

Policy Brief No.4

BORROWING FOR DEVELOPMENT IN LIBERIA: A POLITICAL
ECONOMY ANALYSIS



*Empowered lives.
Resilient nations.*

STRATEGY & POLICY UNIT, UNDP
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Acronyms

ADF	African Development Fund
CBL	Central Bank of Liberia
DSA	Debt Sustainability Analysis
FDI	Foreign Direct Investment
EFF	Extended Fund Facility
GDP	Growth Domestic Product
IMF	International Monetary Fund
PV	Present Value

Financing Development in Liberia: The implications of different financing mechanisms

Executive Summary

As the Government in Liberia is formulating its national development agenda, financing is an urgent consideration. The implications of fundraising are varied and complex, however this policy paper explores the aspects of different financing mechanisms including commercial and non-concessional loans, and other grants.

The International Monetary Fund (IMF) provides an in-depth Debt Sustainability Analysis (DSA) to assess country debt scenarios with respect to various types of loans for member governments as key in designing borrowing ceilings to maintain debt sustainability. Regardless of this analysis, countries in many cases approach commercial and non-concessional lending. There are both political, institutional and economic reasons for that. Among these factors are the prolonged time needed to negotiate new multilateral arrangements, the urgent need and political pressure to respond and fulfill electoral promises, and to keep the government functioning. By contrast, there are immediate internal and external consequences to such government decisions. The creditors will raise concerns about the choices and its long term impact with respect to the capability of debt sustainability.

Furthermore, while the public needs to know terms and conditions of such loans, recent experiences from Zimbabwe and Mozambique have shown that countries are reluctant to disclose some terms, raising concerns about transparency and accountability. In Liberia, there are current concerns regarding a commercial loan from a Singapore-based company, Eton Financial Private Limited totaling US\$536 million, which is equal to Liberia's entire current budget. There is a lack of transparency and disclosure from the Government regarding this loan.

Under the Government's pro-poor agenda, there is a need to prioritize projects carefully and examine the expected returns and productivity in line with the financing modality, discounting the optimism of project designers and investors, to ensure that they mobilize finances for only highest priority projects whose contributions to development can justify the costs.

The Government needs to develop a sound funding strategy combining alternatives for financing development through different modalities (concessional, commercial, foreign direct investment, etc.). This will allow the government to strategically allocate resources within the context of being additional, complementary or even a possible substitute to foreign direct investment (FDI).

Background

Many developing countries access mainly non-concessional financing for their urgent development needs. Recently, countries have moved away from traditional official's creditors such as multilateral institutions and members of the Paris Club, a grouping of major creditor countries organized to provide debt rescheduling or reduction to debtor's countries in payment distress. They have moved towards non-Paris Club official bilateral creditors, unlike the Paris Club members, do not have ready mechanisms for coordination with other creditors, which is likely to make any needed debt resolution more difficult. The new forms of private credit often come at shorter maturities and higher interest rates, yielding larger debt services when these debts mature.

Higher public deficits and debt levels are not necessarily undesirable. When countries borrow to pay for infrastructure investment that can boost long-term growth, which in turn generates revenues to service debt (IMF, World Economic Outlook, 2017).

Under the Extended Fund Facility (EFF), countries borrow for a period of three to four years and repayments are not due until five to ten years down the line. Member countries can also avail themselves of the EFF's short-term financing facilities. The Supplemental Reserve Facility provides very short-term financing on a large scale to emerging market economies experiencing sudden loss of market confidence as a result of massive outflows of capital while Contingent Credit Lines finances national economic policies aimed at averting an economic crisis precipitated by crisis elsewhere in the world. Both types of financing require repayment within one to two years and carry a surcharge. The Compensatory and Contingency Financing Fund provides loans to countries experiencing shortfalls in export earnings due to unforeseen circumstances, such as natural disasters affecting crop yields. Repayments are made in three and quarter to five years (IMF, 2018¹).

Although their debt has risen, more than half of low-income countries are still at low or moderate risk of defaulting on their debt service obligations. However, the share of countries at elevated risk of debt distress, for example, Ghana, Lao PDR and Mauritania, or already unable to service their debt fully has almost doubled to 40% percent since 2013 (IMF, World Economic Outlook, 2017).

The basic story of current undisclosed loan terms and conditions starts when the Liberia government pursues a commercial loan. The story is not a new one in the African context of governments seeking non-concessional lending. Perhaps, the current move raises questions about why the government approach borrowing under lending on "hard terms" commercial lending at this early stage.

In its eagerness to meet the investment needs to deliver political promises, is the new government going to face difficult time due to non-concessional borrowing rates? Is it justifiable at this early stage? What are the long-term implications to both creditors, government budget and debt service payments over the needs of the poor in the long run? Those are central questions to this background note, which aim to reflect and draw some policy conclusions and recommendations that may trigger positive debate in this arduous road. In many cases as shown by experiences, good intentions – if not well managed – end up with bad results.

¹ For more details see <https://www.imf.org/external/about/lending.htm#changing>

Such a step needs a pragmatic approach to avoid unnecessary political tensions regarding its lack of transparency, as well as worsening the relationships with partners in the long run if not managed well. **Under such circumstances and the need for commercial loans, we believe that the government needs to have excellent policies that aims to combine both domestic and external resources (including FDI), anti-fraud and value-for-money checking systems to avoid fictitious financing, which makes little contribution to development.**

The Nexus between Concessional and Non-concessional loans: *Why governments search for such expensive loans?*

There are different reasons for why governments look for expensive loans. Concessional lending in many cases has high-conditionality attached, is time consuming and ceilings will not allow the government to move beyond traditional project financing under limited financing arrangements. In other words, the government hand with respect to development financing is limited.

