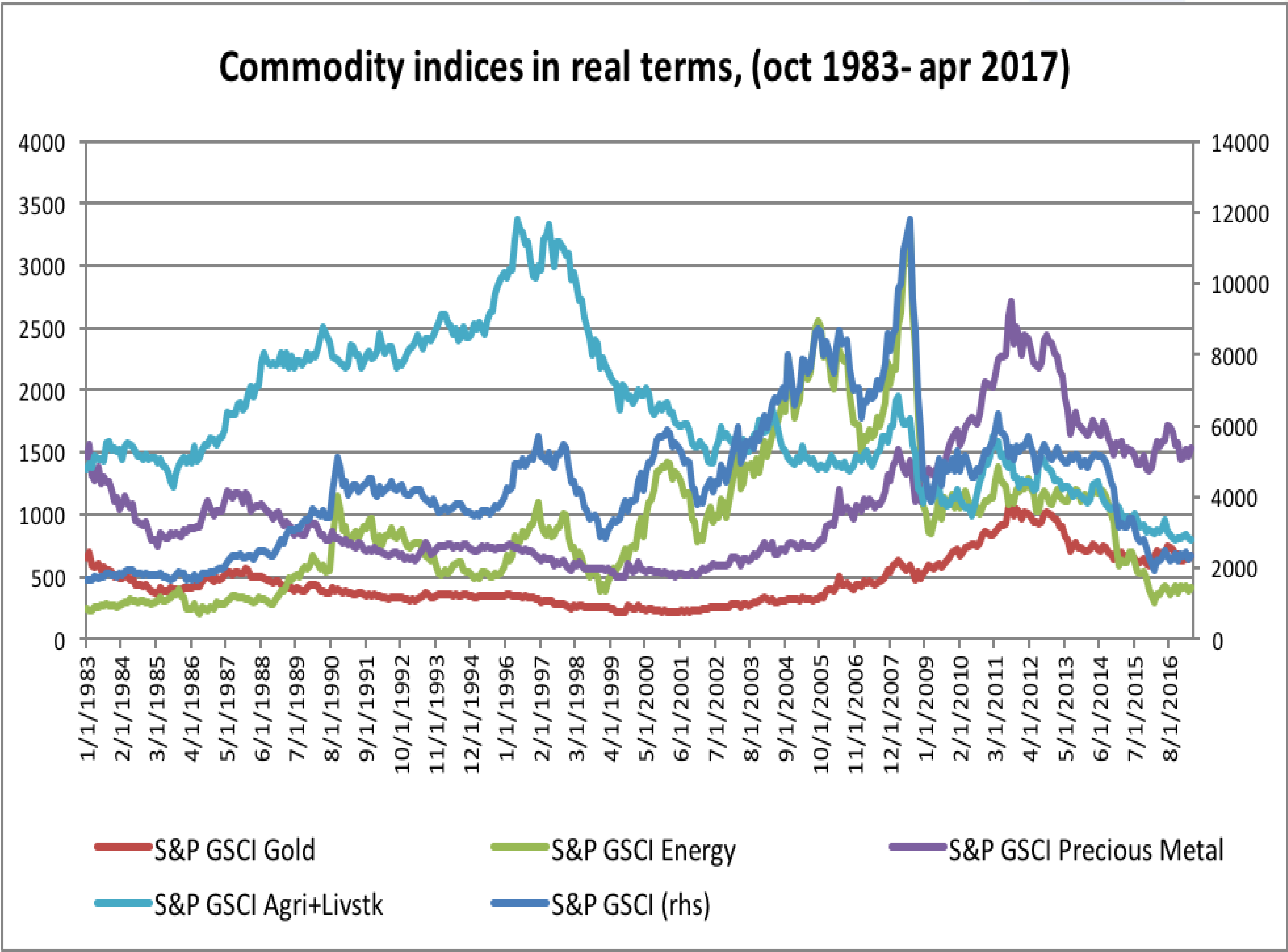
Global trade helps to explain financial interconnection but is not new, nor everything that matters…



