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It contains a series of essays that were initially presented in several workshops held at the height of the pandemic, in 2020.

These essays seek to both understand the debt challenges facing these countries and to offer some policy-oriented suggestions on how they can more effectively address these. They include contributions by global and regional scholars who are seasoned experts and newer researchers and discuss the complexities on debt management and restructuring within the context of the global COVID-19 pandemic. In particular, this presented an opportunity for junior researchers from the region to contribute to international discussions on a topic in which the views of young Africans are not heard as often or as clearly as they should be, especially given the importance of the topic to Africa and its future. Further, this book is expected to stimulate debate among academics, activists, policy makers and practitioners on how SADC should manage its debt.

Pretoria University Law Press
PULP
www.pulp.up.ac.za

ISBN: 978-1-991213-08-2

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THE CASE OF SADC

BRADLOW
AND MASAMBA

PULP

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Edited by **Daniel D. Bradlow**
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Published by:
Pretoria University Law Press (PULP)
The Pretoria University Law Press (PULP) is a publisher at the Faculty of Law, University of Pretoria, South Africa. PULP endeavours to publish and make available innovative, high-quality scholarly texts on law in Africa. PULP also publishes a series of collections of legal documents related to public law in Africa, as well as text books from African countries other than South Africa. This book was peer reviewed prior to publication.

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Printed and bound by:
Pinetown Printers, South Africa

To order, contact:
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Cover design:
Octavia Roodt, Centre for Human Rights, Faculty of Law, University of Pretoria

ISBN: 978-1-991213-08-2

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Acknowledgments

This project has been made possible through collaborations with various individuals and stakeholders, to whom we owe a debt of gratitude.

Firstly, this project would not have been possible without the generous funding of the Open Society Initiative for Southern Africa (OSISA), which is dedicated to deepening democracy, protecting human rights and enhancing good governance in the region.

We would like to thank all the participants that took part in a series of online workshops held in 2020, where authors presented their firs drafts of their chapters.

We owe a debt of gratitude to the following people who generously gave of their time to review the first drafts of the chapters and provided commentary at the online workshops, Anouj Mehta, Bongi Kunene, Prof Cephas Lumina, Dr. Celine Tan, Dr Cyrus Rustomjee, Prof James Gathii, Dr Juan Pablo Bohoslavsky, Prof. Kenneth Mwenda, and Prof Makane Moïse Mbengue.

We would also like to thank that dedicated staff of the University of Pretoria who have played different roles in making this project a reality. Special thanks to Emily Laubscher, Gustav Muller, Lizette Hermann, Simphiwe Khumalo, Thandeka Rasetsoke and Yolanda Booyzen.

Finally, we would like to thank the anonymous peer reviewers who have taken time to review every chapter in this book and provide their expert feedback.

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1 Sovereign debt management and restructuring in SADC: Setting the scene and asking the right question

Daniel D Bradlow and Magalie L Masamba

1.1 Introduction

The COVID-19 pandemic has resulted in the most serious global health crisis of the past century. Its health impacts include hundreds of millions of people being infected with the COVID-19 virus, many becoming sick and millions dying around the world. It has also had profound and adverse economic impacts including hundreds of millions of people losing their jobs or experiencing declines in their incomes and many businesses being forced to close down or substantially downscale. The unprecedented global lockdowns have also dramatically affected the way in which we work, socialise and travel.

For many African countries, this pandemic is also having other social and economic impacts. It is overwhelming or threatening to overwhelm their already fragile welfare systems and is causing many children to prematurely end their educations. In addition, the pandemic has already adversely affected African intraregional and international trade, investment flows, and access to financing, but its full impact is still unfolding. One indicator of the full effect of the pandemic will be its impact on the ability of African countries to make their scheduled sovereign debt payments over the next few years.

This multi-disciplinary publication focuses on the issue of African sovereign debt management and renegotiation/restructuring, with a particular concentration on the countries that are members of the Southern Africa Development Community (SADC). It contains a series of essays that seek to both understand the debt challenges facing these countries and to offer some policy-oriented suggestions on how they can more effectively address these. The essays were initially presented in several workshops held at the height of the pandemic, in 2020. It also has a subsidiary aim of providing a shared platform for global and regional scholars who are seasoned experts and newer researchers to discuss the complexities on debt management and restructuring within the context of the global COVID-19 pandemic. In particular, this presented an opportunity for junior researchers from the region to develop their expertise and to contribute to international discussions on a topic in which the views of

young Africans are not heard as often or as clearly as they should be, especially given the importance of the topic to Africa and its future.

The purpose of this introductory chapter is to place the issue of sovereign debt management and restructuring in the SADC region in context and to introduce the broad themes of the essays in this book. It begins by briefly providing some historical background to the current debt situation in the SADC region. Thereafter, it describes the current debt situation in the region. The third part raises some questions that the book is seeking to address. Finally, it will provide a brief overview of the chapters in the book.

1.2 Sub-Saharan Africa's debt story: Where we are and how we got here?

Sub-Saharan African countries have had a complex relationship with foreign debt. While they have borrowed from both a range of multilateral and bilateral official creditors and private sector lenders, historically most of their debt has come from official sources. They have experienced challenges meeting their obligations to these creditors and so have participated in a number of initiatives designed to assist debtor countries in difficulty. The most notable of these relief programmes were the Highly Indebted Poor Countries Initiative (HIPC) from 1996-1999 and the Multilateral Debt Relief Initiative (MDRI) in 2005.[1] The HIPC, which was initiated after debtor countries had spent many years following the advice of the international financial institutions such as the International Monetary Fund (IMF) and World Bank, which required participating countries to adopt structural adjustment programmes (SAPs) in order to resolve their mounting debts and broader economic challenges.[2] These institutions maintained that these programmes, despite their harsh social impacts, would help place these countries on more predictable and

1 For an overview of the HIPC relief programmes, see IMF 'Debt relief under the Heavily Indebted Poor Countries (HIPC) initiative' (23 March 2021), https://www.imf.org/en/About/Factsheets/Sheets/2016/08/01/16/11/Debt-Relief-Under-the-Heavily-Indebted-Poor-Countries-Initiative (accessed 19 April 2021). For an analysis of the impact of the relief programmes, see S Isar 'Was the Highly Indebted Poor Country initiative (HIPC) a success?' (2012) 9 *Journal of Sustainable Development* 107, 115; S Mustapha & A Prizzon 'Is debt sustainable in the post-HIPC era? A literature review' Overseas Development Institute (February 2014) 3, https://www.odi.org/sites/odi.org.uk/files/odi-assets/publications-opinion-files/9105.pdf (accessed 19 February 2021).

2 See RM Mohs 'Structural adjustment programmes in sub-Saharan Africa' (1988) 23 *Intereconomics* 25-28, https://www.econstor.eu/bitstream/10419/140111/1/v23-i01-a06-BF02929964.pdf (accessed 20 April 2021); S Ponte 'The World Bank and "adjustment in Africa"' (1995) 22 *Review of African Political Economy* 539-558.

sustainable growth paths. Unfortunately, the programmes did not deliver their claimed benefits. As a result, the international community adopted the HIPC, which aimed to reduce to sustainable levels the debt burdens of those over-indebted poor countries that were willing to comply with the HIPC's conditions. It promised to do so by reducing their bilateral, multilateral and commercial debt. Thus, the HIPC offered countries the possibility of a fresh start. However, the programme had various inadequacies, including slow delivery and limited coverage with respect to a narrow category of countries that were eligible to participate due to what were perceived as high eligibility thresholds.

The HIPC was replaced by the Enhanced HIPC programme (EHIPC) in 1999. The main aim of the EHIPC programme was to provide 'deeper, broader and faster' debt relief.[3] Yet, the EHIPC still had noticeable challenges in providing sufficient and timely debt relief, because as in the case of the HIPC, it only covered bilateral official debts and some commercial debts. It was replaced by the Multilateral Debt Reduction Initiative (MDRI).[4] The MDRI programme was launched in 2005 to supplement the HIPD and EHIPC programmes for eligible HIPC countries, that is, primarily IDA-eligible countries. These countries, upon reaching the HIPC Completion Point,[5] received 100 per cent cancellation of all pre-existing African Development Bank (AfDB), IMF and World Bank debt.[6]

Despite their shortcomings, these debt relief programmes did reduce the debt levels of participating countries. In February 2020, 37 post-completion countries were receiving debt relief, including 29 African countries.[7] Between 2001 and 2015 the debt service paid by countries in

3 UNCTAD 'Debt sustainability: Oasis or mirage?' (2004) 11, https://unctad.org/en/Docs/gdsafrica20041_en.pdf (accessed 20 April 2021).

4 UNCTAD 'Contribution to the implementation of the United Nations New Agenda for the Development of Africa in the 1990s: Activities undertaken by UNCTAD in favour of Africa' Report by the Secretary-General of UNCTAD – Trade and Development Board 29th executive session, Geneva (13 September 2002) 15, https://unctad.org/system/files/official-document/tb29d2.en.pdf (accessed 20 April 2021).

5 Mustapha & Prizzon (n 1) 3.

6 The IMF targeted all debt obtained by the end of 2004 for cancellation (amounting to an estimated US $5 billion in debt cancellation). The World Bank and AfDB cancellations targeted debt obtained up to the end of 2003 (amounting to an estimated US $37 billion and US $8,5 billion respectively). MA Weiss 'The multilateral debt relief initiative' CRS Report for Congress (11 June 2012) 3, https://fas.org/sgp/crs/row/RS22534.pdf (accessed 20 June 2021).

7 The HIPC Post-Completion-Point African countries that have received relief include Benin, Burkina Faso, Burundi, Cameroon, Central African Republic, Chad, Comoros, Republic of Congo, Democratic Republic of the Congo, Ethiopia, The Gambia,

the programme had declined by about 1,5 per cent of their gross domestic product (GDP).[8] Following the HIPC and MDRI, only eight African countries were still seen to be at high risk of debt distress. However, they were not designed to, and did not, provide the beneficiary states with access to adequate levels of new non-debt development finance. Consequently, African countries began to re-accumulate debt in sufficiently large amounts that there were fears that debt levels could return to pre-HIPC levels.[9] Between 2011 and 2019 the sub-Sahara African region more than doubled its debt levels from approximately US $259 billion to US $535 billion (see Table 1 Sub-Sahara Africa External Debt Stock by Creditor Type (billion USD) below).[10] Numerous factors contributed to these increased debt levels, including widening primary deficits and exchange rate depreciation from falling commodity prices.[11]

Table 1: Sub-Sahara Africa External Debt Stock by Creditor Type (billion USD)[12]

External debt stock by creditor type	2011	2015	2019
Public and publicly guaranteed debt	178,705.80	250,651.90	392,037.80
Official creditors	113,507.80	152,126.60	225,183.40
Multilateral	62,603.90	81,249.60	123,615.50

Ghana, Guinea, Guinea-Bissau, Côte d'Ivoire, Liberia, Madagascar, Malawi, Mali, Mauritius, Mozambique, Nicaragua, Niger, Rwanda, Senegal, Sierra Leone, Tanzania, Togo, Uganda and Zambia. Meanwhile Eritrea, Somalia and Sudan are at pre-Decision point. IMF 'Debt relief under the Heavily Indebted Poor Countries (HIPC) initiative' (25 March 2020), https://www.imf.org/en/About/Factsheets/Sheets/2016/08/01/16/11/Debt-Relief-Under-the-Heavily-Indebted-Poor-Countries-Initiative (accessed 2 June 2021).

8 IMF (n 6).

9 JE Tyson 'Sub-Saharan Africa international sovereign bonds – Part I. Investor and issuer perspectives' Overseas Development Institute (January 2015) 6, https://www.odi.org/publications/9205-sub-saharan-africa-international-sovereign-bonds (accessed 20 April 2021).

10 Among the countries of which overall debt stock has greatly increased in the period include Ethiopia (885% increase); Ghana (395% increase); Uganda (437%); and Zambia (521% increase). World Bank Group 'International debt statistics' (2020), https://openknowledge.worldbank.org/bitstream/handle/10986/32382/9781464814617.pdf?sequence=7&isAllowed=y (accessed 1 January 2020).

11 World Bank Group (n 10) 35.

12 World Bank Group 'International Debt Statistics' (2021) 31, https://openknowledge.worldbank.org/bitstream/handle/10986/34588/9781464816109.pdf.

Bilateral	50,903.90	70,877.00	101,567.90
Private creditors	65,198.00	98,525.30	166,854.50
Bondholders	36,500.60	52,171.60	109,100.20
Commercial banks and others	28,697.30	46,353.70	57,754.30
Private nonguaranteed debt	80,648.50	108,393.50	142,627.40
Bondholders	13,138.00	15,837.10	18,254.90
Commercial banks and others	67,510.50	92,556.40	124,372.50
Long-term external debt stocks	259,354.30	359,045.50	534,665.20

Concern about the level of debt in African countries predates the pandemic. As early as 2016, African countries were already being cautioned about mounting debt levels and the potential for a debt crisis by the United Nations Conference on Trade and Development (UNCTAD).[13] This was also a concern shared by the World Bank, which had already noted that in 2013, up to eight African countries were at high risk of debt distress.[14] Similarly, in 2014 the IMF's then managing director, Christine Lagarde, raised concerns over the continued mounting debt levels and, in particular, the potential danger of the proliferation of the use of Eurobonds which came at the backdrop of search for yields from investors.[15] Lagarde warned that the growing use of Eurobonds 'is additional financing, but that is an additional vulnerability'.[16]

By March 2018, 18 countries were considered at high risk of debt distress, including more than 40 per cent of sub-Saharan African low-income countries.[17] Given the amount of financing countries need to deal

13 UNCTAD 'Sovereign debt crises more likely, new mechanisms needed' (26 October 2016), https://unctad.org/en/pages/newsdetails.aspx?OriginalVersionID=1364 (accessed 20 April 2021).

14 World Bank 'Africa's Pulse 17: An analysis of issues shaping Africa's economic future' World Bank Group (2018) 25, https://openknowledge.worldbank.org/handle/10986/29667 (accessed 10 December 2019).

15 J Blas & A England 'IMF warns "rising" African nations on sovereign debt risks' *The Financial Times* (29 May 2014), http://www.ft.com/intl/cms/s/0/6ae943e0-e751-11e3-8b4e-00144feabdc0.html#axzz49Ot2Hi9V (accessed 12 August 2016).

16 As above.

17 World Bank (n 14) 25.

with the COVID-19 pandemic, it can be expected that the challenge of debt re-accumulation will grow and make an already vulnerable region more vulnerable.

Already in the first quarter of 2020 it was clear that many countries would need debt payment moratoriums/standstills in order to cope with the crisis.[18] However, the situation has continued to deteriorate and now the continent's financing needs are estimated at being as high as US $1,2 trillion through 2023.[19] The vulnerability that the continent is currently experiencing is well articulated by the IMF's managing director, Kristalina Georgieva, who noted:[20]

> Some countries are confronting high debt burdens forcing them to choose between debt service and additional social and health spending. Current commitments from international financial institutions and official bilateral creditors are expected to fill less than a quarter of this need. With private capital still subdued, we face a projected gap of over $345 billion through 2023 – and nearly half this burden is in Africa's low-income countries.

In November 2020 Zambia became the first African country during the COVID-19 pandemic to default on its debt, when it failed to make the US $42,5 million payments due on its Eurobonds.[21] Currently, there are at least 17 African countries that are also facing increased debt repayment pressures. In response to the challenges globally, the G20 introduced the Debt Service Suspension Initiative (DSSI) which suspended bilateral official debt payments for low-income countries. The G20 encouraged private creditors to provide similar relief but the initiative did not directly address the question of the treatment of private creditors.[22] In addition to the DSSI, the more recent and comprehensive 'Common Framework for Debt Treatments beyond the DSSI' seeks to promote comparable

18 'Senior Africans propose "standstill" on Eurobond debt payments' *Financial Times* (7 April 2020), https://www.ft.com/content/89c6d60f-5fe9-4b72-b327-4a6eb267a9c9 (accessed 20 April 2021).

19 IMF 'Opening remarks at mobilising with Africa II high-level virtual event Yy managing director Kristalina Georgieva' (9 October 2020), https://www.imf.org/en/News/Articles/2020/10/09/sp100920-opening-remarks-at-mobilizing-with-africa-ii-high-level-virtual (accessed 3 March 2021).

20 As above.

21 ST Mrema 'SADC economic integration and statistical framework: Issues of definition, measurement and statistical improvement' IFC Bulletin 32 (January 2020) 125, https://www.bis.org/ifc/publ/ifcb32h.pdf (accessed 20 April 2021).

22 World Bank Group 'COVID-19: Debt service suspension initiative' (19 February 2021), https://www.worldbank.org/en/topic/debt/brief/covid-19-debt-service-suspension-initiative (accessed 3 March 2021).

treatment by and for a broad set of creditors, including the private sector creditors.[23] In light of the vulnerable situation in which the continent finds itself (the worst recession in half a century), the president of the AfDB, Dr Akinwumi A Adesina, has instead called for a more permanent resolution to Africa's over-indebtedness and also called for a governance response by African governments, noting:[24]

> Even more important, the time for one last debt relief for Africa is now. But such relief would require that African countries credibly commit to their share of the deal through bold governance reforms to eliminate all forms of leakages in public resources, improve domestic resource mobilization, and enhance transparency – including on debt and in the natural resource sector.

The current debt landscape demonstrates that debt is going to become a much bigger challenge for the continent. It also suggests that Africa will need to be creative in meeting this challenge so that it can both deal with the debt overhang and ensure that it has sustainable access to financing for its development needs. This raises a number of issues that African states will have to address as they consider how to meet the debt challenge.

First, they will need to consider if there are any flexibilities in the global financial architecture that they can exploit in order to deal with their debt problems. These flexibilities can relate to both the current arrangements for global governance or to the structure of their debt transactions. Consequently, they will need to carefully assess their relationships with international financial institutions such as the IMF and entities such as the G20. In addition, they will need to pay careful attention to the financial and legal characteristics of their debts. A noteworthy initiative in this regard is the proposal by the UN Economic Commission for *Africa* (UNECA) to establish a Liquidity and Sustainability Facility, which is intended to facilitate borrowing by African states. If operationalised, UNECA expects it to lower borrowing costs by promoting more liquid markets for African sovereign debt.[25]

23 Paris Club 'Common framework for debt treatments beyond the DSSI', https://clubdeparis.org/sites/default/files/annex_common_framework_for_debt_treatments_beyond_the_dssi.pdf (accessed 15 June 2021).

24 African Development Bank 'African Economic Outlook 2021' https://www.afdb.org/sites/default/files/documents/publications/afdb21-01_aeo_main_english_complete_0223.pdf?e=1&page=1&embedInfo=theme,293042,151b26,ffffff,ffe358,ffffff; (accessed 15 June 2021).

25 'ECA launches LSF, a vehicle for debt management and fiscal sustainability' (23 March 2021), https://www.uneca.org/stories/eca-launches-lsf%2C-a-vehicle-for-debt-management-and-fiscal-sustainability (accessed 30 April 2021).

Second, every country will need to carefully review its own situation and determine for itself if there is anything that it can do to improve its management of its sovereign debt arrangements. This could mean that it needs to introduce some legislative reforms. It could also require it to work on improving its relations with its existing creditors so that they are willing to be more flexible in their approach to its debt.

Third, African countries will need to consider if they are better served by engaging with their creditors on their own or if they would benefit from some degree of intra-continental coordination.

Finally, they will need to assess how to engage with the multilateral responses to the current debt challenges, such as the DSSI. As Kristalina Georgieva notes, we need to go further and also 'recognise the need to further strengthen the international architecture for debt restructuring'.[26]

1.3 Bringing the challenges to the fore in the context of SADC, and why it matters

While the current challenge of debt sustainability and management are a concern for all African countries, this publication seeks to explore these issues in the specific context of the SADC region. SADC encompasses 16 countries: Angola, Botswana, Comoros, the Democratic Republic of the Congo (DRC), Eswatini, Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, Seychelles, South Africa, Tanzania, Zambia and Zimbabwe.[27] SADC forms one of the regional economic communities (RECs) recognised by the African Union (AU) as forming one of the building blocks of the African Continental Free Trade Area (AfCFTA). SADC was created with the aim, among others, to 'achieve development and economic growth, alleviate poverty, enhance the standard and quality of life of the people of Southern Africa and support the socially disadvantaged through regional integration'.[28] Consequently, part of its economic mandate is dealing with the challenge of unsustainable debt.

SADC countries are at different development levels and have had divergent debt experiences.[29] In 2014 the African Forum on Debt and Development (AFRODAD) grouped SADC countries according to their

26 IMF (n 19).

27 SADC official website, https://www.sadc.int/member-states/ (accessed 1 March 2021).

28 Art 5 SADC Treaty (1992).

29 See Annex 1 World Bank debt statistics per creditor type (excluding Mauritius, Namibia and Seychelles).

debt experiences in a very interesting manner, which in some respects remains true and, in others, has changed:[30]

(1) countries that have benefited from the previous debt relief initiatives, the HIPC and MDRI: Democratic Republic of the Congo, Malawi, Mozambique, Tanzania and Zambia. As if history is repeating itself, today Zambia is a country that is again in debt distress with the Eurobond default and mounting debt burdens.[31] Another country that is again of concern today is Mozambique which has also reached external debt levels that are concerning;[32]
(2) countries that may have relatively lower and stable external debt levels despite this class of debt being an important source of funding: Lesotho, Eswatini (formally Swaziland) and Botswana;
(3) countries that mostly utilised domestic resources to meet their funding goals: Mauritius, Namibia and South Africa. For South Africa today, its total debt levels have reached high levels and external debt is becoming an important source of funding.[33] In fact, the country is among the top ten borrowers globally (which is defined as those countries with the largest end-2019 external debt stock), according to the World Bank 2021 Debt Statistics and, regionally, it recorded the fastest average debt accumulation in 2019;[34]
(4) countries with significant debt burdens: Madagascar, Seychelles and Zimbabwe. Today this list would need to be updated to include Zambia, Mozambique and Angola.[35]

Since 2014 Africa's debt landscape has greatly changed, not only in terms of an increase in debt levels, but also in composition. As a result, African countries may be exposed to newer challenges. Among the major shifts in the debt landscape is the emergence of new bilateral creditors, notably China which is becoming the region's main bilateral creditor.[36] Additionally, the use of privately-held bonds has become more

30 AFRODAD 'Intra-SADC debt – A growing financial phenomenon' (December 2014) 2, https://media.africaportal.org/documents/intra_sadc_debts_policy_brief.pdf (accessed 20 April 2021).

31 See Figure 12 Zambia External Debt Stock by Creditor Type, in Appendix 1.

32 See Figure 9 Mozambique External Debt Stock by Creditor Type, in Appendix 1.

33 See Figure 10 South Africa External Dent Stock by Creditor Type, Appendix 1.

34 World Bank Group *International debt statistics 2021* (2021) 7, https://openknowledge.worldbank.org/bitstream/handle/10986/34588/9781464816109.pdf (accessed 20 April 2021).

35 See Figure 1 Angola External Debt Stock by Creditor Type, 1.4.

36 The AfLSF notes that in 2018 China's lending to African countries had already reached US $60 billion. African Legal Support Facility 'Understanding sovereign debt: Options and opportunities for Africa' (2019) 18, https://www.aflsf.org/sites/default/

important.[37] In the SADC region South Africa has had a very long history of issuing sovereign bonds and is currently the largest sovereign issuer of Eurobonds. Another innovator in this regard is Seychelles which in 2006 issued Eurobonds.[38] In 2011 the country was one of the first in the region to default on its Eurobond payments with the default on a US $230 million Eurobond payment after problematic elections.[39] Various other SADC countries followed South Africa and Seychelles in the issuing of sovereign bonds, including Angola, Mozambique, Tanzania and Zambia.

Today restructuring is going to be more complex than during the HIPC/EHIPC/MDRI era because of the extra layers of complexity added by the Chinese debts (that include project finance and resource-backed loans) and privately-held Eurobonds. Further, a more fully rounded discussion of debt management needs to consider a broader range of issues, including fiscal responsibility, transparency, corruption, human rights and environmental concerns.

1.4 Synopsis of the contents of the book

For the first time, an entire publication is being dedicated to the contemporary issues of sovereign debt management, debt resolution and broader debt governance issues in SADC. The substantive chapters of this publication assess different thematic issues that together will contribute to the global and regional effort to fill gaps in the debt management and restructuring architecture. Among the themes/concerns that this publication explores, and that policy makers in the region should care about in designing a post-COVID-19 approach to debt, are the following:

files/resources/2019-05-31%20Understanding%20Sovereign%20Debt%20Eng.%20v10.pdf (accessed 15 January 2020).

37 See Table 1 Sub-Sahara Africa External Debt Stock by Creditor Type (billion USD).

38 See M Macagni et al ‘Issuing international sovereign bonds. Opportunities and challenges for sub-Saharan Africa’ International Monetary Fund (2 June 2014), https://www.imf.org/en/Publications/Departmental-Papers-Policy-Papers/Issues/2016/12/31/Issuing-International-Sovereign-Bonds-Opportunities-and-Challenges-for-Sub-Saharan-Africa-41341 (accessed 15 June 2016); A Sy ‘Trends and development in African frontier bond markets’ The Brookings Institution (March 2015), https://www.brookings.edu/research/trends-and-developments-in-african-frontier-bond-markets/ (accessed 8 July 2016).

39 S Brooks, D Lombardi & E Suruma ‘African perspective on sovereign debt restructuring’ Centre for Governance Innovation Issues Paper 47 (September 2014) 2, https://www.cigionline.org/sites/default/files/no43_web.pdf (accessed 1 June 2017).

- the challenges of transparency and corruption in debt accumulation;
- the challenges of determining debt sustainability and how fiscal responsibility provisions can be used in regard to ensuring sustainable debt accumulation and management;
- the power imbalance in the debtor-creditor relationship and how this impacts the kinds of debt arrangements the countries in the region enter into; and
- the available debt restructuring options and the extent to which they deal with deeper structural issues such as human rights, environment and promoting sustainable development.

An effective response to these challenges requires a multidisciplinary approach. Therefore, this book included contributions by authors from different disciplines and with different experiences and perspectives. The authors also make use of a mix of quantitative and qualitative approaches to the issues they discuss.

The book is divided into three broad sections. Each section seeks to answer one or more of four pertinent questions relating to SADC's debt – Where are we? How did we get here? Why does it matter? Where are we going?

1.4.1 Section one: What does the current debt landscape look like?

The first section of this publication provides a synopsis of the current debt landscape in the SADC region in the context of the global debt situation and the current COVID-19 pandemic. In chapter 2 'International assistance in catastrophes need not bankrupt countries' Herman discusses the current global approaches to countries facing problems in managing their external debt caused by unforeseen circumstances. Herman acknowledges that many countries faced debt challenges before the pandemic but notes that COVID-19 has left many African countries in more vulnerable situations and has exacerbated the weaknesses in the current global approaches to debt renegotiations. His chapter, written from a political-economy perspective, provides a timely discussion of the constrained external debt and development finance options that may be available to the SADC countries.

Flowing from the above, Kessler in chapter 3 'Deferring debt service in times of crisis: Did it matter and what can it lead to?' surveys fiscal tensions arising from the COVID-19 pandemic for the 16 countries of the SADC region, and the response of the donor community to these tensions. He also assesses the DSSI.

Edwards in chapter 4 'The IMF and debt surveillance in SADC countries' looks at the role of the IMF Article IV surveillance mechanism in general and in the SADC region and its role in warning countries about their financial vulnerabilities. In making his assessment, the author discusses whether or not the IMF provided countries in the region with adequate warnings about the fragility of their finances.

In chapter 5 'Sovereign debt via the lens of asset management: Implications for SADC countries' Gallagher and Wang focus on how debt sustainability is determined and highlight some shortcomings with the current approach to this issue and its implications for the SADC region. Gallagher and Wang propose an innovative 'public sector balance sheet' approach to determining debt sustainability and argue that this would provide a more useful view of debt sustainability than the conventional debt to GDP approach.

1.4.2 Section two: A thematic assessment of the challenges of sovereign debt restructuring

This section of the book concentrates on specific topics relating to the general subject of sovereign debt restructuring.

Muriungi in chapter 6 'Managing and restructuring sovereign debt in the SADC region in the context of the COVID-19 pandemic' assesses the *ex ante* contractual mechanisms and *ex post* legal defences that African countries may use in the face of debt payment defaults and in any litigation arising from debt restructuring during the COVID-19 pandemic.

In chapter 7 'Sovereign debts under bilateral investment treaties: Does the SADC Model BIT navigate the controversy?' Jackson addresses the potential role that bilateral investment treaties (BITs) may play in regard to sovereign debtors in default on their external debts. Jackson expresses concerns about the potential use of BITs by investors who may institute investor-state dispute resolution proceedings during a debt restructuring. Jackson argues that such actions could have disruptive effects in the SADC region and offers some insights into how this possibility could be managed.

In chapter 8 'Sovereign debt restructuring and human rights: Overcoming a false binary?' Masamba explores the link between sovereign debt and human rights and identifies what has become a glaring disconnect between these two fields. She additionally argues that there is a place for human rights in the sovereign debt discourse and maintains

that this is a relatively overlooked issue in the discourse on sovereign debt restructuring.

1.4.3 Section three: What is the situation in the SADC countries and are there possible solutions to their challenges?

This section includes case studies of Mozambique, Namibia, South Africa, Zambia and Zimbabwe. These each of these case studies focuses on particular challenges that the countries in the region face in regard to the management of their debts.

In chapter 9 'Adopting proactive debt management policy strategies to forestall a debt crisis in South Africa' Aren discusses debt management in South Africa. She expresses the concern that South Africa may be heading towards a major sovereign debt crisis and calls for proactive strategies to avoid this outcome. In providing recommendations, the author specifically focuses on the challenges of South Africa's high debt levels and interest rate, increasing level of state capture, and the complex issue of corruption.

In chapter 10 'The renegotiation of sovereign debt tainted by corruption: Mozambique's "secret" debt in perspective' Koen explores the case of Mozambique's secret debt tainted with corruption. He provides background on how the debt was incurred, assesses its legality under Mozambican law, and discusses the validity of the debt under the English governing law. Finally, he draws lessons for other SADC countries that could face the problem of debt that may be tainted with corruption.