Many of the major debtor countries are in fiscal turmoil, even after sharp cuts in government spending in recent years due to the problem of how to use additional finance through commercial loans strategically with highest impact and productivity. The interest due on the foreign debt constitutes such a large proportion of government expenditures (around 30 percent in many of the debtor countries) that it stands later in the way of budgetary reform.

Large fiscal deficits are now being financed, in large part, through an expansion of credit by the central banks, a process that will result in high inflation. As such, borrowing for development with good intentions may result in long run economic disarray. Borrowing for development and the internal economic disarray has been a burgeoning of unilateral actions on the debt, particularly in the democratic countries².

Status of Liberia with its external multilateral creditors: *Debt sustainability*

Liberia's debt-carrying capacity has deteriorated. Its domestic and external public debt remains relatively low compared with regional average and other low income countries. However, external debt has been rising rapidly, from 11 percent of GDP at end-2013 to 23 percent at end-2015, and is expected to increase further over the medium term, pushing the risk of debt distress from low to moderate as indicated in the December 2015 Debt Sustainability Analysis (DSA). The recent updated DSA by IMF shows that the economy is increasingly vulnerable to further shocks reflecting the worsened growth and export outlook. In particular, any further deterioration in exports could push the risk of debt distress to high (IMF, 2017).

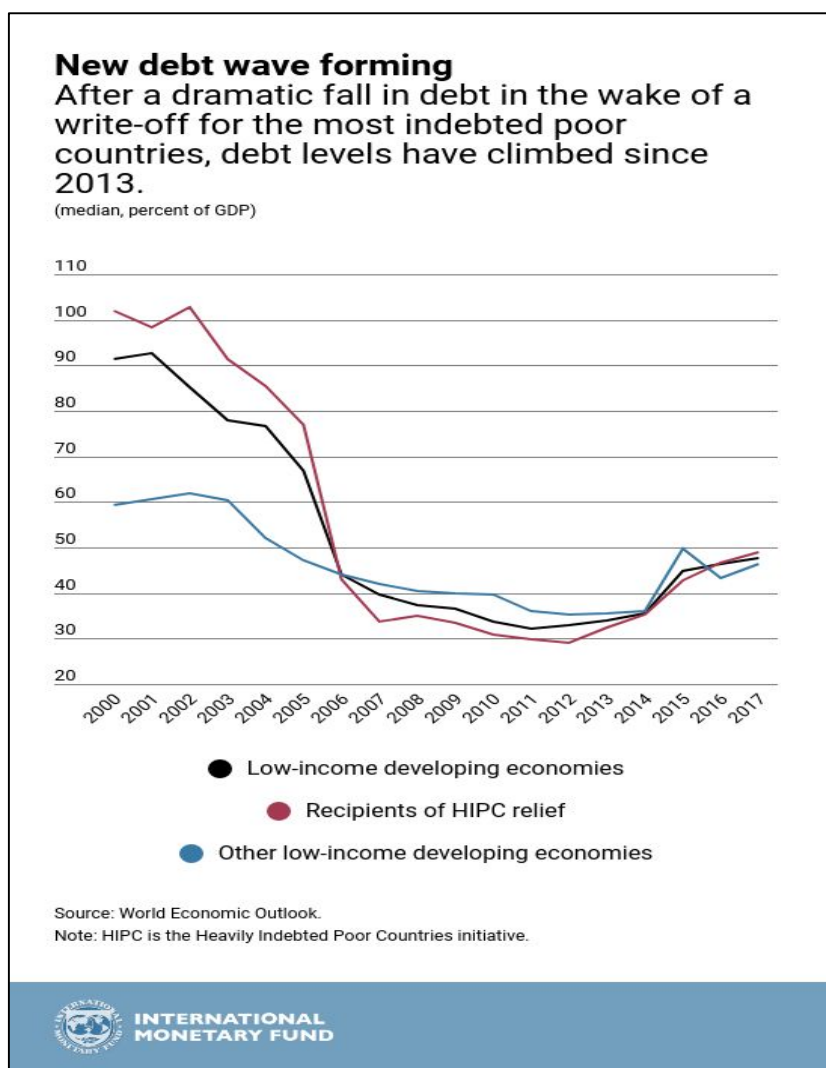
²Debt distress classification. The risk of debt distress determines the proportion of grants in the country allocation according to the following debt-distress classification: (i) low risk of debt distress—no grants, (ii) moderate risk of debt distress—50% grants, and (iii) high risk of debt distress—100% grants. Country debt distress risk classifications are reviewed annually. The debt-distress risk classification is determined by the outcome of a forward-looking debt-sustainability analysis using the debt-sustainability framework for low-income countries of the International Monetary Fund and the World Bank.

