

External Debt Management

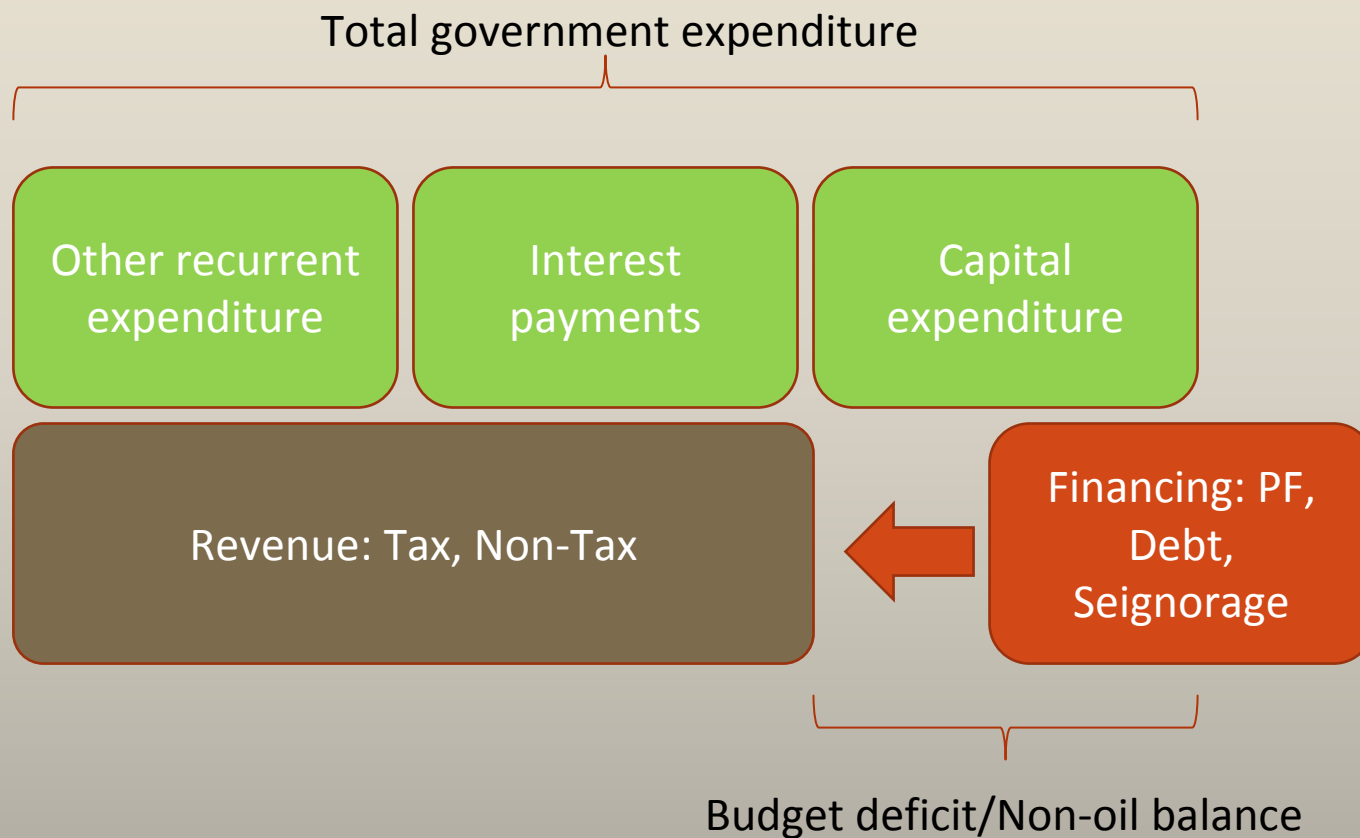
World Bank presentation to the
Comissão de Economia, Finanças e Anti-Corrupção, Parlamento Nacional,
The Democratic Republic of Timor-Leste

