A CASE FOR EXTERNAL DEBT CANCELLATIION FOR EBOLA-AFFECTED COUNTRIES

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"BILATERAL AND MULTILATERAL CREDITORS SHOULD SERIOUSLY CONSIDER CANCELING THE THREE COUNTRIES' EXTERNAL DEBTS."

UNECA (2014, p.45)[1]

Cancelling the external debt of Guinea, Liberia and Sierra Leone, the three countries hardest hit by the EBOLA outbreak, will give these countries the breathing space they need to address the complex social and economic development challenges they now face. In addition to meeting the challenges of the EBOLA outbreak, these countries need to promote positive economic growth, improve public service delivery, meet regular debt service payments and plan their long-term social and economic development. The setback induced by the EBOLA outbreak complicates these challenges and reinforces the compelling case for debt cancellation. Based on available data, this appendix presents the external debt situation of Guinea, Liberia and Sierra Leone, makes the case for debt cancellation, and puts forward recommendations on how to use the resulting freed-up funds.

It is common to call for the cancellation of debts of countries that have been severely affected by sudden shocks such as natural disasters or outbreaks of disease. Haiti, for example, had the debts it owed to major creditors cancelled after the 2010 earthquake. Guinea, Liberia and Sierra Leone already had weak initial conditions, structural vulnerabilities and limited potential to sustain growth and the EBOLA outbreak has pushed them to the limit by widening their fiscal deficits. If the countries have to continue making debt repayments in the absence of significant financial inflows, they will not be able to fulfill their fiscal and balance-of-payment needs. With the present outbreak severely affecting exports, current account deficits, accumulation of debt service arrears and the external financing gap are projected to widen in all three countries (ECA, 2014; UNDP, 2014[2]). The three countries already have high poverty rates, a very low human development index ranking, and weak policy and institutional environments (see table B2). Their overall development outlook is deteriorating day-by-day and the EBOLA outbreak is still claiming lives, severely limiting economic activities and recovery efforts. Our call is not for intermittent debt relief, but for total debt cancellation.

EXTERNAL DEBT SITUATION OF THE EBOLA-AFFECTED COUNTRIES AND THE CASE FOR DEBT CANCELLATION

Since the outbreak, there has been an influx of donor support, both financial and in-kind. Support from international financial institutions to the three countries through, for instance, the Rapid Credit Facility for better emergency response planning and execution, is commendable (IMF, 2014).[3]

1 UNECA (2014) Socio-Economic Impacts of the Ebola Virus Disease on Africa, Addis Ababa, Ethiopia.

2 UNDP (2014). UNDP Africa Policy Note, Vol. 1, No. 3, 24 (October).

3 IMF (2014). Third Review Under the Extended Credit Facility Arrangement and Request for Waiver of Nonobservance of Performance Criteria and Modification of Performance Criterion, IMF Country Report for Liberia, No. 14/197,

TABLE B1: EXTERNAL DEBT AND DEBT RATIOS FOR THE THREE COUNTRIES HARDEST HIT BY EBOLA, 2013

Variable	Guinea	Liberia	Sierra Leone
Debt (Current US$)	1.2 billion	541.5 million	1.4 billion
Debt/GNI (%)	20.9	30.9	31.1
Debt/Exports (%)	190	320	180

Source: IMF and World Bank database accessed in January 2015. Note that debt to exports ratio is not available for 2013 due to lack of data on exports. Hence, the table includes the five-yearly averages prior to 2013 for Guinea and Sierra Leone but the same average can only be computed prior to 2012 for Liberia.

In November 2014, the World Bank proposed a development policy credit for Guinea amounting to $40 million (Emergency Macroeconomic and Fiscal Support Grant). However, this is a loan with a maturity of 38 years and a 6-year grace period, along with a grant of $10 million from the Crisis Response Window of the Bank. Guinea's overall risk rating is "Substantial", suggesting a potential rise in the risk of debt distress and debt overhang.

The 2013 external debt of Guinea, Liberia and Sierra Leone in current dollars is $1.2 billion, $542 million and $1.4 billion respectively, for a total of $3.1 billion. The external debt burden of the three countries is high relative to their GNI and exports as summarized in table B1. At between 21% to 31%, the external debt burden of the three countries is not a negligible proportion of their GNI, with exports falling far below their debt obligations. In the wake of the EBOLA outbreak, both exports and the capacity to raise revenue via taxes have been severely affected due to the significant slump in economic activities, EBOLA leading to debt distress and strained government budgets.

The above debt ratios clearly indicate the limited capacity of the three countries to repay their debts, resulting in a debt overhang problem (Moses and Oladeji, 2014[4]; Nissanke, 2013[5]). The debt burden and macroeconomic situation of the three countries mean that they remain vulnerable to external shocks. The decline in exports following the EBOLA outbreak is likely to be deepened by the recent sharp decline in commodity prices, because of the heavy reliance of the three on resource exports. In this regard, major creditors such as the World Bank and IMF recognize that the countries, particularly Guinea, face varying but intensifying risks of debt distress.[6] In conjunction with declining growth, exports and government revenue, these distress levels are likely to rise with continuous debt servicing and the pressure to settle previous debt service arrears.

External debt cancellation[7] would give the three countries breathing space to better address the short-term economic and social challenges of the EBOLA outbreak and to plan their long-term recovery on a solid footing. It should be recognized that the

Washington, D.C. These measures include the Heavily Indebted Poor Countries (HIPC) initiative and the Multilateral Debt Relief Initiative (MDRI).

4 Moses, E. and S. Oladeji (2014). External Debt, Servicing and Debt Relief Transmissions in Nigeria, Journal of Economics and Sustainable Development, Vol. 5(20):11-33.