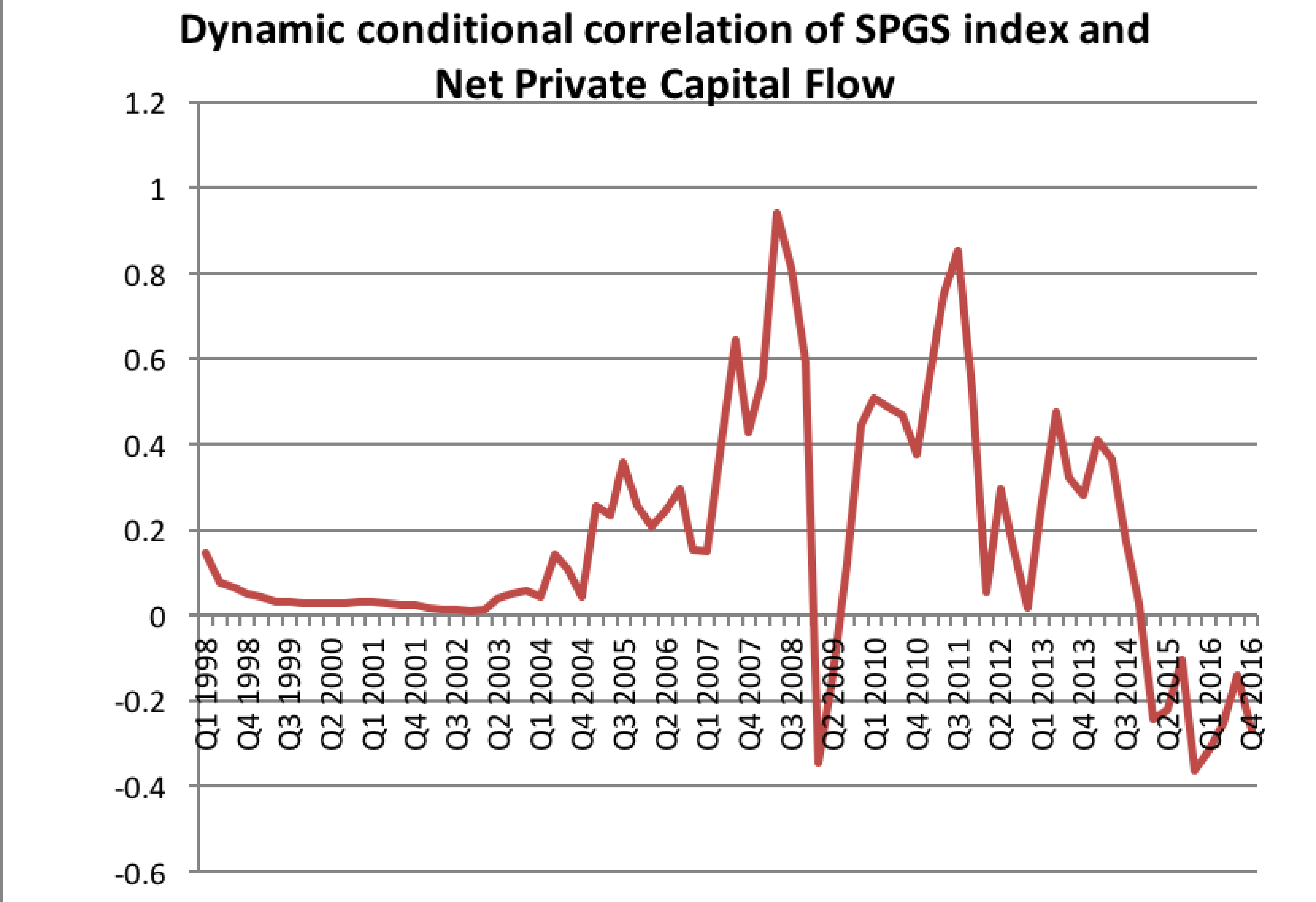
Source: Deutsche Bank



Source: UNCTAD secretariat calculations and TRE



Commodity indices in real terms, (oct 1983- apr 2017)
4000
3500
3000
2500
2000
1500
1000
500
0
14000
12000
10000
8000
6000
4000
2000
0
1/1/1983
2/1/1984
3/1/1985
4/1/1986
5/1/1987
6/1/1988
7/1/1989
8/1/1990
9/1/1991
10/1/1992
11/1/1993
12/1/1994
1/1/1996
2/1/1997
3/1/1998
4/1/1999
5/1/2000
6/1/2001
7/1/2002
8/1/2003
9/1/2004
10/1/2005
11/1/2006
12/1/2007
1/1/2009
2/1/2010
3/1/2011
4/1/2012
5/1/2013
6/1/2014
7/1/2015
8/1/2016
S&P GSCI Gold
S&P GSCI Energy
S&P GSCI Precious Metal
S&P GSCI Agri+Livstk
S&P GSCI (rhs)