Public Debt Dynamics in Liberia

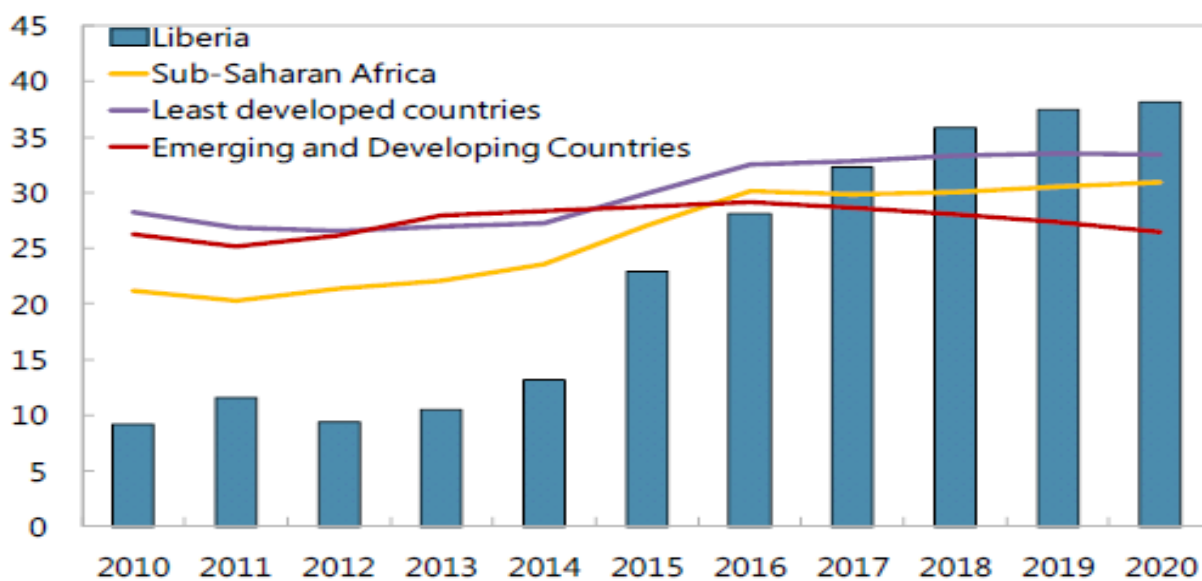
Liberia was hit by falling commodity prices, including iron ore and rubber, just as the devastating Ebola outbreak of 2014-15 was receding. This combination has constituted a big setback and contributed to the rising debt-to-GDP ratio as a result of slowing growth and diversion of fiscal resources to combat the epidemic. While still relatively low, public debt has doubled as a share of GDP between 2013 and 2015. Dynamics are expected to remain adverse over the medium term as a result of large primary deficits (driven in part by needed infrastructure investments) as well as slowing growth.

Given its fragility, very low per capita income and high poverty rate, it would be advisable for Liberia to aim for extended maturities and concessional terms. While debt relief under HIPC-MDRI was completed in 2010 and created fiscal space for new borrowing, the dynamics are adverse as noted above. Liberia also faces tension between debt sustainability and continuing with much-needed infrastructure investments, as noted in IMF Country Report 16/238. Furthermore, the factors that contributed to the violent conflict that ended in 2003 have not diminished. These include ethnic differences, extreme inequality and food insecurity. For all these reasons, Liberia would not be able to cope with MCLs lending terms (IMF, 2017).

With respect to the African Development Bank (AfDB), since the November 2015 mid-term review of ADF-13, it has become increasingly clear that donors' capacity and willingness to provide pure grants has diminished on account of entrenched fiscal and political problems in their own countries. One consequence has been the potential inclusion of concessional loan instruments in the funding mix for ADF, something that has already transpired for the recently concluded ADF-14 replenishment. For these countries, exchange rate collapses have been a major factor spurring unsustainable public debt outcomes over the past few years. Minimizing exchange rate volatility requires good macroeconomic policy, economic



Text Chart 2. Stock of External Public Debt
(In percent of GDP)



Source: IMF staff estimates and projections.

diversification and making local currencies a credible store of value through transparent and sound monetary policy. But this is a medium-to-long term program. There are no immediate fixes. Donors can help by lengthening loan maturities beyond 40 years while also increasing grace periods³. The primary deficit is large, and together with the real exchange rate, drives debt dynamics. As a result, public debt increased rapidly between 2013 and 2015, which the IMF attributes to an expansion in public investment. The share of domestic debt is high, but the nominal interest rate on domestic debt seems to remain under control. Instead, the interest rates on forex debt have increased markedly driven by currency depreciation (Felino and Brian (2017)).

According to the IMF (2017), the external debt stock has been increasing at a fast pace, in part due to scaled-up infrastructure spending and multiple adverse shocks. Since September 2016 to June 2017, the total debt stock has increased from US\$597 million to US\$736 million. Currently, the external debt stock comprises mostly multilateral loans (Text Table 1). In FY2017, around US\$218 million of external loans have been ratified, and the debt accumulation is expected to continue.

³ Luisa Teixeira Felino and Brian Pinto (2017) ADF Policy Innovation Lab Working Paper Series, No 3, African Development Bank

Underlying assumptions of current DSA

Text Table 1. Composition of External Debt Stock

	End of June 2017	
	Millions of \$US	% of Total
Total debt stock	736	100
(as % of GDP)	35	
By creditors		
Multilateral including IMF	683	93
<i>Of which:</i>		
IMF	199	27
World Bank	291	40
AfDB	70	9
Bilateral	54	7

Sources: Liberian authorities; and IMF staff calculations

GDP projections have deteriorated while the outlook for export growth has improved both in the short- and medium-term. In the short run, GDP projections for FY2017 have been revised downward due to stronger than-expected effects from the withdrawal of the United Nations Mission in Liberia (UNMIL) and lower commodity production in the second half of 2016. In FY2017, GDP growth is expected to contract by -2.2 percent, and exports are also expected to contract by -3.4 percent. At the same time, export growth

projections have improved, mainly due to improved gold production and opening of an iron ore mine site. In the medium term, the GDP growth projection is also slightly lower than previously estimated, while export growth is more favorable than previously estimated. Nonetheless, the baseline scenario remains subject to significant risks. On the downside, an unexpected deterioration in the security condition or a recurrence of Ebola could disrupt economic activity and investor sentiment and put additional pressure on fiscal balances. Conversely, a peaceful transition of power in January may release pent-up investment demand, lead to some repatriation of capital, and provide a boost to growth in 2018 (IMF, 2018).

What will happen when the loans are not able to generate enough external economics (loan productivity)?

The issue of non-concessional lending attracts attention not only from the fact that the money is expensive, but also in term of uses of the borrowed resources. Experience has shown that authorities must be cautious about the sector or leading projects where the government plan to use the resources. Those resources either to be considered additional development resources to the development agenda, or complement the domestic resources need for certain projects or ultimately, substitute domestic borrowing. Anyone of the suggested uses above has its own economic implications with respect to growth, stagnation, inflation and employment and long term austerity measures.

