# Debt Burden Weighing Down on Economies:

## How is the International Community prepared for Another Looming Global Financial Crisis?

May 2019

## Introduction

Debt slavery relates well loss of freedom and until a debt is cleared whatever the circumstance, bondage hangs over debt freedom. Debt is only easier to accommodate if its investment will grow in value or generate long-term income.[1] The limited practice of optimum fiscal governance and predatory risky behaviour by government leaders (political and technical) often define the fiscal position of any economy. If national debt levels are high, the flexibility of fiscal policy to respond to economic shocks is limited which increases sustainability concerns. Breaking the chain of debt slavery requires fiscal discipline and non-predatory behaviour by implementers to gain value from the debt. Low government indebtedness gives enough fiscal space for government to stabilise the economic cycle and makes it easy to extend credible guarantees to the financial sector.[2] Current rising debt trends are not new to some governments especially during the pre-HIPC era which calls for learning from previous experiences to inform next steps as economies are faced with a looming global financial crisis. Besides, how is the international community prepared to address the crisis in case it ever comes?

In Uganda, greater investments are being focused on real estate, building up shopping malls and importation of goods for sale with inadequate opportunities to create sufficient taxable jobs as a domestic saving and resource mobilization strategy towards addressing the debt problem. Besides, such businesses are mainly owned by individuals whose contribution to economic growth may not impact on the livelihoods of the majority.[3] The fiscal discipline, tax regime and revenue generation measures are the major bottlenecks in achieving a substantial amount of domestic savings which are contributory factors for enhancing debt payment.

The international community has already raised alarms at the current global debt trends especially with the African continent increasingly shifting interest towards non-concessional loans from bi-lateral lenders like China. The World Bank (2019) already noted that the total external debt of low- and middle-income countries rose by 10 percent in 2017 to $7.1 trillion, a faster pace of debt accumulation than the 4 percent increase in 2016.[4] This calls for collective responsibility in ensuring its debt sustainability and the international community to effectively position it's in the circumstances.

## The role of economic growth in determining the path of debt ratios

A high debt to GDP ratio is not only contributed to by high levels of debt but also the low economic growth level amidst limited range of options for reducing debt. According to ACODE (2014), Uganda's population is comprised of a high Youth unemployment rate standing at between 64% and 70%, and that about 400,000 youths are released annually into the job market to compete for approximately 9,000 available jobs. Moreover, youths who remain unemployed or underemployed and do not exploit their full potential, are often associated with high incidences of drug abuse and gambling.[5] These cannot contribute a substantial or required amount of tax revenue to the consolidated fund from which debt can be repaid. The effects are bound to gradually affect economic growth rate in the long run as an underlying factor causing increases in the government debt-to-GDP ratio.[6]