Source: UNCTAD secretariat calculations and TRE

Boom and bust periods

2000-2008:

Strong GDP and export in combination with the debt relief initiatives of the 1990s led to a drop of **total debt stocks to GDP** from 36 per cent in 2000 to 22 per cent in 2008 and **debt service to exports** shrunk from 22 per cent in 2000 to 9 per cent in 2008.

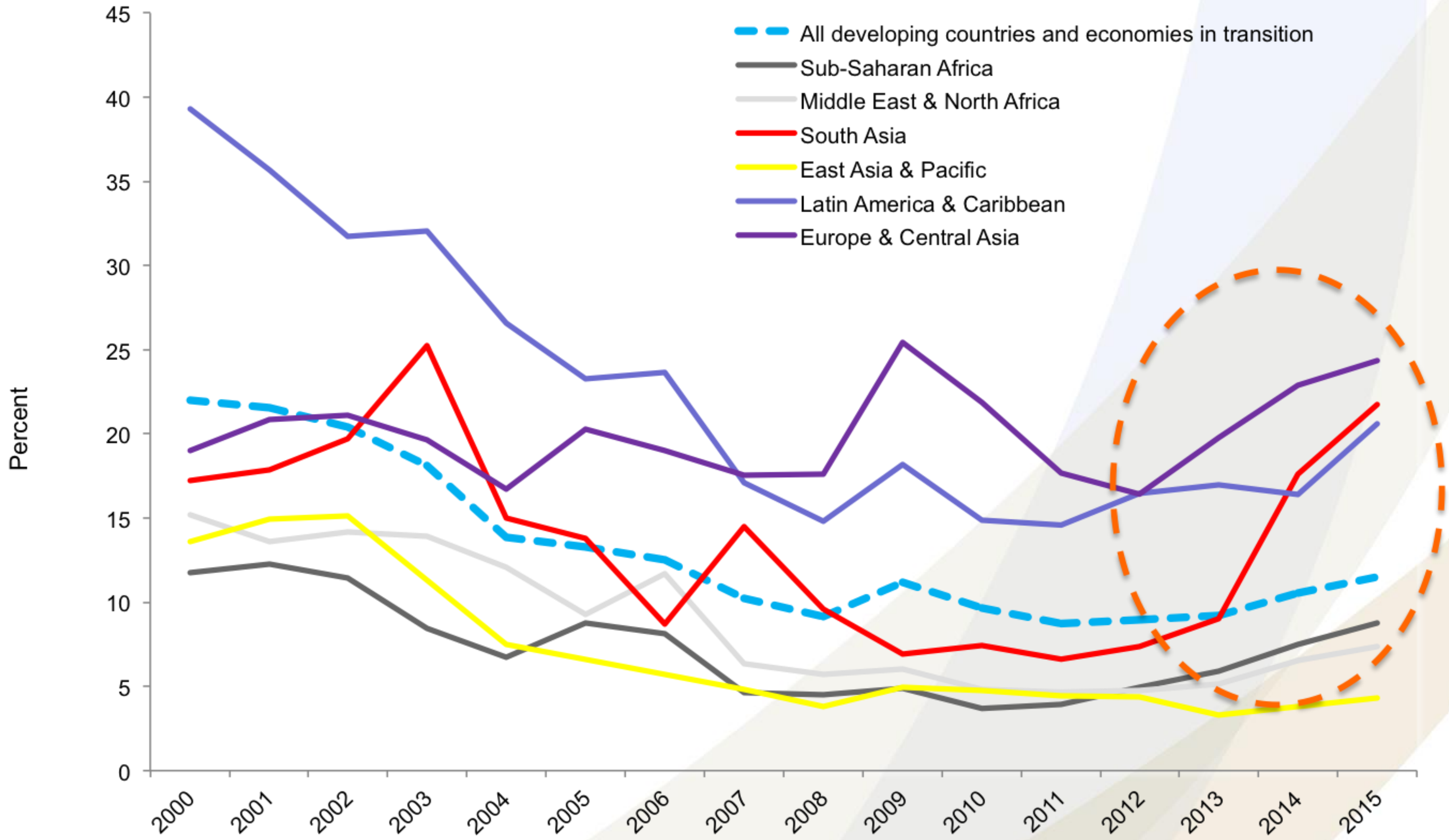
2009-2015

Marked drop in **export growth rates** from 16.6 percent per year in 2000-2008 to 6.5 per cent in 2009-2015

Overall gradual deterioration of debt ratios, as total debt to GDP crept up to an average 25 per cent of GDP by 2016 and debt service to exports increased to 11.5 per cent.

But clear regional variations

Debt service as % of Exports of Goods and Servies By region, 2000-2015



Source: UNCTAD Secretariat calculations based on the World Bank and IMF on line database.

‘It’s not the level (along). but the composition’

- Public and Publicly Guaranteed (PPG) debt owed to private creditors accounted for 41 per cent of the total in 2000, but had increased to 62 per cent by 2016.
- The period since 2000 was also marked by an important increase of private non-guaranteed (PNG) debt as a share of total long-term external debt stocks.
- For developing countries overall, this rose from 28 per cent in 2000 to 49 per cent in 2015.
  - in Sub-Saharan Africa private external debt increased sevenfold, from $10 billion in 2000 to approximately $70 billion in 2015. In South Asia, it rose from 12 per cent to 46 per cent, in East Asia and the Pacific from 35 to 54 per cent, and in Europe and Central Asia from 25 to 60 per cent in the same period.

‘It’s not the level (along). but the composition’