Ng'ambi discusses the case of Zambia in chapter 11 'Sovereign debt: A case study of Zambia'. Zambia is the first African country to default on its Eurobonds during the COVID-19 pandemic. Ng'ambi provides an overview of the country's recent debt history and of the economic and social impact of the current debt crisis. He also argues that the Zambian debt crisis should be managed within the framework of the Basic Principles on Sovereign Debt Restructuring Processes.[40]

In chapter 12 'Steeling for the next public health crises through fiscal responsibility: Namibia's trial of strength' Zongwe focuses on Namibia's fiscal landscape and the tension that arises when a country needs to balance short-term liquidity needs, for example, due to a pandemic, with long-term solvency concerns. He argues that the country should introduce

40 UN General Assembly Basic Principles on Sovereign Debt Restructuring Processes (29 July 2015), https://unctad.org/system/files/official-document/a69L84_en.pdf (accessed 10 April 2021).

fiscal responsibility laws in Namibia that can provide guidance to policy makers in managing these tensions. Zongwe utilises the examples of budget system laws in other countries to support his case.

In chapter 13 'Resource-backed loans, COVID-19 and the high risk of debt trap: A case study of Zimbabwe' co-authors Mutondoro, Hobi, Dhliwayo and Chiname assess the legal and social aspects of natural resource-backed loans in Zimbabwe. The co-authors raise the concern that resource-backed loans in the already fragile Zimbabwe are negatively impacting the country's debt burden, and increasing the risks of corruption and human rights violations.

In chapter 14 'Towards utilisation of domestic resources in settling Zimbabwe's sovereign debt' Pfumorodze discusses the complex challenge of Zimbabwe's massive debt overhang and how it has been compounded by COVID-19. He also describes the government's previous unsuccessful debt-restructuring strategies. The chapter concludes with some suggestions for debt restructuring and relief for Zimbabwe.

Finally, in chapter 15 'Building back better post-COVID-19: Lessons learnt and the future of sovereign debt management and restructuring in SADC' Bradlow and Masamba draw lessons from all the contributions that they maintain will be useful to policy makers, industry experts and academics interested in the management of sovereign debt in the SADC region.

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Annex 1: World Bank debt statistics per creditor type (excluding Mauritius, Namibia and Seychelles)

Figure 1: Angola External Debt Stock by Creditor Type[41]

	2009	2015	2016	2017	2018	2019
Summary external debt stock by creditor type						
Long-term external debt stocks	**16,789**	**47,571**	**52,040**	**46,827**	**48,227**	**47,776**
Public and publicly guaranteed debt from:	13,630	27,301	34,463	33,892	35,557	35,031
Official creditors	4,661	11,909	21,333	22,567	21,451	19,388
Multilateral	448	1,602	2,018	2,239	2,268	2,847
of which: World Bank	385	929	940	1,025	1,042	1,636
Bilateral	4,213	10,307	19,314	20,328	19,183	16,541
Private creditors	8,969	15,392	13,131	11,325	14,106	15,643
Bondholders	..	2,500	2,500	2,500	6,000	8,000
Commercial banks and others	8,969	12,892	10,631	8,825	8,106	7,643
Private nonguaranteed debt from:	3,158	20,270	17,577	12,934	12,669	12,745
Bondholders	..	..	..	..	..	..
Commercial banks and others	3,158	20,270	17,577	12,934	12,669	12,745
Use of IMF credit	787	532	396	389	1,374	1,861

Figure 2: Botswana External Debt Stock by Creditor Type[42]

	2009	2015	2016	2017	2018	2019
Summary external debt stock by creditor type						
Long-term external debt stocks	**1,395**	**1,772**	**1,670**	**1,552**	**1,451**	**1,346**
Public and publicly guaranteed debt from:	1,395	1,772	1,670	1,552	1,451	1,334
Official creditors	1,394	1,741	1,648	1,538	1,447	1,334
Multilateral	1,251	1,667	1,583	1,476	1,389	1,287
of which: World Bank	5	131	159	151	174	172
Bilateral	143	75	65	63	58	47
Private creditors	2	31	22	13	4	0
Bondholders	..	..	..	..	..	..
Commercial banks and others	2	31	22	13	4	0
Private nonguaranteed debt from:	..	0	..	..	0	12
Bondholders	..	0	..	..	..	..
Commercial banks and others	..	..	..	..	0	12
Use of IMF credit	90	80	77	82	80	79

Figure 3: Comoros External Debt Stock by Creditor Type[43]

	2009	2015	2016	2017	2018	2019
Summary external debt stock by creditor type						
Long-term external debt stocks	**258.6**	**99.9**	**162.5**	**170.1**	**232.0**	**243.3**
Public and publicly guaranteed debt from:	258.6	99.9	162.5	170.1	232.0	243.3
Official creditors	258.6	99.9	162.5	170.1	232.0	243.3
Multilateral	213.0	56.9	53.2	54.2	54.0	68.0
of which: World Bank	120.4	13.5	12.9	13.3	12.7	12.3
Bilateral	45.6	43.0	109.3	115.8	178.0	175.3
Private creditors	..	..	..	..	..	..
Bondholders	..	..	..	..	..	..
Commercial banks and others	..	..	..	..	..	..
Private nonguaranteed debt from:	..	..	..	..	..	..
Bondholders	..	..	..	..	..	..
Commercial banks and others	..	..	..	..	..	..
Use of IMF credit	23.4	29.2	26.6	26.1	22.3	30.7

41 World Bank Group 'International debt statistics' (2021) 35, https://openknowledge.worldbank.org/bitstream/handle/10986/34588/9781464816109.pdf (accessed 19 February 2021).

42 World Bank Group (n 41) 46.

43 World Bank Group (n 41) 58.

Figure 4: DRC External Debt Stocks by Creditor Type[44]

Summary external debt stock by creditor type	2009	2015	2016	2017	2018	2019
Long-term external debt stocks	**10,873**	**4,065**	**3,817**	**4,004**	**4,023**	**4,099**
Public and publicly guaranteed debt from:	10,873	4,065	3,817	4,004	4,023	4,099
Official creditors	10,525	4,055	3,816	4,003	3,993	3,997
Multilateral	4,186	1,872	1,724	1,995	2,037	2,122
of which: World Bank	2,497	841	827	942	1,098	1,288
Bilateral	6,339	2,182	2,091	2,008	1,956	1,875
Private creditors	349	11	2	1	30	102
Bondholders	..	..	..	..	..	..
Commercial banks and others	349	11	2	1	30	102
Private nonguaranteed debt from:	..	..	..	..	..	..
Bondholders	..	..	..	..	..	..
Commercial banks and others	..	..	..	..	..	..
Use of IMF credit	1,601	1,098	989	954	839	1,130

Figure 5: Eswatini External Debt Stock by Creditor Type[45]

Summary external debt stock by creditor type	2009	2015	2016	2017	2018	2019
Long-term external debt stocks	**428.0**	**286.0**	**359.7**	**397.7**	**424.4**	**533.0**
Public and publicly guaranteed debt from:	428.0	286.0	359.7	397.7	424.4	533.0
Official creditors	389.7	272.2	344.9	381.9	412.0	520.3
Multilateral	261.1	156.2	177.4	208.3	219.4	234.8
of which: World Bank	10.0	21.8	27.6	38.8	39.8	36.4
Bilateral	128.6	116.0	167.6	173.6	192.6	285.6
Private creditors	38.3	13.7	14.7	15.7	12.4	12.7
Bondholders	..	..	..	..	..	..
Commercial banks and others	38.3	13.7	14.7	15.7	12.4	12.7
Private nonguaranteed debt from:	..	..	..	..	..	..
Bondholders	..	..	..	..	..	..
Commercial banks and others	..	..	..	..	..	..
Use of IMF credit	75.7	66.9	64.9	68.8	67.2	66.8

Figure 6: Lesotho External Debt Stock by Creditor Type[46]

Summary external debt stock by creditor type	2009	2015	2016	2017	2018	2019
Long-term external debt stocks	**687.8**	**773.8**	**774.8**	**827.5**	**810.3**	**859.1**
Public and publicly guaranteed debt from:	687.8	773.8	774.8	827.5	810.3	859.1
Official creditors	672.6	770.1	771.5	824.1	807.1	856.2
Multilateral	614.0	655.8	648.5	703.5	697.9	724.5
of which: World Bank	313.2	283.7	284.1	321.4	338.3	362.8
Bilateral	58.6	114.3	123.0	120.6	109.2	131.7
Private creditors	15.2	3.7	3.3	3.5	3.1	2.9
Bondholders	..	..	..	..	..	..
Commercial banks and others	15.2	3.7	3.3	3.5	3.1	2.9
Private nonguaranteed debt from:	..	..	..	..	..	..
Bondholders	..	..	..	..	..	..
Commercial banks and others	..	..	..	..	..	..
Use of IMF credit	75.7	114.6	108.3	108.1	93.8	79.3

Figure 7: Malawi External Debt Stock by Creditor Type[47]

Summary external debt stock by creditor type	2009	2015	2016	2017	2018	2019
Long-term external debt stocks	**846.5**	**1,453.9**	**1,507.0**	**1,789.8**	**1,926.2**	**2,026.1**
Public and publicly guaranteed debt from:	846.5	1,453.9	1,507.0	1,789.8	1,926.2	2,026.1
Official creditors	840.7	1,453.9	1,507.0	1,789.8	1,926.2	2,026.1
Multilateral	547.0	1,013.0	1,087.9	1,369.4	1,487.0	1,600.2
of which: World Bank	212.8	588.2	642.2	862.2	916.7	969.3
Bilateral	293.7	440.9	419.1	420.4	439.2	425.9
Private creditors	5.8	0.0	..	..	..	..
Bondholders	..	..	..	..	..	..
Commercial banks and others	5.8	0.0	..	..	..	..
Private nonguaranteed debt from:	..	..	..	..	..	..
Bondholders	..	..	..	..	..	..
Commercial banks and others	..	..	..	..	..	..
Use of IMF credit	230.9	254.7	295.9	318.9	314.1	339.5

44 World Bank Group (n 41) 59.

45 World Bank Group (n 41) 70.

46 World Bank Group (n 41) 95.

47 World Bank Group (n 41) 98.

Figure 8: Madagascar External Debt Stock by Creditor Type[48]

Summary external debt stock by creditor type	2009	2015	2016	2017	2018	2019
Long-term external debt stocks	**1,914**	**2,522**	**2,470**	**2,765**	**2,994**	**3,239**
Public and publicly guaranteed debt from:	1,895	2,509	2,465	2,735	2,902	3,120
Official creditors	1,887	2,422	2,387	2,609	2,738	2,966
Multilateral	1,486	1,973	2,015	2,254	2,349	2,491
of which: World Bank	1,105	1,412	1,433	1,595	1,648	1,686
Bilateral	401	450	372	355	390	475
Private creditors	8	86	78	127	164	154
Bondholders	..	..	..	..	..	..
Commercial banks and others	8	86	78	127	164	154
Private nonguaranteed debt from:	19	13	5	30	92	119
Bondholders	..	..	..	..	..	..
Commercial banks and others	19	13	5	30	92	119
Use of IMF credit	284	281	301	440	465	545

Figure 9: Mozambique External Debt Stock by Creditor Type[49]

Summary external debt stock by creditor type	2009	2015	2016	2017	2018	2019
Long-term external debt stocks	**5,114**	**13,249**	**13,569**	**14,671**	**17,399**	**18,493**
Public and publicly guaranteed debt from:	3,400	9,821	10,003	10,794	10,929	10,888
Official creditors	3,373	7,759	8,183	9,051	9,265	9,390
Multilateral	1,967	3,590	3,716	4,073	4,214	4,432
of which: World Bank	1,356	2,461	2,555	2,822	2,904	3,039
Bilateral	1,406	4,168	4,466	4,978	5,051	4,958
Private creditors	27	2,062	1,820	1,743	1,664	1,498
Bondholders	..	850	727	727	727	727
Commercial banks and others	27	1,212	1,094	1,016	937	771
Private nonguaranteed debt from:	1,714	3,428	3,566	3,877	6,470	7,606
Bondholders	..	..	..	..	..	..
Commercial banks and others	1,714	3,428	3,566	3,877	6,470	7,606
Use of IMF credit	342	399	355	343	303	375

Figure 10: South Africa External Dent Stock by Creditor Type[50]

Summary external debt stock by creditor type	2009	2015	2016	2017	2018	2019
Long-term external debt stocks	**55,818**	**92,805**	**110,068**	**138,411**	**133,758**	**151,214**
Public and publicly guaranteed debt from:	23,201	44,065	58,413	78,678	71,647	86,307
Official creditors	227	3,783	4,602	7,999	8,298	7,783
Multilateral	227	3,495	4,175	5,466	4,794	4,631
of which: World Bank	21	1,785	2,343	2,686	2,277	2,239
Bilateral	0	288	426	2,534	3,504	3,153
Private creditors	22,974	40,282	53,811	70,679	63,349	78,523
Bondholders	17,097	28,807	40,271	55,713	46,626	55,075
Commercial banks and others	5,876	11,474	13,540	14,966	16,723	23,448
Private nonguaranteed debt from:	32,617	48,740	51,655	59,732	62,111	64,907
Bondholders	8,485	10,309	9,878	10,116	11,187	11,634
Commercial banks and others	24,132	38,431	41,776	49,616	50,923	53,273
Use of IMF credit	2,799	2,474	2,400	2,543	2,483	2,469

Figure 11: Tanzania External Stock by Creditor Type[51]

Summary external debt stock by creditor type	2009	2015	2016	2017	2018	2019
Long-term external debt stocks	**5,656**	**12,961**	**13,809**	**15,765**	**16,317**	**17,484**
Public and publicly guaranteed debt from:	4,640	10,765	11,135	12,670	12,854	14,115
Official creditors	4,520	9,469	10,023	11,246	11,857	12,560
Multilateral	3,573	7,490	7,795	8,930	9,432	10,121
of which: World Bank	2,598	5,399	5,621	6,467	6,815	7,341
Bilateral	947	1,979	2,228	2,316	2,425	2,439
Private creditors	119	1,295	1,111	1,424	997	1,555
Bondholders	..	..	..	..	..	..
Commercial banks and others	119	1,295	1,111	1,424	997	1,555
Private nonguaranteed debt from:	1,016	2,197	2,674	3,095	3,463	3,369
Bondholders	..	..	..	..	..	..
Commercial banks and others	1,016	2,197	2,674	3,095	3,463	3,369
Use of IMF credit	628	592	515	459	364	301

48 World Bank Group (n 41) 97.

49 World Bank Group (n 41) 107.

50 World Bank Group (n 41) 128.

51 World Bank Group (n 41) 135.

Figure 12: Zambia External Debt Stock by Creditor Type[52]

	2009	2015	2016	2017	2018	2019
Summary external debt stock by creditor type						
Long-term external debt stocks	**2,120**	**10,132**	**13,646**	**15,686**	**17,667**	**25,839**
Public and publicly guaranteed debt from:	1,100	6,487	7,060	8,785	9,920	11,104
Official creditors	1,095	3,222	3,763	4,226	4,701	5,701
Multilateral	871	1,295	1,408	1,620	1,822	2,117
of which: World Bank	407	698	760	894	1,003	1,108
Bilateral	224	1,927	2,356	2,606	2,879	3,584
Private creditors	5	3,265	3,297	4,558	5,219	5,403
Bondholders	..	3,000	3,000	3,000	3,000	3,000
Commercial banks and others	5	265	297	1,558	2,219	2,403
Private nonguaranteed debt from:	1,020	3,645	6,586	6,902	7,748	14,736
Bondholders	..	..	..	..	..	..
Commercial banks and others	1,020	3,645	6,586	6,902	7,748	14,736
Use of IMF credit	1,080	907	813	794	715	667

Figure 13: Zimbabwe External Debt Stock by Creditor Types[53]

	2009	2015	2016	2017	2018	2019
Summary external debt stock by creditor type						
Long-term external debt stocks	**3,974**	**6,129**	**7,888**	**8,323**	**8,786**	**8,275**
Public and publicly guaranteed debt from:	3,876	4,207	4,248	4,341	4,308	4,386
Official creditors	3,409	3,796	3,828	3,899	3,883	3,967
Multilateral	1,646	1,659	1,575	1,434	1,232	1,226
of which: World Bank	985	912	885	907	896	890
Bilateral	1,764	2,137	2,253	2,466	2,651	2,741
Private creditors	467	411	419	441	425	419
Bondholders	0	0	0	0	0	0
Commercial banks and others	467	411	419	441	425	419
Private nonguaranteed debt from:	98	1,922	3,640	3,983	4,478	3,889
Bondholders	..	..	..	..	..	..
Commercial banks and others	98	1,922	3,640	3,983	4,478	3,889
Use of IMF credit	542	464	455	482	471	468

52 World Bank Group (n 41) 150.

53 World Bank Group (n 41) 151.

2 International assistance in catastrophes need not bankrupt countries

*Barry Herman**

2.1 Introduction: The problem is generic

Incurring debt – being able to borrow to make purchases beyond what is possible with only current income or savings – is a powerful social mechanism; indeed, it is one that may have been at the centre of human relationships for 5 000 years.[1] The nature of the obligation to repay those loans or their interest charges when they fall due has engaged philosophers and theologians for probably just as long, as they attempt to specify what borrowers and lenders *ought* to do when facing the challenges as well as the opportunities thrown up by the loans and by life in all its uncertainties. This chapter deals with a subset of situations in which borrowers should not pay lenders and lenders should not expect borrowers to pay.[2]

While such considerations may help shape bankruptcy laws and their enforcement by courts around the world, there is a special problem in addressing debtor/creditor controversies when the debtor is a sovereign government. Unlike corporations, the final remaining assets of which can be distributed to their creditors, governments do not disappear in bankruptcy. Rather, after a shorter or longer period, some resolution of the insolvency is agreed, disappointing different creditors to different degrees, while usually also increasing poverty and worsening the distribution of income in the indebted country. This further challenges governments to honour their human rights obligations.[3]

* An earlier version of this chapter was presented at an interdisciplinary online conference at the University of Pretoria, 9 and 12 November 2020. Comments received therein and subsequently from the conference organisers and an anonymous reviewer are much appreciated. All errors are my own.

1 D Graeber *Debt, the first 5 000 years* (2011).

2 A useful classification of when borrowers ought to pay, might ethically pay and should not pay their creditors and when creditors ought to expect and demand payment, might expect payment and ought not ask for payment is given by C Barry & L Tomitova 'Fairness in sovereign debt' in C Barry, B Herman & L Tomitova (eds) *Dealing fairly with developing country debt* (2007) 41.

3 JP Bohoslavsky 'Economic inequality, debt crises and human rights' (2016) 41 *Yale Journal of International Law* 177.

Moreover, while individual creditors can sometimes seek enforcement of their specific repayments in national courts, there is no supranational court to which appeal can be made to address an over-indebted government's full debt stock, to force it to make some payments, relieve it of some other payments, or devise an overall settlement, as in a national bankruptcy court. In addition, there are few widely-accepted principles that might guide judgments of such a court if one were somehow established,[4] although philosophy and theology do point in certain directions.[5]

In fact, there have been a disconcertingly large number of sovereign insolvencies across recorded history, involving virtually every country at one point or another, and in some periods entrapping up to half of the world's countries.[6] Power differences have largely determined how individual governments faired in bankruptcy, albeit within each era's understanding of acceptable standards of international financial and political relations. While governments no longer send warships on behalf of their bondholder citizens to collect funds that developing countries owe, they do support a complicated negotiating game between the indebted government and each class of its creditors (bondholders, bankers, governments, international institutions). Each party deploys the powers at its disposal to maximise its benefit, whatever the consequence for the people of the country or the other creditors.[7] Governments have considered ways to make the game fairer and reach solutions more expeditiously, but different interests have regularly blocked systemic reforms.[8]

In some situations, reckless political leaders and accommodating creditors push countries into default, but in other situations, unforeseen environmental, public health, financial or economic catastrophes can pull countries into the morass of bankruptcy. Given the unmitigated social and economic harm caused by sovereign insolvency, policies that

4 For an unsatisfying argument that property and creditor rights are more widely accepted than human rights, see AC Porzecanski 'Human rights and sovereign debts in the context of property and creditor rights' in I Bantekas & C Lumina (eds) *Sovereign debt and human rights* (2018) 45.

5 See, eg, B Herman 'Doing the right thing: Dealing with developing country sovereign debt' (2007) 12 *North Carolina Journal of International Law and Commercial Regulation* 773.

6 C Reinhart & J Rogoff *This time is different: Eight centuries of financial folly* (2009).

7 B Herman 'The players and the game of sovereign debt' in Barry, Herman & Tomitova (n 2) 9.

8 For an insider discussion of the political controversies that undermined the proposed sovereign debt-restructuring mechanism (SDRM), the last serious international consideration of systemic debt workout reform, see B Setser 'The political economy of the SDRM' in B Herman, JA Ocampo & S Spiegel (eds) *Overcoming developing country debt crises* (2010) 317.

reduce instances caused by the latter types of situation should be of serious international policy interest. This chapter discusses approaches to international policy that aim to do just that, based on experiences during the 2020-2021 pandemic that left many developing countries vulnerable to – or in – a debt crisis.

2.2 The expected wave of sovereign debt crises

The COVID-19 pandemic and its economic fallout provide a dramatic illustration of how unforeseen circumstances can threaten countries with sovereign insolvency. This experience also holds suggestions for how to respond better to the next international emergency.

In this case, the situation as the crisis began in early 2020 was already difficult for at least 35 vulnerable and low-income economies that had been assessed by the International Monetary Fund (IMF) and the World Bank as in sovereign debt crisis or at high risk of debt distress.[9] The situation was also unsustainable for middle-income countries such as Argentina, Ecuador, Lebanon and Venezuela. For these countries – and for the developing countries as a whole – international financial support that would not add to sovereign debt was warranted. Unfortunately, for the most part it was underprovided.[10]

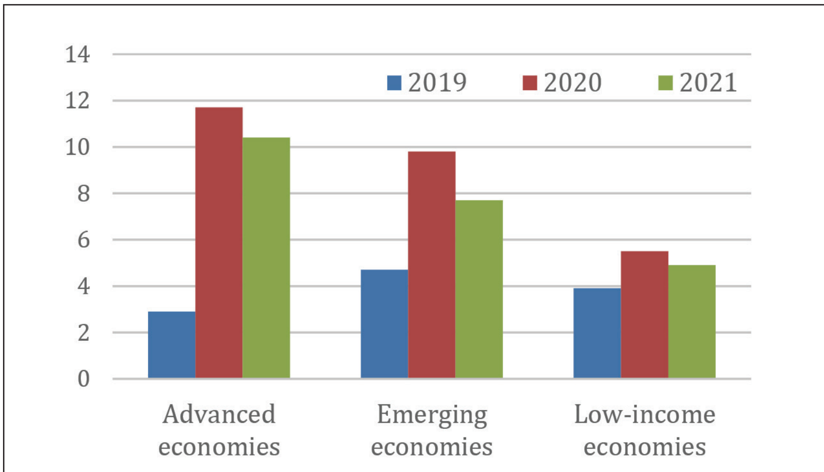
2.2.1 The inescapable surge in foreign borrowing

Beginning in 2020, the world's governments responded to the pandemic by tapping whatever sources of credit they could access, with differing results. While the governments of the countries categorised by the IMF as 'advanced economies' borrowed enough to raise their 2020 fiscal deficits by almost 9 percentage points of gross domestic product (GDP), the middle-income 'emerging economies' could only manage a fiscal deficit increase of about 5 percentage points of GDP and the low-income countries could raise their fiscal deficit by only about 1,6 percentage points (Figure 1). Only modest shrinking of the borrowing of each group was expected in 2021. The inter-country differences in borrowing paralleled differences in counter-crisis spending, both directly health-related and in supporting households and companies that lost income from the crisis (Figure 2).

9 'The evolution of public debt vulnerabilities in lower income economies' (2020) IMF Policy Paper, https://www.imf.org/en/Publications/Policy-Papers/Issues/2020/02/05/The-Evolution-of-Public-Debt-Vulnerabilities-In-Lower-Income-Economies-49018 (accessed 18 October 2020).

10 B Herman 'The looming developing country debt crisis and the fear of imposed austerity' *Pandemic Discourses* (15 October 2020).

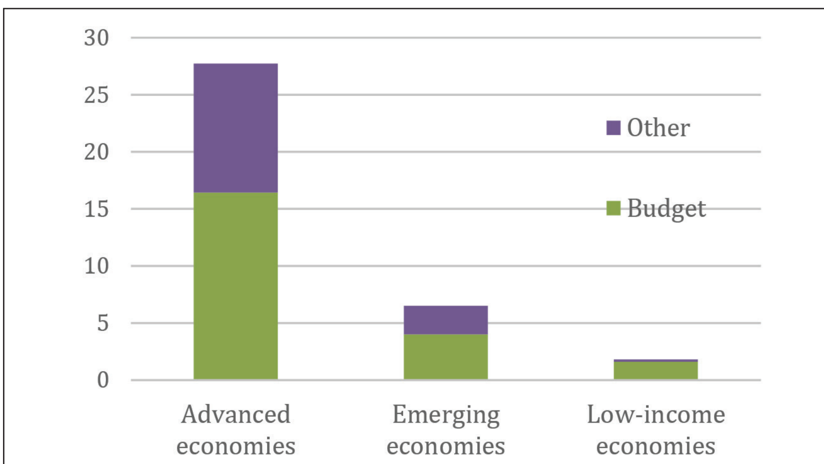
Figure 1: General government deficits in groups of countries, 2019-2021 (Percent of GDP)



Source: IMF, *Fiscal Monitor Database*, April 2021

Note: General government includes sub-national government and social security funds; IMF projection for 2021.

Figure 2: Fiscal response to pandemic in groups of countries (Amount added as percent of GDP, January 2020 to 17 March 2021)



Source: IMF, Fiscal policies database in response to COVID-19

Note: Data include measures announced or taken by 20 advanced, 25 emerging and 14 low-income countries; 'budget' measures include additional discretionary spending and foregone revenues; 'other'

measures include loans, equity and guarantees that do not immediately or necessarily impact budgets.

Advanced economy countries could borrow more than lower-income countries because there is a reliably strong demand in domestic markets (to which foreign investors have access) for the domestic currency bonds of their governments. Middle-income country governments also sell domestic currency bonds at home and abroad but may also raise funds in international markets in foreign currencies to meet their financing needs. For lower-income countries, the domestic financial markets of which are less developed, issuing bonds in foreign currency is the only practical way to access bond financing.

For example, the South African government has long borrowed both in United States (US) dollars and in rand. It has addressed its pandemic financing needs in 2020 mainly by selling bonds denominated in rand to domestic and foreign investors, which in October 2020, just to illustrate, were paying interest rates of about 9 per cent (against an inflation rate of about 3 per cent, making for a 'real' return of about 6 per cent).[11] Around the same time, South Africa's US dollar bond yields were on the order of 4 to 5 per cent. By way of comparison, certain middle-income countries in Latin America and elsewhere that were rated as 'investment grade' were able to issue new bonds in foreign currency at relatively low annual interest rates in April and May 2020 just on the heels of the financial panic that had erupted in March (for instance, 2,5 per cent for Chile and 5 per cent for Mexico for bonds maturing in 2031).[12]

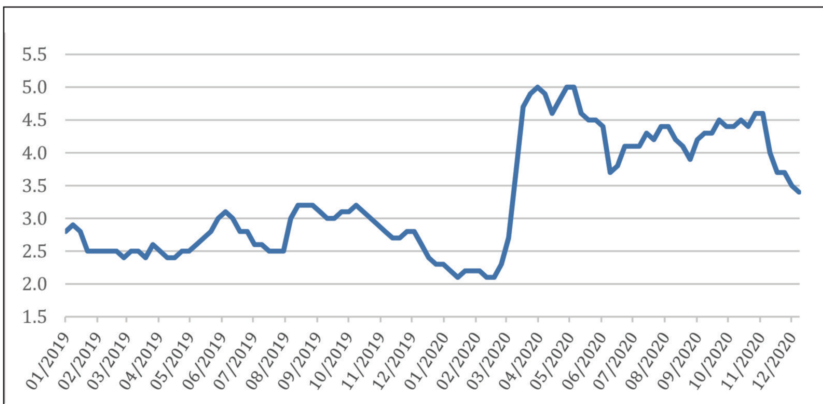
However, for governments considered as being at higher risk of not being able to repay their creditors, the onset of the crisis had a devastating impact. Financial market assessments collapsed, leading to sharp declines in the prices of their bonds. Since the interest yield on a bond is calculated as the contracted annual interest payment divided by the market price of the bond, the fall in bond prices increased the yields. Figure 3 shows how the yield on foreign currency bonds of the higher-risk countries jumped in March 2020 relative to the 'investment grade' bonds of other developing countries. While the spread eventually eased, it remained elevated for the rest of the year.

11 The yield on 10-year government bonds was 9,35% in October 2020 (data of Trading Economics), https://tradingeconomics.com/south-africa/indicators (accessed 18 October 2020).

12 JA Ocampo 'Financing and debt management for emerging market economies' Brookings Institution future development blog (26 May 2020) https://www.brookings.edu/blog/future-development/2020/05/26/financing-and-debt-management-for-emerging-market-economies/ (accessed 18 October 2020).

Clearly, 2020 was not a propitious year for high-risk sovereigns to borrow in international financial markets, as the bond yields show how high the interest rate would have had to be for these countries to attract buyers were they to try to issue new bonds. Nevertheless, some countries did issue such bonds, including El Salvador, which took on an apparently onerous debt burden in July 2020 when it raised US $1 billion through a bond that was scheduled to mature in 32 years, paying an annual interest rate of 9,5 per cent.[13] It is hard to believe that El Salvador will not have to restructure its obligations on that bond at some point and it seems that the buyers of the bond were in effect building that expectation into the interest rate they demanded to be paid. It is not something that borrowing governments should contemplate, as restructuring is costly. Indeed, Argentina's 100-year bond floated in 2017 did not last three years, as it was part of the debt restructuring negotiations completed in August 2020.[14]

Figure 3: Developing country sovereign bond spreads, 2019-2020 (Percentage point difference between high yield and investment grade bond yields)



Source: World Bank *Global Economic Prospects* (January 2021) 11

Note: Based on data collected for the Emerging Markets Bond Index, based on US dollar-denominated sovereign bonds issued by developing countries; high-yield and investment grade bonds were classified as per Moody's sovereign credit ratings.