The news about the new initiated commercial loan by the Liberian government has come with little surprise where the government is looking for money to fulfil some political promises. There are current reports that Singapore-based firm, Eton Financial Private Limited provided a commercial loan of US\$536 million (equivalent to current budget) paid to the Government of Liberia. Concerns are mounting as the government has not informed the public and the international community. The current move is likely to disappoint partners and the government must work to restore calm and confidence.

Despite the debt sustainability analysis has shown the country status is moderate, however, the productivity of the loan and for what purpose is our major concern and primary discussion. The question is that whether the authority has started discussion with IMF which could have been prevent such move by the government to commercial borrowing or the government convinced that such move is justifiable to fulfil development promises? No doubt that the country's development needs is a justifiable agenda. We knew that the authorities needed resources to urgently address 150 days' plan and other constraints. Perhaps, a more proactive collaboration with some multilateral lender could have prevented the breach of accessing commercial loan. Moreover, the move to non-concessional borrowing poses risks for debt holiday, distress or forgiveness to resolve outstanding dues or arrears in future discussions with creditors down the road.

Are we fair in assessing the authority move to commercial borrowing?

Loan productivity is always critical. Seeking grants and concessional borrowing to finance critical development projects with high economic returns may not be possible or the discussion may take long time to see the dividend. This has political implication to the new government. As such, there are political, financial and economic elements to the move.

In many recent cases, if additional finance is needed from IMF only available at 3% of GDP. In other words, if grants and concessional borrowing are not available or insufficient, limited new non-concessional external debt could be considered for growth-enhancing projects, subject to a continuous ceiling of 3% of GDP.

According to the IMF (2017), Liberia's risk of external debt distress remains moderate. There are no breaches of indicative threshold under the baseline scenario for any debt indicator. The PV of debt-to-GDP ratio has deteriorated slightly since the 2016 December DSA. The PV of debt-to-GDP ratio under the baseline scenario is projected to increase from 23.1 percent in FY2017 to 27.5 percent in FY2019 and to decline gradually afterwards. The peak of 27.5 percent in the PV of debt-to-GDP ratio is higher than previously projected (23.4 percent in the December 2016 DSA). On the other hand, the PV of debt-to-exports ratio has improved mainly due to higher projected commodity prices and a moderate upturn in gold and iron ore mining, and is projected to increase from 76.5 percent in FY2017 and to a peak of 89.2 percent in FY2019, lower than previously projected (99 percent in the December 2016 DSA).

However, debt vulnerabilities remain substantial, with some breaches of thresholds under extreme shock scenarios. Under the most-extreme stress scenarios, either one-time depreciation shock or an export shock, both the PV of debt-to-GDP and the PV of debt-to-exports breach their thresholds even as early as FY2018 and remain breached at least until FY2030. Under the historical scenario case, the PV of debt-to-GDP and the PV of debt-to-

Box 1: IMF Conclusion 2018 Consultations with the Authority

"With the economic shocks and the Ebola crisis now in the past, assuming the implementation of good policies—including measures to improve the business climate and support private sector development—the medium-term outlook appears favorable. The peaceful political transition will offer support to the recovery of the domestic economy (agriculture and service sectors) through improved consumer and investor confidence. Moreover, key commodity sectors are expected to be more active as global commodity price recovery. Better power supply is another positive development factor for both existing and new businesses, though the full effect of the Mount Coffee hydro plant will need to await resolution of the transmission bottlenecks. Over the next few years, the development plan of the new government, with large-scale road construction in its center, will act to expand and connect markets and spur economic development.

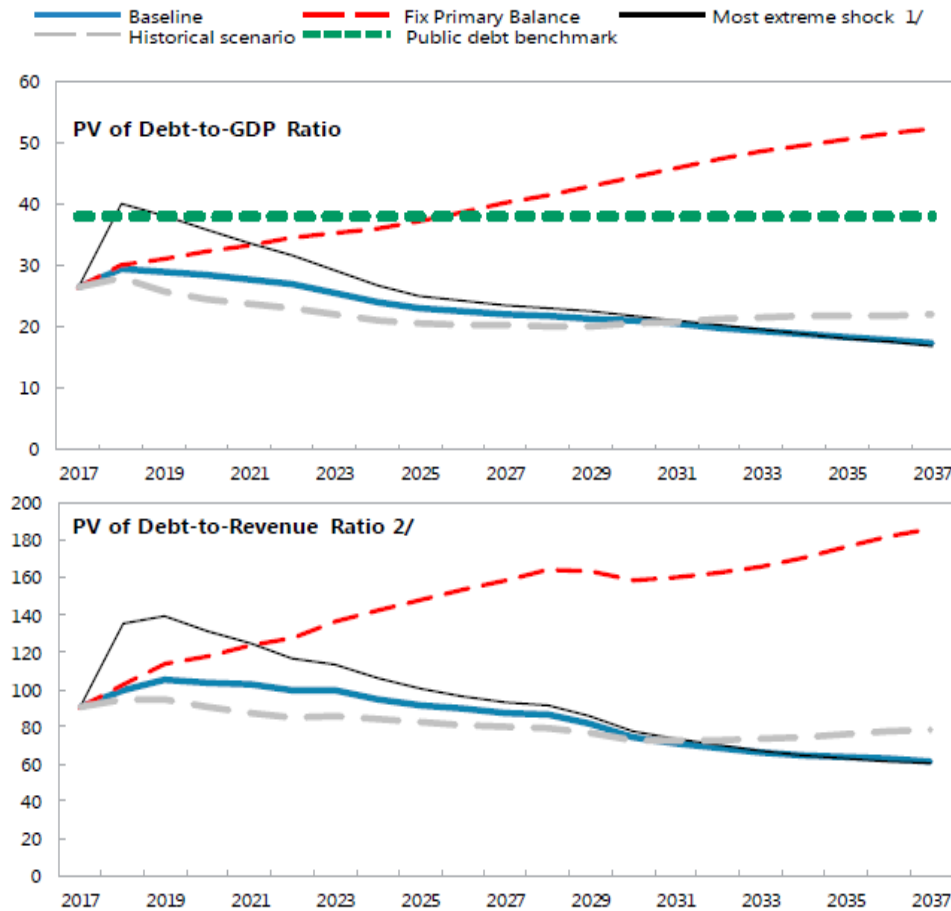
"The team supports the Administration's adoption of a strongly pro-poor agenda. The needs of the poorest segments of the population are clearly large, and it is commendable that the Authorities have made this their policy priority. Within this ambition, it would be particularly important to ensure that the increase in expenditure goes hand in hand with measures to ensure macroeconomic and debt stability, as the impact of instability would fall disproportionately on the most vulnerable groups and "given these potential constraints on resource mobilization, it will be important to not only mobilize significant quantities of additional domestic revenue and secure attractive terms for future contracted debt, but also to improve the efficiency of existing spending to create additional fiscal space. Governance improvements, particularly with respect to inculcating greater fiscal transparency and accountability would be key in this, as would instilling greater order and priority in Government's fiscal relations. Replacing development spending with current expenditure to the extent possible would need to be part of this, including by controlling growth of the wage bill. In addition, Government could also usefully consider adopting a comprehensive program to clear domestic arrears and prevent the emergence of new ones; utilizing realistic revenue estimates for budget formulation; and improving the monitoring of all expenditure, including grant- and loan-financed projects. Maintaining macroeconomic stability will also hinge on effective implementation of monetary policy, a precondition for which would be strengthening of the CBL's balance sheet.

