Debt Management Responses during the Pandemic

AUGUST 2020
Summary

- Immediate Financing Needs and Coordination
- Emergency Facilities
- Primary and Secondary Market
- Sound Debt Management Practices
- Debt Management Issues in Asia-Pacific
Immediate Liquidity and Financing Needs

Background

- Significantly increased financing requirements that debt managers have to fulfill
- Deterioration in market conditions = increased rollover risk and difficulties in meeting larger foreign debt service payments
- For countries without market financing, access to emergency facilities necessary

What can debt managers do?

- Significant COVID-19 changes are a trigger for revising Debt Management Strategy and Annual Borrowing Plan
- Enhanced market communication and consultation essential
- Step-change in immediate financing needs will necessitate increase in financing where there is liquidity available
- Where possible, debt managers can engage in cash-neutral Liability Management Operations (LMOs) to push out redemptions
- May be a trigger for using cash buffers – but requires careful evaluation
Institutional Coordination

Communication between debt management, monetary, fiscal, and regulatory authorities critical

Debt managers may also be required to assume new responsibilities – e.g. where there are government interventions, including guarantee schemes
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Emergency Facilities (US$65bn, over 70 countries)\(^1\)

- Rapid Credit Facility (RCF)
- Rapid Financing Instrument (RFI)
- Catastrophe Containment and Relief Trust (CCRT)

\(^1\)As at August 19, 2020 including CCRT.
G20 Debt Service Suspension Initiative (DSSI)

- The initiative is also supported by the Paris Club, Kuwait, and the UAE.
- Covers all IDA-eligible and UN Least Developed Country (LDC) countries that are current on their debt service to the IMF and World Bank.
- Commitment to reprofile all principal and interest coming due between May 1 and December 31, 2020 from borrowers that request it.
- Paris Club MoU covers terms and conditions in more detail.
- Commercial creditors are called upon to participate working through the IIF.
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Primary Market

Front Office: Executing Funding Changes

• Borrowing programs will need substantial revision

• Increased communication and consultation with market participants, including PDs, will be critical

• Need to align issuance with market demand:
  o Likely rebalancing to shorter-maturity issuance (e.g. T-bills) or use of other instruments, including bilateral loans
  o Increased flexibility in issuance calendar (less pre-commitment or notice)
  o Increased diversity of issuance mechanisms: taps/tenders/syndications/shop windows
Primary Market

Middle and Back Office: Increased Monitoring of Debt Servicing and Investor Base

• Important to step up monitoring of debt servicing – including FX interest payments.

• Time to take any opportunities to improve debt-cash integration given liquidity constraints.

• Improve monitoring of investor base, with a focus on non-resident investors.

• Investor Relations – increased outreach, move to regular production of debt reports/improvements in communications via website – required to maintain and support market access.

• *Important to monitor existing and potential new contingent liabilities and risk transfer to investors.*
Secondary Market

Addressing Market Dislocation

• Debt managers should use existing (and new) market management tools to address market dislocation:
  o Exchanges may be preferred to buy-backs given liquidity pressures.
  o Use and modification of securities lending facilities (less penal, wider eligibility).
  o Cash buffers should be used cautiously, supporting market functioning.

• Use of market management tools should be well communicated to market participants, and clearly distinguished from funding operations.

• Collaboration with central banks and regulatory authorities critical.
A Brief Recap

• Address immediate liquidity risks
• Coordinate within government
• Consult with external stakeholders
• Revise the Debt Management Strategy and Borrowing Plan
• Use market management tools where possible
• Enhance risk monitoring
• Communicate proactively
• Be responsive and adapt plans as appropriate
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Returning to Sound Debt Management Practices

The New Normal in Debt Management

• Post-crisis there will be a need to unwind interventions that have been a departure from sound practices.

• Debt managers will want to undertake an evaluation of risks that crystalized during the crisis, and assess the adequacy of the debt management response.

• Going forward, debt managers will need to re-assess existing debt management strategies over the medium term, taking into account larger debt portfolios where the cost-risk profile will have altered significantly.
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Growing Recourse to Emergency Financing from IFIs amidst Rising Risk to Debt Distress in LICs

Emergency Financing from IMF partially bridged the financing gap

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Half of the LICs in Asia-Pacific are now at high risk of external debt distress

Source: IMF

Risk of External Debt Distress in LICs
(number of countries)

- Low: 6
- Moderate: 4
- High: 11

Source: IMF
Deterioration in Sovereign Risk and Financial Conditions locked out some EMDEs from the International Market

Asia-Pacific sovereigns downgraded - but to a lesser degree

Bond yields for sub-investment grade sovereigns widened significantly

Asian sovereigns relied less on international bond financing

Emerging Market Ratings Downgrades (percent of rated countries)

Emerging Market Sovereign Bond Yields (percent)

Sovereign Bond Issuance by EMDEs (US$ billion)

Sources: Bloomberg LLP; and IMF staff estimates and calculations.

Source: IMF
Domestic Bond Market Briefly Affected in Asian EMs by Global Turmoil

Bond yield volatility experienced in March-April 2020 normalized.

Bond market liquidity restored after brief market turbulence

Source: ADB Bonds Online
Investor Confidence in Local Currency Bond Market Restored by Monetary Accommodation Policies

Exit of foreign investment from EMs reversed but lower than previous level

Unconventional monetary policies helped stabilize bond market volatility

Central Bank Purchase of G-secs during March-June 2020 (percent of GDP)

Sources: Bloomberg Finance L.P.; JP Morgan; and IMF staff calculations
Bond Market Stability Provided Greater Financing from Domestic Market

Bond issuance picked up in the second quarter of 2020

Local currency bond financed (net) around 5 percent of GDP in H1: 2020

Quarterly Local Currency Bond Issuance (US$ billion)

Source: ADB Bonds Online

Stock of Local Currency Bond (percent of GDP)

Source: ADB Bonds Online
Maturity Structure of Local Currency Bonds Maintained in some EMs towards Long-term Securities

Source: ADB Bonds Online

Source: ADB Bonds Online
Debt Management Response in EM-Asia

- Increased short-term borrowings (Philippines and Thailand)
- Increased international sovereign bond issuance (Indonesia)
- WMA limit (India)
- Primary market purchase (Indonesia)
- Secondary market purchase by CB
- Flexibility in CB repos
- MF liquidity (Thailand)

- Duration neutral LMO to retire illiquid bonds (India)
- Cash neutral LMO (Thailand)
- Increased NC bids and window (South Korea)
- Allocate more than offered Competitive bids (Indonesia)
- Use of Private Placements (Indonesia, Malaysia)

Issuance Strategy

Issuance Mechanism

Liability Management Operations

Monetary Support
Thank You