Although private sources account for only about 13 per cent of the sovereign debt of low-income countries in aggregate, their share has been

13 'El Salvador sells cross-border bonds for coronavirus funding' *Latin Finance* (9 July 2020).

14 'Argentina's "preposterous" century bond never got chance to grow old' *Wall Street Journal* (31 August 2020).

growing (Figure 4). It has been expected – and the donor community has encouraged – that borrowing from international banks and through bond sales would take over much more of the external financing needs of low and middle-income countries in future, including in Africa.[15] The pandemic and its associated economic contraction has made this seem less likely in the immediate future.

The lower-income countries nevertheless borrowed more heavily in 2020 to cover the enlarged deficits shown in Figure 1 above. The loans came primarily from multilateral institutions, many of which were disbursed quickly. The IMF has led this effort, approving requests for loans by 85 countries totalling US $110 billion between March 2020 and April 2021.[16] It disbursed US $36 billion (including US $4 billion from prior loan programmes) just between 2 March and 31 July 2020. Regional monetary institutions also responded with increased loans, such as the Arab Monetary Fund, which committed US $1,2 billion to Egypt, Jordan, Morocco and Tunisia in 2020.[17]

In addition, the World Bank Group set up a fast-track COVID-19 facility in March 2020 to disburse up to US $14 billion for emergency support, as part of a US $160 billion commitment in counter-crisis loans that the Bank promised to make available over 15 months, of which US $50 billion would be highly concessional and some of that would be grants. From April to September 2020 the Bank committed US $64 billion of those funds, about 40 per cent of which were disbursed by September. On top of this, the Bank's board of executive directors approved an additional US $12 billion to help developing countries purchase and distribute an anti-virus vaccine.[18] In addition, the African Development Bank (AfDB) created the COVID-19 response facility in April 2020 to provide US $8,6 billion to governments and regional organisations plus another US $1,35 billion for loans to private sector operations in Africa.[19]

15 O Holmey 'Capital markets: Funding Africa's future' *Euromoney* (15 May 2019).

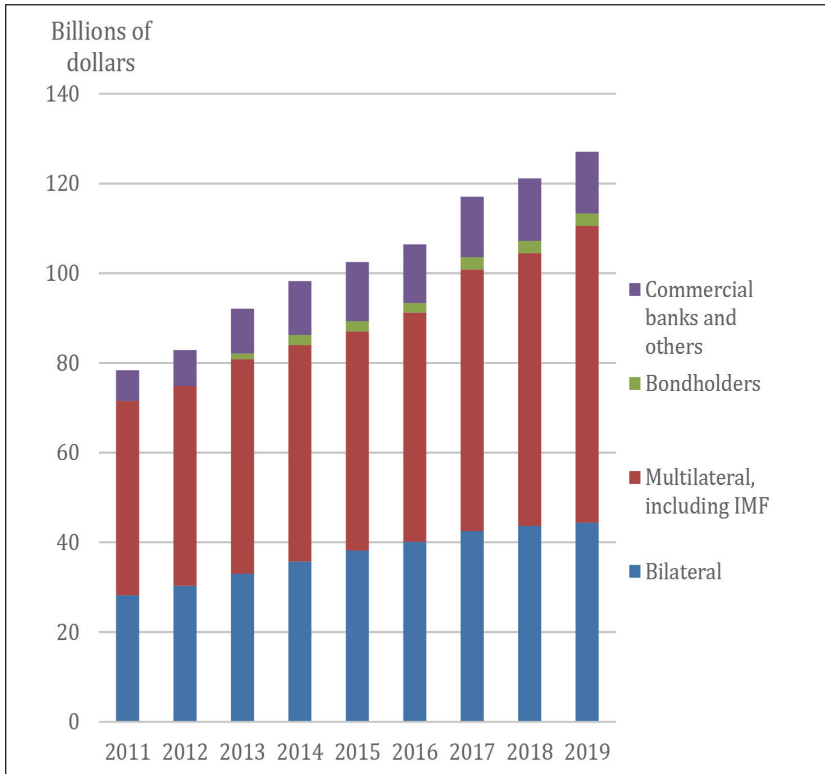
16 IMF 'COVID-19 financial assistance and debt service relief' updated 6 May 2021, https://www.imf.org/en/Topics/imf-and-covid19/COVID-Lending-Tracker (accessed 26 May 2021).

17 Arab Monetary Fund *Annual report* (2020) 14.

18 'Remarks by World Bank Group President David Malpass to the Annual Meetings 2020 Development Committee' (16 October 2020), https://www.worldbank.org/en/news/speech/2020/10/16/remarks-by-world-bank-group-president-david-malpass-to-the-annual-meetings-2020-development-committee.print (accessed 18 October 2020).

19 'African Development Bank Group unveils US $10 billion response facility to curb COVID-19' (8 April 2020), https://www.afdb.org/en/news-and-events/press-releases/african-development-bank-group-unveils-10-billion-response-facility-curb-

Figure 4: ***Composition of public and publicly guaranteed debt of low-income countries, 2011-2019***

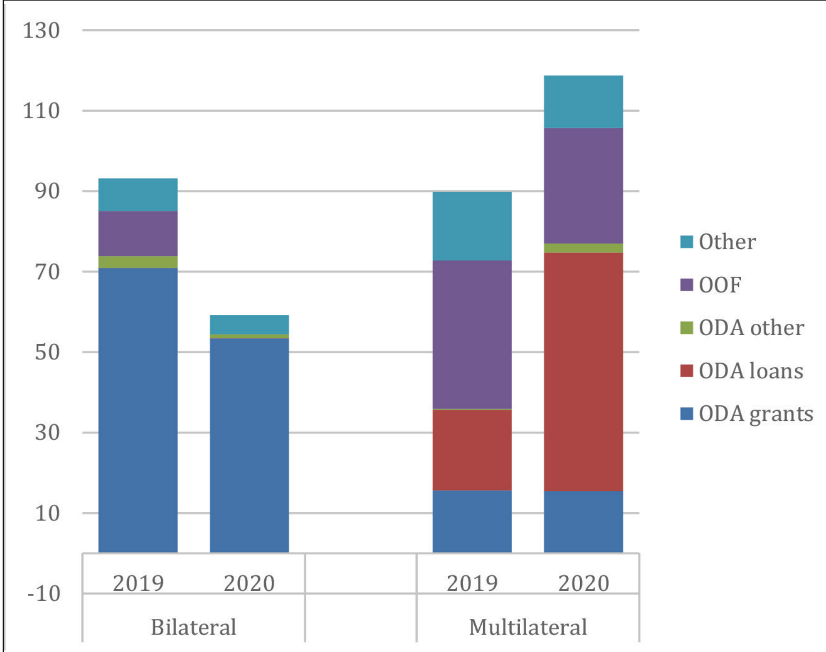


Source: Data of World Bank, *International Debt Statistics*, 2021

It is notable that the surge in official lending just described has come from multilateral sources. Indeed, commitments of assistance reported by public entities in individual donor countries declined in 2020, relative to 2019 (Figure 5). This is especially discouraging, as most of the bilateral official development assistance (ODA) flows are grants, while most of the multilateral ones are loans, although many are on highly-concessional terms. Indeed, the growth in multilateral funding was largely in terms of those concessional loans. In short, almost all the new financing of developing countries in 2020, including the new international bond issues by countries with market access and the new international institution lending, added to the foreign currency debt of those countries.

covid-19-35174 (accessed 18 October 2020).

Figure 5: ***Assistance commitments reported by official entities, January-November, 2019-2020 (Billions of US dollars)***



Source: Data of Development Initiatives, as of 12 February 2021, based on data submitted to the International Aid Transparency Initiative

Note: ODA is official development assistance; OOF (other official flows) are loans that do not qualify as ODA; 'other' are as reported and may include equity investment. Bilateral is government-to-government assistance commitments; multilateral include international financial institutions and development agencies, but excludes IMF lending.

Although not boosting grants in aid, the governments of the Group of 20 (G20) offered in April 2020 to postpone the interest and principal payments of 73 low-income countries that were scheduled to be paid to them from May to December (joined by the members of the Paris Club of government creditors that were not also members of the G20).[20] The offer was subsequently extended to June 2021 and then again in a final extension to December 2021.[21] The G20 'debt service suspension initiative'

20 Communiqué, G20 finance ministers and central bank governors meeting 15 April 2020, http://www.g20.utoronto.ca/2020/2020-g20-finance-0415.html (accessed 14 October 2020).

21 Communiqué, G20 finance ministers and central bank governors meeting, 14 October

(DSSI) functioned as a refinancing of payments rather than as an outright reduction in the debt or debt servicing owed. It provided temporary liquidity but did not ease the debt burden of the countries.

In the event, more than 40 countries requested to participate in DSSI, freeing up more than US $5 billion, not the US $12 billion envisaged.[22] Apparently the countries that did not apply to the DSSI took account of the increased debt servicing that their participation in the DSSI would require in the next few years. They were also concerned that taking G20 relief might unnerve their bondholders, who were not offering any debt-servicing suspension of their own.

The only actual debt service cancellation was offered by the IMF. It initially mobilised funds to pay the debt servicing owed to IMF between April and October 2020 by eligible low-income countries, using grants paid into its unique Catastrophe Containment and Relief Trust (CCRT).[23] The IMF executive board then extended this relief programme until April 2021, when it further extended the relief to October 2021, with the possibility of a further extension until April 2022.[24] While the principle of cancellation of obligations embodied in the CCRT is appropriate in the circumstances of the pandemic, the amount of funds freed for other uses was relatively small, as the 29 beneficiary countries have relatively small economies and the original terms of assistance to them had been generous. That is, US $251 million was cancelled in the period April to October 2020, a further US $237 million was cancelled in the period October 2020 to April 2021, and US $238 million was approved for cancellation from April to October 2021, with African countries receiving 83 per cent of the total.[25] If full

2020, http://www.g20.utoronto.ca/2020/2020-g20-finance-1014.html (accessed 15 October 2020); Communiqué, G20 finance ministers and central bank governors meeting 7 April 2021, https://www.g20.org/wp-content/uploads/2021/04/Communique-Second-G20-Finance-Ministers-and-Central-Bank-Governors-Meeting-7-April-2021.pdf (accessed 26 May 2021).

22 Leaders' Declaration G20 Riyadh Summit, 21-22 November 2020 para 7, https://www.g20riyadhsummit.org/pressroom/?pressroom-category=declarations (accessed 3 January 2021).

23 T Stubbs et al 'Whatever it takes? The global financial safety net, COVID-19, and developing countries' (2021) 137 *World Development* 105171.

24 IMF Press release 20/304 (5 October 2020), https://www.imf.org/en/News/Articles/2020/10/02/pr20304-imf-executive-board-extends-immediate-debt-service-relief-28-eligible-lics-six-months (accessed 17 October 2020); IMF Press release 21/99 (5 April 2021), https://www.imf.org/en/News/Articles/2021/04/05/pr2199-imf-executive-board-extends-debt-service-relief-28-eligible-lics-october-15-2021 (accessed 26 May 2021).

25 Data of IMF (n 16).

relief is granted until April 2022, IMF will have cancelled US $964 million in repayment obligations.

While helpful to the beneficiary countries during the emergency in 2020 to 2021, the G20 and CCRT relief offers have not been adequate. No less than the managing director of IMF, her general counsel and a senior World Bank official expressed concern about a coming wave of sovereign insolvencies and urgently called for action on a set of reforms to improve the negotiating processes for restructuring developing country debt obligations.[26] As with previously recommended reforms in sovereign debt negotiations, these proposals may help if adopted.[27] They are, nevertheless, short of a warranted systemic reform of debt crisis workouts.

The IMF was not alone in its concern, as in November 2020 the finance ministers and central bank governors of the G20 took an additional step (joined again by the government creditors in the Paris Club that were not also G20 members). They published a 'common framework for debt treatments beyond the DSSI',[28] which offers to negotiate additional relief for any of the countries eligible for the DSSI. The new relief would free up some fiscal resources and foreign exchange payment obligations, and thus in effect compliment the funding that the IMF would make available for its adjustment programmes. The relief would apply during the IMF programme period, which could range from one to five years. The negotiation of the actual debt restructuring would apparently operate much like the Paris Club in that the creditor governments would jointly agree to a memorandum of understanding with the debtor that specified the overall terms of the relief, the details of which the debtor would then negotiate with each creditor individually. The debtor would pledge to seek comparable treatment from its other official and private creditors, not including its multilateral creditors. Finally – and most importantly – China was understood to have agreed to participate in the common framework.

26 K Georgieva, C Pazarbasioglu & R Weeks-Brown 'Reform of the international debt architecture is urgently needed' IMF Blog (1 October 2020), https://blogs.imf.org/2020/10/01/reform-of-the-international-debt-architecture-is-urgently-needed/ (accessed 21 October 2020).

27 IMF 'The international architecture for resolving sovereign debt involving private-sector creditors – Recent developments, challenges, and reform options' (23 September 2020), https://www.imf.org/en/Publications/Policy-Papers/Issues/2020/09/30/The-International-Architecture-for-Resolving-Sovereign-Debt-Involving-Private-Sector-49796?utm_medium=email&utm_source=govdelivery (accessed 22 October 2020).

28 Statement, Extraordinary G20 Finance Ministers and Central Bank Governors' Meeting (13 November 2020), https://www.mof.go.jp/english/international_policy/convention/g20/g20_201113_1.pdf (accessed 3 January 2021) Annex I.

Only in 'the most difficult cases' would the creditor governments operating under the common framework contemplate any outright cancellation of debts owed to them, rather than merely rescheduling repayments. Furthermore, the G20 statement notes that there is no consensus on how relief from obligations to the multilateral institutions might be conferred, as none was agreed. Readers familiar with the history of the initiative for the heavily-indebted poor countries and the multilateral debt relief initiative will perhaps see the common framework as being only the first step in a tortured but ultimately inescapable path to creditor recognition of the need for deeper relief, including multilateral debt relief.[29]

2.2.2 Towards a reform agenda

Would it not be valuable if these debt crises could be avoided in the next catastrophe? Could not the international community adopt ways to reduce the number of countries that are forced to renegotiate their sovereign debt after they seek to respond responsibly to a crisis they had not caused, such as the COVID-19 pandemic? For that to happen, the international community needs to be able to expand the amount of non-debt creating sources of financing for developing countries in crisis and offer to cancel or postpone the obligation to pay interest and principal falling due on at least certain categories of sovereign debt of certain countries during crises.

The traditional mechanism for assisting countries that have been pushed into emergencies is government-to-government grant assistance. This mechanism depends on political relationships among countries and feelings of generosity or responsibility and may or may not operate sufficiently in times of national or regional catastrophes. In a global pandemic, moreover, the constraints on the budgets of many donor governments may severely constrain their capacity to assist developing countries in need.

However, there is an international mechanism that can help. It would increase the global stock of an international reserve asset that can help meet the need for emergency supplies of foreign exchange across a wide swath of countries, as has been the case in this pandemic. It is called the special drawing right (SDR) and is created by agreement of the IMF board of governors.[30] The IMF managing director proposed and most countries

29 On that history, see E Cosío-Pascal 'Paris Club: Intergovernmental relations in debt restructuring' in Herman et al (n 8) 231.

30 B Herman 'What you really need to know about the SDR and how to make it work for multilateral financing of developing countries' (2020) 64 *Challenge* 286.

supported an allocation of SDRs, which took effect on 23 August 2021.[31] It might have been agreed in 2020, but the US administration at the time opposed it. The subsequent administration adopted a more positive view. There had been an emergency infusion of SDRs in response to the global financial crisis in 2009 and perhaps such allocations will be made in the future, as the SDR is a good tool for global emergencies. While the SDR was created in the late 1960s to meet a different need, IMF member states should consider how to repurpose this instrument for global emergencies.

However, even with support from this international non-debt creating source, developing country governments will need – and will seek – to boost counter-crisis spending by reallocating domestic expenditures, postponing what can be postponed and rethinking public expenditure priorities. One expenditure that governments do not voluntarily postpone is debt servicing. Usually, the fear that skipping debt servicing payments would cause creditors to cut off access to new loans is enough for governments to do everything in their power to make all payments falling due. Skipping payments to foreign creditors also has legal consequences that can be costly to cure.

The DSSI initiative was an offer by G20 countries to relieve a number of low-income countries from pressure to make the difficult decision to delay payment unilaterally, at least on debts owed to G20 governments. In its DSSI, the G20 called for comparable treatment by the private creditors (and pleaded with the multilateral lenders to contribute to the effort) indicating that the G20 was aware that while offering only bilateral official relief might help fight the pandemic, it also helped to assure enough resources to pay the other creditors. This is easily seen as an unfair public subsidy of private lenders. Nevertheless, no private creditors have stepped forward to voluntarily share the burden with the G20 governments. Investors may or may not be devoid of social conscience, but they can legitimately complain that no one told them such a situation could arise when they bought the bonds. In other words, private lenders need to learn to appreciate that there are circumstances in which they would have to join others in a collective sacrifice to address a higher need. One makes such an arrangement explicit by putting it into the bond and loan contracts.

31 IMF Press release 21/235 2 August 2021 https://www.imf.org/en/News/Articles/2021/07/30/pr21235-imf-governors-approve-a-historic-us-650-billion-sdr-allocation-of-special-drawing-rights (accessed 25 August 2021).

2.3 Financial terms of sovereign borrowing instruments

Any non-payment on a standard debt contract violates the contract and sets up a potential legal contest. The typical contract will say the obligation to pay is fully on the head of the borrower no matter what the state of the world. This is the problem that a different bond contract should seek to ameliorate.

2.3.1 The variety of existing instruments

The first thing to note is that the standard loan contract with its fixed schedule of repayments is not the only model of the lender-borrower relationship. Islamic finance has addressed Islam's prohibition against receiving fixed interest on loans by developing a distinct set of Shari'a-compliant financial instruments, including a medium-to-long-term security known as *sukuk*.[32] The issuer of *sukuk* securities offers for a fixed period an equity-like stake in the project for which the money is borrowed. Instead of interest on the loan, the borrower would receive a specified share of the profit earned on the asset purchased with the proceeds of the *sukuk*. The *sukuk* issuer needs to specify what assets or what project is to be financed by the money. For example, the investor could receive a fixed share of rental income from public housing on land purchased with the proceeds of the *sukuk*. In this way, the borrower would *ipso facto* share in the annual fluctuations in revenue or the loss should the project fail.[33]

Indeed, a thriving sovereign *sukuk* market exists, both domestically, as in Malaysia,[34] and internationally, with an estimated US $109 billion of *sukuk* issued in 2020.[35] While most sovereign issuers are based in Islamic

32 D Dey '*Sukuk* on the world stage' (2014) *The Treasurer* Winter 16; AR Wedderburn-Day 'Sovereign *sukuk*: Adaptation and innovation' (2010) 73 *Law and Contemporary Problems* 325.

33 In an 'asset-based' *sukuk*, the investors do not own the asset but rather enjoy beneficial ownership of the income it produces and thus cannot take over the asset should the project fail, similar to sovereign-risk bonds. This can be compared to an 'asset-backed' *sukuk*, which is more like a collateralised loan (see Bank Alkhair 'Sovereign's infrastructure projects: financing solutions' (November 2015), http://pubdocs.worldbank.org/en/241031448479778427/pdf/islamic-finance-2015-11-18-Ayman-Sejiny.pdf (accessed 24 October 2020).

34 'Malaysian government hails "solidarity" of population for supporting *sukuk* scheme' *Public Finance Focus* (25 September 2020).

35 'Global *sukuk* issuance to pull back from record highs in 2021 as financing needs ease' Moody's Investor Service (24 February 2021), https://www.moodys.com/research/Moodys-Global-sukuk-issuance-to-pull-back-from-record-highs--PBC_1267243

majority countries, other countries are also tapping the *sukuk* market. For example, South Africa issued a US $500 million *sukuk* in 2014 carrying a profit rate of 3,9 per cent with a maturity of 5,75 years.[36]

While there is a growing demand for *sukuk* in domestic and international currencies, most governments mainly borrow by issuing conventional sovereign-risk securities or borrow from banks, the IMF or other official providers, offering no collateral and only the sovereign's promise to repay. There is, however, a class of standard public securities that has one of the features of *sukuk*, namely, that the investor lends money for a specific project, such as a toll road or airport, whose revenues are meant to provide the funds to pay the interest and principal on the bond. In some instances, revenue bonds may be further like *sukuk* in that holders of those bonds are given no recourse to the government in the event of project failure but only to the project itself.[37]

There has been growing interest in bonds that, like *sukuk*, have a targeted use of the funds. In those bonds, issuers pledge to use the proceeds for named social or environmental purposes and furthermore pledge to monitor that the supported projects do meet the relevant criteria.[38] In one variant, the 'social revenue bond', bondholders would be paid from the revenue stream, fees or taxes associated with the projects supported by the bond and bondholders would have no recourse to the issuer in case of project failure. It does not seem, however, that this variant, which is closest in design to the *sukuk*, will become the standard for this type of sovereign debt. For example, investors will have full recourse to the European Union (EU) for interest and principal on its €100 billion social bond issue to support anti-pandemic programmes in 16 EU countries.[39]

However, while project-specific borrowing has an important place in public finance, governments typically also seek unrestricted financing to cover budget deficits for which they issue general obligation bonds (and

(accessed 26 May 2021).

36 'South Africa working on rand-denominated *sukuk* issue' *Salam Gateway* (7 May 2020).

37 AD Flachsbart 'Municipal bonds in bankruptcy § 902(2) and the proper scope of "special revenues" in chapter 9' (2015) 72 *Washington and Lee Law Review* 955.

38 See 'Social bond principles: Voluntary process guidelines for issuing social bonds' International Capital Markets Association (June 2020), https://www.icmagroup.org/assets/documents/Regulatory/Green-Bonds/June-2020/Social-Bond-PrinciplesJune-2020-090620.pdf (accessed 29 October 2020). Comparable guidelines exist for 'green' and 'sustainability' bonds.

39 See 'European Commission to issue EU SURE bonds of up to €100 billion as social bonds' European Commission press release (7 October 2020), https://ec.europa.eu/commission/presscorner/detail/en/ip_20_1808 (accessed 29 October 2020).

short-term notes). Governments typically offer market investors and bank lenders a range of debt instruments with a variety of maturities and specifications of the periodic interest payments. As the relative use of different designs has implications for the overall risk and cost of the government's debt, it has inspired a literature on sound sovereign debt management,[40] and even a theory of the optimal debt portfolio for a sovereign.[41]

Yet not all countries can issue all types of general obligation debt instruments or, rather, cannot issue every instrument at reasonable cost. For example, long-dated bonds are attractive to governments as they delay repaying the principal or rolling over the maturing bond with a new issue. At the time of maturity, will the government be short of funds or will the market demand a high interest rate for the new bond issue? No one can know the answers and the terms of a long-dated bond when initially sold to the public will reflect that uncertainty. For example, the 9,5 per cent annual interest rate on the aforementioned El Salvador 32-year bond reflected that uncertainty. On the other hand, it has been proposed that India could issue at reasonable cost perpetual bonds that never mature, saving the government the need to ever worry about maturity or refinancing risk.[42]

Usually, when innovations depart from standard bond structures, it is to reduce the risk that investors fear they would face in buying a standard bond. For example, there is a long history of protecting bond investors and bank lenders from inflation. That is, the terms of the bond or loan would specify an inflation adjustment to the interest and/or principal payments to compensate the investor for inflation's erosion of the value of the asset.[43] In contrast, there are very few instances of bond or loan structures that intend for investors to share additional risk with the borrowing government, although there are some, as will be discussed

40 T Jonasson et al 'Debt management' in A Abbas, A Pienkowski & K Rogoff (eds) *Sovereign debt: A guide for economists and practitioners* (2020) 192.

41 R Greenwood et al 'The optimal maturity of government debt' in D Wessel (ed) *The $13 trillion question: Managing the US government's debt* (2015) 1.

42 S Mukherjee 'Sovereign perpetual bonds: An idea whose time has come' *The Economic Times* (5 January 2021).

43 While inflation rates have fallen substantially around the world, there remains a significant market for inflation-linked bonds, including in developed economies, such as the United States, and in many emerging economies. On the former, see 'Treasury inflation-protected securities (TIPS)', https://www.treasurydirect.gov/indiv/products/prod_tips_glance.htm (accessed 24 October 2020), and on the latter, see N Upadhyay & O Yangol 'Inflation-linked bonds in emerging markets' (May 2019) HSBC Global asset management, https://investorfunds.us.hsbc.com/resources/documents/articles/EMD/AMUS_Article_EM%20ILB_May19_FINALCopy.pdf (accessed 24 October 2020).

below. The argument of this chapter is that such instruments should be much more common.

2.3.2 Additional instruments for sharing risk with lenders

There are various proposals and some examples of financial instruments in which bond buyers and lenders would share some of the risk of negative developments that developing country governments need to manage but ultimately cannot control. One proposed bond would link the interest it paid to movements in the country's overall economic output. The standard approach in this model is to tie the interest coupon to changes in the growth of the country's GDP.[44] Advocates of this proposal note that the bondholders would not only share the disappointment of poor GDP growth or outright decline, but would also share in the benefit of strong GDP growth. Nevertheless, although a term sheet was drafted for such GDP-linked bonds,[45] no country has stepped forward to issue one yet. One reason is that in addition to the uncertainty of the impact of actual events and policies on economic growth, bond investors appear reluctant to trust that the national account statistics that would determine their interest income would be free from manipulation. They would probably demand an interest premium to overcome that reluctance.

This notwithstanding, in workouts from sovereign insolvency, bondholders have accepted as a 'sweetener' in the new deal inclusion of a warrant that would pay an interest premium based on GDP growing more rapidly than had been expected. This benefit may be viewed as a possible partial offset to the loss in the face value of the new securities that replaced defaulted old ones. Indeed, in 2005 76 per cent of Argentina's bondholders accepted to swap defaulted bonds for new bonds carrying a warrant that would pay a premium if real GDP growth exceeded 3 per cent per annum, which it did.[46]

44 Perhaps the greatest attention paid to this proposal followed the publication of a study authored by a team from the Bank of England, the Bank of Canada and the Central Bank of Argentina, 'Sovereign GDP-linked bonds' (September 2016) Bank of England Financial Stability Paper 39, https://www.bankofengland.co.uk/-/media/boe/files/financial-stability-paper/2016/sovereign-gdp-linked-bonds.pdf (accessed 4 January 2021).

45 'Indicative term sheet – GDP bonds' (London term sheet – English law version 2017) Allen & Overy LLP https://www.icmagroup.org/assets/documents/Resources/Open-docs/GDP_Termsheet_140317.pdf (accessed 24 October 2020).

46 One additional attractive feature is that the warrants could be detached from the bonds and sold by bondholders who did not want to hold speculative assets. On the Argentine case, plus Greece and Ukraine, see SK Park & TR Samples 'Towards sovereign equity' (2016) 21 *Stanford Journal of Law, Business and Finance* 241.

This is all well and good, but a complete deferral or cancellation of debt servicing rather than a reduction may be required during catastrophes. Moreover, dependence on GDP linking is likely to delay the debt service reduction if creditors need to see the actual fall in GDP before accepting the reduced government obligation, as even preliminary data would likely not be reported for several months after the initial shock. The need is for a faster-acting escape clause.

There is an argument that sovereign bonds and loans implicitly already have a catastrophe-based escape clause that would at least temporarily defer debt servicing, although the argument has not been tested in the courts. This argument invokes the international legal concept of 'necessity'. That is, if a sovereign unilaterally deferred debt servicing and one or more of its creditors challenged that in court, the country could invoke necessity as a warranted reason for non-payment during the emergency.[47] While people might quibble whether the emergency actually warranted invoking necessity, it would take a very hard-hearted judge to find for the bondholder in the current situation or in the face of how hurricanes have decimated certain islands in the Caribbean or how food deficits have been exacerbated in Africa owing to drought. Moreover, the delay in payments would be acceptable only for the duration of the crisis, so it might be that creditors would decide to wait and then seek payment rather than immediately press their case in court.

One drawback, however, is that the concept of necessity is said to derive from customary international law, whereas sovereign bonds and loan contracts with private creditors typically specify the municipal law of a specific country as the applicable law for adjudicating disputes.[48] While this might challenge the applicability of the concept to privately held financial instruments, 'necessity' might apply to inter-state debt obligations or to payments owed to international institutions. In fact, we look to those parties to voluntarily step forward to assist developing countries during emergencies such as the current pandemic. As discussed above, limited debt suspension is already a policy of the G20 for inter-state debt and the CCRT is being used to take over payment obligations of certain countries to the IMF. Nevertheless, the concept of necessity – along with a range of desirable considerations of soft law – could be applied to sovereign debts owed to private creditors by explicitly writing them into bond and loan contracts.[49]

47 M Weidemaier & M Gulati 'Necessity and the COVID-19 pandemic' (2020) 15 *Capital Markets Law Journal* 277.

48 As above.

49 SL Schwarcz 'Soft law as governing law' (2020) 104 *Minnesota Law Review* 2471.

In fact, a step in the direction of recognising the concept of necessity in sovereign bond contracts has been taken in the drafting of a model contract that specifies a trigger mechanism that would allow the debtor to defer payments falling due. In this case, a term sheet was drafted for bonds of countries subject to hurricanes, leaving the determination that a debt-deferring event occurred to the decision of an independent body, the Caribbean Catastrophe Risk Insurance Facility.[50] Such terms were introduced into the new bonds that emerged from the debt restructurings of Grenada in 2015 and Barbados in 2019.[51] While bondholders were under pressure to include these clauses as part of the negotiations to resolve the insolvency of the two countries, comparable clauses will apparently be included in subsequent Barbadian bonds, based on the precedent of its debt-restructuring bonds.[52] It will be interesting if the precedent from these two countries carries over to other vulnerable island nations.

A different contingency mechanism has been developed for a class of bilateral official loans, specifically loans that the development ministry of France offers to a group of low-income African countries. These loans, called *prêts très concessionnel contracyclique* (PTCC), were designed as a variant of one of France's standard concessional long-term loans for low-income countries, which have a 10-year grace period and 30-year final maturity. The innovation was to shorten the grace period to an initial five years and allow the borrower to defer ten semi-annual principal payments at any time in the remaining 20-year duration of the loan (if the full deferral were taken, the final maturity would be 30 years as before; interest accrues on the deferred payments). While the decision to defer is left to the borrowing government, a specified economic stress needs to occur to open its availability, such as a collapse in the international price of the country's main commodity export. As of 2016, 16 of these loans worth €344 million had been extended to five African countries.[53]

50 'Indicative heads of terms for extendible hurricane bonds (coupon-preserving maturity extension version-bullet structure)' Clifford Chance and International Capital Markets Association (23 November 2018), https://www.icmagroup.org/assets/documents/Resources/Indicative-Heads-of-Terms-for-Hurricane-Bonds---Bullet-271118.pdf (accessed 25 October 2020).