- “…improvements achieved in the more recent past may not last. New debt obligations have been built up under benign external conditions in the short term and in largely un-coordinated ways, creating a mix of public and private, direct and contingent liabilities, in both foreign and local currency denominations and with both resident and non-resident ownership claims attached to them. The mix could prove treacherous, should those claims have to be unraveled without any overarching legal frameworks in place to address them systematically.”

Shifting to domestic public debt: opportunities and risks

- Poor data availability

- BIS data (65 developing and emerging countries):
  - share of domestic in total debt securities rose from 56% in 2000 to 87% in 2015
  - international debt security issuance by central governments doubled in same period
  - domestic debt issues by 21 central governments increased tenfold in the same period

Shifting to domestic public debt: opportunities and risks

- Advantages under favourable conditions:
  - Governments can shift the currency risk to international lenders and reduce their vulnerability to exchange rate volatility, while international lenders are in search of high yields.
- Dangers:
  - Growing ownership complexities with increased presence of foreign investors in domestic bond markets.
  - Increased maturity mismatch risks, esp, in poorer Developing Countries
  - Pressures to monetize budget deficits in absence of inflation indexation

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Shifting to domestic public debt: opportunities and risks

- Core considerations:
  - Higher productivity Developing Economies with relatively **deep financial systems** may be able to navigate the risks, but in poorer countries higher reliance on domestic debt issuance is more likely to signal insufficient access to external finance
  - Complications for **sovereign debt restructurings**: As an increasing proportion of locally issued public debt is now held by non-residents externally, questions arise as to whether to differentiate between resident and non-resident holders of local-currency debt if a need for debt restructuring arises.