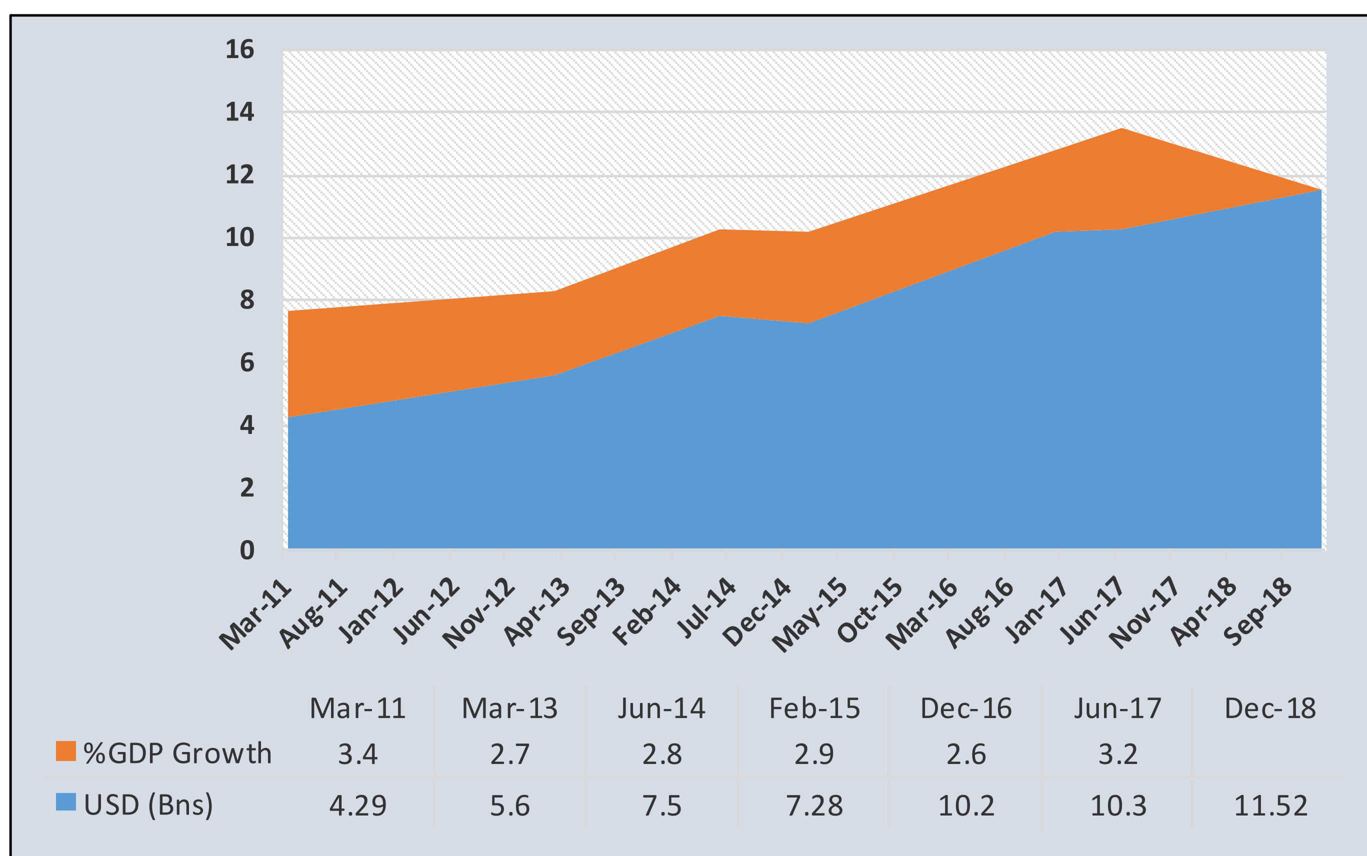
Uganda has made great strides to ensure effective debt management by establishing a relatively sound legislative, institutional and policy framework and Debt and Cash Management Department

1. https://www.theminimalists.com/freedom/
2. https://voxeu.org/article/major-public-debt-reductions-lessons-past-lessons-future
3. https://www.theeastafrican.co.ke/news/ea/Uganda-to-complete-GDP-rebasing-in-December-/4552908-2475226-nubeqyz/index.html
4. The World Bank Group (2019). International Debt Statistics, 2019, Pg 5.
5. ACODE (2014). Youth Unemployment and Job Creation in Uganda: Opportunities And Challenges, Report of Proceedings of the 49th Session of the State of the Nation Platform, (Info-sheet No. 26), 2014
6. Paolo Mauro and Jan Zilinsky (2016). Reducing Government Debt Ratios in an Era of Low Growth, July 2016, pg1

within the Ministry of Finance to ensure effective implementation of these frameworks to improve debt management was also instituted in 2014.[7] While the loan acquisition process is clear, several Auditor General's reports highlight grave concerns on public debt management amidst its rising level.