51 T Asonuma et al 'Sovereign debt restructurings in Grenada: Causes, processes, outcomes, and lessons learned' (2018) 10 *Journal of Banking and Financial Economics* 67; M Anthony, G Impavido & B van Selm 'Barbados' 2018–19 sovereign debt restructuring – A sea change? (2020) IMF Working Paper 20/34 https://www.imf.org/en/Publications/WP/Issues/2020/02/21/Barbados-201819-Sovereign-Debt-RestructuringA-Sea-Change-49044 (accessed 25 October 2020).

52 Avinash Persaud, Chairperson Barbados Financial Services Commission, statement at 'D-DebtCon' (15 September 2020), https://vimeo.com/460146794/46440cf45e (accessed 25 October 2020).

53 The trigger mechanism to allow the moratorium to be invoked is specified in the loan

Apparently, the pandemic would not qualify as a reason to invoke the PTCC payment deferral, as the contingency specified usually pertains to disappointing export earnings (nor would it be necessary now as France is participating in the G20 deferral of debt servicing). In addition, Barbados has sought pandemic debt relief, but it has been told that the relief will not be coming owing to its relatively high level of income per capita among emerging economies.[54] However, relatively high income per capita was not a barrier to inclusion of the hurricane clause in Barbadian bonds, as Barbados is also highly vulnerable to massive weather destruction. The problem was that Barbados was not facing a hurricane in 2020 and there was no provision for debt deferral under any other circumstances. Such bonds are quite specific in what catastrophes they cover.

This brings us, finally, to the limit of the current approaches to what economists refer to as 'state-contingent' debt for developing countries. While the overall GDP link has not found favour among private investors, the triggers that have found favour for debt-servicing deferral are very narrowly and carefully drafted. In particular, the hurricane clauses specify in detail how a country would qualify for relief, leaving no room for interpretation, no room for nuances. Anything less precise puts an extra measure of uncertainty into the valuation of the financial instrument, which reduces its price and raises its yield in the financial markets where sovereign bonds are actively traded.

It seems, in conclusion, that the contractual approach to debt relief needs to be refined with an enabling clause that would recognise the concept of 'necessity' and specify how necessity would be specified in practice, which is discussed in the next part of this chapter. The clause might also say whether the relief would entail a specified deferral or cancellation of payments. If this proposal raised risk premia on sovereign bonds of developing countries, it would only reflect risks that really exist, which seems an improvement over the current practice of risks ignored by creditors and borne only by the sovereign.

contract. A detailed analysis of the loan structure was prepared for the Commonwealth Secretariat. In the end, no British version of the loan was offered to developing countries. See 'Extending countercyclical loans: Lessons from Agence Française de Développement (2016) Commonwealth Secretariat, http://thecommonwealth.org/sites/default/files/inline/Extending%20countercyclical_0.PDF (accessed 25 October 2020).

54 'Barbados told not to expect debt relief' *Barbados Today* (10 October 2020).

2.4 Toward a stronger international policy mechanism

A way is evidently needed to trigger sufficient sovereign debt relief in a catastrophe, and addressing it is unavoidably political. However, that should not be a discouragement as the world's governments do periodically mobilise themselves for collective international reform, even if imperfectly. We have seen this several times in recent years, from the responses to the global financial crisis to the Ebola crisis in West Africa to the extreme hurricanes in the Caribbean and now to the pandemic. Indeed, the excessive increases in the sovereign debt burdens of developing countries in 2020 should stimulate the design of an improved approach that might be applied in future catastrophes.

2.4.1 Engaging private creditors in relief through IMF assessment of need

One weakness in the current approach pertains to the private creditors. As noted earlier, the G20 governments offered to suspend for a short period the debt servicing owed to themselves by a limited number of countries. The G20 invited bondholders and banks to join them but they were not required to also provide debt relief. The most striking feature of the private creditor response was no response. They clearly need a stronger incentive to join in the relief. IMF has a potential tool to deploy here.

If the IMF judges a country to have sovereign debt that is unsustainable or if the country is assessed as 'sustainable with low probability' and seeks exceptional access to IMF loans (loans above its normal quota), then the IMF requires that the private creditors of that country restructure the country's obligations as a condition for the country receiving the additional IMF funds.[55] This imposes essentially a political rather than a legal obligation on the private creditors, indeed, one that all the governments of the member countries of the IMF *ipso facto* endorse when IMF's executive board, on which all member countries are represented, grants the loan.

It is not likely that a disgruntled bondholder who went to court to collect a missed debt payment would receive a favourable response in such a situation of active international cooperation to ease the debt constraint

55 This may entail negotiated debt reductions or 'reprofiling' (ie rescheduling) payments depending on the severity of the debt difficulty. See IMF 'The Fund's lending framework and sovereign debt – Further considerations' (9 April 2015), https://www.imf.org/en/Publications/Policy-Papers/Issues/2016/12/31/The-Fund-s-Lending-Framework-and-Sovereign-Debt-Further-Considerations-PP5015 (accessed 26 October 2020).

on the country, especially when the debtor and its cooperating creditors are simultaneously seeking to reach an agreed restructuring arrangement. The recalcitrant bondholders would thus be incentivised to join the effort to negotiate a restructuring of repayments.[56] This is a feature on which to build.

The IMF annually assesses the debt sustainability and other aspects of the macro-economic situation of its member countries (working jointly with the World Bank on the low-income countries). Based on these analyses, when a catastrophe erupts and is so identified, countries seeking emergency assistance and emergency debt relief may be quickly certified as warranting assistance. As the current experience has shown, IMF staff can quickly assess the need for a quick-disbursing loan, reach a decision on it in the executive board and disburse the emergency funds.[57]

We may thus propose that in future the executive board decisions that approve emergency loans should include statements, where warranted, calling for private creditor participation in the emergency relief. On that basis, the debtor government would be empowered to withhold the debt servicing payments falling due to its private creditors. Implicitly, if not explicitly, the government that then did not make a payment would be invoking the concept of 'necessity' that was noted earlier, now validated by the IMF assessment. This should discourage bondholders from rushing to the court house. The government would in any case be expected to enter discussions with its creditors on a timely basis on how its missed payments would be reprogrammed or cancelled.

We should acknowledge at this point that an IMF decision on granting an emergency loan and debt relief to a member country is unavoidably political. That is, appreciating the technical expertise of IMF staff and hoping for the apolitical character of their recommendations, the actual IMF decisions are made by the government representatives that sit on the executive board. While all member countries are represented on the board (most through constituencies, only one of whose members actually sits on the board), country votes are unevenly distributed and the individual members with the most votes are perforce the most influential. While the board has a tradition of seeking consensus decisions,[58] certain board

56 This should be complemented by legislation in the major creditor countries to discourage 'vulture funds' from disrupting collective creditor decisions; see IMF (n 27) paras 46-47.

57 See IMF (n 16).

58 L van Houtven *Governance of the IMF: Decision making, institutional oversight, transparency, and accountability* (2002) 20-31.

members with a large number of votes and strong political feelings about one or another IMF member country or about a policy of that country could block it from receiving a loan. That was Iran's experience in 2020.[59]

Acknowledging that the IMF thus is a 'political' institution, one may ask whether it would be more appropriate that the Security Council of the United Nations (UN), the primary international political institution, should instead be making the decisions in the loan/debt relief process. There is a reason to argue that it should in that a Security Council resolution has the force of law on all member states of the UN, which opens a path to a legally-enforceable debt moratorium on private creditors of developing countries.

There is also a precedent for engagement of the Security Council arising from the case of Iraq. In 2003 the Security Council adopted Resolution 1483, which prohibited any creditor from attaching any of Iraq's oil exports during a specified period as a way to preserve its oil earnings for its economic recovery and to push the creditors to step away from the courts and negotiate a restructuring with the government to resolve their claims against the country.[60] The prohibition on attaching Iraqi assets thus had the force of law, although it was debated whether this was the case in the United States absent implementing US legislation.[61]

It does not seem, however, that the Security Council would be a propitious body for dealing with developing country debt situations. Certainly, the Council would be susceptible to blocking action by one or another of its members with veto power. It would also be unusual for the Council to assert competence to render decisions on economic and financial matters that did not have a direct security dimension, as had been the case regarding Iraq. We thus set aside this approach and propose that IMF be responsible for triggering the release of warranted relief from servicing sovereign bonds and private-sourced loans, with the hope that transparency and global solidarity might limit the number of times

59 'Iran's Rouhani says US blocking $5 billion IMF loan to fight COVID' *Iran International* (12 September 2020).

60 S Hinrichsen 'Tracing Iraqi sovereign debt through defaults and restructuring' (2019) London School of Economics and Political Science Economic History Working Paper 304, https://www.lse.ac.uk/Economic-History/Assets/Documents/WorkingPapers/Economic-History/2019/WP304.pdf (accessed 26 October 2020).

61 FL Kirgis 'Security Council Resolution 1483 on the rebuilding of Iraq' (2003) 8 *ASIL Insights*.

that unrelated political issues would trump urgent human-rights based obligations.

2.4.2 Engaging international official lenders to expand relief

In addition to engaging the private sector in sovereign debt relief, there are some country debt situations in which relief will not be deep enough unless the obligations to international financial institutions are also included. Indeed, the G20 explicitly called for their participation.[62] However, the IMF is alone among these institutions to have arranged such relief, albeit for only 29 of the poorest countries through its CCRT, as noted earlier.

While declining to offer any comparable relief, the World Bank instead promised to deliver a net positive cash flow to each of its client countries; that is, the Bank promised that the total disbursements from new and existing loans (and grants for the poorest) from the World Bank Group of institutions would exceed the interest and principal payments falling due.[63] The Bank's approach, however, seems most unhelpful. While it provided a net transfer of financial resources during 2020, it further raised the countries' debt.[64]

The reluctance of the World Bank and the other international development banks to offer relief has been attributed to a fear that if they relieve repayment obligations of their poorest developing country clients, they will pay for it in future. This is based on a fear of how such relief would impact the primary business model of the banks. That is, in the loan programmes for mainly middle-income countries, which is the bulk of their business, the banks essentially function as a financial intermediary, borrowing cheaply in financial markets and then loaning out the funds at an interest rate that covers the borrowing cost of the banks plus a mark-up to cover the cost of administering the institution. The arrangement is attractive to the client countries because the development banks can borrow at substantially lower interest rates and for longer maturities than the borrowing countries.

62 Communiqué, G20 finance ministers (n 20) 7; October Communiqué (n 21) 7.

63 'World Bank COVID-19 response' Factsheet (14 October 2020), https://www.worldbank.org/en/news/factsheet/2020/10/14/world-bank-covid-19-response (accessed 26 October 2020).

64 In the event, most bank clients received a net positive transfer of financial resources in 2020, but not all. See J Duggan et al 'Is the World Bank's COVID-19 crisis lending big enough, fast enough? New evidence on loan disbursements' (2020) Centre for Global Development Working Paper 554, https://www.cgdev.org/sites/default/files/world-banks-covid-crisis-lending-big-enough-fast-enough-new-evidence-loan-disbursements.pdf (accessed 26 October 2020).

In fact, the bonds of the international development banks are mostly rated AAA and carry very low interest rates because the financial markets know that the government shareholders of the banks, including the world's richest countries, have arranged for a strong level of paid-in shareholder equity, backed by the legal obligation to pay the callable portion of shareholder subscriptions if needed. The fear, as stated by the World Bank president, nevertheless is that granting relief from the obligations of any of its client countries would make investors who buy their bonds fear that the bonds had greater risk of default than previously thought and that investors would thus demand higher interest coupons on subsequent bond issues.[65]

The intention of the G20 was only to offer relief to the poorest countries, whose loans from the development banks are, in fact, not primarily funded by bond issues. Loans to low-income countries are largely funded by triennial replenishment contributions by high-income shareholder governments, recycled loan repayments and a share of profits from loans to middle-income countries. It thus must be that the World Bank worried that offering relief to the poorest countries would set a precedent that would lead to relief for middle-income borrowers, whose repayment obligations are larger. The G20 acknowledged this concern in its invitation to the development banks to participate in DSSI. It stated that their participation should not impair the current high market ratings of their bonds and low cost of funding.[66] However, it strains belief that the major shareholder governments of the World Bank and the regional development banks – which are members of the G20 – would allow the institutions, which are well capitalised, to miss a coupon payment. Moreover, the DSSI offered only to postpone debt servicing, not cancel it, and only for the lowest income countries.

In other words, one might propose that if the G20 actually wished for World Bank and regional bank participation in the DSSI programme, it should have given assurances in its Communiqués that would have assuaged any bondholder fears of heightened 'credit risk' (risk of non-payment) in their bonds. Alternatively, the G20 could have motivated the World Bank and the regional banks to adopt variants of the CCRT, wherein donors would pay the debt servicing for a target group of debtor

65 'World Bank Group President David Malpass: Remarks at high-level event on financing for development in the era of COVID-19 and beyond' (28 May 2020), https://www.worldbank.org/en/news/speech/2020/05/28/world-bank-group-president-david-malpass-remarks-at-high-level-event-on-financing-for-development-in-the-era-of-covid-19-and-beyond (accessed 27 October 2020).

66 Communiqué, G20 finance ministers (n 20) 7; October Communiqué (n 21) 7.

countries so that the institutions would have received their payments while the debtor obligations would have been cancelled.

Should the development banks create CCRT-like facilities, additional funding would be required, the traditional source of which has been donor country aid budgets. However, as bilateral aid flows are also necessary components of the catastrophe response, there is a high opportunity cost of this financing source. There is an alternative: The funds to cover multilateral debt relief could be drawn from SDR balances held at the IMF by rich countries.[67] For example, almost all the countries that are eligible for DSSI relief borrow from the International Development Association (IDA), the concessional lending arm of the World Bank Group.[68] IDA is a 'prescribed holder' of SDRs, meaning that G20 members can transfer some of their holding of SDRs to IDA, which could use them to cover the interest and repayment obligations coming due. However, IDA lends 'hard' currencies, not SDRs, and so one might expect IDA to return the SDRs to the donor government in exchange for the equivalent in hard currency. In effect, the donor would thus reduce the share of its reserves in hard currency and increase the share in SDRs. In fact, governments could directly transfer some of their foreign exchange reserves without reducing total reserves in light of having received their SDRs.[69]

Governments holding surplus SDRs have actually been considering a different approach, wherein potential SDR recyclers would loan their SDRs but insist they maintain their reserve nature, which is to say be assured that the SDRs have virtually zero risk of losing value or liquidity (i.e., being immediately exchangeable into a hard currency) and can also be immediately returned to the providing country on demand.[70] SDRs could be lent to an institution for some agreed period, such as the duration of its regular replenishment cycle, and thus expand its lending capacity during that cycle. This approach, however, would add to borrowing country debt, not reduce its debt servicing.

67 B Herman 'An easy way to provide debt relief for the world's poorest countries' *The Globalist* (17 July 2020).

68 Angola is the one exception; while it is eligible for DSSI as a member of the group of least developed countries, it graduated from eligibility to draw from IDA in 2014 (World Bank 'IDA graduates', http://ida.worldbank.org/about/ida-graduates (accessed 8 January 2021).

69 'Using the United Kingdom's SDRs to tackle Covid-19 and climate change' Catholic Agency for Overseas Development (May 2021) https://cafod.org.uk/content/download/56376/774304/version/1/file/Using%20the%20UK%20SDRs.%20CAFOD%20discussion%20paper%20May%202021.pdf (accessed 8 November 2021).

70 M Plant 'The challenge of reallocating SDRs: a primer' Centre for Global Development (August 2021) https://www.cgdev.org/sites/default/files/challenge-reallocating-sdrs-primer.pdf (accessed 7 November 2021).

2.5 Reform requires deeper international cooperation

Pulling different pieces of the argument together, we can see that there were missed opportunities to provide sufficient non-debt creating international assistance and adequate emergency debt relief. The latter was in part because contractual provisions of financial instruments, even when they are state-contingent, do not take account of the diverse and multiple sources of emergencies that ought to ease country repayment obligations, and because international organisations have largely eschewed relief. Many developing countries have had little choice in fighting the pandemic but to increase their external debt burden until its sustainability became questionable. It did not have to be this way and should not be this way in the next crisis, but that requires more effective international cooperation at global and, where relevant, at regional level.

2.5.1 Revitalise global financial cooperation

The discussion here has highlighted how the G20 took upon itself the burden of directing the international financial response to the pandemic. Although concerns about the legitimacy of the G20 as an intergovernmental forum have never been resolved,[71] there is no other practical option. However, the G20 needs to function better.

Recall that the government leaders of what became the G20 were brought together by US President George W Bush in November 2008 to address the unfolding global financial emergency which, it was apparent, could not be adequately addressed by individual nations or through existing coordinating bodies in which the US government, in particular, had sufficient confidence. The G20 expanded its remit to include development in 2010, under which it built up a work programme on development finance, focused on as yet unfilled expectations of a larger role for international private finance in development. Apparently by default, the G20 then became the primary inter-governmental forum for addressing financial aspects of the coronavirus pandemic and its economic consequences. This is not because of any public health expertise in the G20 but because it has the potential to mobilise a lot of money, which it did – if inadequately – through multilateral if not bilateral channels (also, trade wars had to be put on pause).

71 J Jokela *The G-20: A pathway to effective multilateralism?* (2011) European Union Institute for Security Studies.

As the G20 is an informal club of large nations without a permanent secretariat, it necessarily relies on the existing system of international organisations for expertise on technical issues that demand international cooperation in such areas as communications, transportation, trade, financial regulation, macro-economic stabilisation, public health, food and hunger, weather, and, more generally, sustainable development and scientific cooperation. Because the G20 members are the largest financial contributors to these organisations, they exert leadership over them, shaping their work agendas and largely determining their financing.

It has been in the mutual interest of the G20 countries (and all the other government members of the organisations on which the G20 rely) that the technical work prepared for them be independent, reliable and shielded from political interference. Until recently, one could say that the family of international institutions had the relevant experts – if often not enough of them – to assess, design, implement and monitor outcomes of their priority programmes. Unfortunately, the ability to maintain that standard at the World Health Organisation (WHO) was challenged by the United States for domestic political reasons and with unfortunate heavy consequences.[72] While underlying concerns still needed to be addressed, the situation at the WHO improved in 2021 under the succeeding US administration. Nevertheless, for the G20 to continue to serve as the confidence-inspiring coordinator of emergency responses to catastrophes, it needs to resolve disputes that arise among its members in the 'front line' international organisations on which it perforce must depend.

A further imperative for the G20 is to fully appreciate that effective and inclusive recovery from the pandemic will need to be nurtured. Unfortunately, the long history of international financial assistance to developing countries shows this not to have been the case. Recovery programmes have usually been underfunded, which is to say they have traditionally forced socially-harmful austerity on adjusting countries as well as delayed development, as has been documented in studies of the numerous national programmes of recovery from the global financial crisis.[73] This time, however, the IMF has led the international community in promoting more reassuring levels of spending by governments to meet the challenge of the pandemic.[74] However, international civil society is

72 LO Gostin et al 'US withdrawal from WHO is unlawful and threatens global and US health and security' (2020) 396 *The Lancet* 293.

73 I Ortiz & M Cummins 'Austerity: The new normal: A renewed Washington consensus 2010-24' (2019), https://ssrn.com/abstract=3523562 (accessed 28 October 2020).

74 V Gaspar & P Mauro 'Fiscal policies to protect people during the coronavirus outbreak' IMF Blog (5 March 2020), https://blogs.imf.org/2020/03/05/fiscal-policies-to-protect-people-during-the-coronavirus-outbreak/?utm_medium=email&utm_

worried that the IMF under G20 oversight will quickly revert to tradition and soon re-emphasise austerity.[75] Preliminary indications that give some credence to this fear have been seen in IMF conditions for receipt of loans to developing countries in 2020.[76]

Early in its history, the member states of the IMF realised that they needed to pressure national policy makers to maintain 'sound' macro-economic policies and to insist on corrective policy measures as a condition for financial support when assisting countries to change unsustainable policies.[77] This led to annual macro-economic surveillance of all IMF members and to setting specific sets of conditions for receiving IMF loans. As views naturally evolve on what constitutes appropriate policies and as experience accumulates with existing policy requirements, the IMF periodically reviews its principles and practices of programme 'conditionality'[78] and country surveillance.[79]

However, IMF surveillance and conditionality do not exist in a policy vacuum, nor do decisions on how large or small IMF and other multilateral loans should be. A broader global forum of governments should address – and sometimes it does address – such broader sets of questions, namely, the General Assembly of the United Nations.[80] For example, IMF, the World Bank and the G20 have all embraced the sustainable development goals (SDGs) adopted by the General Assembly in 2015.[81] In 2020 the UN hosted a policy dialogue, including at heads of

source=govdelivery (accessed 28 October 2020).

75 'Over 500 civil society organisations signed the civil society organisations' statement against continued IMF austerity' (6 October 2020), https://www.eurodad.org/civil_society_organisations_open_letter_to_imf_austerity (accessed 28 October 2020).

76 'Arrested development: International Monetary Fund lending and austerity post COVID-19' Eurodad report (October 2020), https://www.eurodad.org/arrested_development (accessed 28 October 2020).

77 S Dell 'On being grandmotherly: The evolution of IMF conditionality' (1981) Essays in International Finance 144 Princeton University, https://ies.princeton.edu/pdf/E144.pdf (accessed 9 January 2021).

78 The most recent review of conditionality was concluded in 2019. See '2018 review of programme design and conditionality' (2019) IMF Policy Paper, https://www.imf.org/en/Publications/Policy-Papers/Issues/2019/05/20/2018-Review-of-Program-Design-and-Conditionality-46910 (accessed 9 January 2021).

79 See '2021 comprehensive surveillance review – Overview paper' IMF Policy Paper (May 2021), https://www.imf.org/en/Publications/Policy-Papers/Issues/2021/05/18/2021-Comprehensive-Surveillance-Review-Overview-Paper-460270 (accessed 27 May 2021).

80 B Herman 'United Nations as a forum for reform of global institutions' *Economic and Political Weekly* (Mumbai) (8 November 2008).

81 United Nations 'Transforming our world: The 2030 agenda for sustainable

state level, on how to respond to the pandemic, how to 'build back better',' and how to get on track, finally, to deliver the SDGs by 2030, their target date.[82] Further discussions at the UN have taken place in 2021 on some of the policy initiatives proposed in 2020, in particular in the Financing for Development Follow-up Forum in the Economic and Social Council and in *ad hoc* initiatives. It was unclear as of October 2021 that they would reach actionable conclusions in the UN that might be carried forward by the more specialised bodies of the international system.

While the UN remains a credible forum about development principles and for negotiation under treaty bodies, such as the UN Climate Convention,[83] the UN has only in exceptional circumstances been a forum that forges agreement on international economic and financial policies.[84] In the current global configuration, that work is perforce done at the G20 or not at all.

2.5.2 Strengthen regional cooperation: The SADC opportunity

Any new global policy framework that emerges to address recovery from the pandemic and its successor crises in developing countries will necessarily be quite broad. A crucial question thus is how the cooperation policies would be implemented at country level and that seems increasingly a function of how effective national policy making is and is seen to be. National policy inevitably reflects the contest between different stakeholders pursuing what they perceive to be their own interest along with – it may be hoped – their perception of the national interest. Some countries have been more successful than others in shaping such political contests into developmentally-effective policy making. Regional cooperation organisations, where they exist, may help strengthen the political forces in member countries that are working to strengthen national policy making. The Southern African Development Community (SADC) is a case in point.

development' General Assembly Resolution 70/1 adopted 25 September 2015.

82 See 'Initiative on financing for development in the era of COVID-19 and beyond, co-convened by Canada, Jamaica and the United Nations' (2020), https://www.un.org/en/coronavirus/financing-development (accessed 29 October 2020).

83 United Nations, 'What is the Paris Agreement?' https://unfccc.int/process-and-meetings/the-paris-agreement/the-paris-agreement (accessed 27 August 2021).

84 One such circumstance was the 2002 Monterrey Conference on Financing for Development; see B Herman, 'The politics of inclusion in the Monterrey process,' in JF Green & WB Chambers (eds) The Politics of Participation in Sustainable Development Governance (2006) 153.

From a financial perspective, the question may be phrased in terms of the budget constraint. Every country has one, but the amount of public expenditure it allows is not God-given. In other words, the funding envelope for public programmes will reflect, not only the adequacy of international cooperation, but also the willingness of societies to raise tax revenues from those enterprises and households capable of contributing more, while also limiting corruption, tax avoidance and other leakages, efficiently managing public programmes, and avoiding spending that reflects priorities that are demonstrably not national priorities. The techniques for drafting development plans, medium-term expenditure and revenue frameworks, annual budgets, public financial management programmes and post-expenditure audits are well known. The difficult part is forging the domestic agreement to achieve the desired results. Engagement with peers from neighbouring countries on policy matters that also affect the neighbours can contribute.

It may be helpful, in other words, if political energy is put into cooperation among regional partners. In this regard, it may be of some note that SADC celebrated its 40th Anniversary Summit in August 2020, when it adopted a new vision document (SADC Vision 2050) and a new ten-year cooperation plan to operationalise the vision document (Regional Indicative Strategic Development Plan 2020-2030).[85]

SADC has a long and mixed history of economic cooperation, including both successes and failures in implementing policy agreements.[86] Its 16 members include high-income diversified economies, commodity-dependent middle-income economies, landlocked and island nations, and least developed countries.[87] Their heterogeneity and the primacy of their integration into the global trading environment have served as centrifugal forces against which the forces for closer economic integration have had to contend.[88] Nevertheless, the 2020 joint political commitment to the new

85 SADC 'Communiqué of the 40th ordinary summit of SADC heads of state and government' (17 August 2020), https://www.sadc.int/files/8115/9767/2537/Communique_of_the_40th_SADC_Summit_August_2020_-ENGLISH.pdf (accessed 9 January 2021).

86 SADC Secretariat 'Status of integration in the Southern African Development Community' (2019), https://www.sadc.int/files/9915/9154/2991/Status_of_Integration_in_the_SADC_Region_Report.pdf (accessed 9 January 2021).

87 SADC member states are Angola, Botswana, Comoros, Democratic Republic of the Congo, Eswatini, Lesotho, Madagascar, Mauritius, Mozambique, Namibia, Seychelles, South Africa, Tanzania, Zambia and Zimbabwe.

88 R Mafurutu '40th SADC Summit and the anticipated key trade issues on the agenda' Tralac blog (Trade Law Centre) (14 August 2020), https://www.tralac.org/blog/article/14848-40th-sadc-summit-and-the-anticipated-key-trade-issues-on-the-agenda.html (accessed 9 January 2020).

documents and the urgency of more effective cooperation in the present circumstances in which a pandemic does not pay attention to borders, could strengthen policy making across many dimensions.

One such dimension is macro-economic. SADC long ago adopted the goal of becoming an economic union whose citizens would enjoy the free flow of people, trade and finance across their borders, eventually adopting a common currency. To this end, SADC countries adopted a memorandum of understanding on macro-economic convergence in 2002,[89] one of the commitments of which was to draft a binding protocol on finance and investment, which was adopted in 2006.[90] The objective has been to work together toward macro-economic stability, including low and stable inflation and prudent fiscal stances.[91] The countries also agreed to mutual surveillance of their macro-economic policies and have sought common statistical standards by which to monitor their respective performance, upgraded most recently in the 2020 summit by agreeing to include high-frequency data in the Surveillance Mechanism.[92] Moreover, civil society in the SADC region is poised to assist in capacity building on public finance and sovereign debt for legislators in the region.[93] The structures thus are in place, the political commitments have been freshly made and civil society is offering support. Perhaps it is a propitious moment.

2.6 Conclusion: A reform agenda

By way of conclusion, the proposals that the analysis leads to may be brought together here. The starting point is recognition that the kind of economic and natural catastrophes that the world increasingly seems to be throwing at its more vulnerable people are beyond the capacity of most developing countries to address alone. Some countries may be able to self-insure by accumulating a huge stock of liquid reserve assets; however, holding huge reserves rather than investing them in development has a

89 See https://www.sadc.int/files/6513/5333/7917/Memorandum_of_Understanding_on_Macroeconomic_Convergence2011.pdf (accessed 9 January 2021).

90 The Protocol entered into force in 2010. See https://www.sadc.int/files/4213/5332/6872/Protocol_on_Finance__Investment2006.pdf (accessed 9 January 2021).

91 SADC Memorandum of Understanding (n 90), art 2.

92 SADC Communiqué (n 86) para 10.

93 African Forum and Network on Debt and Development (AFRODAD) 'COVID-19 debt sustainability impacts and economic rescue packages analyses in Southern African Development Community (SADC) region' (6 July 2020) 13, https://www.africaportal.org/publications/covid-19-debt-sustainability-impacts-and-economic-packages-analyses-in-southern-africa-development-community-sadc-region/ (accessed 9 January 2021).

huge opportunity cost. Most developing countries, especially the poorest among them, will need international assistance. It should be available, especially in emergency situations.

One form is government-to-government emergency grant assistance to spend on responding to a crisis. The traditional form of assistance has been donor government humanitarian and development assistance, but as seen in the current pandemic, there has not been an adequate response from donor governments. Governments left it to the multilateral institutions to provide the necessary funding, which they quickly expanded, albeit primarily in the form of loans. However, there is a form of international non-debt creating finance that can and has been expanded by the IMF in global crises called the special drawing right (SDR). It requires the governments in IMF to agree to allocate additional SDRs when the need arises. They did so act in response to the global financial crisis, and again – if with a delay –in the pandemic. A policy to use the SDR this way in future catastrophes should be considered.

A second form of international assistance would ease the external debt burden of poor country governments. As we have seen, the G20 governments (joined by members of the Paris Club that were not also members of the G20) offered to temporarily suspend debt servicing owed to them, which thus was at no long-term cost to themselves. These creditors were subsequently willing to acknowledge that there may be exceptional circumstances in which they ought to reduce repayment obligations of certain countries. However, no other creditors, neither private creditors nor multilateral institutions, with the exception of the IMF, has offered any prospect of debt relief. The question thus becomes how to design the relief programme in a way that responds to crises and engages all groups of creditors fairly.

