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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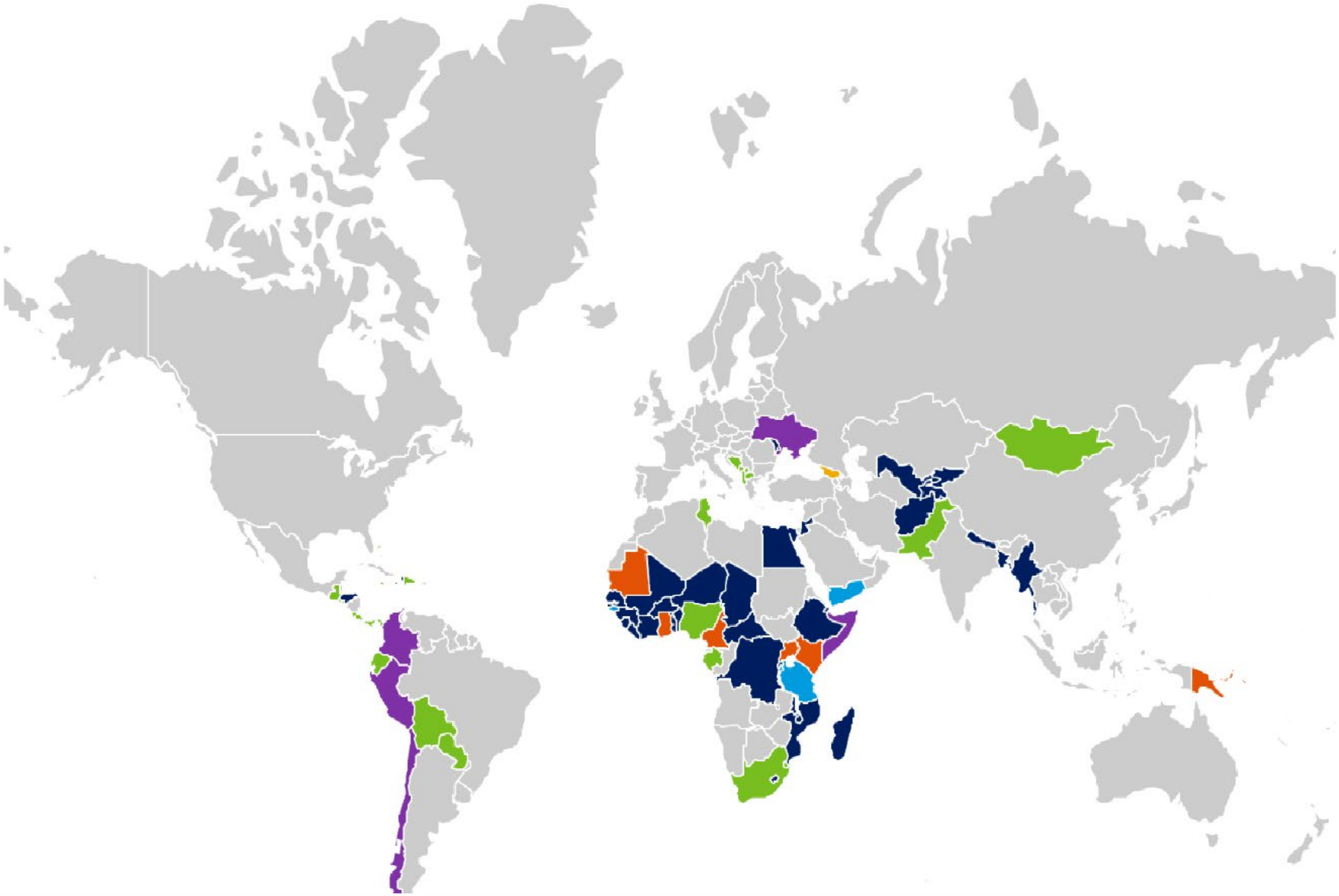
Emergency Facilities (US$65bn, over 70 countries)[1]

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



[1]As at August19, 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:
  - Likely rebalancing to shorter-maturity issuance (e.g. T-bills) or use of other instruments, including bilateral loans
  - Increased flexibility in issuance calendar (less pre-commitment or notice)
  - 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:
  - Exchanges may be preferred to buy-backs given liquidity pressures.
  - Use and modification of securities lending facilities (less penal, wider eligibility).
  - 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