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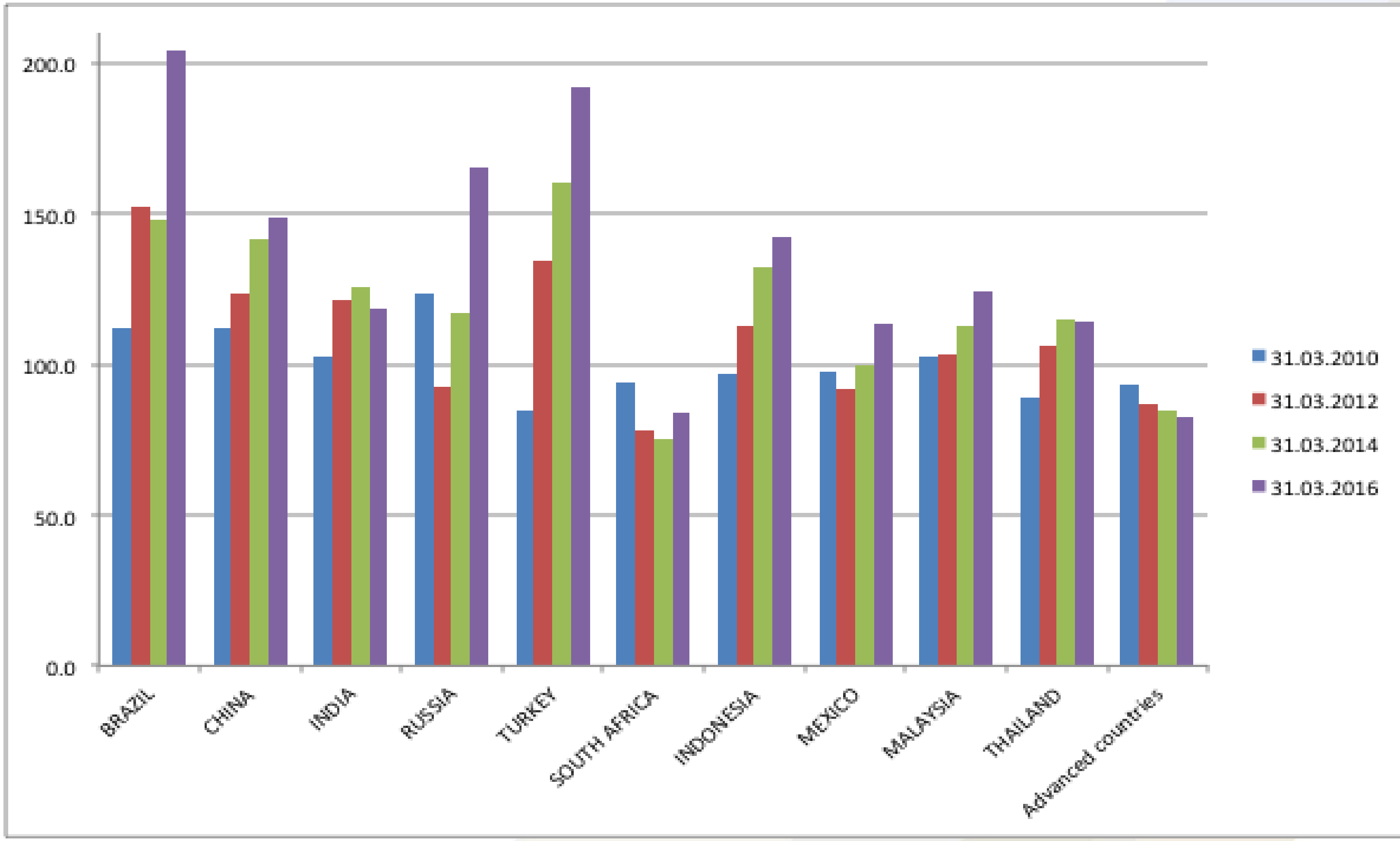
Rising indebtedness of non-financial corporations