Uganda's Public debt was USD1.9bn in 2008/09[8] compared to USD11.52Bn in December 2018 representing an increase of 463% over the 10 year period and an average annual increase of 46.3%. And, total public debt was USD10.24Bn by end of December 2017 which increased to USD11.52 billion (December 2018) showing an increase of 12.5 percent[9] while economic growth was 4.2% and 6.2% in the same period respectively. This underpins the argument that low economic growth compounds the debt burden amidst high borrowing rate. Uganda's relatively low and fluctuating economic growth, in comparison with rate of borrowing could lead to fiscal crises degenerating even into defaulting in future. The IMF's report (Jan. 2017) on the 7th Policy Support Instrument noted that vulnerabilities to debt distress have increased and the Fund continues to concern over significant and large looming vulnerabilities against debt sustainability.[10]

**Uganda's Debt Vs GDP Annual Growth Rate (%): 2011 - 2017**




| | Mar-11 | Mar-13 | Jun-14 | Feb-15 | Dec-16 | Jun-17 | Dec-18 |
|---|---|---|---|---|---|---|---|
| %GDP Growth | 3.4 | 2.7 | 2.8 | 2.9 | 2.6 | 3.2 | |
| USD (Bns) | 4.29 | 5.6 | 7.5 | 7.28 | 10.2 | 10.3 | 11.52 |

Source: Compilation from various Government Reports.

Also refer to: **https://data.worldbank.org/indicator/ny.gdp.mktp.kd.zg**

## The Narrative of Natural Disasters amidst rising debt, low Economic Growth and implementation of Global Debt Policy Commitments

Most African Governments are characterised by weak or limited fiscal consolidation practices hence borrowing to reconstruct country systems and infrastructure is usually a quick option in addition to any Aid and grants received. The growing level of any government debt is an important development determining

7. eg the Public Finance Management Act (2015), Public Debt Management Framework 2013 (under review), Annual Medium Term Debt Management Strategies, the Public Private Partnership Act (2015), Guidelines for Loan/Grant Negotiations in Government (July 2018), Cabinet Adequacy Checklist for Borrowing and Loan Approvals (2018); Public Financial Management Reform Strategy 2018 and Cash Management Policy (under formulation). A Debt and Cash Management Department within the Ministry of Finance ensure effective implementation of these frameworks to improve debt management was also established in 2014.
8. 
9. MoFPED (2019). Report on Public Debt, Guarantees, other Financial Liabilities and Grants for FY 2018/19, Pg3
10. IMF (2019). Uganda: Staff Concluding Statement of the 2019 Article IV Mission, February 14, 2019

public financial management and which strategies to use to ensure effectiveness. Growing debt to GDP ratios undermine the sustainability of public finances and reduce fiscal space and so any beneficial results is dependent on sound public financial management.

Persistent rising debt levels of this magnitude are likely to; i) cause Uganda to remain dependent on other economies due to more borrowing, lower the quality of living as its cost gets higher since government will be taxing the population more to collect revenue to repay the loan, and pass on large fiscal burdens to future generations.[11] Creditors are likely to charge even higher interest rates in a scenario where they assume a country's credit worthiness is questionable in their analysis. This situation worsens in the case where there is need to contract new debt from the same creditor. It's worth noting that a grade "A" debtor through its debt repayment path may easily turn into a grade "D" debtor, usually as there is no guarantee of constant behaviour of events that could lead to a default.

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For instance, in March 2019, a destructive natural disaster, cyclone Idai caused great death in Southern African countries of Mozambique, Zimbabwe and Malawi which will require lots of resources to reverse some of the effects. Government debt to GDP in Zimbabwe was expected rise to 94 per cent of GDP in 2018, and further up to 117 per cent in 2020.[12] While Malawi's debt to GDP reduced from 59.85% in 2017 to 57.85% in 2018 representing only 2.3%.

This is still high with challenges like fiscal laxity, lower tax revenue, growth shocks, government commitment to policy reforms among others still in existence[13]. Monetary tightening in most developed economies and the associated rise in interest rates create doubts on the sustainability of debt dynamics in some countries.[14] According to a report by United Nations on World Economic Situation and Prospects (2019), the debt position in the East African region is expected to deteriorate in the next few years. The region continues to record relatively high fiscal deficits reflected by high infrastructure investment alongside weak domestic resource mobilization forcing governments to fill the gap by external financing.[15] Hence, more pressure on debt servicing is expected, increasing the risk of external debt distress in these countries (IMF, 2018b).