<u>The New Normal in Debt Management</u>

- 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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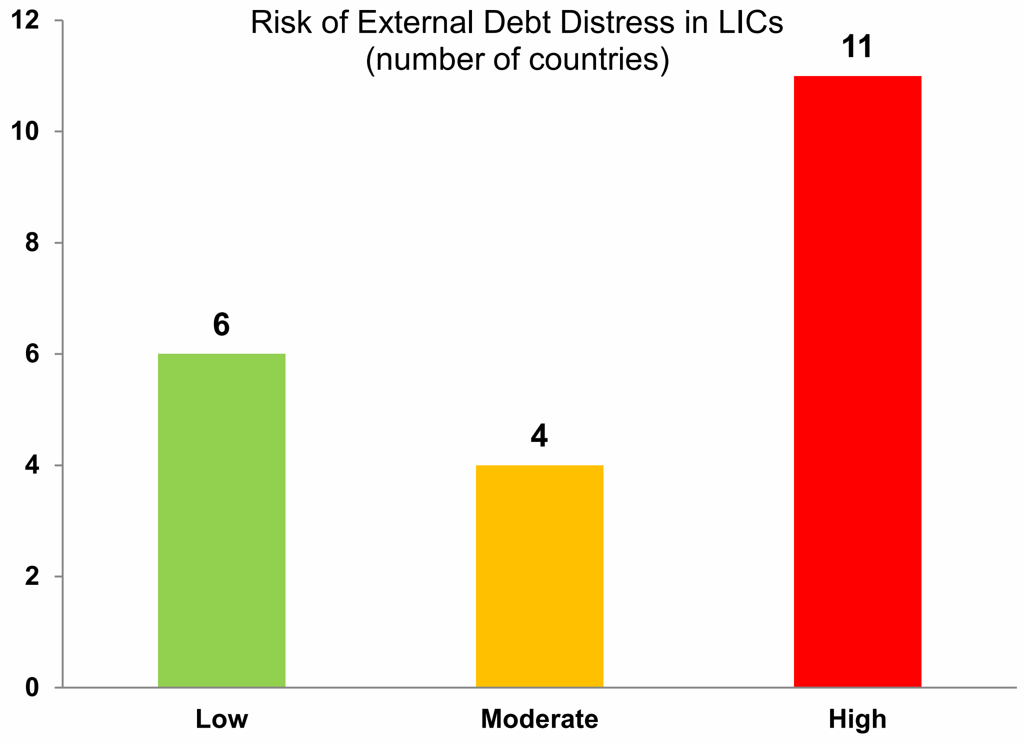
Growing Recourse to Emergency Financing from IFIs amidst Rising Risk to Debt Distress in LICs

Emergency Financing from IMF partially bridged the financing gap

	CCRT	DSSI	RCI/RCF
Afghanistan	x	x	x
Bangladesh			x
Maldives		x	x
Mongolia			x
Myanmar		x	x
Nepal	x	x	x
Papua New Guinea		x	x
Pakistan		x	x
Samoa		x	x
Solomon Islands			x
Tonga		x	