Wednesday 21 October, 2009

Overview

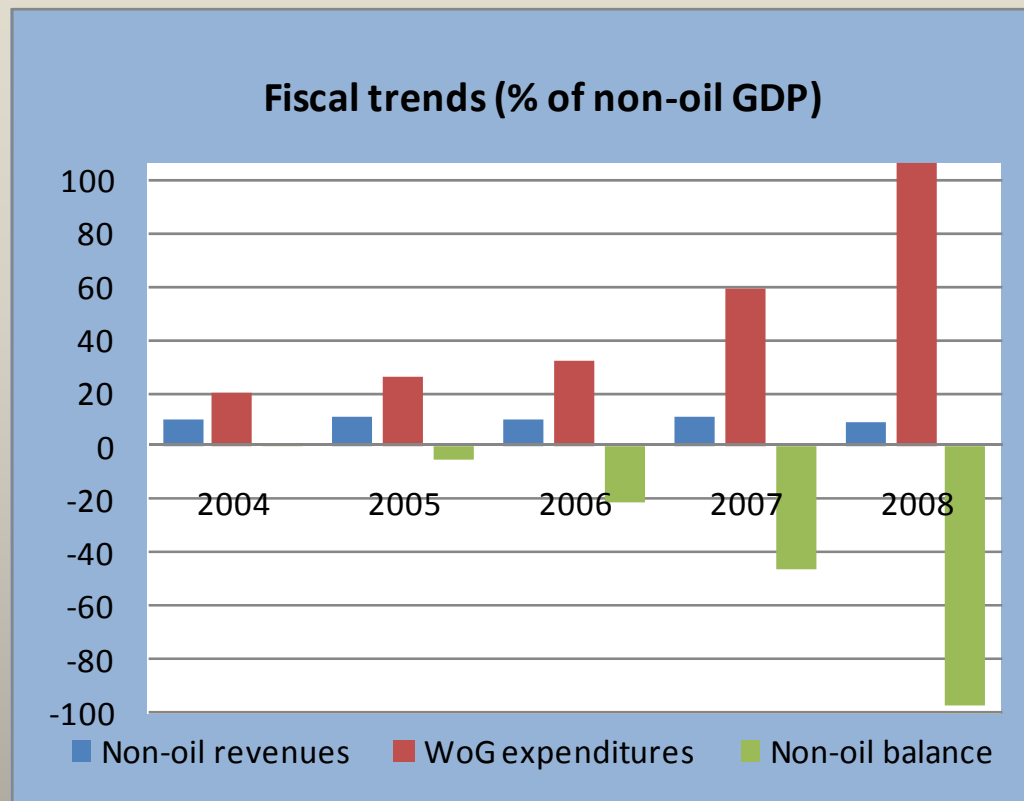
- External loans to finance the budget deficit
 - Government operations
 - Economics of external borrowing
- Managing external debt
 - Governance and strategy
 - Coordination with macroeconomic policies
 - Operational risk management
 - Debt records and reporting
- Experience from other countries
 - Borrowing for public investment
 - Debt relief
 - Small states

