BUDGET ALERT

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THE NATIONAL DEBT DILEMMA

A high national debt will be a legacy of the Covid-19 induced recession. In Grenada, similar to the other countries of the Eastern Caribbean Currency Union (ECCU), the steep decline in Gross Domestic Product (GDP) and the accompanying deterioration of the government's fiscal performance will result in a higher national debt.

The extent of the expected decline in economic activity can be gleaned from the assessment in the International Monetary Fund (IMF) October World Economic Outlook. In this report, the global economy is projected to contract by 4.4 percent in 2020, with the main trading partners of the ECCU, the USA contracting by 4.3 percent, the UK by 9.9 percent and Canada by 7.2 percent.

In this global context, the ECCU is forecasted to decline by 16 percent in 2020. The Grenada economy, which is highly dependent on tourism, is projected to contract by 12.2 percent. Higher national debt will be an outcome of this recession.

The debt dynamics during the financial and economic crisis of 2008 is instructive. Total public sector debt of the combined governments of the ECCU increased from 73.9 percent of GDP in 2007 to 78.8 percent of GDP in 2010. Grenada's national debt increased from 86.5 percent of GDP to 95.4 percent of GDP over that same period. A combination of debt restructuring, economic growth and improved fiscal performance contributed to a decline in the debt to GDP ratio commencing in 2014.

The Covid-19 induced recession will push countries to debt levels that are considered unsustainable. Grenada will need to contain the growth in public sector debt to avoid high and unsustainable debt.

Grenada's total public sector debt was reported at $1.89 billion or 57.7 percent of GDP in 2019. The decline in GDP of 12.2 percent in 2020 and the acquisition of new debt pushed the debt to GDP ratio to 68.6 percent in 2020, equivalent to a debt of $1.94 billion. It was reported that with a projected economic growth of 6 percent, the total public sector debt is expected to be 65.7 percent of GDP in 2021, which is equivalent to $1.99 billion. The debt to GDP ratio is projected to further decline to 62.7 percent of GDP in 2023 which would be equivalent to $2.14 billion. The trend in the debt to GDP ratio will depend on the rate of contracting of new debt and the pace of economic recovery.

Grenada's Medium-term Fiscal Framework is based on the steady decline in the debt to GDP ratio from the 65.7 percent in 2021 to 62.7 percent in 2023. This is in the context of the restoration of the Fiscal Responsibility Act and the implementation of the Recovery Plan Memorandum in 2022. The decline in the debt to GDP ratio is expected to be achieved by a reduction in both recurrent and capital expenditure. Following the expansionary fiscal policy position in 2021, a more contractionary fiscal policy position will be adopted for 2022 and 2023 as outlined in the Medium-term Fiscal Framework. In 2023, recurrent expenditure is projected to decline from 19.5 percent of GDP to 16.3 percent of GDP. Capital expenditure is projected to contract from 7 percent of GDP in 2022 to 5.6 percent of GDP in 2023.

The projection for the debt to GDP ratio is based on a rapid reduction in expenditure and sustained economic growth. The fiscal risks are high, and if materialized, could hinder the achievement of the projected debt to GDP ratio of 62.7 percent by 2023. Additionally, the treatment of the settlement of the Grenada Electricity Company (GRENLEC) matter and the loan with the EXIM Bank of the Peoples Republic of China for the upgrade of the Maurice Bishop International Airport has the potential of pushing the debt to GDP ratio to more than 70 percent. Along with the debt to GDP ratio, the servicing of the debt must be considered.

With the contraction in domestic revenue, the capacity to repay debt was reduced. In the 2021 Budget, debt payments, comprising interest and principal payments, were estimated at 55 percent of recurrent revenue. Debt servicing is estimated to be 50 percent of recurrent revenue in 2022 and 48 percent in 2023. The national debt needs to be carefully managed to avoid high and unsustainable debt. At this stage, the focus should be on ensuring the efficiency and effectiveness of all government expenditures and a strategic approach to the management of the national debt.

Consequently, it is important to implement the institutional arrangements for the management of the public debt as outlined in the Debt Management Act (The Act). The underlying principle of the Act is for a systematic approach to the contracting of debt and the management of the debt. The Debt Management Act makes provisions for a Public Debt Coordinating Committee, chaired by the Permanent Secretary of the Ministry of Finance and consisting of the Head of the Budget Department; the Head of the Debt Management Unit; the Head of the Policy Unit; the Accountant General or his or her designate; a representative of the Attorney-General; and a representative of the Public Sector Investment Programme. Among its functions, the Public Debt Coordinating Committee is required to consider proposals for the assumption of new debt obligations and review the annual public sector borrowing plans. The Committee is expected to meet at least monthly and to report to the Minister of Finance. The Debt Management Unit is supposed to provide technical and administrative support to the Public Debt Coordinating Committee.

The functions of the Debt Management Unit are comprehensively outlined in the Debt Management Act. Under the supervision of the Minister, the Debt Management Unit is required to rigorously examine debt to be contracted, monitor the public debt, and advise on debt developments. The Unit is expected to prepare reports on the implementation of the Debt Management Strategy for the approval of Cabinet within one month of the end of the quarter. These technical processes are stipulated to ensure efficiency in the contraction and management of the national debt.

The Debt Management Act also makes provision for transparency in the management of the national debt. It requires the submission of a Medium-term Debt Management Strategy to Parliament at least two months before the beginning of the fiscal year; and the submission of an annual borrowing plan and a public debt management report to Parliament at the time of the presentation of the annual Budget. The Act also makes provisions for reporting on the national debt. Under the Act, (Subsection 24) states "***The Minister shall cause to be maintained and published on a website of the Government in a timely basis, accurate records of outstanding debt, guarantees, and lending transactions***." The Act further requires the publication of a statistical debt bulletin periodically.

In this high debt environment, effective debt management is critical. It is therefore necessary to adhere to the provisions of the Debt Management Act for the effective management of the national debt and for improving fiscal transparency.

"***Knowledge is power, and experience is the greatest teacher***".

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Ms Bain has undertaken assessments of the economies of the Eastern Caribbean Currency Union (ECCU) and research on fiscal policy and taxation issues in the ECCU. She is the Author of the books: Fiscal Policy The Economy and The Tax Structure of the Member Countries of the ECCB. Ms. Bain has worked extensively with international development agencies and regional institutions.

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