Source: IMF

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

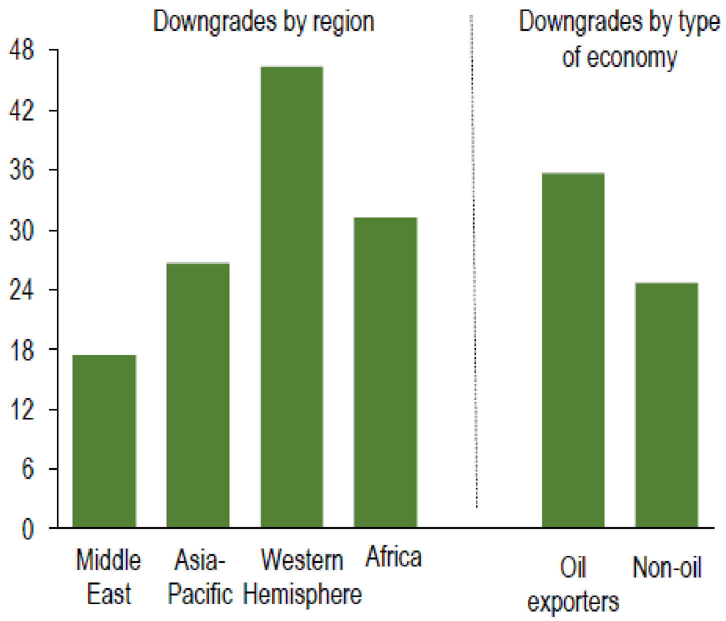


Source: IMF

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

Asia-Pacific sovereigns downgraded - but to a lesser degree

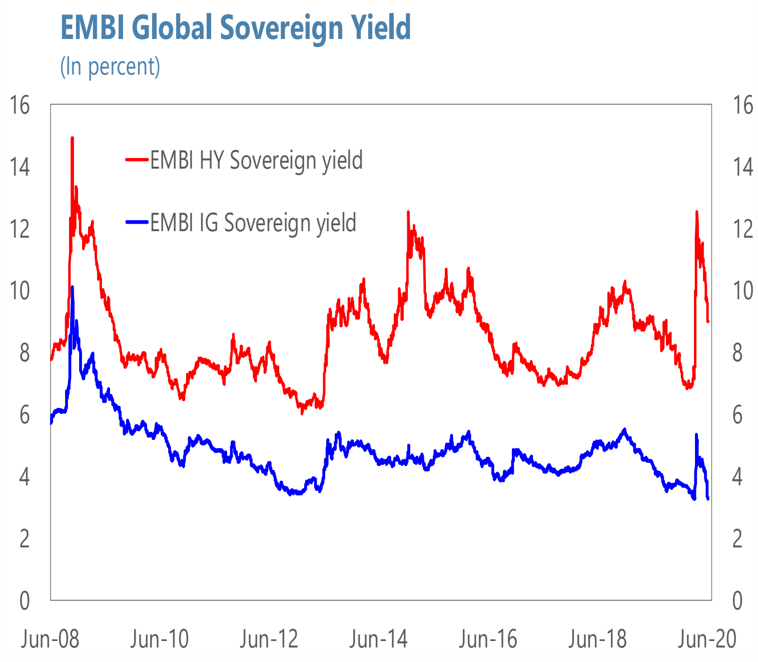
Emerging Market Ratings Downgrades
(percent of rated countries)



Source: IMF

Bond yields for sub-investment grade sovereigns widened significantly

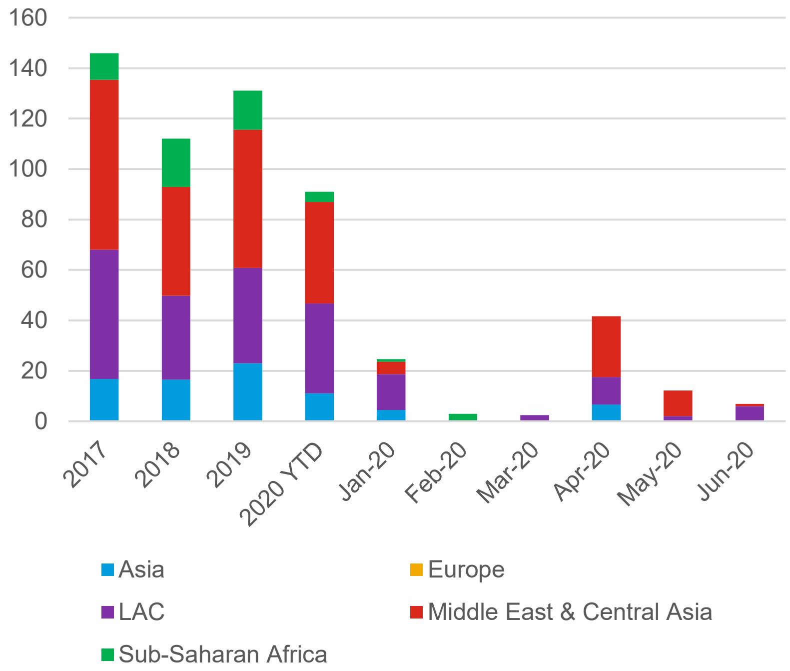
Emerging Market Sovereign Bond Yields
(percent)