This further undermine commitments and actions intended for Debt Sustainability as highlighted in the Inaugural report (2016) on Monitoring Commitments and Actions signifying a challenge of compliance to Debt Policy Commitments as outlined in the AAAA (2015).

The AAAA (2015) commitments to address Global debt burden point to the achievement of a global consensus on responsible lending and borrowing by establishing global legal frameworks to enhance stability in economies; including, i) development and formalisation domestic principles of lawful bankruptcy for improved debt restructuring processes, ii) Comprehensive and transparent loan negotiation process accompanied with neutral arbitration, and iii) drafting a framework for sustainable financing for the hurricane prone small islands and Caribbean countries. The agenda also acknowledges the UNCTAD Principles on Responsible Sovereign Lending and Borrowing, recognizes the applicable requirements of the IMF debt limits policy and the World Bank Group's non-concessional borrowing policy, and notes that the OECD Development Assistance Committee has introduced new safeguards in its statistical system to enhance the debt sustainability of recipient countries[16]. However, non-compliance to the implementation of AAAA (2015) Debt Policy commitments are glaring.

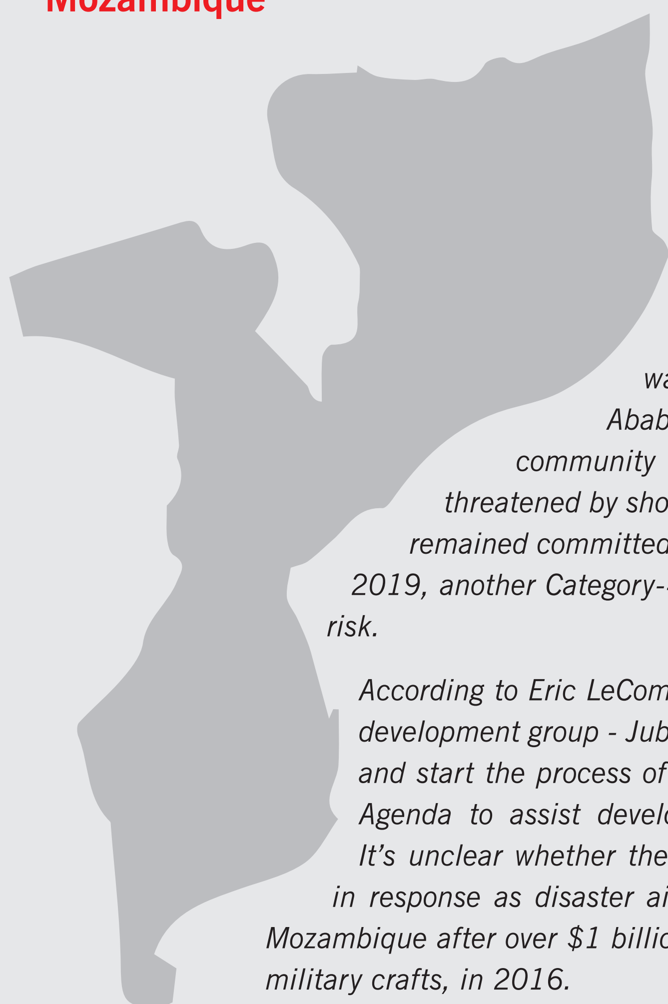
11. Policy Brief (2004). The Brookings Institution March 2004 Policy Brief #130, How to Balance the Budget ALICE M. RIVLIN AND ISABEL V. SAWHILL
12. United Nations. World Economic Situation and Prospects 2019, Pg 126
13. IMF (2016). 7th and 8th 7th and 8th reviews under the Extended Credit Facility Arrangement: Debt Sustainability Analysis for Malawi, June 2016.
14. United Nations. World Economic Situation and Prospects 2019, PG 126
15. The shift is towards increased borrowing from China and the international bond market
16. Jubilee USA Network (2019). Implementing Debt Policy Commitments from the Addis Ababa Action Agenda; United Nations Financing for Development Forum, April 2019. Also refer to: https://www.jubileeusa.org/press