Sources: (IMF, 2018)

exports breach after FY2030 or later. These breaches confirm the Liberian economy's vulnerability to external shocks such as the Ebola shocks, commodity price shock as a commodity exporter, and a sharp decline in the

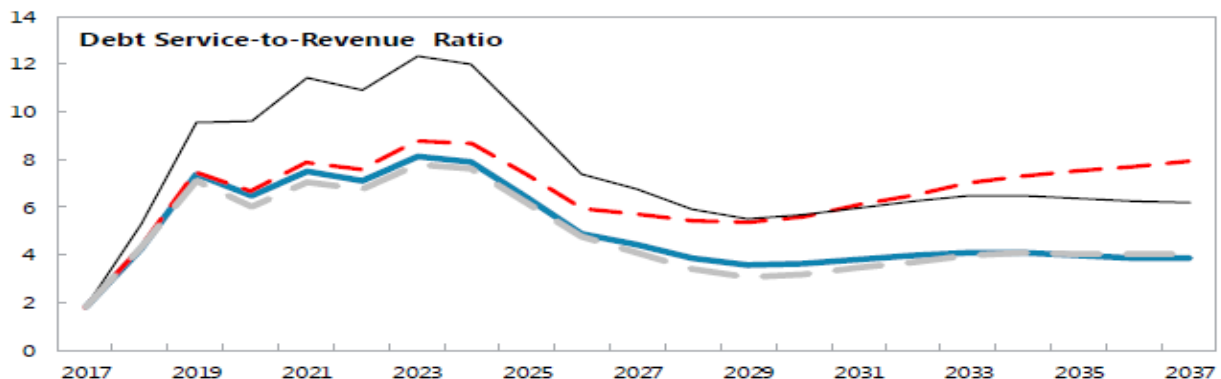
exchange rate and underscore the technical rating of moderate risk of external debt distress. Based on the probability approach, all the indicators under the baseline scenarios remain below the threshold. However, the PV of debt to GDP ratio is close to breach, reflecting Liberia’s debt vulnerability.

Liberia: Indicators of Public Debt under Alternative Scenarios, 2017–37^{1/}



Source: IMF (2017)

By contrast, when allocating their aid budget, development agencies need to decide whether to give outright grants or use concessional loans that blend a grant and credit element. Theory suggests that the degree of concessional loans should be negatively correlated with debt sustainability. Several donors use the World Bank/ IMF Debt Sustainability Framework to guide their aid decisions. They give loans to low-risk countries, a blend of loans and grants to medium-risk countries, and only grants to high-risk countries. The paper shows that there are problems with this approach and proposes an alternative allocation mechanism based on GDP indexed concessional loans. Perhaps this is good reason justify the current mover by the government to such commercial loan. Grants and the ceiling of concessional lending may not offer enough financial buffer to the government to pursue its big promises.



Sources: Country authorities; and staff estimates and projections.
 1/ The most extreme stress test is the test that yields the highest ratio on or before 2027.
 2/ Revenues are defined inclusive of grants.

There is a second, and more sophisticated, argument that favors commercial loans over grants over concessional loans. If private capital flows timely and to specific projects, the government has the upper hand unlike concessional lending, which is slow and restricted. Therefore, the argument goes, it is better to access such loan only and only if the government has put the necessary measure to ensure highest impact and oversight together with expected high productivity of the loan. This is call for commercial loan to be effective rigorous economic and financial analysis is needed to guide the government in preferred sector focus.

It has also been argued that grants and loans have different incentive effects and that grants are more likely to be wasted and result in excessive government consumption and lower tax effort. The general argument dates back to Schmidt, 1964). Djankov et al. (2004) find that grants increase government consumption, but Morrisey et al. (2006) find that the choice between loans and grant has no effect on tax revenues⁴.