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

Asian sovereigns relied less on international bond financing

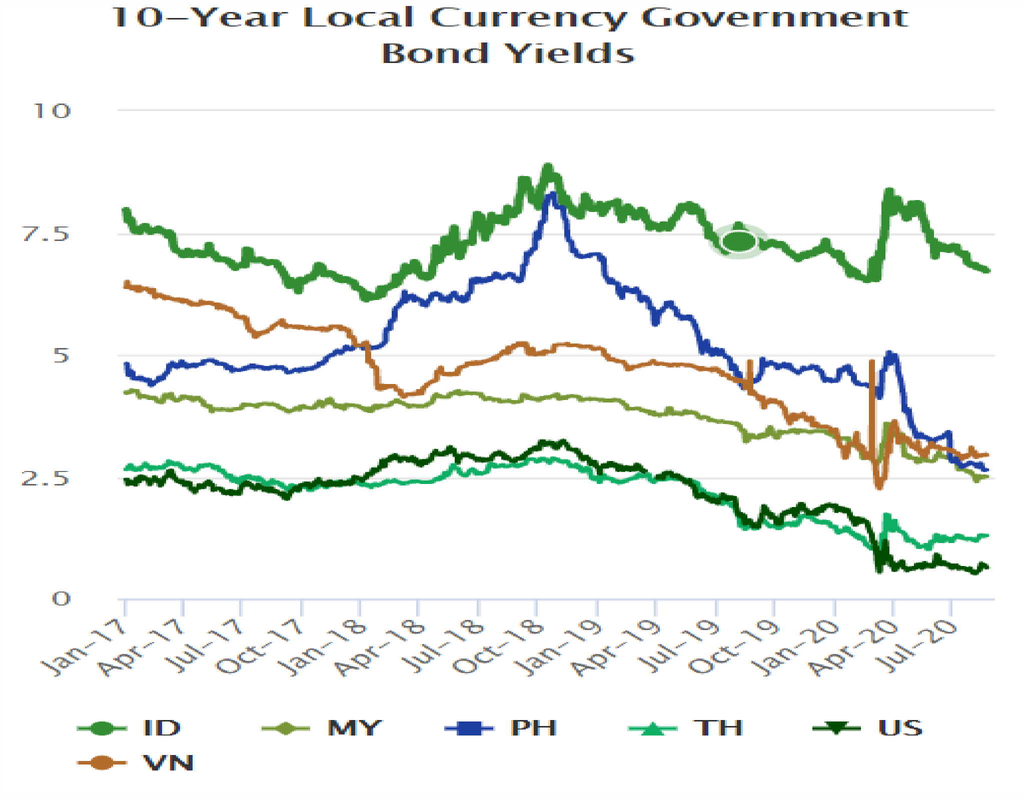
Sovereign Bond Issuance by EMDEs
(US$ billion)



Source: IMF

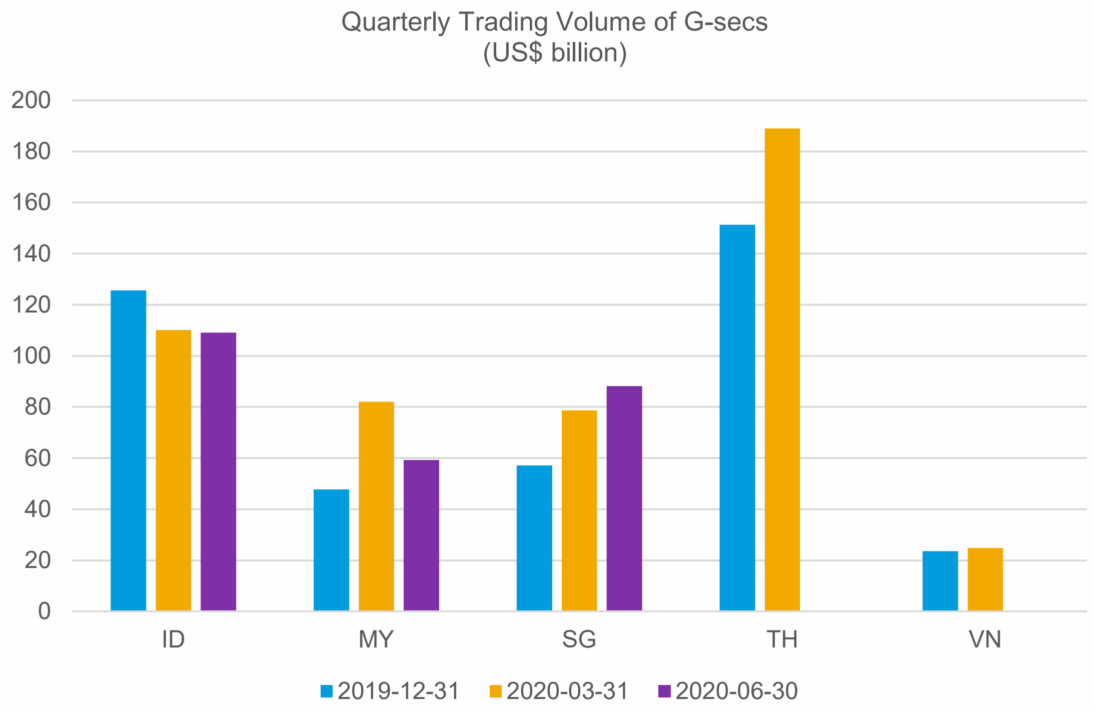
Domestic Bond Market Briefly Affected in Asian EMs by Global Turmoil