## A Case Study of Disaster Events in Mozambique

A financial rating agency – Fitch, expected Mozambique's public debt to reach 102.5% of GDP by end of 2018 amidst slow growth rate.[17] However due to the disaster caused by cyclone Idai, IMF was prompted to loan Mozambique an amount worth US$118.2Million as a Rapid Credit Facility Assistance expected to address large budgetary and external financing gaps to meet reconstruction priorities.[18] This action was in alignment with the commitment made in the Addis Ababa Action Agenda (2015) which calls on the international community to offer support to countries whose debt sustainability is threatened by shocks and natural disasters. While the Mozambique authorities remained committed to macroeconomic stability, just six weeks later on 26th April 2019, another Category-4 Cyclone Kenneth hit the country leaving 16,000 people at risk.[19]

During the IMF & WB Spring meetings in April 2019, Eric LeCompte, a United Nations debt expert and Head of the religious development group - Jubilee USA, *"It's time to move away from loans for Mozambique and start the process of debt relief,".* [20] This strategy is also recognised by the Action Agenda to assist developing countries in attaining long-term debt sustainability.[21] Its unclear whether the international community will adopt and act on this option in response as disaster aid for recovery, considering that the IMF stopped financing Mozambique after over $1 billion in secret loans were discovered to outfit fishing boats into military crafts, in 2016. [22]

## The Impact of Natural Disaster on National Debt and Economic Growth - Mozambique



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17. https://clubofmozambique.com/news/mozambique-public-debt-set-to-hit-102-5-of-gdp-this-year-fitch/, 26th Nov. 2018. Viewed on 28th March 2019
18. International Monetary Fund (2019). IMF Executive Board Approves US$118.2 Million Rapid Credit Facility Assistance to the Republic of Mozambique in the Wake of Cyclone Idai, Press Release No. 19/121, April 19, 2019
19. Federal News Network (2019). 160,000 at risk in Mozambique after 2nd cyclone in 6 weeks, April, 28th 2019 Also refer to: https://federalnewsnetwork.com/world-news/2019/04/flooding-begins-in-mozambique-in-wake-of-cyclone-kenneth/
20. https://www.jubileeusa.org/pr_cyclone_kenneth_mzbq
21. UNDESA. Financing for Development; Briefing Note on the Addis Ababa Action Agenda, 13-15 July 2015.
22. https://www.jubileeusa.org/pr_cyclone_kenneth_mzbq

## Implications of Economic Rebasing on National Debt

Rebasing which reflects current economic developments in most cases raises the GDP position of an economy and even cause an increase in GDP per capita changes but doesn't necessarily mean an increase in household incomes. The new figures provide the basis for more accurate economic indicators that are critical for evidence-based policy making. On the other hand, it lowers the overall debt profile (*public debt-to-GDP ratios*) thereby improving debt dynamics. Following the rebasing exercise in 2014, Uganda's GDP rose from Ush60 trillion ($21.4 billion) in 2002 to Ush68.4 trillion ($24.2 billion) at the end of the FY 2013/14, measured against 2009/10 data.

Uganda's total public debt stock increased from $4.29Bn in March 2011 to $7.5Bn in June 2014 (showing 74.4% increase) compared to an increase from $7.5Bn in June 2014 to $11.52Bn in December 2018 (53.6%).[23] While more economic activities have been incorporated into the productive bracket, it's not clear whether the reduced rate (in increase of public debt) in the latter period is attributed to effective repayment or due to the economic rebasing exercise carried out in 2014 compared to the high rate in the former period. The current GDP position is likely to be deceptive as the debt situation may appear better mostly on account of rebasing but may portray a contrary position for the debt service-to-revenue ratio[24].