Government operations

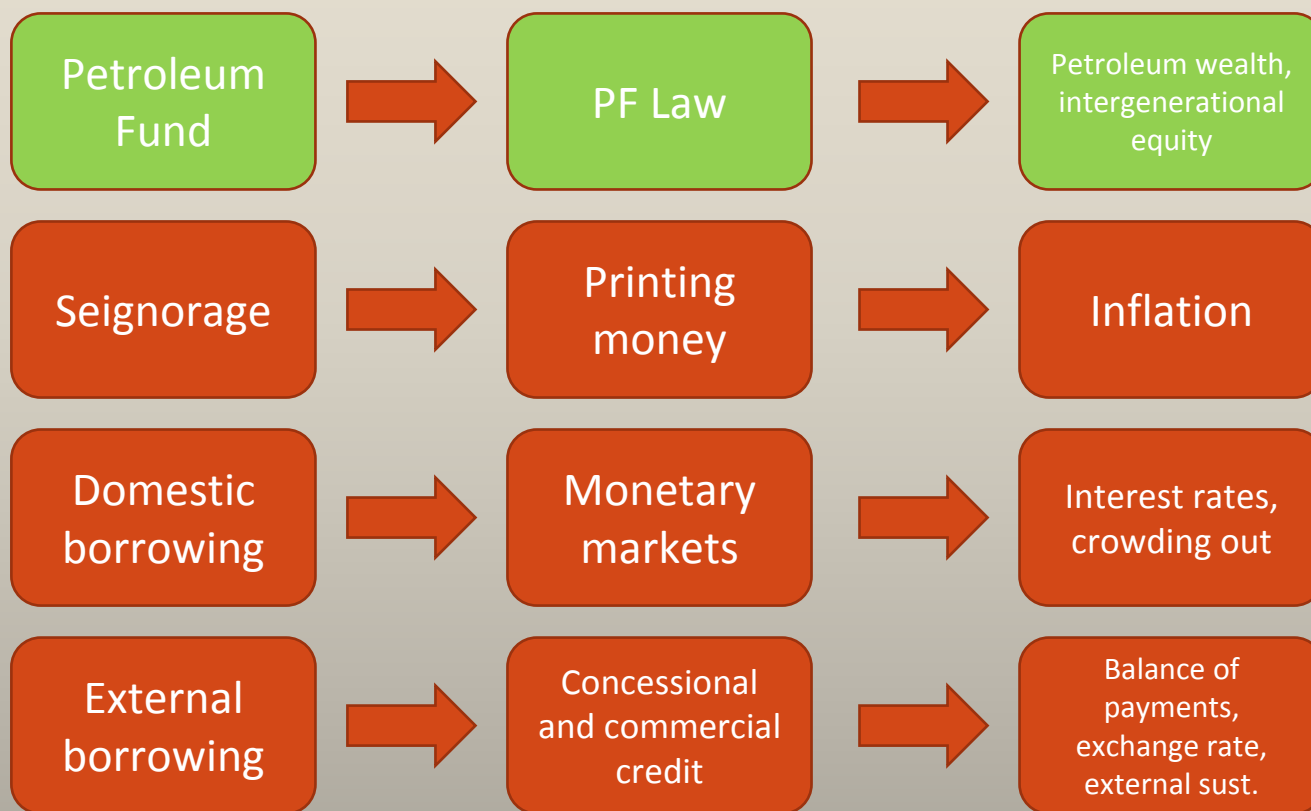


Government operations

Rapid rise in the non-oil fiscal deficit in Timor-Leste...



Government operations



Economics of external borrowing

- Different options for creating fiscal space:
 - Increase in grant aid
 - Improved expenditure efficiency
 - Improved revenue effort
 - New borrowing.
- Borrowing for what purpose:
 - Scaling up public investment.
 - General government expenditure.
- Terms and conditions of external loan:
 - Cost characteristics: concessional or market rate?
 - Risk characteristics: grace, maturity period, fixed vs. variable rate, currency denomination?
 - Benefits and restrictions: tied vs. untied, technical assistance?