Bond yield volatility experienced in March-April 2020 normalized….



Source: ADB Bonds Online

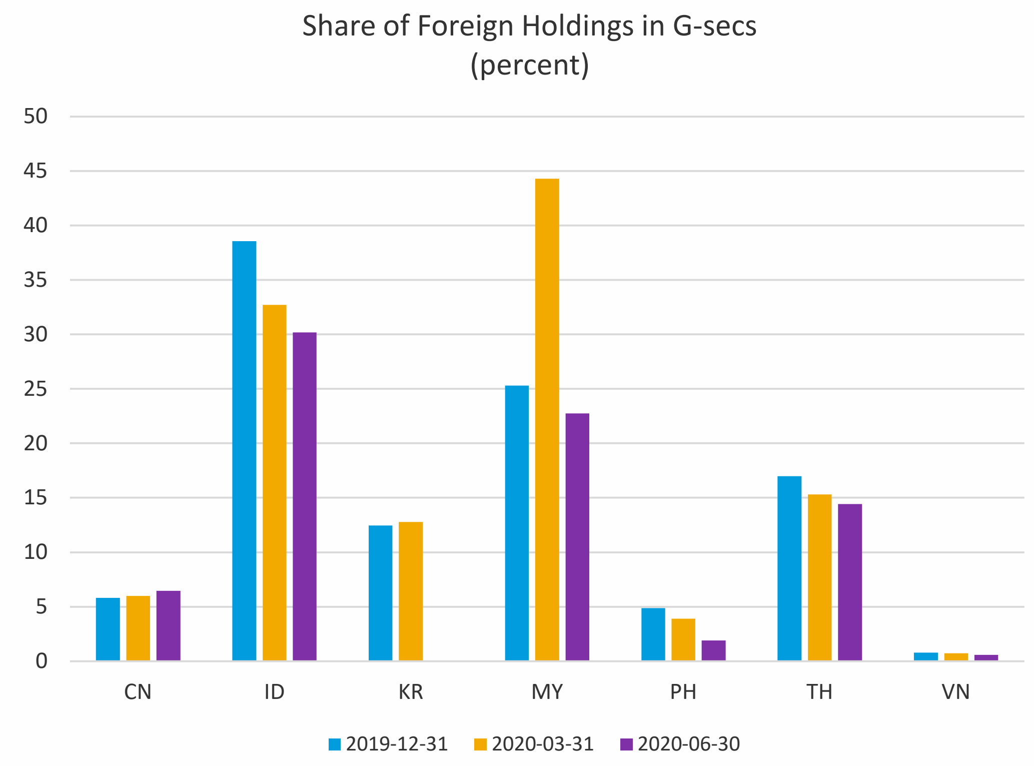
Bond market liquidity restored after brief market turbulence