Despite an increase in Government's total tax revenue from UGX 6.22 trillion in 2011/12 to UGX 11.59 trillion in FY 2015/16 noting a 79% increase, tax revenue to GDP ratio stagnated at around 12.6 percent.[25] On the other hand, Uganda's debt to GDP ratio fell from 39.8% to approximately 29.2%, while tax to GDP ratio declined from 13% to 11.8% at the end of 2013/14.[26] Due to an improvement in the debt to GDP ratio, it's tempting to increase government's need to borrow but this compounds the risk of debt distress if revenue mobilization continues to stale. It's usual that the debt-to-GDP and fiscal deficit-to-GDP ratios decline but it shouldn't necessarily give lee-way for more borrowing or even register larger deficits as the ability to absorb more debt will have seemingly improved. This is because tax revenues and export receipts which are great contributors to debt servicing remain unchanged[27]. In addition, the contribution of some sectors to the current GDP will decline while others will increase. This will obviously require focusing more attention (technically and through investment by encouraging collective investment schemes) to those sectors that now contribute more to the GDP position to avoid the risk of any market crash from happening.

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23. Computation from MoFPED Report on Loans and Grants and Guarantees for FY 2010/11 (Pg 6), Uganda Debt Sustainability Analysis Report, Dec 2014 (Pg 3) and Report on Public Debt, Guarantees, other Financial Liabilities and Grants for FY 2018/19, March 2019, (Pg 3)
24. IMF (2016). 7th and 8th reviews under the Extended Credit Facility Arrangement: Debt Sustainability Analysis for Malawi, June 2016.
25. SEATINI (2017). Taxation in Uganda: Review and Analysis of National and Local Government Performance, Opportunities and Challenges,
26. The East African. Mixed prospects for Uganda after rebasing economy Saturday December 13 2014: Also refer to https://www.theeastafrican.co.ke/business/Mixed-prospects-for-Uganda-after-country-rebases-economy/2560-2554724-hblf4hz/index.html
27. http://blogs.worldbank.org/opendata/kenya-s-re-based-national-accounts-myths-facts-and-consequences

# Extracts of Cross-cutting testimonies on Rising Debt

1. **IMF (2019) -** *Uganda has formally adopted a debt target in the Charter for Fiscal Responsibility but needs proper implementation for **an effective fiscal management**. Since 2013, capital investments have been lowering than planned. There is deterioration in debt metrics leading the budget currently to spend one in five shillings collected in revenue on interest payments which is more than the allocations for health or education. However, Government envisages that the ongoing work to develop the 2019-2024 Public Debt Management Framework will help keep debt at sustainable levels.*[28]

2. **United Nations (2019) –** *"Global levels of public and private debt continue to rise. The impact of the sharp drop in commodity markets in 2014/15 also continues to weigh on fiscal and external balances and has left a legacy of higher levels of debt. All East African countries continue to experience relatively high fiscal deficits. The resulting savings gap is filled by external financing (e.g., the shift towards increased borrowing from China and the international bond market). The debt position in the region is expected to deteriorate in the next few years, increasing the risk of external debt distress in a number of countries.*[29]

3. **Jubilee Debt Campaign (April, 2019)** – *Debt crisis deepens as global South debt payments increase by 85%. The average government external debt payments across the 124 developing countries for which data is available have increased from 6.6% of government revenue in 2010 to 12.2% of government revenue in 2018, an increase of 85%. This is the highest level since 2004, when such payments were 13.8% of government revenue. The growing debt crisis was a key discussion at the IMF and World Bank Spring Meetings in Washington DC from 9$^{th}$ -14 April, 2019 and will continue in the G20 Finance Ministers meeting 8-9 June 2019 in Japan.*[30] Tim Jones, Head of Policy at the Jubilee Debt Campaign noted that,

> *"…….. A vital first step is to require that all loans to governments are publicly disclosed, allowing parliaments, media and civil society to hold governments to account for new borrowing. In addition, when crises arise, the IMF should stop bailing out reckless lenders, and require debts to be reduced instead, so that the costs of crises are shared between borrower and lender. All too often, the lenders who helped to cause the crisis are bailed out, while all the costs of irresponsible lending are born by people in the borrowing country……."*

28. IMF (2019). Uganda: Staff Concluding Statement of the 2019 Article IV Mission, February 14, 2019
29. Unite Nations. World Economic Situation and Prospects, 2019
30. https://jubileedebt.org.uk/press-release/crisis-deepens-as-global-south-debt-payments-increase-by-85