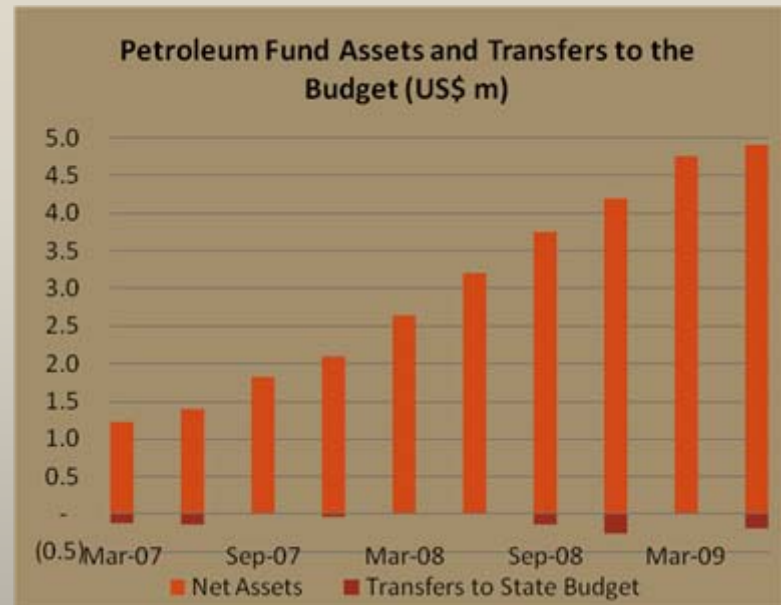
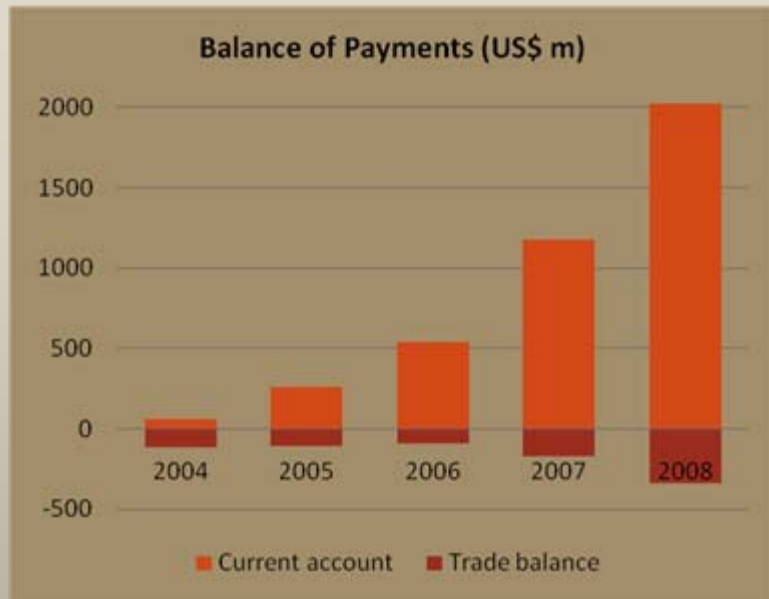
Economics of external borrowing

- **Trade-offs:**
 - Cost of borrowing vs. returns on the Petroleum Fund.
 - Wider macroeconomic impact.
- **Debt sustainability:**
 - Debt thresholds and quality of policies and institutions.

	Institutional strength and quality of policies		
	Weak CPIA<3.25	Medium 3.25<CPIA<3.75	Strong CPIA>3.75
NPV of debt-to-GDP	30	40	50
NPV of debt-to-exports	100	150	200
NPV of debt-to-revenue	200	250	300
Debt service-to-exports	15	20	25
Debt service-to-revenue	25	30	35