Therefore, grants, concessional loans and commercial loans are not equivalent and there are trade-offs involved in the choice between grants and concessional loans. With grants, the recipient country does not have an obligation to repay but it receives a smaller flow of foreign resources. With concessional loans, the recipient country receives a larger foreign transfer, but it also accumulates external debt obligations like any commercial debt.

Experience from Africa

Borrowing on a huge scale always has implications and consequences with respect to development partners supporting government budget and long-term impact causing sovereign debt to swell to unsustainable levels. The information available indicates that the loan procurement process lacked parliamentary approval, had contravened the constitution, and violated budget laws. This will further constrain the government's room for maneuver and damaged investor confidence with respect to financing the next five years' plan.

Sub-Saharan Africa is slipping into a new debt crisis, with 40 per cent of the region's countries now at high risk of debt distress — double the proportion of five years ago. With the number of countries already unable to service their debts doubling in the past year to eight, officials at the IMF are urging all African countries to raise taxes to provide more scope for paying interest, which has increased to levels last experienced at the start of the century. The officials caution that any debt relief required in future is set to be much more difficult than in the past because most recent lending has come from commercial sources less amenable to debt forgiveness than are national governments (Financial Time, 2018). Masood Ahmed, president of the Center for Global Development, a

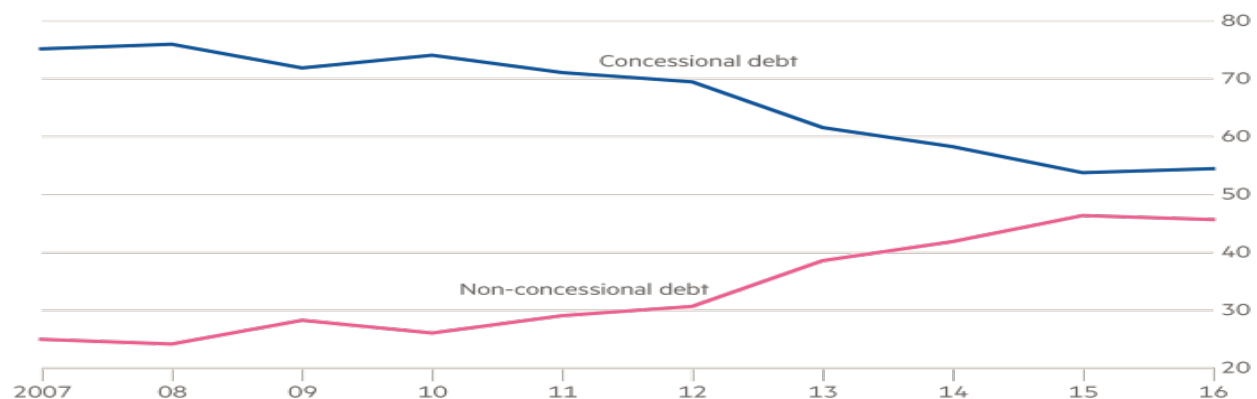
⁴ Another often used argument is that, in any given country, grants should be used to finance activities that do not generate an immediate increase in revenues (such as social expenditure) and loans should be used to finance projects that generate revenues stream (such as power generation of toll highways). Money is fungible and I do not find this line of reasoning very compelling.

development think-tank, said the region's increased debt had been facilitated by commercial lenders searching for higher-yielding assets. Mr. Ahmed led the World Bank's Heavily Indebted Poor Countries Initiative in the 1990s — a program that significantly reduced debt burdens.

"While debt ratios are still below the levels that led to HIPC, the risks are higher because much more of the debt is on commercial terms with higher interest rates, shorter maturities and more unpredictable lender behavior than the traditional multilaterals," (Financial times, 2017).

Low-income developing countries: share of non-concessional funding

% of total public and publicly guaranteed debt, 2007-16



Source: IMF/World Bank
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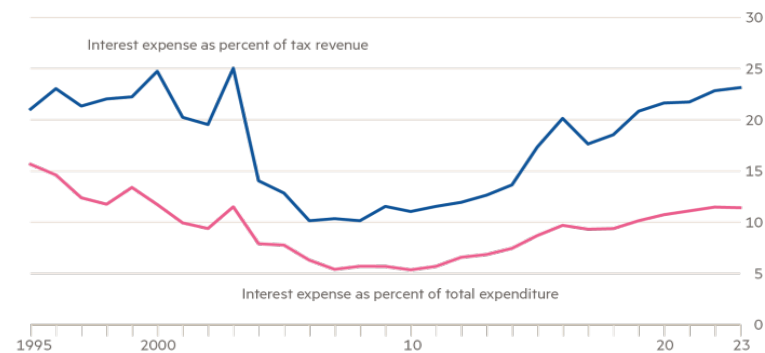
The fear is that many African countries will become stuck in a debt trap, undermining economic development, just 13 years after the Multilateral Debt Relief Initiative, which cancelled debt for countries that met economic-management and poverty-reduction criteria.

By contrast, Abebe Selassie, director of the African department at the IMF, stressed that "while the rise in debt was a concern", the picture in sub-Saharan Africa was very diverse and many countries could stabilise debt burdens quickly if they mobilised revenues.

But in its Fiscal Monitor, a twice-yearly survey of governments' balance sheets, the fund noted that few countries with debt problems had benefited from much higher investment and strong growth rates. "The deterioration in fiscal balances over the past five years does not reflect a scaling up of investment," the report said. Commodity exporters such as Nigeria, Chad, Congo and Zambia have suffered a plunge in revenues from the extraction of oil and metal ores. The recent rise in commodity prices has given some a little breathing space, according to an IMF official, but many are in distress. Other African countries "let spending drift upwards across most items," the IMF Fiscal Monitor said, a

Interest expense as a share of tax revenue and total expenditure

Per cent



Source: IMF/World Bank
© FT

category it said included Ethiopia, Ghana and Gambia. Some countries had been hit because they had borrowed in foreign currencies and were finding debt hard to finance after a significant depreciation, including Côte d'Ivoire, Senegal and Zambia. Substantial fraud and corruption, including the reporting of previously undisclosed debt, where the state is responsible for often opaque contingent liabilities of state-owned enterprises, has hit countries such as the Republic of Congo, Mozambique and Angola. The result has been significantly rising debt burdens, with the IMF estimating the public debt burden in low-income countries has increased by 13 percentage points of GDP in the past five years.