One proposal made earlier in this chapter (part 4.1) was that when the IMF board approves a quick-disbursing loan for emergency needs or accords emergency debt relief through its CCRT, it should include in its announcement, when appropriate, a statement warranting private and official creditor relief of obligations of the country falling due during the emergency period. With that endorsement, the debtor government could temporarily suspend its debt servicing and offer to negotiate with its creditors how it would cover the suspended payments. Standard term sheets might be made available in advance of such situations to simplify the negotiations.

A more permanent version of this proposal might also be considered, beginning with the introduction of standard clauses into bond and

loan contracts that would recognise that there are situations in which a temporary (ultimately possibly permanent) suspension of government debt servicing payments to foreign creditors was warranted. Because it seems impossible to specify each and every contingency requiring relief, it was proposed that the responsibility for the decision to invoke the relief clause be given to the IMF executive board (under the supervision of the IMF's board of governors), advised by the relevant international agency having expertise in the source of the catastrophe, such as the World Health Organisation in the case of a pandemic. Such a decision would trigger the relief the possibility of which had already been envisaged in the clauses of the bond, bank loan, bilateral or multilateral credit contracts. As the kind of relief offered in each case would be expected to follow a set of standardised term sheets and model contracts, the question of a fair sharing of risk among different creditor classes would also be addressed before the crisis erupted.

Moreover, if in a future catastrophe the G20 were to call on multilateral financial institutions to join in the debt relief programme, as it did without effect in its DSSI programme for the pandemic, it could remind the financial markets in its Communiqué that the G20 members are the major shareholders in the institutions and not only are obligated to cover the debt servicing of institution bonds, but they also fully intend to ensure there would be no interruption in payments. In other words, the G20 should ease the fear of the World Bank that offering any debt relief to its poorest member countries would somehow jeopardise its AAA bond rating. In addition, the World Bank could adopt an initiative such as that of the CCRT at the IMF under which all debt servicing owed by covered countries falling due during the emergency period would be paid to the institution on their behalf. Indeed, the SDRs that boosted the total reserves of rich countries could justify those countries transferring some of their other reserves to fund such facilities.

Finally, it seems that instituting such reforms requires a deeper level of international cooperation than was apparent in 2020. The G20, with its collective influence on the financing of the multilateral system, thus needs to reinvigorate and arrange better funding of the specialised agencies that carry out the technical analyses on which collective responses to crises depend. In addition, governments should use the inclusive and legitimate forum of the UN to update broad guidelines on appropriate policies of international cooperation, including on the issues discussed in this chapter. In addition, the international community will inevitably scale its assistance to the confidence sustained in the effective use of international funding. To this end, it was suggested that regional organisations, such as SADC, could contribute to that confidence – not to mention improve

the economic situation in the countries themselves – by furthering mutual cooperation of peers on their adopted regional priorities, including on macro-economic policy.

Certainly, this is an ambitious agenda. That does not make it any less warranted.

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3 Debt service suspension in Southern African Development Community countries

*Martin Kessler**

3.1 Introduction

In 2020, as the COVID-19 pandemic was spreading from China to the developed world, its impacts on health were compounded by a global financial and economic shock. Even in developing countries that were relatively less affected by the pandemic, the external shock was spreading through lower exports and falling financial flows. Indeed, for a few weeks in March 2020 financial systems froze, before central banks stepped in and provided ample liquidity to markets. Globally, private external financial flows to emerging markets declined by 13 per cent in 2020, especially through lower amounts of loans and portfolio flows.[1] Sovereign borrowers in 'frontier markets' (which are often relatively rare and recent emitters of Eurobonds) were not able to access markets for several months. In the Southern Africa Development Community (SADC), countries with outstanding Eurobonds such as Tanzania, Zambia and Seychelles have experienced increases in interest rates by 4 to 10 percentage points. In sub-Saharan Africa, Eurobond issuance declined to about US $5 billion in 2020 compared to US $14 billion in 2018.[2]

In addition to the financial shock, exports plunged and economic activity collapsed that lead to a decline in government revenues. Sub-Saharan Africa experienced a negative gross domestic product (GDP) growth rate for the first time in decades, with 40 million people falling in poverty in 2020. As advanced economies mobilised trillions of dollars in their domestic response to the crisis, low and middle-income countries had limited fiscal space to provide the necessary support to firms and households. Low revenues, high spending needs, and the limited ability to borrow abroad constrained the ability to take health measures strictly. The burden of high debt service due made this constraint even tighter.

* This chapter represents only the views of the author and does not represent the views of OECD members nor those of its Secretariat.

1 IMF 'Macro-economic developments and prospects in low-income countries – 2021' (2021), https://www.imf.org/en/Publications/Policy-Papers/Issues/2021/03/30/Macroeconomic-Developments-and-Prospects-In-Low-Income-Countries-2021-50312 (accessed 16 November 2021)

2 World Bank 'Africa's Pulse 23 – April 2021. Sub-Saharan Africa' (2021).

Therefore, as the economic forecasts worsened, finance ministers and Central Bank governors from countries in the Group of 20 agreed to a 'time-bound suspension of debt service' for 73 vulnerable countries.[3] Depending on whom you ask, this Debt Service Suspension Initiative, or DSSI, was a major success of global cooperation in the midst of the worst economic crisis since World War II, or a drop in the bucket of the needs of developing countries. Paradoxically, both those apparently contradictory positions have truth to them: The amounts involved were indeed small in most cases, but were significant in others. This heterogeneity is apparent in the context of the SADC, where the sums deferred varied between 0,1 per cent of GDP (in Comoros) and 3 per cent of GDP (in Mozambique). This chapter aims at putting those numbers in the broader context of the challenges faced in those countries and the external environment. It illustrates how the DSSI can work in some cases and much less in others, depending on debt stock and creditor composition. With some countries already in a status of default or at high-risk of debt distress and others with sustainable debt positions, a case-by-case approach is necessary. The challenge for the donor community will be to meet the increased financing needs of SADC countries after years of decline.

An important element for this evaluation is the fact that depressed economic activity in 2020 will have lingering impacts: The COVID-19 crisis reduced ability to repay debt over time. In other words, it not only affected the liquidity of countries' sovereign debt, but also its sustainability. The DSSI only supports the former, but not the latter, as it only allows countries to defer payments to later years. However, the agreement laid the foundations for another step forward, the 'Common Framework for debt treatment beyond the DSSI' (Common Framework), adopted by the G20 on 13 November 2020. The Common Framework recognises the need for coordinated debt relief in cases where sovereign debt is clearly unsustainable. Its implementation started in 2021, is likely to be challenging, and to take longer than the DSSI. It would allow countries to reduce the stock of their debt and treat private sector debt with equivalent terms.

3 This includes Least Developed Countries (LDCs) as well as countries eligible for loans from the International Development Association (IDA), the concessional window of the World Bank, except four countries not current on their terms with the IMF or the World Bank.

3.2 The build-up in debt vulnerabilities pre-dated the COVID-19 crisis

The first part illustrates the pre-existing challenges arising from debt evolutions prior to the COVID-19 crisis. One country was already in debt distress (Mozambique) while others were close to a default situation (Angola, Zambia). Another group of countries has maintained relatively low debt, but their equilibrium was derailed by the COVID-19 crisis.

As a way of context, it is important to recall that SADC countries are remarkably heterogeneous. It includes high-income countries (Seychelles and Mauritius) which are about 25 times more affluent than the low-income countries of the community. Medium and high-income countries can also be confronted with tensions on public debt sustainability (most notably, Mauritius and South Africa have been downgraded during the current crisis) but the nature of the challenges and solutions is different. This chapter focuses on developing economies, and in particular on those eligible for the DSSI (Table 1). The remarkable diversity of economic structure among the 16 SADC members, both in terms of income level and dynamics and in terms of public debt, is analysed in this first part.

Table 1: SADC countries: country classifications, income and debt

Country	**DSSI-eligibility**	GNI per capita	Population (million)	Public debt (% of GDP)	Income group	LDC	IDA-eligibility
Malawi	**Yes**	1080	18.6	59	LIC	Yes	Yes
Democratic Republic of the Congo	**Yes**	1110	86.8	16	LIC	Yes	Yes
Mozambique	**Yes**	1310	30.4	103	LIC	Yes	Yes
Madagascar	**Yes**	1660	27.0	38	LIC	Yes	Yes
Tanzania	**Yes**	2700	58.0	38	LMIC	Yes	Yes
Zimbabwe	**Yes**	2740	14.6	112	LMIC	No	Inactive
Comoros	**Yes**	3210	0.9	25	LMIC	Yes	Small economy terms
Lesotho	**Yes**	3330	2.1	49	LMIC	Yes	Blend terms
Zambia	**Yes**	3560	17.9	94	LMIC	Yes	Blend terms
Angola	**Yes**	6380	31.8	107	LMIC	Yes	No
Eswatini	**No**	8090	1.1	40	LMIC	No	No
Namibia	**No**	9780	2.5	60	UMIC	No	No
South Africa	**No**	12670	58.6	62	UMIC	No	No
Botswana	**No**	17140	2.3	15	UMIC	No	No
Mauritius	**No**	26840	1.3	83	HIC	No	No
Seychelles	**No**	29470	0.1	58	HIC	No	No

Source: World Bank, World Development Indicators, IMF World Economic Outlook

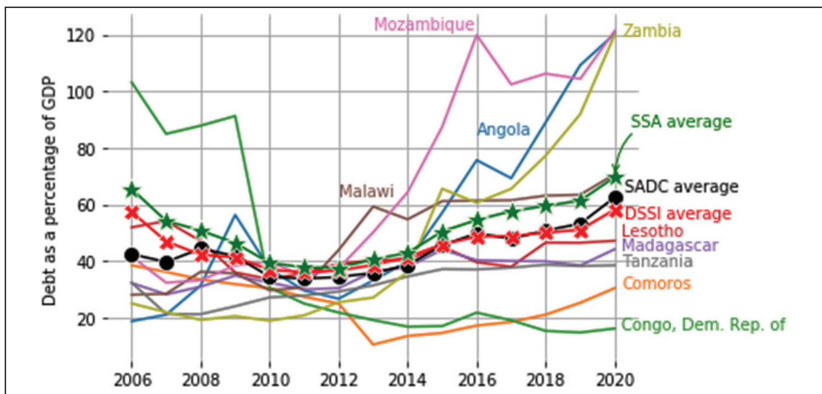
Note: Data for 2019. GNI per capita is on Purchasing Power Parity terms. Zimbabwe accumulated arrears to IDA and is thus considered inactive

3.2.1 The rising tide of public debt

The broader context of rising indebtedness for developing countries and in sub-Saharan Africa in particular is well known. After a decade of decline

linked to Heavily Indebted Poor Countries (HIPC) and Multilateral Debt Relief Initiative (MDRI) initiatives, public debt levels rose from about 38 per cent of GDP in 2011 to 60 per cent in 2019 on average (Figure 1). SADC countries followed a similar trend: from 35 per cent to about 50 per cent of GDP in 2019, with a sharp rise of about 10 percentage points is expected by the International Monetary Fund (IMF).[4] Even among the nine SADC countries eligible to the DSSI (SADC-DSSI countries), debt dynamics have diverged. Three countries have debt-to-GDP ratios OF over 100 per cent, of which two countries are in the situation of outright default: Mozambique has restructured its Eurobonds in 2016 and again at the end of 2019; Zambia missed a payment on its Eurobonds on 13 November 2020. Angola's public debt stock was projected to be over 90 per cent of GDP already before the crisis. Others were much more prudent, both as a matter of fiscal strategy and according to IMF or World Bank Debt Limit Policies, which limit countries' access to non-concessional finance. The Democratic Republic of the Congo (DRC), Comoros, Tanzania, Madagascar and Lesotho are all projected to maintain indebtedness of below 50 per cent of their GDP.

Figure 1: Gross public debt to GDP ratios for SADC countries eligible to DSSI



Source: IMF, World Economic Outlook (October 2020)

4 In most cases the data used in this chapter dates from end-2020. Most numbers for 2020 thus are projections.

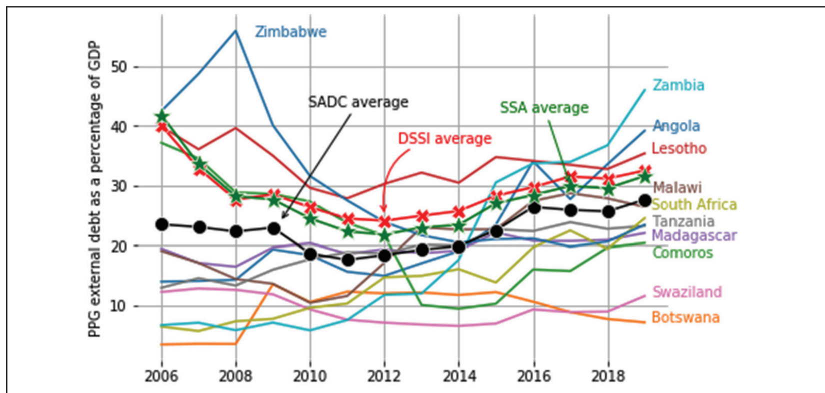
Box 1: Definitions

Gross public debt is defined by the IMF as the General Government debt, including domestic and external. Public and Publically Guaranteed (PPG) debt comprises long-term external obligations of public debtors, including the national government, public corporations, state-owned enterprises, development banks and guaranteed private debt. External public debt is PPG debt owed to non-residents.

Source: IMF (2020)

In general, both domestic and external debt[5] contributed to this increase. For SADC as a whole, public and publically guaranteed (PPG) external debt represented about 25 per cent of GDP in 2019, or half of the total public debt stock, up from 18 per cent in 2010. SADC-DSSI countries, which on average are poorer and have less developed domestic debt markets, are more dependent on external financing: In their case, external PPG debt was 32 per cent of GDP in 2019 (Figure 2). Higher income countries in SADC have a different debt structure, relying less on official borrowing and more on private markets, including domestically (in particular South Africa).

Figure 2: External public and publicly guaranteed (PPG) debt of select SADC-DSSI countries



Source: World Bank, IDS

Note: This excludes Mozambique and DRC to improve visualisation.

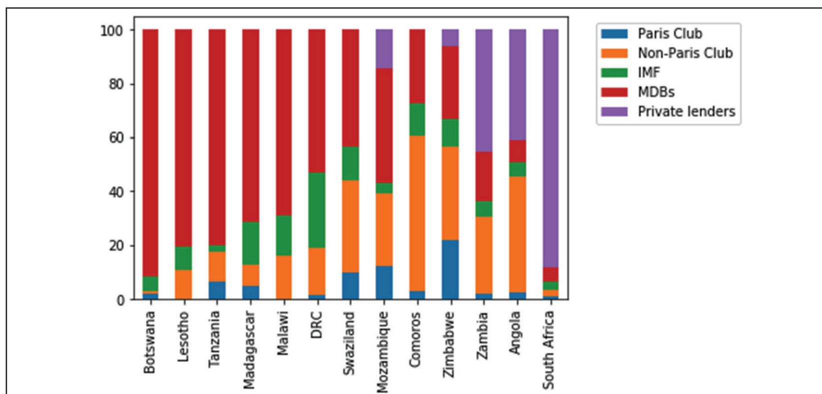
5 See Box 1 for definitions.

In addition, debt stock measures do not tell the whole story: Debt composition has changed away from multilateral and Paris Club official donors towards non-Paris Club bilateral creditors and private markets. In sub-Saharan Africa this diversification in the sources of finance came with risks: Cost of debt tends to be higher and maturities lower.[6]

3.2.2 Change in composition of borrowing made debt more expensive

Divergence across SADC countries did not occur only on the level of debt stock, but also on its composition (Figure 3). Multilateral lenders, and in particular the World Bank, tend to play a pre-eminent role for SADC-DSSI countries. Indeed, all DSSI-eligible countries except Angola have by definition access to concessional IDA loans. As a result, the share of multilateral debt in the composition was relatively high in 2019 ranging from 19 per cent (Zambia) to 90 per cent (Botswana). In general, there is a stark difference between countries with access to markets, which have Eurobonds or international loans outstanding, and others.

Figure 3: Composition of debt stock by creditor type



Source: World Bank, International Debt Statistics 2021

Bilateral lenders make between a small percentage of external government debt (Botswana) and close to half (Comoros and Zimbabwe). The World Bank recently published external debt data with detailed information by creditors, allowing a description of these evolutions with a finer grain.[7]

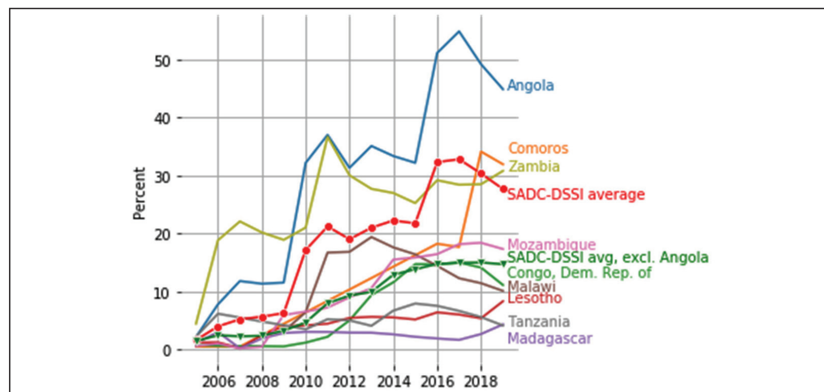
6 C Calderon & AG Zeufack 'Borrow with sorrow? The changing risk profile of sub-Saharan Africa's debt' Policy Research Working Paper 9137 (2020).

7 World Bank (2020), International Debt Statistics 2021.

Paris Club members have played a declining role within this group: They now represent less than a third of bilateral external loans in each country except Zimbabwe. The main non-Paris Club lenders in SADC-DSSI countries are China, with India also playing a significant role in Malawi (70 per cent of official bilateral debt), while Saudi Arabia is a major official lender to Lesotho.

Focusing on China specifically, its role as an official bilateral creditor has grown significantly in the SADC region, including DSSI countries. Overall, the debt stock recorded by World Bank data represented US $16 billion in 2019 for SADC-DSSI countries as a whole, of which US $10 billion was lent to Angola. As a share of total external public borrowing, this represents an increase from 5 per cent to 15 per cent in the last ten years (Figure 4). In countries such as Comoros, Zambia, Mozambique and Malawi, China has become the main official bilateral creditor, sometimes by far, with an acceleration concentrated around 2010-2015, and stabilisation since then. Its share among bilateral lenders between 20 per cent (Tanzania and DRC) and 90 per cent (Angola), with an average for SADC-DSSI countries close to 50 per cent, even after excluding Angola.

Figure 4: Share of China in external lending



Source: World Bank, International Debt Statistics: DSSI

There are, however, major doubts on data accuracy and suspicion that those figures are under-estimated. This would undermine any debt relief initiatives, the DSSI included. Opacity of sovereign loans is often linked with lack of capacity, such as for direct loans to State Owned Enterprises without overview from the Ministry of Finance, or within complex public-private partnerships where some government guarantees can be hard to

estimate.[8] The complexity of the ecosystem, between official and private institutions, is well described in the case of Zambia by Brautigam.[9] Loans originating from Chinese institutions often include strict confidentiality terms[10] which reinforce opacity. Recent research on Chinese 'hidden loans'[11] would indicate that for 12 SADC countries, about $45 billion was owed to China in 2017, against $28 billion for the World Bank database. This difference of $17 billion represents about 2,5 per cent of GDP on aggregate, spread between South Africa ($5,5 billion, but only 1,6 per cent of GDP), Zambia ($3,5 billion, 13,7 per cent of GDP, the most significant), Tanzania ($3 billion) and a few others to a lesser extent.[12]

While the opacity implies uncertainty on the true level of external debt, another source of concern is the degree of seniority and the riskiness of new sources of debt. Resource-backed loans, often under the form of guaranteed payments from specific revenue sources, are also complex and need to be taken into account.[13] There is little direct evidence on interest rates owed on loans from China, but they are more likely to be on a commercial basis. This is implied, for example, by the correlation between the share of China in total official borrowing and the share of concessional loans or the interest bill. China's policy framework for concessional development finance revolves around zero-interest loans from the Ministry of Commerce, concessional loans and preferential export credits from the Chinese ExIm Bank.[14] On the other hand, a large share of the portfolio stems from non-concessional loans from state-owned banks, in particular

8 Debt reporting in LIDCs; IMF 'The evolution of debt vulnerabilities in lower income economies' (2020), https://www.imf.org/~/media/Files/Publications/PP/2020/English/PPEA2020003.ashx (accessed 16 November 2021)

9 D Brautigam 'Zambia's Chinese tragedy of the commons', presentation at the 2021 SAIS-CARI conference 'China's Overseas Lending in Comparative Perspective' (2021), http://www.sais-cari.org/event-details/2021/4/6/cari2021conference (accessed 16 November 2021)

10 A Gelpern et al 'How China lends: A rare look into 100 debt contracts with foreign governments' Peterson Institute for International Economics, Kiel Institute for the World Economy, Centre for Global Development, and Aid (2021), Data at William & Mary.

11 S Horn, C Reinhart & C Trebesch 'China's overseas lending' April 2020, NBER Working Paper 26050 (2020).

12 Those of Brautigam et al differ slightly, and would point to reduce the estimates of hidden debt for South Africa and Tanzania (by US $4 billion and $1 billion respectively). D Brautigam, Y Huang & K Acker 'Risky business: New data on Chinese loans and Africa's debt problem' CARI Briefing Paper 3 (2020).

13 Brautigam et al (n 12).

14 S Morris, B Parks & A Gardner 'Chinese and World Bank lending terms: A systematic comparison across 157 countries and 15 years' (2020), https://www.cgdev.org/publication/chinese-and-world-bank-lending-terms-systematic-comparison (accessed 16 November 2021)

China Development Bank, which represents about 28 per cent of lending to developing countries, and which lends on commercial terms. Indirect evidence indicates that borrowing has become more expensive.

3.2.3 Debt sustainability has also deteriorated in some cases

Low-income developing countries' debt risk overall has deteriorated in the past decade, but the situation is more nuanced for SADC countries, with a few notable exceptions. Out of 73 countries with a debt sustainability analysis (DSA), the number of sovereigns with 'low' or 'moderate' risk has decreased from 80 per cent in 2014 to less than half in 2019. In contrast, for SADC, ratings have remained broadly stable (Table 2): Out of 8 SADC-DSSI countries with DSA ratings,[15] two have a low risk of external distress (Madagascar and Tanzania[16]) and four had moderate risks (Comoros, DRC, Lesotho, Malawi). Mozambique and Zambia, as noted above, have moved towards debt distress.

Table 2: Risk rating in the IMF/WB Low-income Country Debt Sustainability Analysis (LIC-DSA) for SADC-DSSI countries

Country	Risk of external debt	Risk of overall debt	Date of DSA
Comoros	Moderate	Moderate	August 2019
Congo, Dem. Rep.	Moderate	Moderate	December 2019
Lesotho	Moderate	Moderate	July 2020
Madagascar	Low	Moderate	April 2020
Malawi	Moderate	High	December 2019
Mozambique	In distress	In distress	May 2019
Tanzania	Low	…	January 2018
Zambia	High	High	August 2019

Source: World Bank, https://www.worldbank.org/en/topic/debt/brief/covid-19-debt-service-suspension-initiative

Countries with market access have experienced a decline in their ratings. Economies with market access are subject to a different debt sustainability framework called Market Access-DSF, or MAC-DSF, which is not always

15 Angola is considered a 'market access country', and does not use the same DSA template.

16 The latest published DSA for Tanzania dates back to 2018 due to a lack of consensus between the IMF and government authorities about economic data. Debt sustainability analyses performed by other organisations using government sources show that prospects have not changed much in the recent path. They underline growing risk of currency mismatches, however. M Were & L Mollel 'Public debt sustainability and debt dynamics: The case of Tanzania' WIDER Working Paper (2020).

published and does not have a directly comparable risk assessment. Recent debt analyses in this framework show a deterioration of prospects: For South Africa, it reveals increasing vulnerabilities, in particular due to high external and fiscal financing needs, low growth and contingent liabilities. They tend to have credit ratings from agencies, which have shown a steady deterioration in the past years: South Africa has been subjected to two downgrades by credit rating agencies. Botswana was also downgraded in mid-2020 by S&P and Moody's, while Mauritius was placed under negative outlook watch for the first time in eight years by Moody's, as was the case for Namibia by Moody's and Fitch.

This first part illustrated that while some countries in SADC have followed trends from the developing world, the picture is nuanced: Several lacked access to borrowing sources, whether due to prudent management or to a lack of access to non-concessional funding sources. The next part focuses on the COVID-19 recession and its impact on those precarious balances.

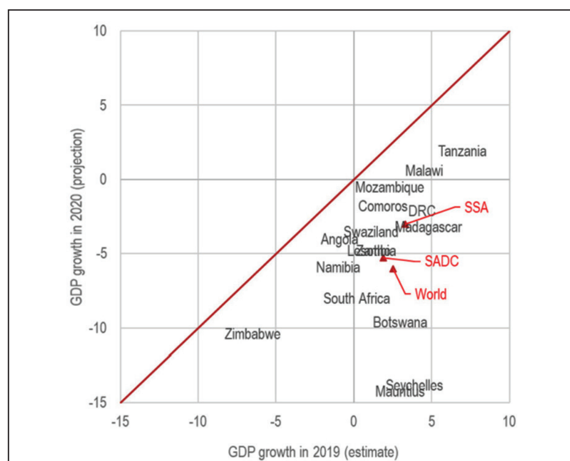
3.3 Economic shock and policy response

3.3.1 The COVID-19 shock and its impact

Beyond the obvious major impact on health, COVID-19 of course is a major economic shock for the world, and for sub-Saharan Africa in particular. SADC countries shifted from a modest average growth performance of 2 per cent in 2019 to a -5 per cent recession in 2020,[17] below that of sub-Saharan Africa (Figure 5). Some countries, such as Tanzania and Malawi, would still have GDP growth in 2020 (though with a reduction of 4 to 6 percentage points since 2019) whereas countries dependent on tourism, commodities and/or remittances suffer from among the worst downturns globally (in SADC, Mauritius and Seychelles).

17 Those numbers are based on the WEO October 2020 database.

Figure 5: The magnitude of the 2020 recession compared to growth in 2019



Source: IMF, World Economic Outlook (October 2020)

In relative terms, the economic crisis in low-income countries was less dramatic but their economy is also less resilient.[18] Low-income countries were less directly affected by the virus, social distancing restrictions were less tight, and their smaller integration to the global economy slowed the spread of the virus and its economic repercussions. On the other hand, they had major weaknesses, such as large informal sectors with less buffers. Their fiscal policy responses, with stimulus policies of 2,5 per cent on average, were well below that of high-income economies, which injected 16,1 per cent of their GDP into the economy. For SADC economies, the averages are 4,4 per cent for non-DSSI countries and 2,5 per cent for DSSI countries (Figure 6). While desirable stimulus sizes do not need to be equal, they are expected to be in line with the economic downturn, but this was not the case: The Organisation for Economic Cooperation and Development (OECD) estimates that the size of the gap was of $700 billion to $1 trillion in 2020 for developing economies, including about $100 billion for low-income economies.[19] The reason for these differentials are due to the access to markets in advanced economies and large emerging markets, which had the ability to finance their fiscal deficits by emitting bonds to investors (who were happy to buy safe bonds in a

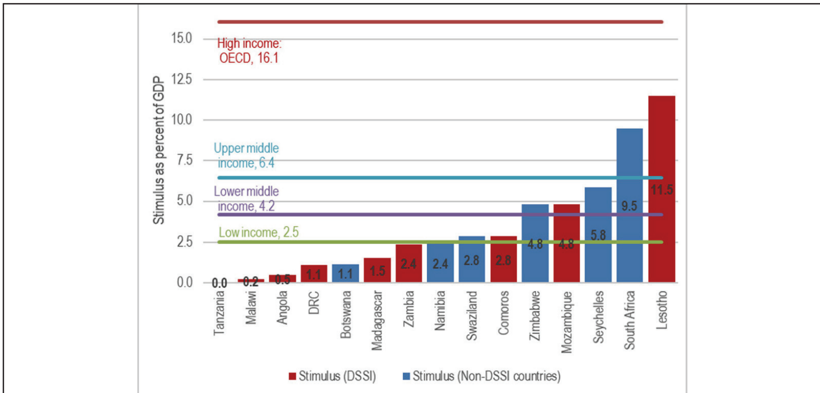
18 IMF WEO (October 2020) ch 1.

19 OECD 'The impact of the coronavirus (COVID-19) crisis on development finance' OECD Policy Responses to Coronavirus (COVID-19) (24 June 2020), http://www.oecd.org/coronavirus/policy-responses/the-impact-of-the-coronavirus-covid-19-crisis-on-development-finance-9de00b3b/ (accessed 16 November 2021).

time of uncertainty) as well as through central banks' purchases. Frontier markets, on the other hand, were much less able to access liquidity.

Despite this, some countries were able to provide a larger stimulus package, either by raising public spending or by reducing or waving taxes. Lesotho, for example, suspended a corporate income tax and Mozambique lowered its VAT, financed by external development partners. On the other hand, Tanzania, which is projected to have one of the smallest declines in growth in 2020, implemented no stimulus measure, according to the IMF.[20] Tanzania is the only low-income SADC country without an IMF programme, which it could have requested to finance further fiscal measures: Given the downside risks on medium-term growth,[21] fiscal measures would have been important.

Figure 6: Magnitude of the stimulus for SADC countries compared with income groups



Source: IMF, Fiscal Monitor database (October 2020)

Note: This chart excludes Mauritius, which had among the highest fiscal stimulus of SADC countries, with 35 per cent of GDP according to the IMF.

20 See also V Masubo 'COVID-19 in Tanzania: Is business as usual response enough?' International Growth Centre blogpost (July 2020), https://www.theigc.org/blog/covid-19-in-tanzania-is-business-as-usual-response-enough/ (accessed 16 November 2021).