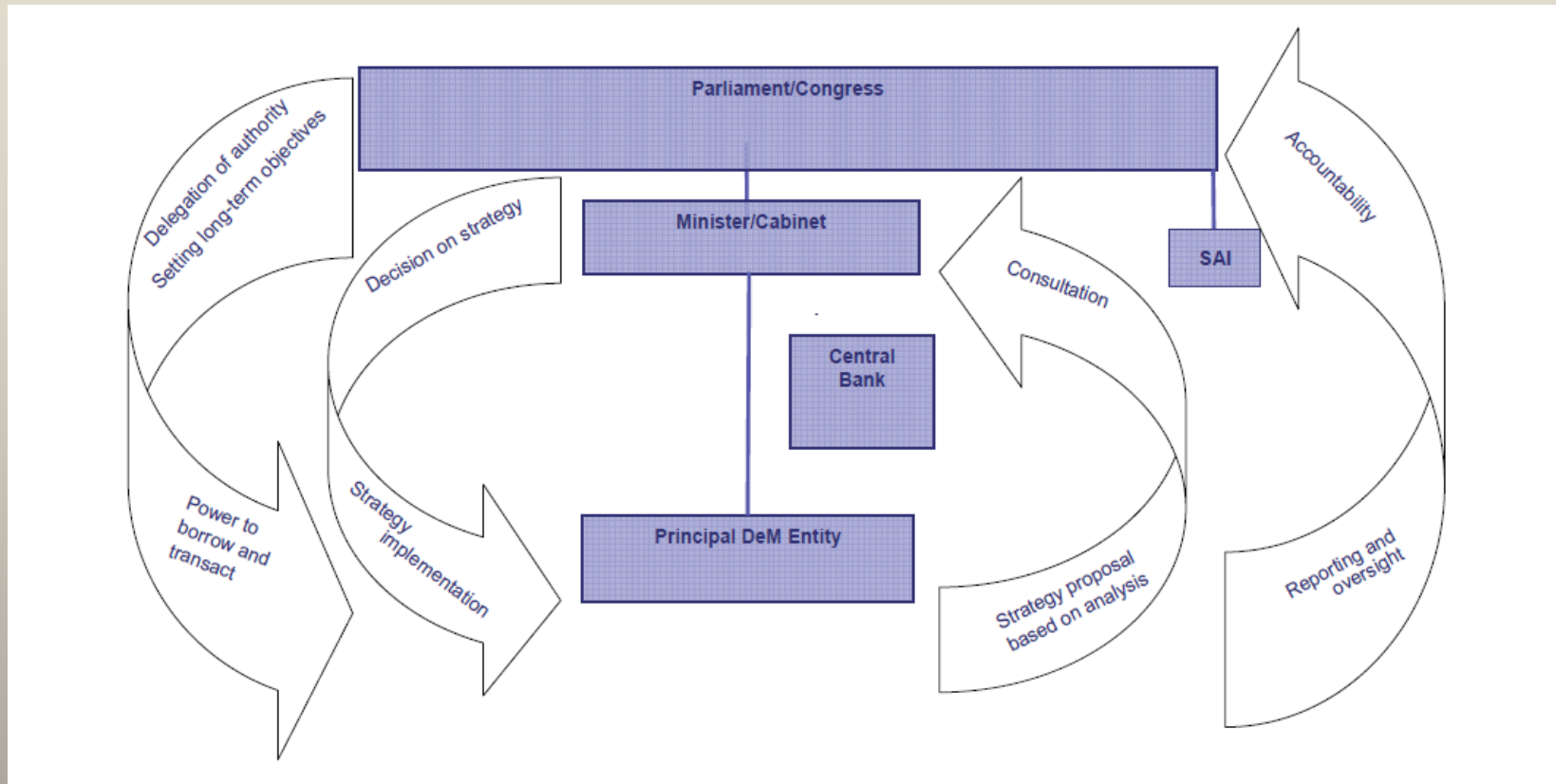
Economics of external borrowing

Timor-Leste has a strong external position ...



Managing external debt

- Governance and Debt Management Strategy:



Managing external debt

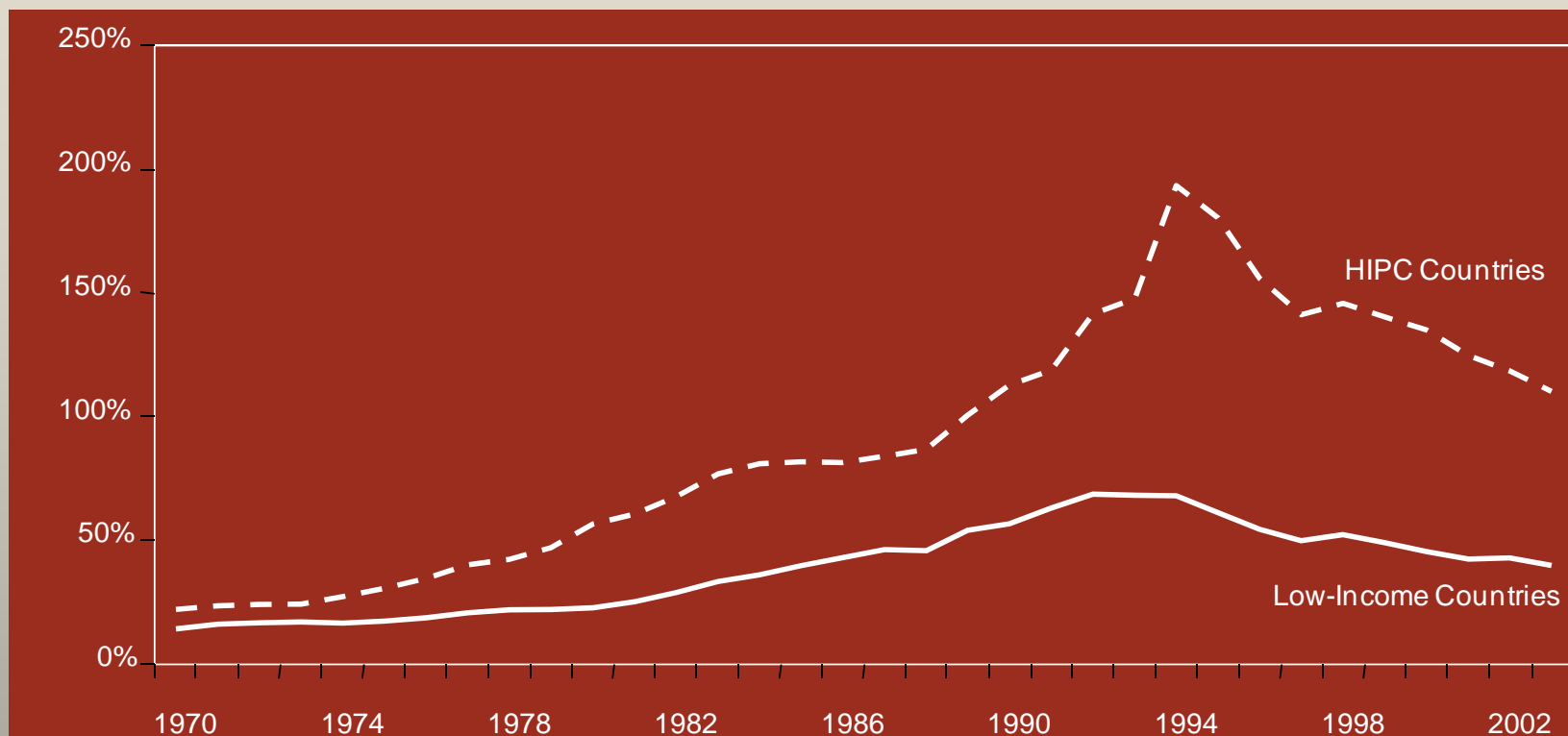
- Coordination with macroeconomic policies:
 - Fiscal.
 - Monetary.
 - Exchange rate policies.
- Operational risk management:
 - Debt administration and data security.
 - Segregation of duties, staff capacity, and business continuity.
 - Debt records and reporting:
 - Debt records.
 - Debt reporting.

Borrowing for public investment

- Impact of debt-financed investment on economic growth is a function of several factors including:
 - Quality of public investment.
 - Composition of public expenditure.
 - Crowding-in effect of public investment.
 - Existing stock of physical capital.
 - Effectiveness of public administration.

Debt relief

Dramatic rise in the debt burdens in some Low Income Countries from 1973 to 1993 (% of external debt/GDP in NPV terms)...



Source: World Bank

Small states

- High government expenditure in small states
 - Remoteness and limited economies of scale.
 - Lack of diversification and vulnerability to shocks.
 - Open economy and exposure to changes in international prices.
 - Volatility in government revenue and expenditure.
- Increased recourse to external debt:
 - Rise in external debt for small states.

Conclusion

- Assess options for creating fiscal space and financing the budget deficit, ensuring quality of expenditure.
- Develop governance and strategic framework for debt management including coordination with macro policies, operational risk management, and transparency.
- Regular monitor evolution of external debt burden to ensure sustainability.