Source: ADB Bonds Online

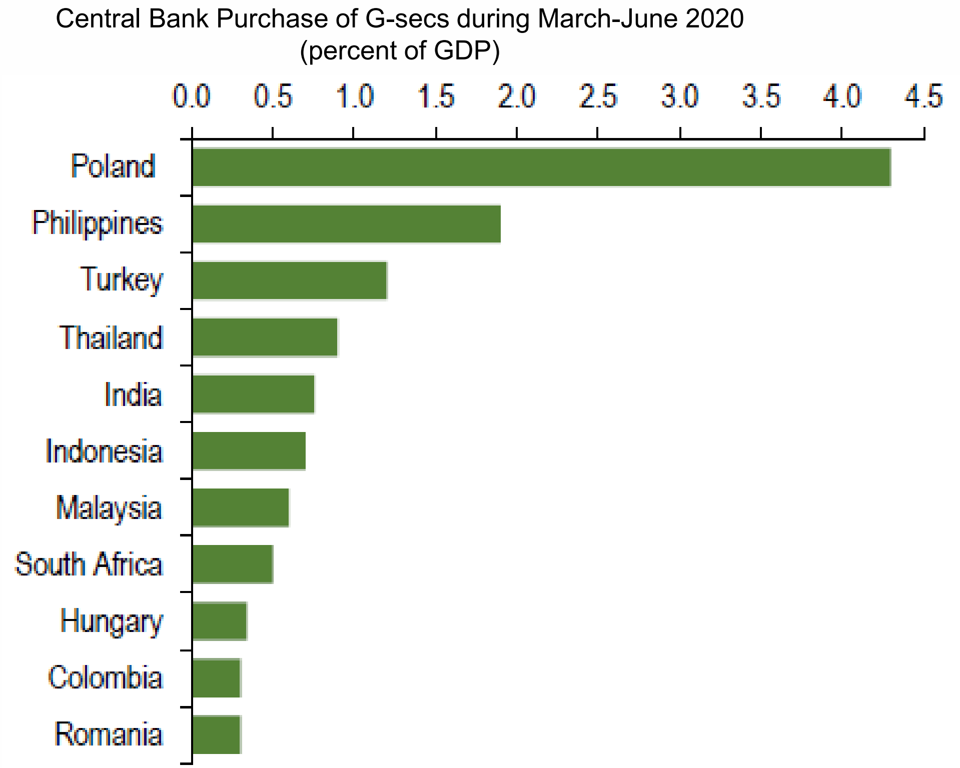
Investor Confidence in Local Currency Bond Market Restored by Monetary Accommodation Policies

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



Source: ADB Bonds Online

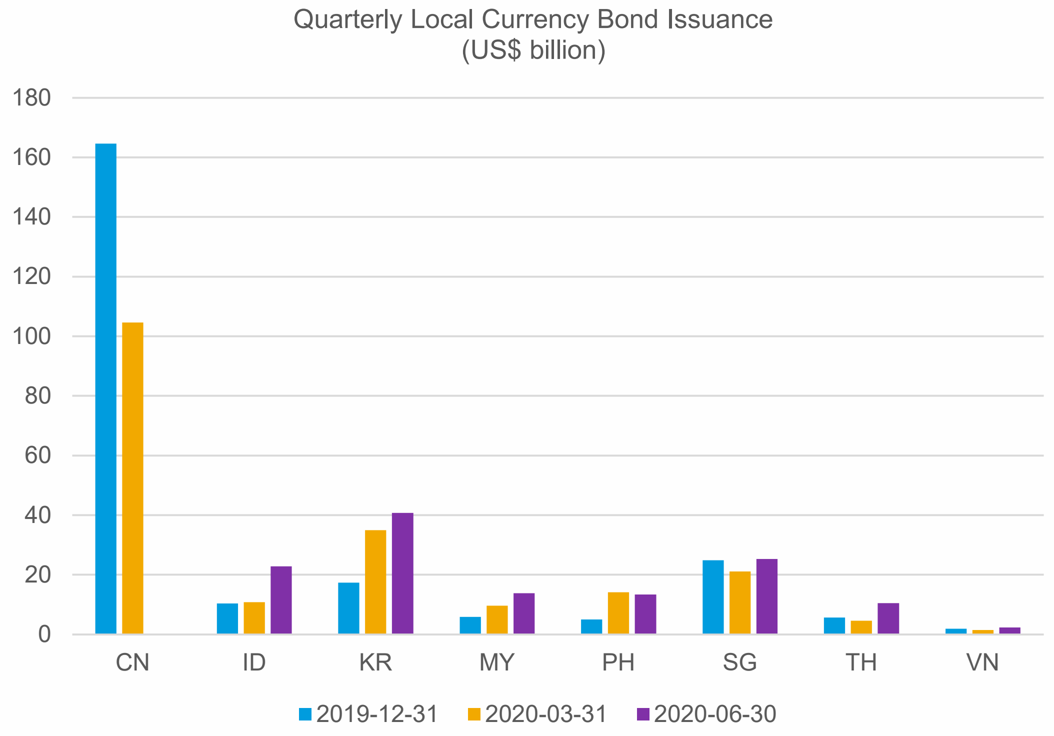
Unconventional monetary policies helped stabilize bond market volatility