5 Nissanke, M. (2013). Managing Sovereign Debt for Productive Investment and Development in Africa: A critical appraisal of the Joint Bank-Fund Debt Sustainability Framework and Its Implications for Sovereign Debt Management, mimeo, School of Oriental and African Studies.

6 IMF (2012). Joint Debt Sustainability Analysis under the Debt Sustainability Framework for low-income countries, prepared by the staff of the World Bank and IMF, Washington D.C. IMF (2014) Requests for Disbursement under the Rapid Credit Facility (RCF) and for modification of performance criteria under Extended Credit Facility Arrangement, IMF Country Report No. 14/298.

7 Lenders to the three countries include all bilateral and multilateral lenders such as the World Bank, IMF and AfDB.

cancellation of debt does not automatically lead to the availability of funds. However, the financial resources earmarked for debt repayments could instead be invested into the countries' health-care systems, including training of health professionals, equipping health centres and ensuring the fair distribution of health personnel between rural and urban areas. These funds could also be used to benefit other strategic sectors of their economies that have been hit hard by EBOLA, including education, agriculture and food security, and services.[8] The impact of EBOLA on agriculture and food security has been particularly serious given that the outbreak started in rural agricultural areas just as farmers were preparing to start sowing. In this regard, financial resources freed up by debt cancellation could be channeled into short-term emergency food relief programmes. In the medium term, the three countries will need food imports from neighbouring countries, as the food currently being provided by WFP is not necessarily the same as the customary diet of people in the affected countries. In the long term, the funds from debt relief could be directed towards agricultural policies that support farmers through micro financing and the marketing of agricultural produce. Debt cancellation would undoubtedly provide more fiscal space for the three countries to achieve their social development goals in the context of the post-2015 development agenda, boosting their growth and recovery prospects.

Until the outbreak of EBOLA, the countries were making encouraging economic and social progress and notable post-conflict recovery. However, if the current level of fiscal distress continues into 2015, growth will suffer even more, which in turn will deepen poverty and weaken their recovery. Indeed, the investment potential of the three countries has already been weakened and growth continues to be revised downwards by forecasters (ECA, 2014; World Bank, 2014[9]). Continued high external debt and debt servicing burdens are likely to discourage future investment in key social sectors such as health and education.

RECOMMENDATIONS FOR POST-DEBT CANCELLATION MEASURES

The three countries need to make effective use of the funds that would be freed up to contain the Ebola outbreak and to finance long-term social and economic development initiatives. The EBOLA outbreak is a public health crisis as well as a humanitarian one. Evidence shows that past debt relief through the HIPC initiative did help many African countries to improve spending on social sectors such as health, supporting the call for cancelling the debts of the three most EBOLA-affected countries (Temah, 2009[10]). Any funds from the debt cancellation should be targeted at strengthening the weak national health systems of the three countries, improving sanitation, establishing social protection programmes, improving education, and securing access to food for those living in rural areas, many of whom have been badly affected by the outbreak. Creditors could establish mechanisms for the effective monitoring of the use of funds after debt cancellation.

Budget reallocations need to focus on upgrading existing social services and health systems to the level required by international protocols (for instance, WHO standards) and to purchase and stock Ebola virus disease vaccines when developed. The immediate priority is to use the fiscal space created by stopping debt repayments to mitigate the adverse effects of EBOLA, including a significant rise in the allocation of funds for long-neglected health infrastructure, training of health personnel at all levels and timely payment of the salaries of health-care sector workers.

As countries emerging from conflict, Guinea, Liberia and Sierra Leone continue to suffer from weak institutional capacities for policy implementation and public sector management (see their CPIA index, table B2). This calls for additional support

8 ECA (2014). Socioeconomic Impacts of the Ebola Virus Disease on Africa, Addis Ababa.

9 World Bank (2014) The Economic Impact of the 2014 Ebola Epidemic, Short- and Medium-term Estimates for West Africa, Washington D.C.

10 Temah, C. (2009) Does Debt Relief Increase Public Health Expenditure? Evidence from Sub-Saharan African Countries, mimeo, Addis Ababa, Ethiopia.

from donors for the three countries to effectively use the policy space provided by debt cancellation to strengthen public financial management systems to ensure sound macroeconomic management, prudent fiscal policies and debt management.

It should be noted that debt cancellation should not lead to lack of confidence about the viability and credit worthiness of the three countries for future lending by creditors. Development partners, especially international financial institutions, should promote special lending initiatives and support for the three countries to access external loans with a significant grant element (for instance, 100% grant for $60 million by AfDB), long grace periods and very low or near zero interest on the amount borrowed. As in the case of Haiti, post-catastrophe debt relief in the form of debt cancellation must be provided for these three West African countries, which continue to feel the effects of a catastrophic disaster that is yet to be contained.

TABLE B2: RECENT ECONOMIC, SOCIAL DEVELOPMENT & POLICY PERFORMANCE INDICATORS (2014)

Variable	Guinea	Liberia	Sierra Leone
Population (in mill.)	12.0	4.4	6.2
Per capita income (US$)	460.0	454.0	679.0
Poverty rate (head count rate)	55.2%	64.0%	52.9%
HDI ranking*	179/187	175/187	183/187
CPIA score	3.1	3.0	3.3

Source: Except for the HDI figures which came from UNDP, all data is obtained from the World Bank.

* All of the three countries are in the bottom of the list of countries classified by UNDP as countries with HDI characterized by 'low human development' (UNDP, 2014).

All figures are for 2014 except CPIA that are for 2013.