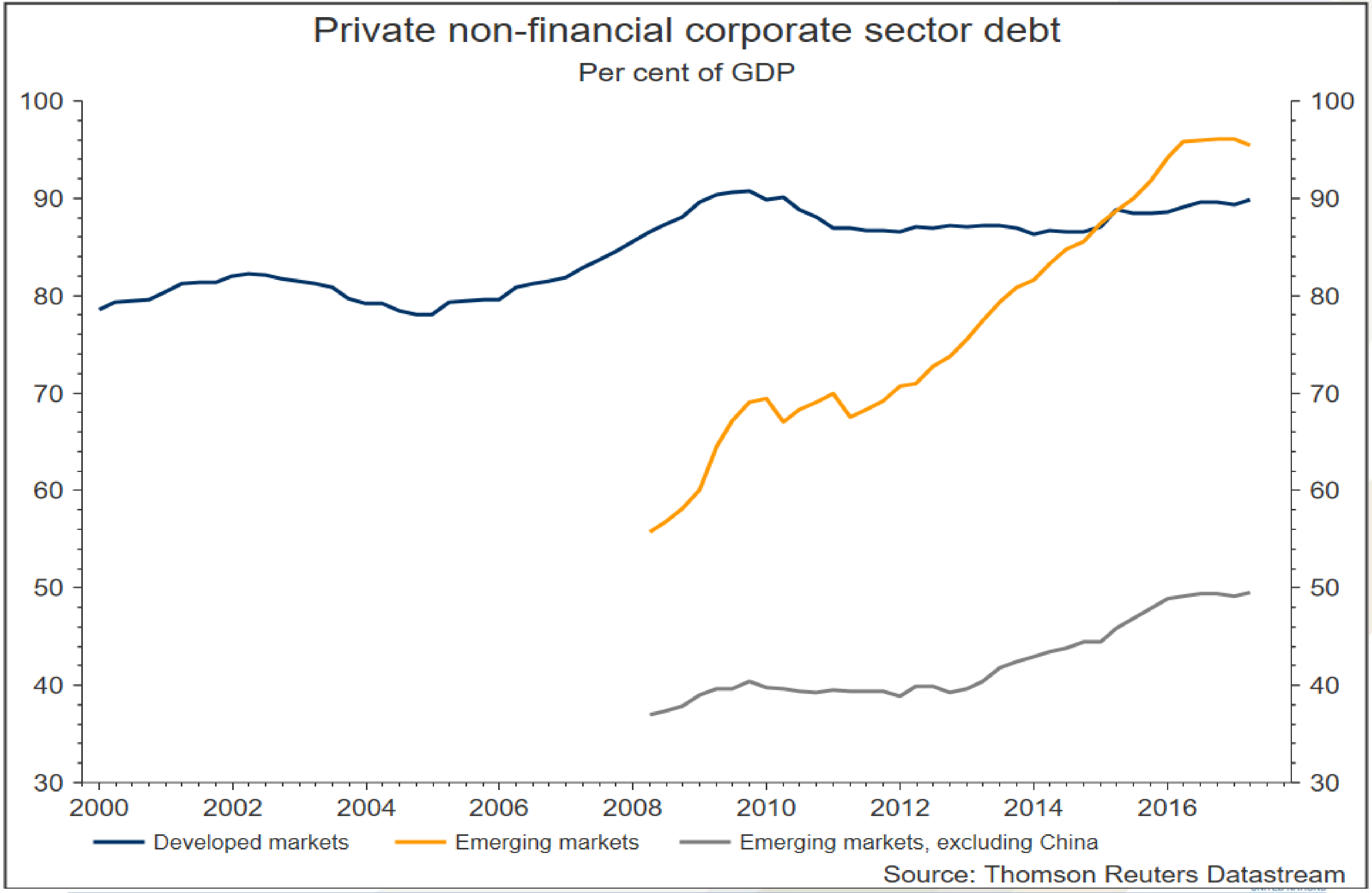
- Non-financial sector debt worldwide has reached $166 trillion by the end of 2016.
- The debt of non-financial corporations in emerging and large developing economies more than tripled from $7.6 trillion at the end of 2008 to $24.5 in the first quarter of 2016, reaching just over 100% of GDP on average.

Debt service-to-income ratio of the private non-financial sector of developing and developed countries, 2010-2016 (Index numbers, 2007 Q4 = 100)