4. **Auditor General (Dec, 2018)** – *Uganda's debt increased by 22% from UGX 33.99trillion as at 30th June 2017 to UGX 41.51trillion as at 30th June 2018. Although debt to GDP ratio of 41% is still below the IMF risky threshold of 50% and compares well with other East African countries, it is unfavourable when debt payment is compared to national revenue collected which is the highest in the region at 54%. Interest payments during the FY 2017/18 was 17% of total revenue collections, above the limit set in Public Debt Management Framework 2013 of 15% and has been on the rise for the last 4 financial years.*[31]

5. **PwC Uganda (April 2018)** - *The increasing public debt levels is now a major concern as it may put a drag on the economy if not managed well. In addition, there are perceptions in the market that Uganda may not be able to service its rising debt levels. The debt burden has been growing faster than the government's own resources. Debt as a percentage of revenues rose by 54% since 2012 and was expected to exceed 250% in 2018.*[32] *For debt to remain sustainable, the real GDP has to grow at a rate higher than the average real interest rate on government debt.*

6. **IMF (2018)** - *Many LIDCs are currently faced with Debt burdens arising from vulnerabilities reflecting a mix of factors including exogenous shocks (falling commodity prices, civil conflict), loose fiscal policies, gaps in public debt data, weak governance, fraud/corruption, sluggish per capita growth and falling public investment levels . While the majority of LIDCs remain at low or moderate risk of debt distress, the number of countries at high risk or in debt distress increased from 13 in 2013 to 24 in January 2018, representing an increase from 40% up from 2%. Moreover, nine of twelve countries that moved from "low/moderate risk" to "high risk/in debt distress" are in sub-Saharan Africa. Uganda's debt accumulation characterised by increased commercial borrowing, including from domestic markets and large fiscal deficits reflecting weaker fiscal revenue.*[33]

31. Office of the Auditor General (2018). Report of the Auditor General to Parliament for the FY 2017/18, Dec 2018
32. Bank of Uganda (220160. State of the Economy Report, December 2016
33. International Monetary Fund (2018). Macroeconomic Developments and Prospects in Low-Income Developing Countries, Policy Paper, March 2018

# Strategic Moves for Debt-slavery to debt-freedom

1) Practice fiscal adjustment by exercising expenditure cuts especially with a focus of having smaller and manageable administrative centres. Reduced expenditure on public administration yet properly funded will ensure effective and efficient functioning in an effort to save resources.

2) The decisions made on how borrowed resources are utilized determines the extent to which financial Freedom is gained to facilitate slipping out of debt. Government should adopt the practice of developing a simple budget within reasonably available resources while planning effectively and have maximum control of the available finances. Although MDAs usually set performance targets, the limited capacity/resources (human, financial and physical) many times impede their attainment.

3) With the in-coming of the DRM strategy, through its effective implementation, Government should step up efforts to boost public savings and also expand domestic revenue mobilization towards increasing space for public investment. To raise Tax to GDP ratio, enhanced strategies for collecting more taxes like broadening the tax base or the introduction of more innovative tax collection measures on already existing taxes should be reviewed and implemented.

4) There is great need for fiscal prudence and with greater data transparency from the debtors and creditors for improved debt management.

5) Government should arise to the realisation of the importance of investing more in the agriculture sector which employs over three quarters of Ugandans. Effective planning and coordination is key among competing agencies mandated to deliver in the sector including, considering a merger strategy for those duplicating roles to save resources for allocation to other votes.

6) While rebasing in most cases exposes structural inadequacies pointing to unbalanced growth pattern, Government should stimulate the economy to create sustainable job and high disposable incomes and low poverty. If these are not addressed, the new improved GDP measures will not solely improve economic performance or prosperity enough to support debt repayment.

7) Government should emphasis investment in sectors that have greater contribution towards GDP position to avoid the risk of any market crash from happening by encouraging collective investment schemes. This will boost the domestic revenue generation process to support debt repayment.

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