IMF officials at the spring meetings in Washington have urged African countries to increase the efficiency of public expenditure, hand over public investment to the private sector, and fully implement fiscal consolidation plans, including seeking new revenues from consumer taxes. But some are pointing the finger at the IMF itself for being asleep at the wheel while debts increased significantly (Financial Time, 2018).

Mozambique

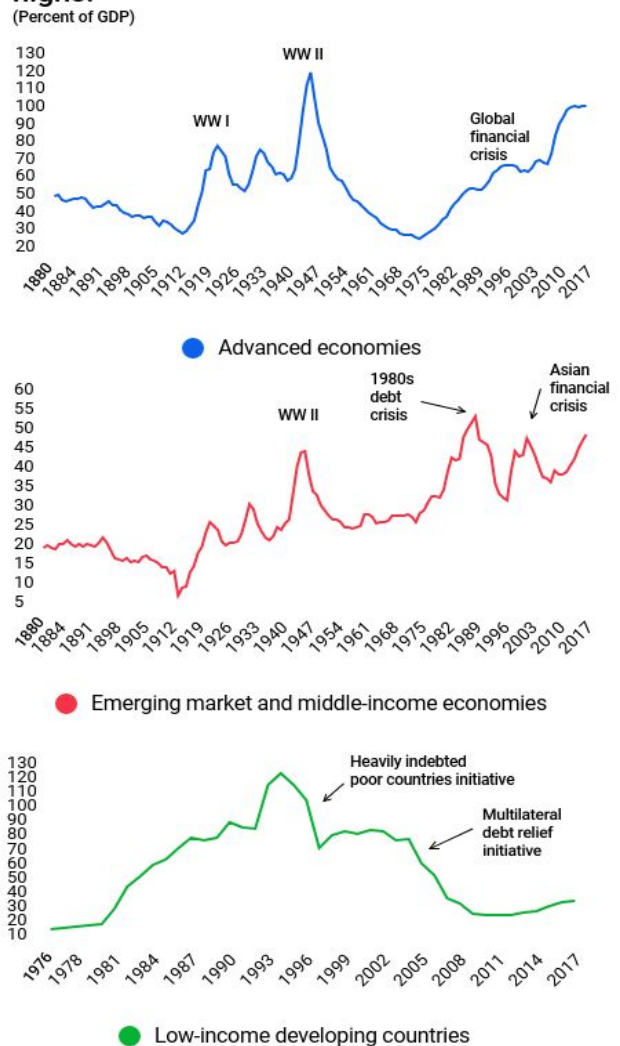
With respect to Mozambique's recent scandal for undisclosed loans, some suggest that the government is particularly reluctant to allow scrutiny because of the personal involvement of president at the time the loans were made. In Mozambique, the donors, who had provided about a quarter of the impoverished country's state budget, have demanded a full investigation of the scandal by the ruling Frelimo party before they resume financial assistance. The crisis put the brakes on what had been one of Africa's fastest growing economies and forced Maputo to default on its debt last year.

The loans were taken out in 2013 when the impoverished southern African nation said it wanted to set up a state-backed tuna fishing company. But they were hidden from the IMF and donors, and their discovery plunged what had been one of Africa's star economic performers into a financial crisis. Donors, which provided about a quarter of the government's budget, suspended aid and the government defaulted on the state-backed loans just as it was hoping to develop vast offshore gas fields and attract greater foreign investment.

This scandal has triggered a flurry of revelations that have relegated the country from international darling to the international doghouse. That loan scandal, and Mozambique's subsequent outright default on its debts this year, cast a pall over a country that was considered one of Africa's brightest prospects (Financial Time, 2017).

Government Debt

Average debt-to-GDP ratios are at historic highs.



Sources: April 2018 Fiscal Monitor
 Note: Average is calculated using GDP at purchasing power parity. Dashed lines refer to the debt level in 2017.



Ghana

The recent report by Jones (2016)⁵, *The fall and rise of Ghana's debt: How a new debt trap has been set*, shows how Ghana is in a new debt crisis just a decade after having significant amounts of debt cancelled by international lenders. While debt cancellation in 2004 and 2005 gave the country breathing space to increase spending on public services, the commodity price crash and currency shocks since 2013 have seen debts rapidly building up once again.

Ghana's new debt crisis is the result of a gradual increase in lending to the country following the discovery of oil and the boom in commodity prices since the mid-2000s. More money was then borrowed to try to cope with the impact of the commodity price crash since 2013, whilst the Ghanaian currency, the cedi, has halved in value against the dollar, increasing the relative size of the external debts. Around 30% of government revenue is now being spent on external debt payments each year. Such huge payments are only possible because more money is being lent by institutions such as the IMF to pay private lenders, as happened in Greece after 2010.

The high interest rates on the private external debt show that the original lenders thought it was quite likely Ghana would default at some point before the interest and debt was due to be fully repaid.

"Schools were rehabilitated over the last decade; more classrooms were added. Other than that, there have been no other developments in the area. The sugar factory shut down more than 20 years ago, and the textiles factory 15 years ago. Since then they've not been replaced by any other industry. Most people are reliant on farming, whilst the youth all move to Accra to do donkey work."