21 World Bank 'Protecting the poorest countries: Role of the multilateral development banks in times of crisis, exploratory note' (2020), http://documents1.worldbank.org/curated/en/601251595023594564/pdf/Protecting-the-Poorest-Countries-Role-of-the-Multilateral-Development-Banks-in-Times-of-Crisis-Explanatory-Note.pdf (accessed 16 November 2021)

These large differences will affect the recovery in the long run. Between April 2020 and October 2020, the IMF revised its forecast positively for advanced economies but negatively for low-income developing countries (LIDCs) economies, reflecting the differences in stimulus as well as in access to vaccination. The economic impact of the current shock will linger in the long run without sufficient fiscal support to the recovery, as employment and long-term investment fell while access to education and health were disrupted.[22]

3.3.2 The DSSI is not at scale: Too small for low-debt countries, too narrow for high-debt countries

In this context, the DSSI has come as an important scheme to alleviate immediate liquidity pressure. Importantly, as stated in the 15 April 2020 Communiqué, it has three key conditions. First, it requires that countries apply for the DSSI and to all their creditors equally, and that they receive approval or formally request emergency financing from the IMF.[23] A second set of conditions is linked to transparency: Countries commit to use fiscal space for social, health and economic support, as monitored by International Financial Institutions (IFIs). They also have to disclose all public sector financial commitments, with technical assistance from IFIs. Third, they accept to limit new non-concessional debt during the suspension period, as defined by the limitations set by the World Bank and the IMF.

Those conditions were designed to elicit borrower's participation and creditor coordination, as well as to use DSSI as an opportunity to improve debt management more broadly. Voluntary participation ensured that it did not disrupt financing conditions for countries that thought it could disrupt their access to markets. However, the equality of treatment implied that once a country participates, it requires similar conditions from all its official bilateral creditors. Transparency was meant to ensure the legitimate use of proceeds of the DSSI, in the framework of emergency IMF programmes. Finally, limits on non-concessional loans, meant to avoid piling new debt on old debt, were circumscribed in the end and did not go beyond existing IMF and World Bank policies.

22 IMF 'Macro-economic developments and prospects in low-income countries – 2021' (2021), https://www.imf.org/en/Publications/Policy-Papers/Issues/2021/03/30/Macroeconomic-Developments-and-Prospects-In-Low-Income-Countries-2021-50312 (accessed 16 November 2021)

23 Either through Rapid Financing Instrument (RFI), which is an IMF lending mechanism without a fully-fledged programme, and thus with minimal conditionality, or the Rapid Credit Facility (RCF), its equivalent for countries eligible for the Poverty Reduction and Growth Trust (PRGT), on which the interest rate is zero.

As a result, sums mobilised for 2020 are relatively small compared to the needs. In total for 2020, DSSI brought an estimated $5,7 billion of debt service deferral, over a total potential amount of $8,6 billion.[24] The limitations are now well known. The agreement was only constraining for official bilateral creditors, and even among them, it was imperfectly implemented: Some creditor institutions that were expected to be considered as 'official' did not participate in some cases. The most prominent example is that of China Development Bank (CDB), which considers itself commercial in nature and thus as not part of the perimeter. However, CDB has stated that it has voluntarily deferred $748 million,[25] although without providing a breakdown by country.

On aggregate, the DSSI seems to have allowed countries to maintain their public expenditures in a time of major crisis. According to the IMF and the World Bank,[26] countries that applied to obtain the DSSI have increased their spending towards health, economic and social support by 2 per cent of GDP on average while government revenues were decreasing. Overall current expenditure remained constant, but countries had to cut in their investment spending, resulting in stable or slightly declining public expenditure.

Among SADC countries, Angola would be by far the main beneficiary. Data on actual debt deferred has not been published: This analysis on debt service as recorded by the World Bank, as if DSSI had been perfectly applied for all bilateral creditors. Considering only debt service to official bilateral creditors, Angola owed about $1,8 billion in debt service in the initial suspension period (May-December 2020, Figure 7). According to press reports, and given the fact that a large share of these flows are owed to CDB, it is unlikely that amounts deferred were as high. Mozambique and Zambia follow, with about $294 million and $165 million respectively, owed to Brazil and China mainly for Mozambique, and at 80 per cent to China for Zambia. Brazil, as a G20 member country, participated in the DSSI as creditor. DRC and Tanzania also had significant bilateral debt service (about $160 million). As a percentage of 2019 GNI, Mozambique actually seems to benefit as much as Angola relative to its size, with about 2 per cent of GNI. Even with imperfect implementation, the DSSI thus

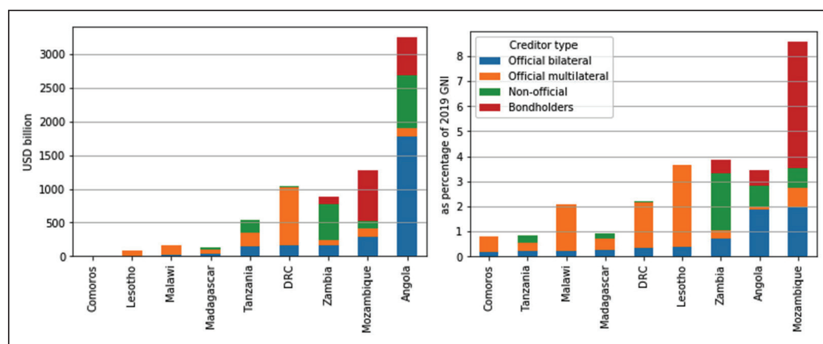
24 IMF and World Bank 'Joint IMF-WBG staff note: Implementation and extension of the debt service suspension initiative' Joint note for the Development Committee (2020).

25 http://www.cdb.com.cn/English/xwzx_715/khdt/202011/t20201104_7894.html (accessed 16 November 2021)

26 IMF and World Bank (n 24).

provides sizeable liquidity for some countries in SADC, but much less to others.

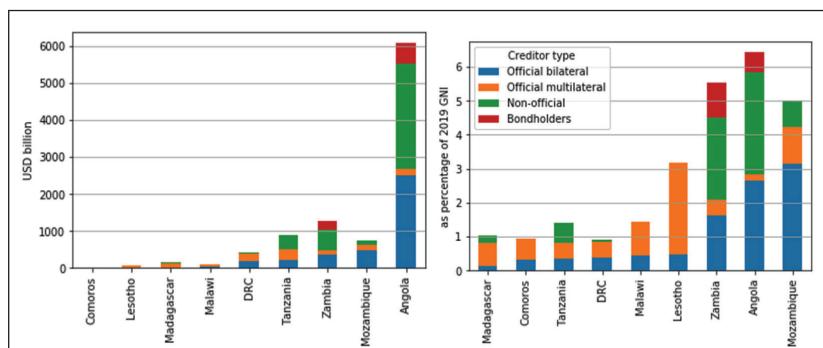
Figure 7: Debt service for May-December 2020 by country



Source: World Bank, IDS:DSSI

In November 2020 the DSSI was extended until June 2021, and later until the end of 2021. This entire period would allow DSSI-eligible countries to postpone about $15 billion in debt service payments. Indeed, as a group, they owe $43 billion in debt service on their external debt, or 2,5 per cent of GDP, with around one-third for each of the creditor group (official bilateral, private, and multilateral). For SADC countries, the total potential amount for the nine countries is about $3,7 billion, of which two-thirds stem from Angola only. For Comoros, Tanzania, DRC, Malawi and Lesotho, amounts deferred from the DSSI (between 0,3 per cent and 0,5 per cent of GNI) remain small (Figure 8).

Figure 8: Debt service for all 2021 by country



Source: World Bank, IDS:DSSI

The DSSI also called upon private creditors to offer similar conditions to countries that would request it. This aspect, however, has not been successful. In 2020, 46 countries out of 73 had requested DSSI to their official creditors but none had done so to private creditors. Some countries with market access feared to send a signal to private creditors and rating agencies, although perceived stigma diminished with time. For example, Kenya applied to the DSSI only in late 2020. Other countries had little to no debt service due to bilateral borrowers, and thus little to gain. In the case of SADC countries, all eligible countries applied to their official creditors, often quite early in the process, but did not reach out to their private creditors.

Debt service owed to the private sector is significant for three high-debt countries. According to the data from the World Bank, Mozambique had a large bond payment in end-2020, but almost none in 2021. Applying it to private creditors of Angola and Zambia, which are both in a status of debt distress, could have reduced immediate outflows, and helped in the restructuring process. Outside those countries, Tanzania is the main case where participation of private creditors could have brought significant liquidity. In all other cases, debt service to private creditors was limited, as few had engaged in borrowing from the private sector. Is official creditor money leaking to private lenders? If countries do not restructure debt eventually, this would not be the case: Official creditors would recoup deferred debt service. If they do restructure, however, it could imply that private creditors were paid on their loans at the expense of official creditors. In those cases, a faster resolution would have helped avoid this outcome.

3.3.3 Multilateral lending in response to COVID-19 crisis

A more complete assessment of the DSSI leads to consider the broader context of the global financial safety net (GFSN) and its role in supporting countries in times of crises. The DSSI is a blunt instrument in the sense that it only supplied liquidity for countries that had borrowed massively, from a narrow group of official creditors. Participation of private creditors would have made it more significant and fairer. However, the role of multilateral development banks (MDBs) and the IMF was also important in providing liquidity, in a more targeted manner.

A first debate has focused on whether MDBs should have participated in the DSSI as well. While debt service to MDBs was high in 2020 and 2021 for SADC countries, the case for their participation is limited. The G20 initially called on MDBs to explore the possibility to participate in the DSSI, which they have resisted, as it could reduce their credit rating

and, hence, their ability to lend. Humphrey and Mustapha[27] argue that for low-income countries as a whole, the application of DSSI to MDBs would lower their ability to provide net resources in 2020. This was controversial: Several non-governmental organisations (NGOs) have called for debt service suspension from the MDBs,[28] arguing that debt service was a large drain of resources of developing countries and that MDBs could withstand a temporary shortfall in revenues and retain access to low interest rates. Within the G20, some member countries would have favoured their participation.

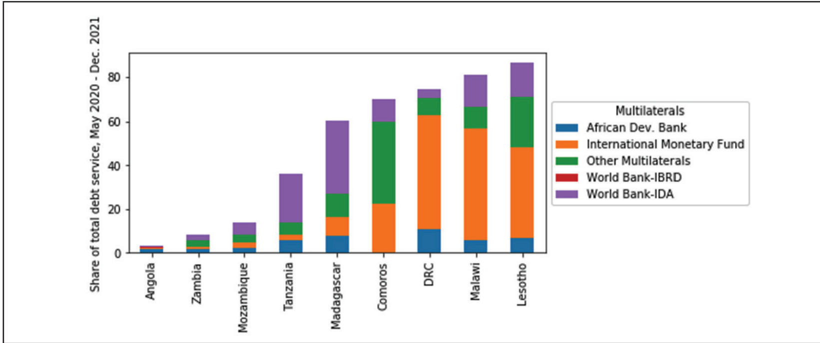
The World Bank and African Development Bank (AfDB) were net providers of finance in 2020 for almost all SADC-DSSI countries. Multilateral debt service represents the largest share of external debt service for six out of nine countries, so would SADC countries have benefited from extending DSSI participation to MDBs? Probably not, as the net flows were clearly positive for most institutions individually. First, for several countries (DRC, Lesotho, Malawi and Comoros to a lesser extent) a large share of this debt service is owed to the IMF (Figure 9). Second, the World Bank represents a large share of total debt service in two cases only (Madagascar and Tanzania), and is significant for Lesotho and Malawi. Despite slow disbursements of funds in some cases,[29] gross disbursements of loans in 2020 were about 10 times larger than debt service. For other countries this ratio varies, but is generally above 5. Third, the AfDB committed more than its debt service owed in 2020 for DRC and Madagascar, the two countries where it makes more than 5 per cent of debt service.

27 C Humphrey & S Mustapha 'Lend or suspend? Maximising the impact of multilateral bank financing in the Covid-19 crisis' ODI Working Paper (July 2020).

28 See eg the call for the cancellation of all debt payments by the Jubilee Debt Campaign, https://jubileedebt.org.uk/a-debt-jubilee-to-tackle-the-covid-19-health-and-economic-crisis-2 (accessed 16 November 2021).

29 S Morris, J Sandefur & G Yang 'Tracking the Scale and Speed of the World Bank's COVID Response: April 2021 Update'.

Figure 9: Debt service owed to multilateral creditors during DSSI period (May 2020-December 2021)



Source: World Bank, IDS:DSSI

The IMF was already delivering two large programmes prior to the crisis: an extended fund facility (EFF) with Angola, signed in December 2018 for $3 billion until 2021 and an extended credit facility (ECF), the concessional equivalent, with Malawi, signed in mid-2018 for about $150 million. Both were extended, prior to the onset of the COVID-19 crisis for Malawi and in September 2020, due to immediate liquidity needs for Angola.[30]

In addition, the IMF deployed two instruments to meet the needs with light conditionality, the rapid financing instrument (RFI) and rapid credit facility (RCF). Both instruments aim at providing low-access, rapid, and financial assistance to countries facing an urgent balance of payments need, without *ex post* conditionality. The RCF is concessional, with a zero-interest rate. The RFI is similar but targets countries not eligible to the concessional window of the IMF, the Poverty Reduction and Growth Trust (PRGT). The total capacity of both was raised to expand it further.

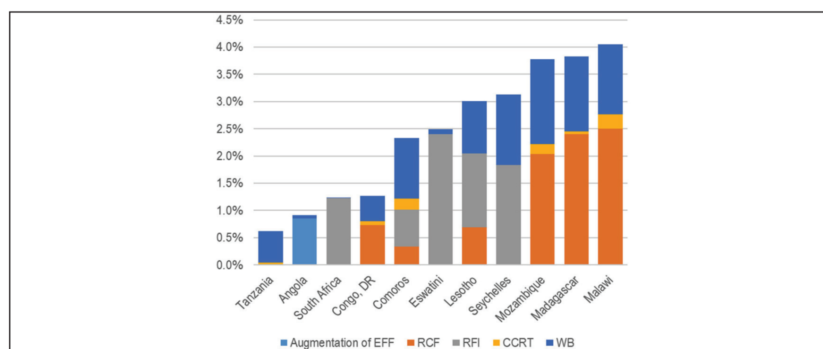
In 2020 eight SADC countries borrowed $1,2 billion under the RCF and $4,5 billion under the RFI. This infusion of liquidity thus is significant: It represents 1 to 2 per cent of GDP for countries with access to those programmes. The bulk of resources allocated to the RFI went to South Africa, which borrowed $4,3 billion. In total, DSSI-eligible countries received about $1,3 billion, an amount similar to the sum freed by the

30 https://www.imf.org/en/Publications/CR/Issues/2021/01/19/Angola-Fourth-Review-Under-the-Extended-Arrangement-Under-the-Extended-Fund-Facility-and-50024 (accessed 16 November 2021).

DSSI. It was also better targeted: Whereas most of the deferred amounts under the DSSI went to Angola, loans under the RFI were allocated by quota, representing about 2 per cent of GDP in Mozambique, Madagascar and Malawi. When adding support from the World Bank, support from IFIs is 2 to 10 times larger than what was implied by the DSSI (Figure 10). Tanzania is the only DSSI-eligible country with no programme in place (which is surprising since it is a requirement in the DSSI term sheet).

With support from donors, the IMF also forgave debt payments for 29 low-income countries, including six SADC countries. Under the Catastrophe Containment and Relief Trust (CCRT) the IMF can provide debt service relief financed by grants from donors. With relatively restrictive eligibility criteria (a low income per capita) this programme is targeted towards a small set of countries, including six SADC countries. This reduces the interest bill due to the IMF, which is a substantial share of multilateral – and total – debt service in some cases. It could be possible for donors, in select cases, to extend such an initiative to other MDBs.

Figure 10: IMF lending in SADC countries in 2020



Source: IMF

Finally, the G20 has called on the IMF to prepare a new allocation of SDRs, for about USD 650 billion, which was approved by the IMF Board in August 2021. The allocation key is the proportion of IMF quotas, so the share of this total will be relatively small for SADC countries, and even smaller for SADC-DSSI countries. However, proposals for advanced countries to give or lend part of their SDR allocation to developing

countries or to the IMF itself through the Poverty Reduction and Growth Trust could increase liquidity for those countries.[31]

This part has shown that the DSSI is a limited tool, but can be significant in providing liquidity for a subset of countries. One of the limitations to the initial design of the initiative is that the DSSI is not debt relief, but debt respite**.** This limited scope was essential for reaching the necessary consensus at the G20 but, as a result, the programme provides immediate breathing space by pushing immediate debt payments outflows to later years. Might it create larger 'walls of debt' in the years after 2024? The next part turns to the consequences in the longer run.

3.4 Debt on the brink: Financing the recovery after COVID-19

3.4.1 Persistent high financing needs

Existing forecasts point to a persistent need for liquidity for at least two years. The IMF conducts regular debt sustainability analyses (DSAs) for low-income countries, updating them for several countries as the COVID-19 crisis unfolded. This provides a credible lens on the possible fiscal paths in the medium run. This analysis relies on DSAs of six countries, highlighting future financing needs for low-income countries.[32] They show that gross financing needs for public sector debt (the sum of fiscal deficits and maturing debt to refinance) increased sharply in 2020 for five out of six countries at a similar pace, jumping from about 5 per cent of GDP in 2018 to 13 per cent GDP in 2020.

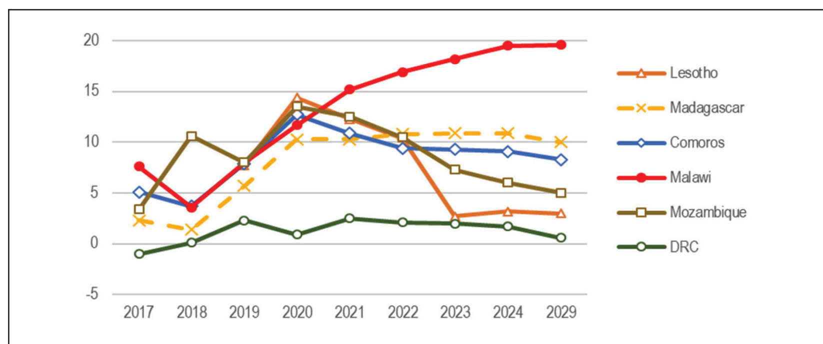
After 2022 the IMF expects a divergence even though GDP growth is expected to recover in those six countries. The opposite is the case for Malawi, which relies largely on domestic markets, at higher interest rates than from international sources. As a result, there is a clear risk of permanently high needs, which could lead to a fiscal crisis. Lesotho, and Mozambique to a lesser extent, represent the opposite evolution: After two years of high liquidity needs it is expected to manage to reduce its debt service (for Mozambique, thanks to treatment of existing debt). Madagascar and Comoros trace an intermediate path, where financing needs fall below their emergency level of 2020, but remain elevated,

31 M Plant & D Andrews 'What is the best way to allocate new SDRs?' Centre for Global Development, Commentary and Analysis (2021), https://www.cgdev.org/blog/what-best-way-allocate-new-sdrs (accessed 16 November 2021)

32 Among SADC-DSSI countries, only Tanzania and Zambia did not have DSAs in 2020. For both, this delay is due to discrepancies in the underlying debt and macro-economic data.

close to 10 per cent of GDP. Finally, DRC presents an exception due to optimistic projections in terms of GDP growth and government revenues, as well as expected growth in aid flows.

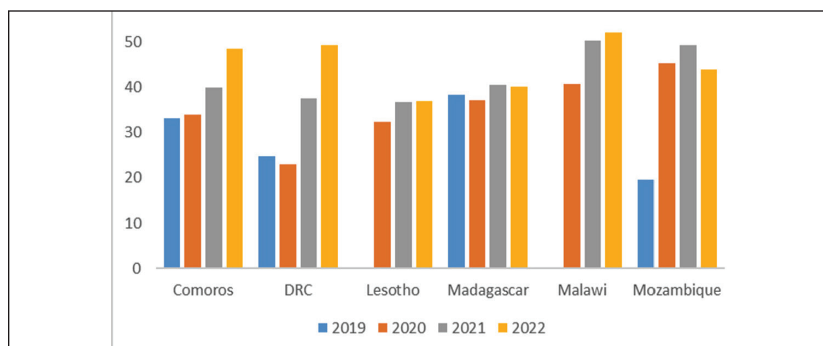
Figure 11: Future Gross Financing Needs for selected countries as a percentage of GDP



Source: World Bank/IMF Debt Sustainability Analyses

For those low-income countries, aid flows will be the major resource to tap in future years. Again, using countries for which recent (post-COVID-19) DSA projections are available, concessional finance will be a major source of financing for those needs. Indeed, it is expected that the grant element of the public sector, that is, the relative concessionality of aid flows, would rise for all countries in the sample financing (Figure 12), to close to 50 per cent for the poorest ones (Comoros, DRC and Malawi).

Figure 12: Grant element of new public sector borrowing (in percent)



Source: World Bank/IMF Debt Sustainability Analyses

This sustained increased in aid flows comes in contradiction with recent trends. Official development assistance (ODA) from bilateral donors to the SADC region declined in recent years, from 5,5 per cent of GNI to 3 per cent, and 9 per cent from 7 per cent when including multilateral donors. Another notable trend is the increase in the share of loans since 2010. The medium term will thus be risky, with countries vulnerable to a drop in growth. In other words, either ODA decline should be reversed, or countries will need to reduce sharply the deficit during a fragile recovery phase at the risk of derailing it. Another option, however, is to restructure debt and reduce financing needs in the future.

3.4.2 Is it necessary to restructure debt?

The previous parts have shown that immediate debt restructuring is necessary for only a few SADC countries. For others, the main constraint is not due to the current outflows linked to debt service, but the ability to finance current expenditure to meet the needs of the crisis, and thus the lack of adequate concessional resources. The medium-term financing needs will also require a strong growth rebound, but indicated high vulnerability: A tepid recovery, for example, which would stem from a failure to end the health crisis; or the lack of exchange rate pressure, could trigger a debt crisis.

This makes the establishment of a coherent debt resolution framework an important task. The Common Framework for Debt Treatments beyond the DSSI, adopted on 13 November 2020 by finance ministers of the G20, will be tested over 2021. Designed as a coordination platform for official creditors, it is close in spirit to the Paris Club, with an extended membership. If a debtor country's debt is determined to be unsustainable, creditors will agree to share the reduction in debt stock in a comparable manner. In this case, and unlike the DSSI, the country will then be required with its private creditors with terms as least equivalent. As a result, the creditor base will be broader.

As of early 2021, the framework has started to be tested. Three countries have applied to the Common Framework: Ethiopia, Chad, and Zambia. Given the difficulties in coordinating the DSSI, there is no doubt that the Common Framework will require G20 lenders to go beyond sharp disagreements on the way to restructure official debt. Given the importance of China as a bilateral creditor, it is likely to crystallise disagreements: on the status of CDB, for instance, and on transparency. Recent experience has shown that China agrees to restructure its loans

relatively frequently, but on an *ad hoc* and uncoordinated basis.[33] With no direct mechanisms constraining private sector actors, negotiations with banks and bondholders will also be difficult, but the Common Framework will help as a backstop. A key lesson from the Brady plan in the 1980s in Latin America is that building consensus is difficult[34] and that deep restructuring will take time.

3.5 Conclusion

Given the scale of the crisis for developing economies, the role of official finance is thus bound to become more prominent. In times of disasters or major crises, as markets retreat, official finance tends to take over as the main engine of development finance. Horn et al[35] have illustrated this fact across history and shown the ebbs and flows of official finance. Their evidence points to three reasons to expect a resurgence of official finance in the next years, which could thus meet the financing needs of developing countries. First, official finance surges in times of crises and thus is highly countercyclical. Second, it tends to be more important when the world is more integrated. Third, the current trend has been one of increasing importance of official finance, whether through the emergence of new actors (China and other emerging markets, Gulf countries) or through new instruments such as central bank swaps.

SADC countries would benefit from such inflows of official finance, reversing several years of decline in aid flows. This is especially the case for countries that entered the COVID-19 crisis with a debt situation already in distress or very close thereto. For others, which have managed to keep a relatively low risk on their debt, a strong economic growth would allow limiting the consequences of COVID-19, but risks of lingering high debt are notable.

Multilateral institutions are best placed to disburse rapidly. In this sense, the DSSI places the right balance in the comparative advantage of each. The rapid finance from the World Bank and IMF, to the tune of 3 to 4 per cent of GDP, was the general background for the DSSI, which constituted a complementary effort from bilateral lenders, although in a less well-targeted manner. In aggregate, the sums were significant, but

33 A Kratz, M Mingey & D d'Alelio 'Seeking relief: China's overseas debt after COVID-19' (2020).

34 T Truman 'Sovereign debt relief in the global pandemic: Lessons from the 1980s' Peterson Institute for International Economics, Policy Brief, PB20-13 (2020).

35 Horn et al (n 11).

tend to be by definition directed towards countries with higher official bilateral debt and less concessional terms.

Perhaps most importantly, the DSSI also paved the way to deeper debt restructuring. In a sense, its success is more political than its impact on actual debt service: It provided a possible framework for collaboration at the G20 level that was not realistic before. In countries where debt relief will materialise, this political buy-in comes at a cost: transferring money from official to private creditors during the suspension period. This is the case for all emergency financing, including IMF programmes. However, the lesson that defaults need to be recognised early is difficult to apply in the midst of a global recession. In many cases, the DSSI was an important complement to other financing measures from the multilateral system. Eligible SADC countries have well understood the possible benefits, as all of them participated in the initiative. Extending to other vulnerable countries, in particular small island developing states, could be a way to complement the approach.

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4 The International Monetary Fund and debt surveillance in SADC countries

*Martin S Edwards**

4.1 The question and its importance

With the COVID-19 pandemic turning developing country finances upside down, the danger of a new debt crisis is a very real one. This moment is an essential one for us to evaluate the central role of the International Monetary Fund (IMF). In the pages below, I focus on the role of IMF surveillance over selected economies in the Southern African Development Community (SADC). Specifically, I evaluate the Fund's Article IV missions to these member countries to assess how the IMF evaluated debt levels in a key subset of SADC members. Did the Fund adequately warn countries about the fragility of their finances?

While there are concerns about the effectiveness of IMF surveillance, the evidence suggests that the Fund is making appropriate recommendations to member countries. In a subset of SADC member countries that have shown large increases in external debt, I find that IMF Article IV reports indicate a willingness to be critical about the current state of the economy, and they also discuss debt sustainability as a future risk. I find clear evidence of warnings in five of the six cases. However, discussions of foreign debt sustainability are not always topline results in the Fund's communications, as foreign debt was only mentioned by the executive board in its press release in two of six cases. These findings raise important questions about the robustness of country transparency about surveillance and raise larger questions about how the information from surveillance is used domestically.

Developing a better understanding of the IMF's role in the field of debt surveillance is important not only for academic practice, but for policy practice as well. Scholars have paid much more attention to IMF lending and conditionality than they have to the day-to-day surveillance work of the IMF. Even though surveillance is something that includes all IMF members, a check of Google Scholar reveals that there are almost three times as many citations on IMF conditionality than there are on surveillance.

* The author's research on the International Monetary Fund has been supported by the National Science Foundation.

I start by discussing the importance of this research question for both theory and practice, and I recap what the academic research tells us about IMF surveillance. I then discuss the current challenge of debt in developing countries, and in the final parts of the chapter I turn to findings and conclusions.

Theoretically, understanding surveillance helps us better understand how well monitoring works for international organisations more generally. The advice in IMF Article IV missions is just that. While there is an obligation to submit to surveillance, the IMF does not penalise countries for failing to adopt its recommendations, and the advice often is not too precise as well.[1] With this backdrop, it could be difficult to see how surveillance can make a difference, especially if countries are not likely to borrow from the Fund in the coming years. More broadly, there are many examples of weak monitoring mechanisms still making a substantive difference.[2] Where, then, does surveillance fit in?

The case for surveillance pessimism (or, rather, monitoring pessimism) should be leavened. It understates the fact that the content of IMF surveillance is information, and it further limits the potential influence of surveillance by keeping the focus solely on the state itself and asking whether the government does what the IMF wants. This is not a fruitful way to think of this question, since it often reduces to a simple formulation of 'does surveillance work or not?' The informational content of surveillance can have important value for domestic political actors as well as third parties. We need to better understand the pathways by which IMF advice can lead to policy change.[3]

Understanding IMF surveillance helps address policy questions as well. At a most basic level, we cannot claim to fully understand the IMF's role in debt management if we neglect the interaction of countries with the Fund in pre-crisis periods. The pandemic most certainly is an exogenous shock without parallel. Without understanding the IMF's role in debt surveillance in pre-crisis periods, we lose the ability to properly assess its role in the politics of adjustment as countries switch to drawing on IMF financing.

1 B Momani 'Assessing the utility of, and measuring learning from, Canada's IMF Article IV consultations' (2006) 39 *Canadian Journal of Political Science* 916.

2 MS Edwards *The IMF, the WTO, and the politics of economic surveillance* (2018); X Dai *International institutions and national policies* (2007); CD Creamer & BA Simmons 'Do self-reporting regimes matter? Evidence from the Convention Against Torture' (2019) 63 *International Studies Quarterly; O* Hathaway 'Do human rights treaties make a difference?' (2002) 111 *Yale Law Journal* 1935.

3 Edwards (n 2).

At this moment, the influence of the IMF over states and over markets is increasingly being challenged. Outstripped by country lenders, and with its claim of unusual expertise increasingly under attack, it is easy to be critical of the Fund. However, understanding the Fund's role in debt surveillance speaks to the broader issue of the current and future influence of the IMF.

Lastly, surveillance is emerging from a pause at the IMF. With over a hundred countries making inquiries about financial assistance, the IMF paused Article IV consultations for six months in April 2020. The idea behind the pause was to focus staff and country energies where they were most needed. The only country with an Article IV released during this timeframe was the United States in July, and the only lower middle-income country to have an Article IV consultation in the latter part of 2020 was Morocco. The only other countries to have an Article IV in the latter half of 2020 were Spain, the United Kingdom, Mexico, Brazil and China.

Just as countries are emerging from lockdown, the IMF's Comprehensive Surveillance Review has just been released. Understanding the IMF's role in debt surveillance helps to inform this process, carrying implications for what surveillance should look like as the world emerges from the pandemic.