Sources: Bloomberg Finance L.P.: JP Morgan; and IMF staff calculations

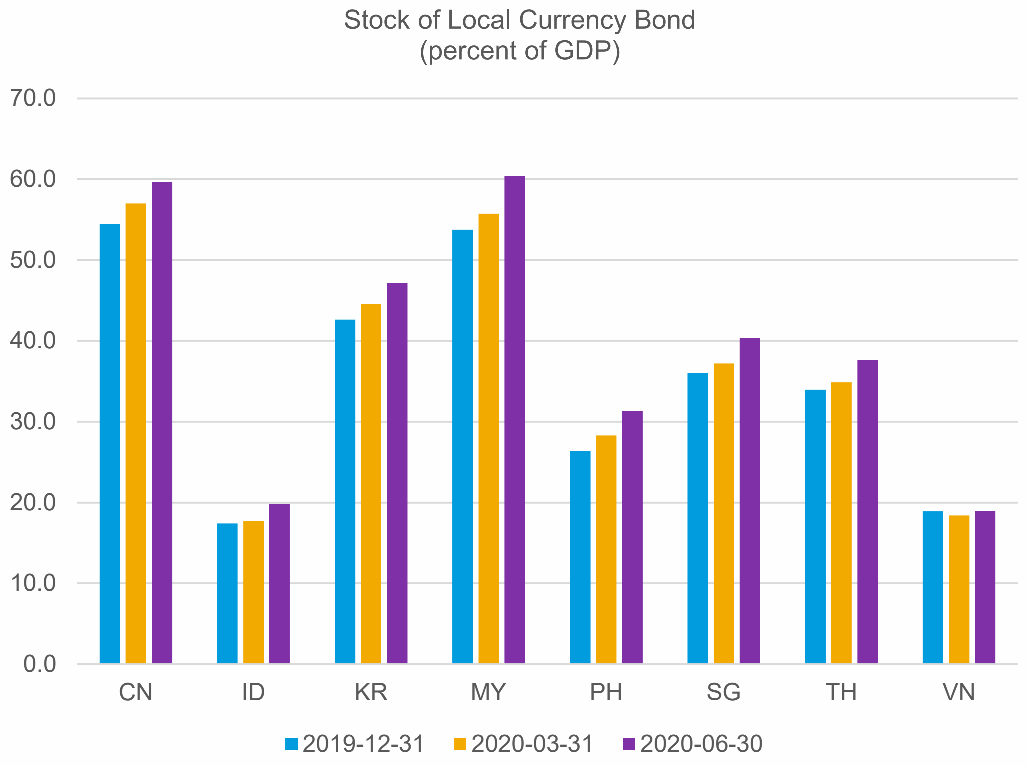
Bond Market Stability Provided Greater Financing from Domestic Market