Madam Maatyo Dedo Azu, Somanya, Eastern Region

"The underlying causes of Ghana's new debt crisis are that neither borrowers nor lenders have learned from past mistakes, and that its economy remains reliant on primary commodities, leaving it extremely vulnerable to the recent global commodity price crash. The people of Ghana should not have to suffer through yet another debt crisis while lenders who speculated on their economy reap huge profits out of high interest loans guaranteed by the World Bank."

"Ghana's debts need to be reduced or restructured to escape another prolonged debt trap, while regulation of lending, more responsible borrowing, and tax justice are essential to end this cycle of debt crises once and for all."

Sarah-Jayne Clifton, Director of the Jubilee Debt Campaign, UK

"Debt should not be a bad thing, but if money is borrowed in the name of poor people, not spent well, and people are slapped with austerity as a result, that is a gross injustice."

Bernard Anaba, Integrated Social Development Centre in Ghana

⁵ Source: <https://jubileedebt.org.uk/report/fall-rise-ghanas-debt-new-debt-trap-set>

Private external debt risk and long-term implications to the Liberia Government

There is no free lunch in both modalities on whether the government should choose concessional loans with grant or commercial elements. Concessional versus commercial loans both has advantages and disadvantages. Commercial loans in some cases is an opportunity for development, not taking it may also be considered as a missed opportunity, however, misuse is a serious threat. In many cases, authorities may have an internal logic to pursue such non-concessional lending. The question is how to weigh both the economic and political benefit.

In Ghana's case, private lenders effectively bet on the oil and other commodity prices that Ghana was dependent on for paying the debt. However, vulture funds could choose to buy up bonds then block a restructuring in a particular bond issue, then sue, even if other creditors accepted the restructuring. In 2012, vulture funds bought up particular bond issues by Greece and then blocked the restructuring for those particular issues. Unfortunately, Greece continued to pay the vulture funds in full, which meant the speculators made huge profits on what they paid for the debt. Any threat to default or default on this debt would mean it would probably become impossible to borrow more from private external lenders (though after debt has been reduced private lenders tend to be willing to lend again surprisingly quickly).

The bigger question will come later is whether defaulting or threatening to default on external private debt would affect the decisions of multilateral institutions and other governments. This would ultimately be a political decision.

In the April 2018 *Fiscal Monitor*, we urge policymakers to avoid fiscal policies that provide unnecessary stimulus when economic activity is already picking up. Instead, most advanced, emerging market, and low income developing countries should deliver on their fiscal plans, and put deficits and debt firmly on a downward path. They should also enact fiscal reforms that increase productivity and promote human and physical capital. It is imperative that low income developing countries strengthen their tax capacity. This will allow them to service their debt. It will also allow them to finance spending priorities—such as health, education and public infrastructure—to attain the Sustainable Development Goals.

Conclusion

The best case scenario for the Minister of Finance is to convince the public about the move and make use of the loan in highly productive sector. The ongoing transparency discussion in the media may cause a lasting negative image to the government over what exactly happened, and the widespread belief the legacy of high-level corruption will galvanize media to raise the alarm about the loan. For example, recent scandals and non-concessional lending has raised a number of questions with respect to Mozambique, Zimbabwe and Ghana; the first two were accessing expensive commercial loans results in worsening the relation with multilateral creditors. Recently the World Bank has been accused of helping to fuel a new debt crisis in Ghana after it was revealed it has broken its own rules against lending to countries with high-risk debts. The Bank gave a \$400 million guarantee to a high-interest private loan to the country, the first such guarantee it has given for 15 years.

The government through the Debt Management Department, needs to watch out and develop diversified long term scenarios compatible with the financing needs for development and resources envelope for the upcoming Five Years Plan. Perhaps, this is also call for need to proceed prudently on taking up new debt, focusing more on attracting foreign direct investment in areas where FDI can substitute loans and boosting tax revenues at home.

Continued debt vulnerabilities for Liberia call for a prudent debt management policy, a credible path of revenue mobilization and fiscal consolidation, and structural reforms to promote growth and economic diversification. The

DSA shows that Liberia's risk of debt distress remains moderate. As Liberia remains vulnerable to external shocks (e.g., commodity price fluctuations) as a commodity exporter, the authorities need to be committed to a prudent borrowing strategy, the prioritization of pro-growth projects versus pro-poor agenda need serious debate on where to allocate resources between productive and social sector. For doing so, the government needs to initiate a number of background analyses to inform sources of economic growth, pro-poor growth and the pillars stimulating long term growth and diversification.

No one can predict the ebb and flow of countries' economies. Prudent and successful governments prepare in good times to face the storms looming on the horizon.

Recommendations

- For the economic and political stability of the government, governance and transparency, we advise the authority to seek or establish independent committee (financial responsibility) for oversight and assessment of the economic and social impact of projects funded with non-concessional loans. The step will help the authority to restore long term building confidence with public and creditors as well. This could create bad publicity with speculation in media and citizens, potential negative perception with respect to transparency measures and worsening the relation with partners and caused donors to suspend aid to the government in future.
- The government needs to develop sound strategy combined different alternatives for financing development through different modalities (concessional, commercial, FDI, etc.). This will allow the government to strategically allocate resources within the context of being additional, complementary or possible substitute like FDI.
- As part of the upcoming five-year plan, design finance strategy, The Debt Management Office needs to work closely with the Finance and planning team designing the resources envelop and maintain a comprehensive and credible computerized database of all public and publicly guaranteed external debt. As such, designing an external new financing strategy includes a comprehensive assessment of potential new financing options from concessional and non-concessional sources , as well as possible grant inflows, with main desire and focusing on how best to mobilize diversified resources with the highest quality financing to support the pro-poor development priorities agenda and ensure debt sustainability. This strategy may include combination of project approach financing and sector wide approach and budget support.

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