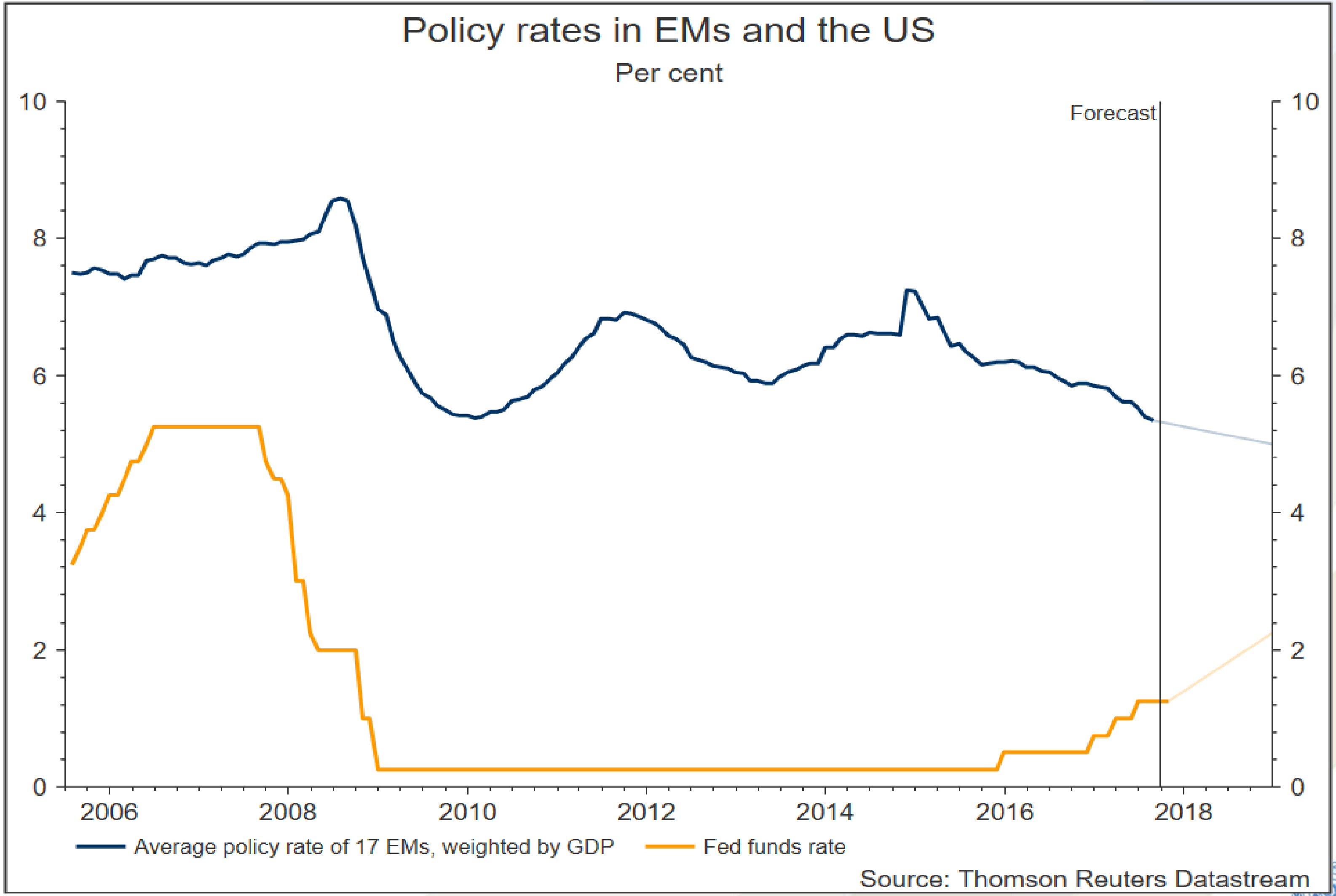


Source: UNCTAD secretariat calculations based on Bank for International Settlements debt service ratios statistics.
Note: Chart shows average for advanced countries (France, Germany, Japan, the United Kingdom and the United States).

Risks associated with AE monetary policies



The risks associated to AE monetary policies



Why aren’t there more sovereign defaults?

- Implicit defaults not captured in the data
- Better anti-cyclical policy regimes in some countries (esp. emerging markets)
- The shocks are yet to come, once ‘normalised’ monetary policy takes hold in AEs

Conclusions

- Less enabling global environment makes it increasingly difficult for Developing Countries to leverage debt financing for sustainable development
- Direct implications for the FfD follow up process and the implemenation of the 2030 Agenda : Financing Gap and inadequacy of financing mechanisms
- Improved early warning indicators
- Need to re-open debates on systemic reform in particular in the area of monetary regimes (primarily regional)
- In addition to SDR, regional clearing unions?