Bond issuance picked up in the second quarter of 2020



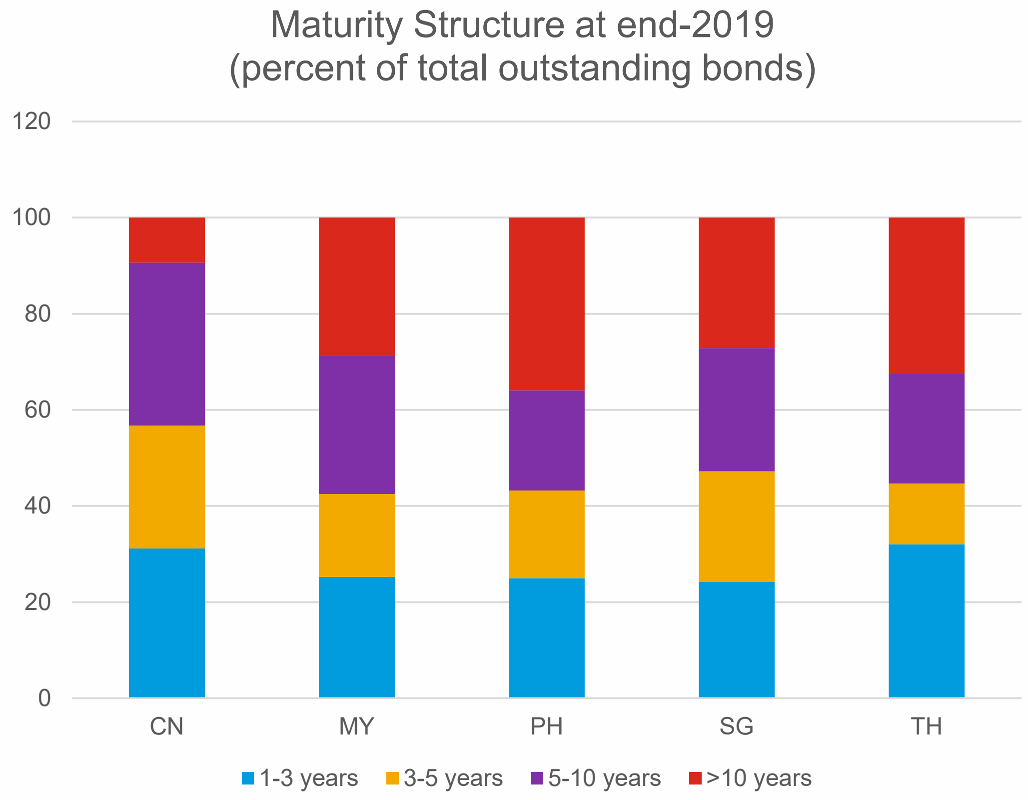
Source: ADB Bonds Online

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

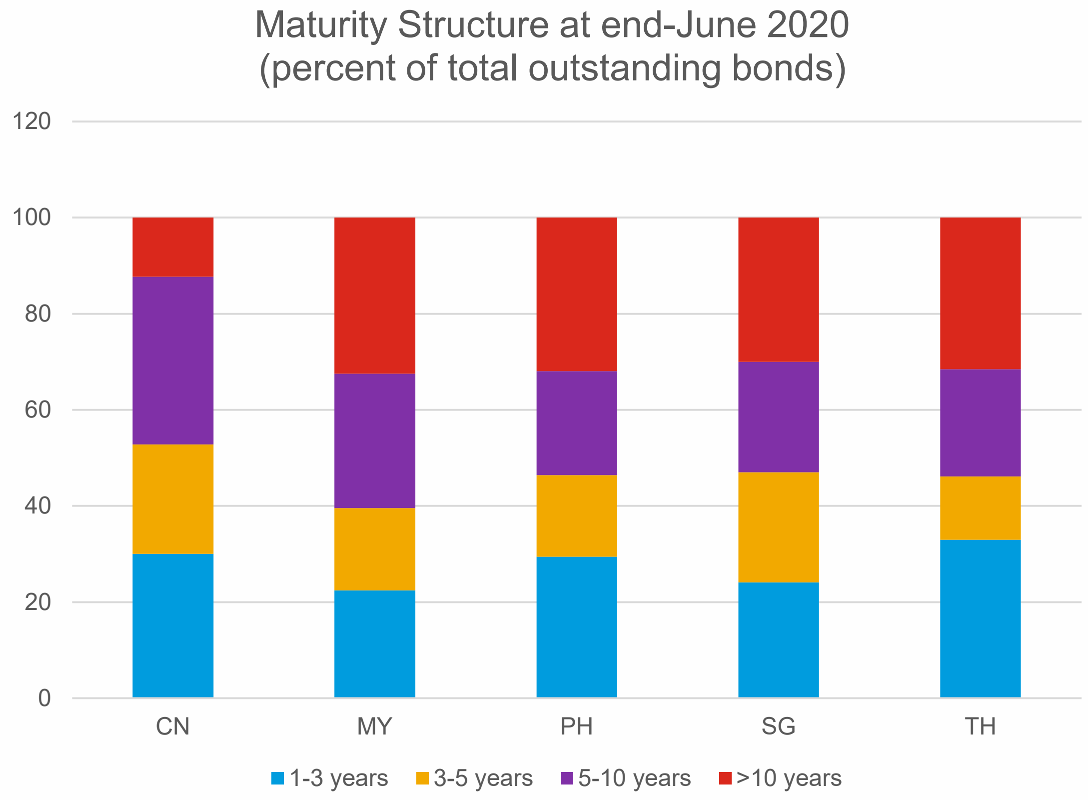


Source: ADB Bonds Online

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)

- Increased NC bids and window (South Korea)
- Allocate more than offered Competitive bids (Indonesia)
- Use of Private Placements (Indonesia, Malaysia)

- Duration neutral LMO to retire illiquid bonds (India)
- Cash neutral LMO (Thailand)

- WMA limit (India)
- Primary market purchase (Indonesia)
- Secondary market purchase by CB
- Flexibility in CB repos
- MF liquidity (Thailand)

Thank You