4.2 The state of surveillance: What do we know? What do we need to learn?

I start by explaining a bit more about what surveillance is, and then turn to findings of studies that evaluate it. Surveillance at the IMF takes the form of annual meetings with countries known as Article IV consultations, so named for the relevant portion of the Articles of Agreement. These meetings are at the heart of the Fund's mandate to ensure that countries are implementing economic and financial policies 'toward the objective of fostering orderly economic growth with reasonable price stability'. Surveillance takes place in a three-stage process that starts with a visit to the country by an IMF team. The Article IV team conducts a series of meetings with government officials. These discussions with local authorities involve obtaining and understanding the data that will be used to generate economic projections. These projections, in turn, allow the staff to make an assessment of whether national economic policy is optimally contributing to the larger goal of ensuring growth without endangering stability.[4] The analytic work of the Article IV mission is completed in

4 In some countries there may be a statement released at the end of the country mission.

Washington, as the mission members and other staffers members produce a staff report. The staff report is the mission's reporting document that will be discussed by the IMF executive board. Finally, the purpose of the executive board review is to allow the representatives of other countries to weigh in on the findings and recommendations of the mission. This is the peer-review portion of surveillance, and it is at this phase that other countries offer additional recommendations. Importantly, the norm that documents from surveillance missions should be made publicly available has over time been strengthened at the IMF, and the full staff report can be accessed from the IMF website.

One of the consequences of academic inattention to surveillance is that we do not know a great deal about how it works or how well it works.[5] Many of the studies that exist focus on developed countries, which presents a real problem in dealing with the emerging crisis. Below I focus on two studies on the Eurozone, two studies on Ireland, and one study on emerging markets. There are important unanswered questions on the extent to which these findings are portable. In addition, these studies give us some pause in assuming that the IMF's warnings are automatically heeded by countries and result in corrective policies.

One of the key findings across studies of surveillance in the Eurozone is that the IMF's warnings came either too little too late or were sent to the wrong places. Prior to the Eurozone crisis, a detailed evaluation of IMF surveillance found that the Fund failed to fully appreciate the challenges of governance in a common currency area, and that the IMF did not faithfully play its role as an independent watchdog.[6] In particular, the design of surveillance being bilateral produced a problem of cumulativity applied to the Eurozone as a whole, and a corresponding inability to see how problems within member countries became problems within the Eurozone more generally. The deeply-ingrained assumption that 'Europe was different' and somehow innately capable of overcoming these challenges muted the depth of the Fund's analysis. The good news is that after the crisis broke, the Fund's surveillance of the Eurozone improved considerably. Not only did the tone of surveillance change, as the Fund increasingly spoke out against austerity, but the content of surveillance

During the pandemic these visits have all been virtual.

5 For more on what the IMF itself 'sees' when it evaluates surveillance, see Edwards (n 2).

6 J Pisani-Ferry, A Sapir & G Wolff *An evaluation of IMF surveillance of the Euro area* (2011).

changed as well, focusing more on the banking sector.[7] In this manner, it became more focused and more valuable to member countries.

This having been said, a further finding is that not all Eurozone member countries were treated the same. The Fund's desire for uniform solutions to regions in crisis has gotten it into trouble in the past, most notably in framing the East Asian crisis as a general problem of fiscal profligacy.[8] In the Eurozone, undifferentiated advice after the crisis broke led to some challenges in some countries by making matters worse. This finding is supported by textual analysis of the tone of Article IV staff reports across the region before the crisis.[9] This work finds that the IMF provided the strongest warnings in the wrong places, focusing criticism on Luxembourg, Malta, Portugal and Slovenia. In this analysis Italy was viewed positively, and Greece, Ireland and Spain were indistinguishable from the rest of the European Union (EU) countries. It is no accident that governance of the IMF complicates its efforts at being a neutral arbiter of member country economies, and that the Fund's challenge of being a 'truth -teller' becomes complicated when the truth needs to be told to leading countries on the executive board. This makes discussions of reforming the IMF complicated.

With this backdrop, it would be useful to look at a different level of analysis by evaluating IMF surveillance with respect to specific countries. It is no accident that scholars have focused on the Fund's view of the Irish economy. O'Leary notes that the IMF failed to identify how Irish public finances were becoming increasingly fragile.[10] Even if the IMF had diagnosed these vulnerabilities correctly, framing Ireland as a poster child with lessons for other countries sent a mixed message which would have not resulted in appropriate reforms. Breen concurs, noting as well that the quality of surveillance reports deteriorated considerably in 2006 onwards as a result of budget cuts within the Fund, weakening its impact at the worst possible time.[11]

7 As above.

8 T Murase 'Economic surveillance in East Asia and prospective issues' (2007) 76 *Kyoto Economic Review* 67.

9 L Golubovskaja 'IMF fiscal surveillance during the Eurozone crisis' (2016) 5 *International Journal of Signs and Semiotic Systems* 1.

10 J O'Leary 'External surveillance of Irish fiscal policy during the boom' Economics, Finance and Accounting Department Working Paper Series n210-10.pdf 14 (2010), Department of Economics, Finance and Accounting, National University of Ireland.

11 M Breen 'IMF surveillance of Ireland during the Celtic Tiger' (2012) 27 *Irish Political Studies* 431.

In a sample of developing countries, Edwards evaluates whether the Fund gave 'early warning' to five emerging market economies (Brazil, India, Indonesia, South Africa and Turkey).[12] Here the focus is the 2010-2013 period. Across these countries, US monetary stimulus has induced some concerns over fragility. I sought to understand how the IMF discussed the risks of changes in US interest rates to cause these capital inflows to dry up. I found that the IMF gave clear signals about this potential vulnerability across all five countries.

Taken as a whole, these papers raise some questions. There certainly are governance challenges that complicate IMF surveillance, but the magnitude of these dangers is unclear. The Fund seems to face greater threats to speaking truth to power in developed countries as opposed to developing countries. Certainly, there are concerns over how effectively the IMF is able to diagnose and communicate dangers before economies move into crisis. With these concerns at the fore, I now turn to discuss selected facets of the SADC experience with debt and evaluate the role of IMF surveillance in dealing with this issue.

4.3 Toward a growing debt crisis

While debt is not a new problem, the pandemic has considerably aggravated it. Governments all over the world face a two-fold crisis: a higher demand for government spending to mitigate the crisis coupled with shrinking tax revenue stemming from lockdowns. Pre-pandemic debt levels had been on the rise as governments sought to take advantage of favourable economic conditions. Low-income countries have been particularly vulnerable, as about half of them were already in, or at high risk of, debt distress prior to the pandemic. It is not an accident that IMF first Deputy Managing Director Geoffrey Okamoto has termed debt a pre-existing condition for greater risk.[13]

For sub-Saharan African countries, the problems are worsened still further by a collapse of tourism, prices for commodity exports, and a fall-off in remittances. With lockdowns in place across the globe, sub-Saharan Africa was particularly vulnerable to a drying up of tourism revenue, as 95 per cent of tourists in Africa are from another continent.[14] At the same

12 Edwards (n 2).

13 G Okamoto 'Resolving global debt: An urgent collective action cause' Opening remarks at the Peterson Institute for International Economics Conference, 1 October 2020, https://www.imf.org/en/News/Articles/2020/10/01/sp100120-resolving-global-debt-an-urgent-collective-action-cause. Accessed November 1, 2020.

14 UN Economic Commission for Africa 'Economic report on Africa 2020' (December 2020).

time, by early 2020 prices for more than two-thirds of African exports had fallen, affecting key sectors such as petroleum, metals, cotton, tea and coffee.[15] After years of impressive growth, the remittances market in sub-Saharan Africa shrank by an estimated 8,8 per cent in 2020 and another estimated 5,8 per cent in 2021.[16] The sources that governments might count on for foreign exchange were drying up.

Despite these hardships, relief may not be on the horizon, as the conventional strategies that governments would use to address economic downturns are not available. International capital markets are less of a ready opportunity compared to previous years, as borrowing costs are higher now compared to the same time period during the global economic crisis.[17] Increases in official development assistance have been modest and not enough to close the gap, as bilateral official development assistance (ODA) increased by only 4,1 per cent between 2019 and 2020.[18] The effects of the pandemic on government fiscal balances is expected to be especially acute in the coming year, and it is no accident that predictive work suggests that the probability of short-term debt distress has doubled.[19]

It is no surprise that additional external financing will be needed, and the *United Nations Conference on Trade and Development* (UNCTAD) places the estimate of needed resources at $2,5 trillion.[20] Recent research evaluating the IMF's current programme portfolio suggests that its resources are not up to the task and are not being used enough.[21] The IMF's workload to date has been putting strains on the organisation to adapt. With almost a hundred countries making inquiries about financial assistance, the focus of the Fund has moved from surveillance to lending and Article IV consultations have slowed to a trickle as staff have been

15 As above. It is important to note that many of these commodity prices increased in 2021.

16 D Ratha et al 'Migration and development brief 33: Phase II: COVID-19 crisis through a migration lens' (2020).

17 International Monetary Fund 'Regional economic outlook. Sub-Saharan Africa: A difficult road to recovery' (October 2020).

18 OECD 'COVID-19 spending helped to lift foreign aid to an all-time high in 2020 but more effort needed' (13 April 2021).

19 J Zettelmeyer et al 'Pandemic sovereign debt risks' Presentation at Peterson Institute for International Economics (1 October 2020), https://www.piie.com/system/files/documents/zettelmeyer-2020-10-01ppt.pdf (accessed 1 November 2020).

20 UNCTAD 'From the great lockdown to the great meltdown: Developing country debt in the time of COVID-19' Trade and Development Report Update, Geneva (2020).

21 T Stubbs et al 'Whatever it takes? The global financial safety net, COVID-19, and developing countries' (2021) 137 *World Development* https://doi.org/10.1016/j.worlddev.2020.105171 (accessed 4 January 2021).

adjusted. Given what we know about surveillance, the looming crisis makes the question at the heart of this chapter compelling. How well did the IMF evaluate this 'pre-existing condition'?

To best answer this, we need data and we need to look in the right place. I gathered data from the most recent issue of *International debt statistics* to classify SADC countries.[22] I classified 14 SADC countries (Namibia and Seychelles are not reported in this system) in terms of external debt stocks as a percentage of exports for 2010-2018. I grouped countries by changes in these levels over time. While this is useful to help underscore the scope of the problem, the primary value of this exercise was to better limit the countries on which I focus in evaluating IMF surveillance.

Based on this data, I organised countries together in a three-fold set of country groups. The corresponding charts can be found in Figures 1 to 3. First, there are high-risk countries: those with significant increases in external debt service since 2010. These countries would correspond to those with Okamoto's 'pre-existing condition': Angola, Malawi, South Africa, Tanzania, Zambia and Zimbabwe. Second, there are moderate-risk countries that correspond with an increase in external debt service, but at less alarming levels since 2010: Lesotho, Mauritius and Mozambique.[23] Finally, there are lower-risk countries, corresponding to a debt service level that is either constant or decreasing since 2010: Botswana, Comoros, the Democratic Republic of the Congo (DRC), Eswatini and Madagascar.

Below, I look at the record of IMF surveillance in these six high-risk countries. These are a 'most likely' test for the claim that surveillance is not up to the task.[24] Some basic information on these six countries is detailed in Table 1 below. In the pages that follow, I reference the Article IV consultations of each of these six countries to ascertain what the IMF says about each country's *current economic situation* with respect to debt, as well as what the IMF says about *future risks* in each country with respect to debt.

22 World Bank *International debt statistics 2021*, World Bank. doi:10.1596/978-1-4648-1610-9.

23 As noted in Figure 2, the debt levels for Lesotho and Mauritius are largely flat or have a lower slope than the high-risk countries. Mozambique decreased its debt levels in recent years, though the shift here came about because of debt restructuring in the wake of a 2016 default rather than fiscal prudence; K Strohecker 'Mozambique debt crisis: What does the country owe and to whom?' *Reuters* (9 September 2019), https://www.reuters.com/article/us-mozambique-debt-creditors-factbox/factbox-mozambique-debt-crisis-what-does-the-country-owe-and-to-whom-idUSKCN1VU1WE (accessed 5 June 2021.

24 Admittedly, while there is value in a more longitudinal appraisal tracking surveillance both across countries as well as over time within countries, the 'most likely' nature of this test suggests that such an approach is not necessary.

The focus for the selection of most likely countries is on levels of foreign debt, since these have a direct link to economic stability, which is the focus of the IMF's mandate. It is also the focus of much of the policy debate about the need for debt relief. However, in reading the Article IV documents, I note discussions of both foreign and domestic debt where relevant.

It should be noted that my focus is on the presence of warnings rather than the appropriateness of those warnings. While concerns about the Fund's dangerous fixation with fiscal policy continue to abound, and these certainly are important concerns, I want to focus more on the presence of warnings and the framing of risk rather than the correctness or the potential downside costs of the advice itself.[25]

So, how do we know warnings when we see them? Here I evaluate the record of surveillance. I look at both the press release issued following the executive board discussion as well as the staff report to make this appraisal. The focus for this part is how the IMF views the state of the economy at the time that the consultation was conducted.

An example will suffice to make this clearer. The statement below is from the press release issued following Namibia's most recent Article IV consultation.[26] Namibia's data does not appear in *International debt statistics*, therefore it is not classified in terms of foreign debt risk levels in Figures 1 to 3.

The authorities have implemented significant fiscal adjustment. However, public debt remains on a rising path, and government's growth financing needs are elevated. International reserves improved, albeit remaining below adequate levels.

Further in the press release, the summary of the executive board discussion mentions the following:

25 N Daar & N Tamale 'A virus of austerity? The COVID-19 spending, accountability, and recovery measures agreed between the IMF and your government' (2020), https://www.oxfam.org/en/blogs/virus-austerity-covid-19-spending-accountability-and-recovery-measures-agreed-between-imf-and Accessed April 25, 2021; D Munevar 'Arrested development: International Monetary Fund lending and austerity post-COVID-19' (2020), https://www.eurodad.org/arrested_development (accessed 25 April 2021).

26 IMF 'IMF executive board concludes 2019 Article IV consultation with Namibia' Press Release 19/331 (13 September 2019).

> After a period of exceptional growth and rising macroeconomic imbalances, public debt remains on a rising path, international reserves below adequate levels, and growth has come to a halt … The authorities' fiscal consolidation objectives strike an appropriate balance between stabilising public debt and supporting the economy, but actions are needed to deliver this outcome.

While this example does not refer to foreign debt *per se*, it suffices to clarify what a warning would look like in practice.

A second example comes from Seychelles, which is also not mentioned in *International debt statistics*, and not classified in terms of foreign debt risk levels in Figures 1 to 3. The press release for the 2019 Article IV consultation noted the following: 'International reserves are expected to remain at an adequate level, anchored by prudent macro-economic policies. Downside risks to the outlook stem largely from the external sector.'

The rest of the discussion in the press release focuses more on public rather than foreign debt. This is not a concern in so far as whether it constitutes a warning because public debt is at the heart of Seychelles' challenges in the coming years.[27]

To preserve medium-term sustainability, the authorities should maintain their debt reduction goal and take a phased approach in executing their ambitious infrastructure and climate investment projects. Implementing permanent saving measures in the 2020 budget and stepping up efforts to reduce fiscal risks arising from Air Seychelles will be important. The large public investment projects planned in coming years should be implemented within the envelope of the programme's fiscal targets. The authorities would need to create further fiscal space over the medium term beyond that required to secure the debt reduction goal to accommodate these priority investments.

In a strict sense here, this is also a warning but clearly not on foreign debt. This makes sense because it is not the problem. Since we know that these six high-risk cases (Angola, Malawi, South Africa, Tanzania, Zambia and Zimbabwe) have demonstrated a growing level of foreign debt greater than exports, these constitute an ideal test case for evaluating how well the warning mechanism in IMF surveillance works.

27 IMF 'IMF executive board completes third review under the policy coordination instrument for Seychelles and concludes 2019 Article IV consultation' Press Release 19/225 (14 June 2019).

4.4 Findings

It is worth noting that the Article IV documents do not mention the pandemic. This reflects timing rather than omission. The press release on South Africa was prepared shortly after the World Health Organisation (WHO) declared COVID-19 a public health emergency, and the press release on Zimbabwe mentions that the policy discussions and the board meeting occurred before the coronavirus was classified as a pandemic. The March 2020 statement on Tanzania, which was circulated to the media the day after the Fund team left the country, does not mention COVID. While the nature of this statement (an end of mission press release rather than a press release summarising the executive board discussion) could account for this in part, the omission may also be attributed to the views of the former Tanzanian President, whom the Fund staff visited in person after the WHO declaration. As noted below, the press release and staff report for the 2019 consultation were not released by the Tanzanian government.

A brief summary of each of the high-risk countries appears in Table 2. Speaking across these individual country findings gives us three key lessons. First, information about foreign debt is not always clear in the press release. This is somewhat surprising given the growing importance of this issue in these six countries. We would glean evidence about the state of foreign debt in these countries only from the cases of the press releases for Zambia and Zimbabwe. These two cases, given their status as countries in default or near default, are absolutely most likely cases, and this is a reassuring finding.

In other cases the information from the press releases alone is not sufficient to help us answer the question of whether the Fund is sending clear warning signals. In Angola and South Africa the focus in the press release is more on public/domestic debt, and in the case of Malawi, the press release mentions that donor support has tailed off in recent years, but it is not explained why that is the case.

To infer from these three cases that the Fund's documents *on the whole* did not send warnings about foreign debt, however, would be a mistake. There is plenty 'under the hood' in the staff report on each of these countries. Significantly, Article IVs now include two common documents to sharpen the analytic insights of the country team. They now include debt sustainability analyses that evaluate the effects of different kinds of shocks to the country's debt profile, and risk assessment matrices that discuss prospective risks and offer potential strategies for addressing them should they emerge. There is ample discussion of warning about reserve

levels and foreign debt in five of these high-risk countries. It is not always communicated as a top-line item.

A further finding is that these countries lack fiscal space to combat the pandemic, and they are doubtless now more fragile because of the economic downturn produced by it. The growing concern over the robustness of global financial safety net is very real.[28] In five of the six countries, there were already considerable concerns about the level of foreign debt. As noted in Table 1, three of these countries have moved into borrowing, and the other three still have work to do to convince the IMF of their credibility. The presence of warnings about debt, which predate the pandemic, coupled with the absence of debt relief solutions, raises important concerns about the robustness of the global financial safety net. They also advance an urgent need for jump-starting discussions of an African Monetary Fund to provide additional liquidity for countries in the region.[29]

To be fair, one can go too far here. It would be a mistake to think that any surveillance can prevent countries from accumulating excessive debt in the first place. However, if there are country warnings, and increasing awareness that this is a global problem, and the international community only provides piecemeal solutions, the case for more urgent action clearly is strengthened.

Third, there are concerns about transparency avoidance, but this does appear to be an isolated problem. The reason why there is no information about Tanzania is that no information from the 2019 consultation ever saw the light of day. The government departed strongly from precedent by refusing to release any information about the 2019 staff report, going so far as to deny that they blocked it in the first place.[30] It seems that this was a once-off occurrence not emulated by other countries. For the three previous years, 100 per cent of African staff reports were published. The fact that there was not a cascade of countries following in the steps of

28 K Gallagher et al 'Safety first: Expanding the global financial safety net in response to COVID-19' Boston University Global Development Policy Centre GEGI Working Paper 0037 (2020).

29 D Bradlow & W Kring 'Why the African Monetary Fund is a good idea and what can be done to get it going' *The Conversation* (5 July 2019), https://theconversation.com/why-the-african-monetary-fund-is-a-good-idea-and-what-can-be-done-to-get-it-going-119827 (accessed 4 January 2021).

30 F Ng'wanakilala 'Tanzania denies blocking release of scathing IMF report' *Reuters* (23 April 2019), https://www.reuters.com/article/us-tanzania-economy-imf-idUSKCN1RZ1CP (accessed 4 January 2021).

Tanzania is a good thing, as departing from IMF norms about transparency of surveillance would harm everyone.

4.5 Broader implications

There are many debates about the state of the global financial safety net, but in these cases, IMF surveillance looks to have its eyes on the proverbial ball. Based on this review of cases, it is diagnosing risks and making warnings appropriately, and this focus predates the pandemic, so the IMF is not new to this issue. As the crisis is sure to deepen, having high-quality information is essential, so the Fund is well prepared to transition these countries from surveillance to lending.

One implication for reforming surveillance comes forward in these findings. In the case of Ireland there were problems with the messages being mixed as the press release said one thing, and the staff report said quite another. In these cases, the problem is not one of mixed messages, but one of having the staff report distilled in a more concise form for the reader. Moving toward a more standard format for these press releases ensures equality of coverage.

All of this raises the question of whether surveillance can be made more influential. The comprehensive surveillance review is intended to focus on how to increase the ‘traction’ of surveillance. Article IVs have limited influence, though information from them is clearly used by market actors to price sovereign debt.[18] The growing attention paid to the pandemic may make the IMF’s words more effective in the coming months, as the findings from surveillance missions carry greater weight domestically. However, more work is necessary not only to ensure that the Fund conveys a consistent message, but also to better assess the links between information and policy change.

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Figure 1

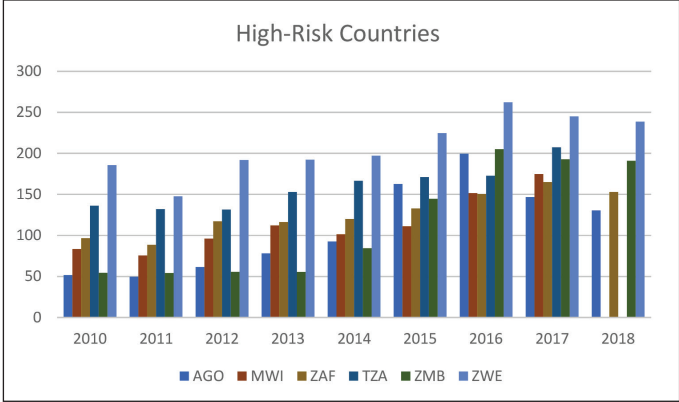


Figure 2

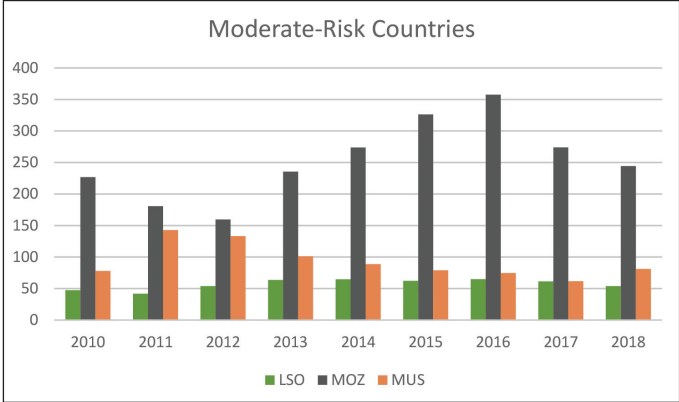


Figure 3

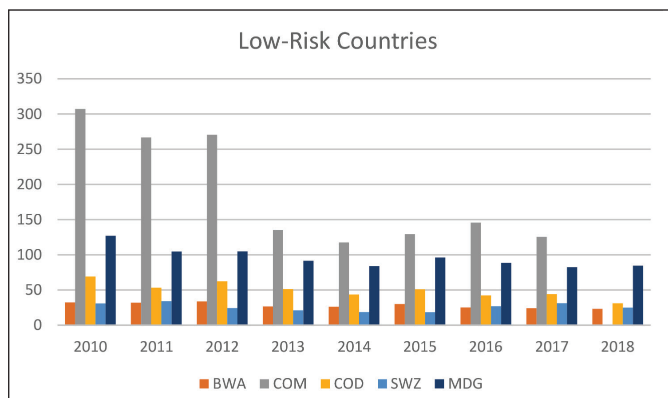


Table One: IMF Engagement with SADC High Debt Risk Countries

	Date of Last Article IV	**Lending**
Angola	5/18/2018	EFF approved 12/18
Malawi	4/30/2018	Three year ECF approved 4/2018; RCF 5/15/20
South Africa	1/24/2020	RFI approved 7/27/20
Tanzania	3/18/2019	PSI ended 1/2018; CCRT debt relief 6/10/2020
Zambia	7/24/2019	June and July 2020 discussions on RCF
Zimbabwe	2/24/2020	Staff monitored programme approved 5/20/2019

CCRT: Catastrophe Containment and Relief Trust
ECF: Extended Credit Facility
EFF: Extended Fund Facility
RCF: Rapid Credit Facility
RFI: Rapid Financing Instrument
PSI: Policy Support Instrument

Table Two:	***Summary of Article IV Documents***
Angola	Press release focuses on public debt and diversifying revenue sources. Debt Sustainability Analysis addresses vulnerability of foreign debt. Risk Assessment Matrix mentions debt profile vulnerable to tightening external conditions.
Malawi	Press release focuses on public debt, while mentioning that donor support has withdrawn in recent years. Recommend tax reforms and agriculture reforms to reduce budget burdens. Debt Sustainability Analysis frames risk of external debt distress as moderate. Excessive External Borrowing is a key element of the Risk Assessment Matrix.
South Africa	Press release mentions ballooning expenditure and slow growth in revenue leading to high budget deficits. Recommend expenditure based fiscal consolidation. Debt Sustainability Analysis finds external financing needs increasing, with depreciation risk the largest factor shaping vulnerability. Risk Assessment Matrix mentions debt profile vulnerable to rapid shift in global risk premia.
Tanzania	2019 Staff Report and Press Release not published as authorities deny consent. 2020 Article IV completion statement references adequate reserves and manageable foreign debt.
Zambia	Press release mentions international reserves less than three months cover, and government has a heavy reliance on non-concessional debt. Public debt on unsustainable path, but Executive Board welcomed decision to postpone new non-concessional loans. Debt Sustainability Analysis frames the risk of external debt distress as high. Risk Assessment Matrix mentions debt profile vulnerable to rapid shift in global risk premia.
Zimbabwe	Press release mentions international reserves very low. Govt has yet to clear arrears with World Bank and other multilaterals. Cautions against ‘continued recourse to collateralized external borrowing on commercial terms.’ Debt Sustainability Analysis classifies as ‘in debt distress.’ Risk Assessment Matrix mentions urgent need to reengage international community to clear arrears; debt profile vulnerable to rapid shift in global risk premia.
Sources: Country staff reports listed at www.imf.org.	

5 Sovereign debt via the lens of asset management: Implications for SADC countries

*Kevin Gallagher and Yan Wang**

The COVID-19 pandemic has laid bare the fact that 'hyper-globalisation' has made it impossible to contain crises within national borders. Multilateral international cooperation no longer is a choice but a necessity. This chapter attempts to address debt sustainability issues from two different angles for Southern African Development Community (SADC) countries – a conventional 'debt-to-GDP ratio' approach and a 'public sector balance sheet' approach. In addition, we assess whether and to what extent Chinese debt is a significant source of debt distress for SADC countries, and develop a series of potential policy options for alleviating the debt burden of countries in debt distress.

Part 5.1 below provides an overview of the economic impact of COVID-19 on SADC countries. Part 5.2 reviews the previous literature related to debt sustainability and the Heavily-Indebted Poor Countries (HIPC) initiatives; part 5.3 examines the sovereign debt situation using the traditional debt-to-GDP ratio; part 5.4 introduces an approach focusing on asset and liabilities – the public-sector balance sheet approach. Part 5.5 discusses the overall strategy of debt relief via investment. Part 5.6 proposes patient capital that is important for sustainable development, while part 5.7 presents a few policy options.

5.1 Economic impact of COVID-19

The world economy suffered the biggest shock since World War II due to the COVID-19 pandemic and the 'great closedown'. There was a 'sudden stop' of capital flows and unprecedented capital outflows from emerging market and developing economies (EMDEs) in March and April 2020.[1] The International Monetary Fund (IMF) had estimated in October 2020 that global economic growth would be -4,9 per cent in 2020, worsening by 1,9 percentage points from its April forecast. Such a major contraction

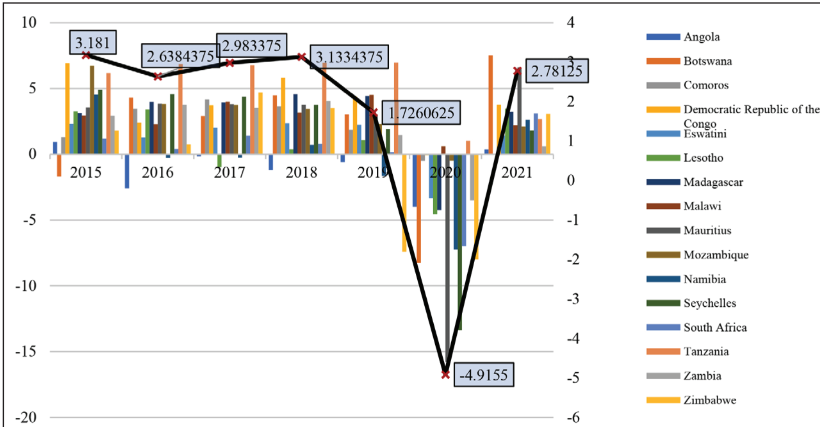
* The authors are grateful to Justin Yifu Lin for co-authoring earlier studies, to Dag Detter, Marilou Uy and Chunlin Zhang and three discussants at the University of Pretoria Conference for comments, and to Yinyin Xu for excellent research assistance.

1 IIF *Capital flows report: Sudden stop in emerging markets* (April 2020).

may have repercussions for years to come. In the latest World Economic Outlook in April 2021 the International Monetary Fund (IMF) estimated that the global growth is projected at 6 per cent in 2021, moderating to 4,4 per cent in 2022. The projections for 2021 and 2022 are stronger than in the October 2020 forecast, reflecting the additional fiscal support in a few large economies, the anticipated vaccine-powered recovery, and the continued adaptation of economic activity to subdued mobility. However, the high uncertainty remains.

Before the pandemic the SADC was the home of the largest amount of intraregional trade in Africa.[2] Based on IMF estimates of the impact of the pandemic in the region, the average gross domestic product (GDP) growth rate of SADC countries will have dropped to -4,91 per cent through 2020 (Figure 5.1). The IMF has also provided an overall optimistic projection for the recovery of the SADC group at 2,78 per cent in 2021. However, even before the pandemic, SADC countries' development aspirations were challenged, as massive financing needs had led to rapidly-increasing public debt.

Figure 5.1: Real GDP growth rate, SADC countries and the average, %



Source: IMF WEO data, updated 19 May 2021

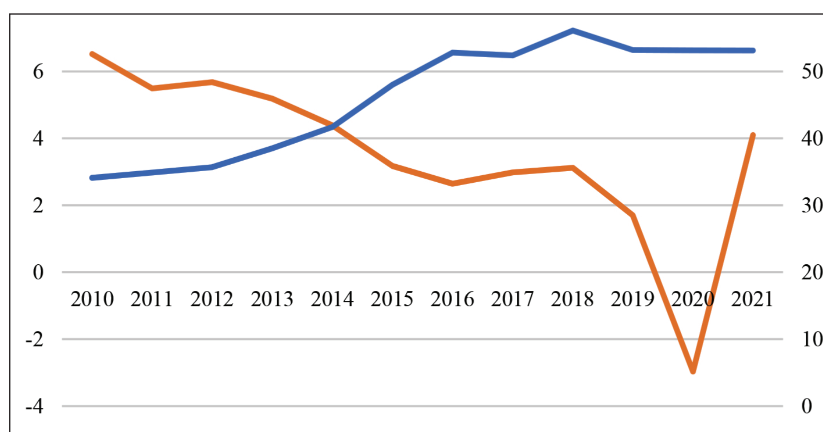
Debt: The current wave of debt accumulation, which began in 2010, has reached record highs and spread worldwide – private sector debt has risen

2 The SADC is comprised of 16 countries, which are Angola, Botswana, Comoros, Democratic Republic of the Congo, Eswatini, Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, Seychelles, South Africa, Tanzania, Zambia and Zimbabwe.

rapidly, and public sector debt almost doubled for all economies in the past decade. In the case of the EMDEs debt has risen from 38 per cent of GDP in 2000 to 62 per cent in the past decade. The same trend can be found in low-income countries: Their public debt-to-GDP ratio now is 47 per cent of GDP, up from 29 per cent of GDP in 2010.

To foster macro-economic stability, the SADC has set a target of 60 per cent with respect to the government debt as a percentage of GDP. Based on the African Development Bank (AfDB) data, the group has stayed within its target (Figure 5.2). Nevertheless, the SADC countries have experienced a slow-down in economic growth while the government debt is getting closer and closer to the preset target. Country performance varies dramatically; some have a debt-to-GDP ratio of less than 15 per cent, while others, such as Angola and Mozambique, have a higher than 100 per cent public debt-to-GDP ratio. In addition, Zambia defaulted in October 2020 and entered into restructuring talks with private creditors and China Development Bank (CDB).[3]

Figure 5.2: SADC real GDP rate against government debt as a % of GDP



Source: IMF and AfDB databases. Note: Gov't debt using right axis.

The initial threat in March and April 2020 was of a global liquidity crunch due in part to large capital outflows from EMDEs, leading to the loss of official foreign exchange reserves and local currency depreciation in many

3 A debt deferral agreement has been reached between the government of Zambia and CDB on 28 October 2020, according to the Treasury Secretary of Zambia. (Eric Olander, Oct 28, 2020)

countries. Although capital inflows to some emerging markets resumed in the second half of 2020, the liquidity shortage is far from over.

The pandemic is not the only challenge lying ahead. Global warming and climate change have devastated the living conditions in many countries, rich and poor, small and big, bringing a multi-dimensional effect. New thinking such as ‘asset-based refinance’ (ABF), the debt-for-climate swaps are now being discussed.

5.2 Indicators of debt sustainability: Definitions, and pros and cons

Although, historically debt has been an instrument of development, over-borrowing and over-lending, in the presence of volatile capital flows in the globalised economy, should be avoided. This part briefly reviews the previous debt waves and the respective international debt frameworks during each period, and we will provide our comments and critiques of the conventional indicators.

5.2.1 Debt sustainability: Pre/post-HIPC

The global economy has experienced three waves of debt crises and restructuring over the past 40 years: the 1980s, 1990s and in 2008. The historic peak of the total debt of emerging market economies reached almost 170 per cent of GDP in 2018. Despite initiatives led by the World Bank and the IMF on global debt sustainability analysis, the existing frameworks are not sufficient, as reflected by the continuous criticism from scholars and civil society.

First, Fischer and Easterly, in their seminal work, explained debt dynamics using the following identity:

$$Change\ in\ d = (primary\ deficit/GNP) - (seignorage/GNP) + (real\ interest\ rate - growth\ rate) \times d \quad (1)$$

Where ***d*** denotes the debt ratio, or the ratio of government debt to GNP.

The authors provided a simple and intuitive explanation with the equation that the non-interest deficit has to be financed with new debt to the extent that this deficit exceeds the amount of money created by the central bank. Additionally, nominal interest expenditures have to be financed with new debt. However, many researchers have pointed out the weaknesses in the above formulation.

- Debt dynamics given above are significantly affected by the difference between the growth rate (g) and real interest rate (r), as pointed out by many.[4]
- A major problem is that it completely ignores the public assets a country has, and the saving and investments that could increase public assets. It has blurred the picture of what a government does: to finance consumption or to finance investment in public goods? What is the capital formation rate per dollar of debt borrowed?[5]
- In other words, the framework has a bias against government investment in productive assets including human capital and hard infrastructure, which could later become public sector assets as a cushion for debt sustainability.[6]

5.2.2 Three waves of debt restructuring

The HIPC initiative, originally launched by the World Bank and the IMF in 1996, was designed to address debt problems and poverty reduction. A reduction in the stock of HIPC countries' external debt to sustainable levels occurred on the condition of continued efforts in macro-economic stabilisation, structural adjustment. The initiative sets out the completion point at which HIPCs are required to reduce the net present value (NPV) of external debt to a maximum of 150 per cent of exports, prior to the revision in 2017.

In 2005, with poverty reduction being tied firmly with debt relief, the Multilateral Debt Relief Initiative (MDRI) cancelled 100 per cent of outstanding debts, both bilateral and multilateral, to HIPC countries that reached the completion point. By January 2006, 19 countries were eligible for immediate MDRI relief. Meanwhile, this marks the start of the post-HIPC era, along with a new definition of debt sustainability, as defined below.

In April 2005 the Bretton Woods institutions agreed on a new debt sustainability framework (DSF) for low-income countries, which included post-completion point HIPC countries. The DSF was again revised in 2017. The revised framework associated a country's risk of debt distress with the quality of its policies and institutions as measured by the World

4 For now, we ignore the small difference between GNP and GDP in developing countries. See Sergei Gorbunov and Henning Bohn's studies on Russian Federation and the United States, for example.

5 J Lin & Y Wang *Going beyond aid: Development cooperation for structural transformation* (2017) 66-69.

6 IMF *Fiscal monitor: Managing public wealth* (2018).

Bank's Country Policy and Institutional Assessment (CPIA) scores, on the basis that better-performing countries would be able to bear a higher debt burden (Table 5.1).

Table 5.1: Debt Sustainability Framework (DSF) Country Policy and Institutional Assessment (CPIA)

Debt Sustainability Indicators (%)	**Strong (**		**Medium (**		**Weak (**	
	Old	**2017 Rev.**	**Old**	**2017 Rev.**	**Old**	**2017 Rev.**
PV of debt/GDP	50	55	40	40	30	30
PV of debt/exports	200	240	150	180	100	140
Debt service/ exports	25	21	20	15	15	10
Debt service/ budget revenue	22	23	20	18	18	14

Source: IMF (2017)

However, developing country governments and their economists have had many complaints about the DSF and the mechanism, because countries that violated these benchmarks will be defined as being in 'debt distress', and will lose access to the global capital market.-

- The 2017 version of the IMF DSF was considered 'obsolete' since it only treated the 'total public debt' and missed out the fact that many governments were borrowing at market interest rates, both domestically and externally.[7]
- In our view, this framework has ignored the public-sector assets, including infrastructure assets, and thus has an anti-investment bias.
- The fiscal austerity programme advised by the Troika (the IMF, European Central Bank and European Commission) forced crisis countries such

7 B Pinto 'The 2017 version of the IMF and World Bank's LIC Debt Sustainability Framework: "Significant overhaul" or "obsolete"?' Duke Global Working Paper Series 2019/06 (2019).

as Greece to 'cut public spending to the bone', which 'the IMF later admitted were self-defeating'.[8]

- In addition, the above approach could not deal with the issues of large capital inflows and outflows under 'liberalised capital account'. In this regard, China's experience in avoiding financial crises in the past four decades is worth studying.
- On the other hand, the Washington-based international financial institutions (IFIs) promoted 'capital account liberalisation' before 2012,[9] which had led to a financial crisis in some countries.[10] Therefore, EMDEs must be careful and vigilant against the 'capital flight' as happened in March and April 2020, during which 'temporary capital controls might prove useful'.[11]

5.3 Assessing debt sustainability of SADC countries: All creditors, including China

In this part we first utilise the conventional indicators of debt-to-GDP ratios in our descriptive analysis, and then provide critiques on this measure. An alternative measure of government net worth (as asset minus liability) will be presented in part 5.4.

5.3.1 Sovereign debt databases and SADC data analysis

Using the IMF 2018 Global Debt Database (GDD), we found that four SADC countries have a debt level exceeding the SADC target of 60 per cent. As noted earlier, the debt-to-GDP ratio, of course, is not sufficient as a single indicator to determine debt sustainability (Figure 5.3).

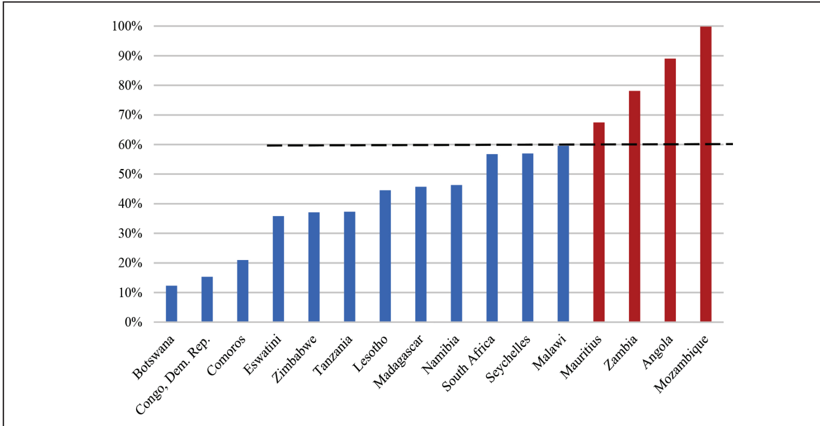
8 M Mazzucato *The value of everything: Making and taking in the global economy* (2018) 234.

9 In 2012 the IMF officially recanted its policy conditionality of opening capital account, as shown by Managing Director Christine Lagarde's speech in Malaysia indicating that temporary capital controls can be used during crises.

10 J Ostry, P Loungani & D Furceri 'Neoliberalism oversold?' (2016) 53 *Finance and Development* 38; KP Gallagher *Ruling capital: Emerging markets and the reregulation of cross-border finance* (2015).

11 Christine Lagarde, speech in Kuala Lumpur, Malaysia (14 November 2012).

Figure 5.3: Government debt-to-GDP Ratio, SADC countries, %, 2018

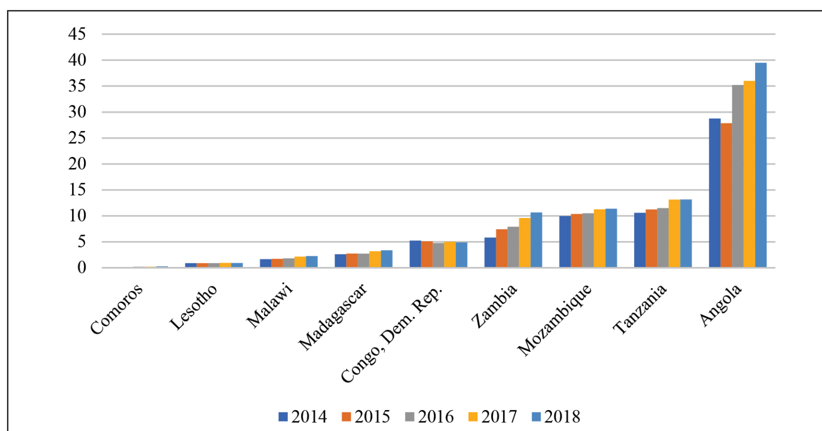


Source: Authors, based on IMF Global Debt Database (GDD). Note: Given the constraint of data availability, we used general government debt (percent of GDP) for the DRC, Mauritius and Tanzania, and central government debt (per cent of GDP) for the rest.

We examine the external debt of nine SADC countries using the international debt database provided by the Debt Service Suspension Initiative (DSSI) and found the following preliminary results for the nine SADC countries with available data.[12] The debt accumulation in the past few years is already a warning for the debtor countries, even without the pandemic. The total debt of the nine countries in 2014 was US $65,54 billion, which had accumulated to over US $86 billion in 2018. In addition, the level of indebtedness varies from country to country. Among the nine SADC countries, Angola is the most indebted country, with a total debt exceeding US $39 billion in 2018. Meanwhile, Zambia, Mozambique and Tanzania for the past few years all have had a total debt of over US $10 billion. Zambia in fact requested a six-month suspension on $42,5 million interest payments from the holders of its $3 billion in Eurobonds in October 2020 – essentially defaulting on those bonds (Figure 5.4).

12 Angola is also eligible under the DSSI for debt suspension, given its high level of indebtedness, despite the fact that it is not a low-income country.

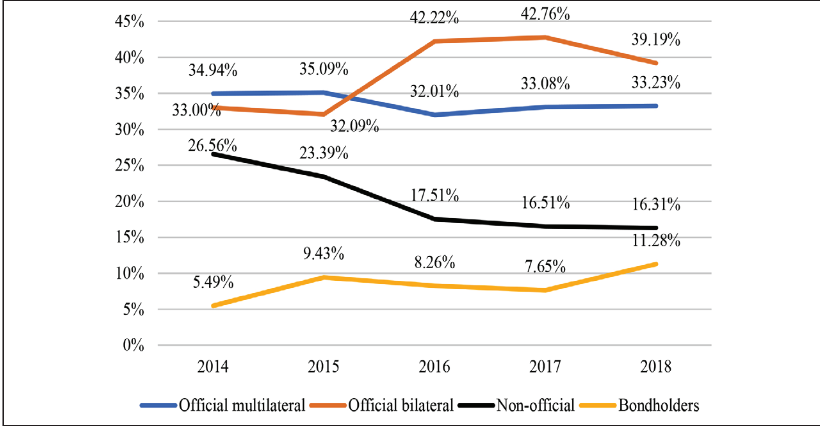
Figure 5.4: Total external debt of nine SADC countries, US$ billion, 2014-2018



Source: World Bank-IMF DSSI database, accessed in October 2020

Major creditor types of these countries vary significantly. In general, the official multilateral and bilateral creditors are the major creditors, to whom these countries owe over 60 per cent of the total external debt. An interesting trend observed is that the amount owed to non-official creditors, such as commercial banks, has been decreasing while the portion owed to bondholders has been rising in recent years (Figure 5.5). However, debt issues are very country-specific. For example, the portion of the external debt of Angola owing to the official bilateral creditors is declining with a growing share owed to the non-official creditors. On the other hand, over 80 per cent of the external debt of low-income countries (LIC) such as Malawi is owed to the official multilateral creditors such as the International Development Association (IDA) of the World Bank, the IMF and the AfDB.

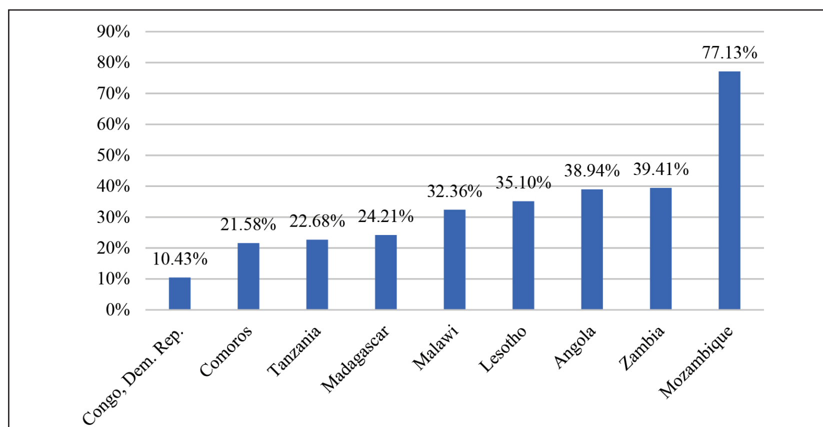
Figure 5.5: External debt of nine SADC countries by creditor type, % of total debt, 2014-2018



Source: World Bank-IMF DSSI database accessed on 17 October 2020

We also calculated the external debt-to-GDP ratio for these nine countries and found that the debt-to-GDP ratio is 31,66 per cent on average. However, there are large differences among countries in terms of the external debt-to-GDP ratio. The external debt is 77 per cent of the GDP for Mozambique, while it is slightly over 10 per cent for the DRC (Figure 5.6). Based on the June 2020 IMF assessment on the risk of external debt distress, Tanzania and Madagascar are among the low-risk group, the DRC, Comoros, Malawi and Lesotho are among the moderate group, while Mozambique (as well as Angola) is regarded as being in debt distress.

Figure 5.6: External debt-to-GDP ratio, nine SADC countries, 2018



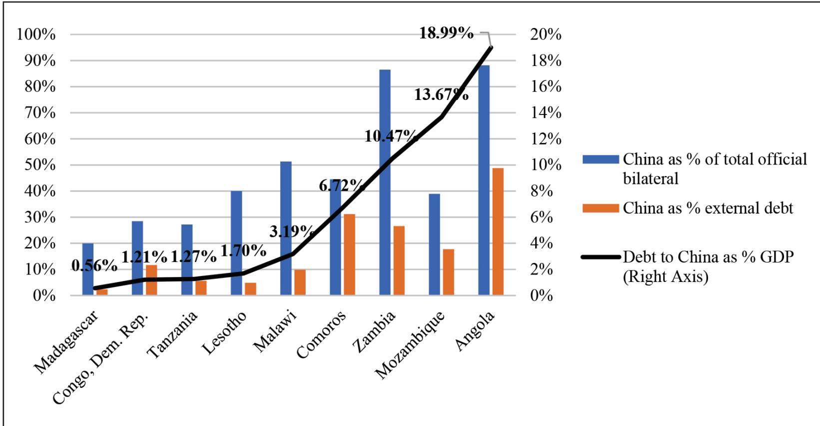
Source: World Bank-IMF DSSI, WDI

5.4.1 China as the creditor: An analysis based on DSSI

China has been portrayed as 'the largest creditor' or, to be more specific, 'the largest official bilateral creditor' in the world. However, in fact, these misperceptions were due to the non-transparency of various Chinese lenders and the lack of data on global sovereign debt, as pointed out by Acker et al.[13] Using the DSSI database, we provide a descriptive analysis on Chinese lending to the nine SADC countries covered by the DSSI initiative (Figure 5.7).

13 K Acker, D Brautigam & Y Huang 'Debt relief with Chinese characteristics' CARI Paper Series (2020).

Figure 5.7: Chinese lending to nine SADC countries, %, 2018



Source: authors, based on DSSI database 2020. Note: Debt owed to China = Official bilateral debt owed to China + non-official bilateral debt owed to China. The left axis is for China as % of total official bilateral debt and China as % of external debt, the right axis is for the debt to China as % of GDP.

On average, China is the creditor of 17,6 per cent of the external debt for SADC countries, including both official and non-official, which is around 6 per cent of the GDP for the nine SADC countries. In the cases of Zambia, Mozambique and Angola, the borrowing from China is over 10 per cent of their GDP. More than 86 per cent of Zambia's official bilateral debt is owed to China, and 88 per cent in the case of Angola. On average, almost half of the official bilateral debt of these nine SADC countries is owed to China. Although the proportions of debt owed to China seemed high in these countries, evidence also shows that the Chinese debt relief for these countries has been going on for many decades.[14]

However, the above analysis using the conventional measure of debt-to-GDP ratio fails to provide a full picture as it ignores the asset side of the public-sector balance sheet, and it neglects the uses of the debt – whether it is for consumption or investment. This bias in measurement has led to a policy bias against investment, especially investment in infrastructure in low-income countries over many decades. We will return to this topic in part 5.5.

14 As above.

5.5 Debt relief through development: Investing in public asset

Investing in public infrastructure is now widely recognised to be beneficial for economic development in developing countries. For example, investment in transportation can greatly reduce the transport cost and facilitate trade. However, building infrastructure is lumpy, risky and takes a long time to complete and, hence, can be very expensive. Here we present another angle of assessing a country's creditworthiness, which encourages investment in public assets. If the public sector asset increases, the cushion for debt distress becomes thicker and stronger.

An alternative measure of debt sustainability: Public sector net worth

Public assets are critical in current debt discussions. The IMF 2018 study on 'Managing public wealth' highlights the importance of using the public sector balance sheet (PSBS), including all government-owned and controlled enterprises, both financial and non-financial assets. In this approach, public sector net worth (= assets minus liabilities) is key to debt sustainability and investor confidence. If the public sector net worth is positive, the country is solvent, but may have a liquidity problem.[15] If the public sector net worth is negative, then the country has a serious issue of insolvency. According to the World Bank on belt and road initiative,[16] investment in transport corridor infrastructure is projected to generate certain trade and growth. In other words, if countries borrow to fill the identified infrastructure bottlenecks, they will see an increase in trade and GDP, from which more public revenue can be derived. For example, China invested massively in infrastructure after the global financial crisis in 2008/2009. As a result, its export competitiveness became stronger and its public sector net financial worth remained positive, at 8 per cent of GDP in 2017, despite also having large amounts of domestic and foreign debt.

Data on public sector net worth is difficult to obtain, especially for non-financial assets such as real estate assets and productive assets, the value of which may fluctuate over time. In fact, good estimates of public assets are currently unavailable for most SADC countries. We only managed to find data for Tanzania and South Africa. The public sector net worth of

15 A caveat is that the value of non-financial assets may fluctuate and be difficult to be liquidated. Hence, financial net worth is more critical in the international credit market.

16 World Bank *Belt and road economics: Opportunities and risks of transport corridors* (2019).

Tanzania was 45,8 per cent of GDP in 2014, and it was 151,5 per cent of GDP for South Africa in 2016 (Tables 5.2 and 5.3).

If all SADC countries can provide a good estimate of their public sector assets, it could help them to boost investor confidence to continue investing in these countries and, thus, facilitate further borrowing. In addition, good management of existing public sector infrastructure can help create jobs, generate revenues for the government, and reduce the need for debt restructuring.

Table 5.2: Tanzania: Public sector balance sheet, 2014, percentage of GDP

	General government	**Non-financial public corps**	**Consolidated public sector**
TOTAL ASSETS	123.7	31.9	101.3
Of which: Non-financial assets	99.7	14.4	73.5
Financial assets	24.0	17.6	27.8
TOTAL LIABILITIES	77.9	31.9	96.2
Of which: Debt securities	6.6	-	4.7
NET FINANCIAL WORTH	-53.9	-14.2	-68.4
NET WORTH	45.8	-	5.2

Table 5.3: South Africa: Public sector balance sheet, 2016, percentage of GDP

	General government	**Non-financial public corps**	**financial public corps**	**Consolidated public sector**
TOTAL ASSETS	208.3	49.6	72.3	269.0
Of which: Non-financial assets	156.7	44.6	2.5	203.7
Financial assets	51.6	5.0	69.9	65.3
TOTAL LIABILITIES	56.8	49.6	72.3	117.5
Of which: Debt securities	47.4	7.2	1.8	41.8
NET FINANCIAL WORTH	-5.2	-44.6	-	-52.3
NET WORTH	151.5	-	-2.5	151.5

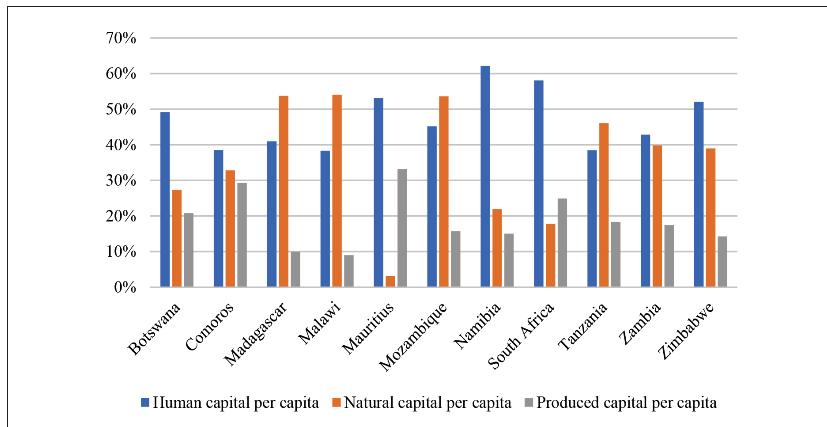
Source: IMF (2018)

What additional assets do SADC countries have?

SADC countries have a good level of produced capital, human capital and natural capital, indicating that the structure of their factor endowment is quite rich and appropriate for balanced growth. Traditional economic growth theory places less emphasis on human than natural capital leading to underinvestment in human capital and over-exploitation of natural capital. The latter, natural capital, includes land, forests, subsoil resources (oil, gas, minerals), water, biodiversity and other natural assets. If the host country continues to invest in all three of these assets, the country's creditworthiness will become stronger.

Building on the foundation of all capitals in various forms, these SADC countries can target their comparative advantages (for example, Mauritius, Namibia and South Africa are human capital-abundant, while Madagascar, Malawi, Mozambique and Tanzania are natural capital-rich) (see Figure 5.8). The human capital-rich countries can develop their human capital-intensive export sectors such as garment, footwear, and other light manufacturing sectors, while natural capital-rich countries can concentrate on agri-business, forestry and mineral export or nature-friendly tourism. For South Africa, it has emerged as the industrial hub of SADC countries.

Figure 5.8: Produced capital, human capital and natural capital of 11 SADC countries, as a percentage of total capital, 2014



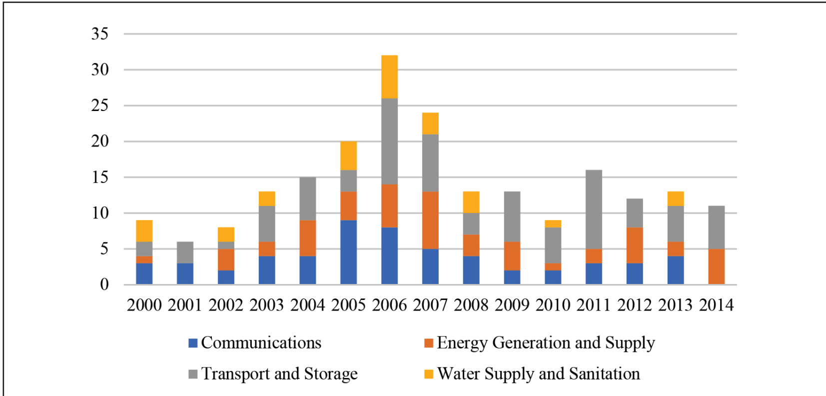
Source: Data based on World Bank, 2018

China has been actively helping African countries to target their respective comparative advantages. It is estimated that approximately 25 per cent

of all infrastructure development in Africa in the past 18 years has been funded by the Chinese government, with the African government contributing an estimated 40 per cent.[17]

China-sponsored and completed projects have addressed Africa's bottlenecks in economic transformation, representing public sector assets, not only debt. In recent research, Lin and Yan Wang[18] identified economic bottlenecks for 54 African countries and found that Chinese-financed projects had matched with African countries' bottlenecks in 78 per cent of the 214 hard infrastructure projects that it supported in 2000 to 2014. The 214 hard infrastructure projects that had been completed covered water (26), energy (52), transport (80) and communication (56). These projects were largely public goods (74 per cent),[19] including electricity, water and sanitation, ports, airports, highways and railways, as well as semi-public goods (26 per cent) which is telecommunication (Figure 5.9).[20]

Figure 5.9: Decomposition of the 214 completed hard infrastructure projects financed or co-financed by China, by sector and year



Source: Lin and Wang 2021, based on completed projects in China Aiddata.com

In sum, we strongly support the approach of using the public sector balance sheet (and net worth=asset minus liabilities) as a more comprehensive

17 YM Wang 'China's BRI could help Africa achieve transformation agenda' *Xinhua* (17 October 2019), https://mp.weixin.qq.com/s/HpwQBZyTPtDkC4Z6aoW7ww (accessed 26 October 2020).

18 J Lin & Y Wang 'Economic transformation in Africa and how best China can support' in A Zeufack & S Wang (eds) *China and Africa in the 21st century* (forthcoming 2021).

19 In economics, a public good is a good that is both non-excludable and non-rivalrous.

20 Lin & Wang (n 18).

measure of creditworthiness and debt sustainability, which encourages public investment in assets. The completed infrastructure projects represent public assets that can potentially generate jobs, government revenue, while promoting economic growth. They provide a thick cushion for any debt distress.

5.6 Chinese state actors are patient capital holders

Chinese state actors are holders of patient capital[21] as illustrated by their long history of providing debt relief for African countries. Acker et al[22] provide an insightful analysis on the history of debt relief with 'Chinese characteristics' for developing countries including those in Africa. The authors pointed out that the Western media has provided misinformation on China and debt distress. Most importantly, 'no asset seizure' is found and no evidence is found to support the so-called 'debt-trap diplomacy' accusation.

China has shown considerable forbearance and flexibility in debt negotiations in the 1980s and 1990s. It is noticed that the cost of violating the contract with Chinese lenders was actually 'quite low' for borrowers. The cases of the Republic of the Congo and Mozambique suggest that 'agreements have been easier to reach with Chinese lenders than with private creditors'.[23] China's approach was even more flexible than the members of the Paris Club, during the HIPC initiative. During recent bilateral negotiations, China has used Paris Club terms/conditions for debt relief, illustrating that China is behaving within the international 'rule of the game', despite the fact that China is not a member of the Paris Club, and that does not agree with all the conditions.

Nevertheless, China is unlikely to write off or forgive a large portion of outstanding debt, as the tradition is that China maintains the policy that only its zero-interest loans are eligible for forgiveness. Alternatively, rescheduling and refinancing are more common in recent years' restructuring of debt (Figure 5.10, based on Kratz et al).[24] Chinese state

21 Patient capital is defined as the ultra-long-term capital invested in a relationship, much like venture capitalists investing in innovative ideas, and equity-like investors holding a stake in the development of a country. Its maturity could be longer than ten years, and their capacity for taking risk is stronger. Lin & Wang (n 5); Mazzucato (n 8).

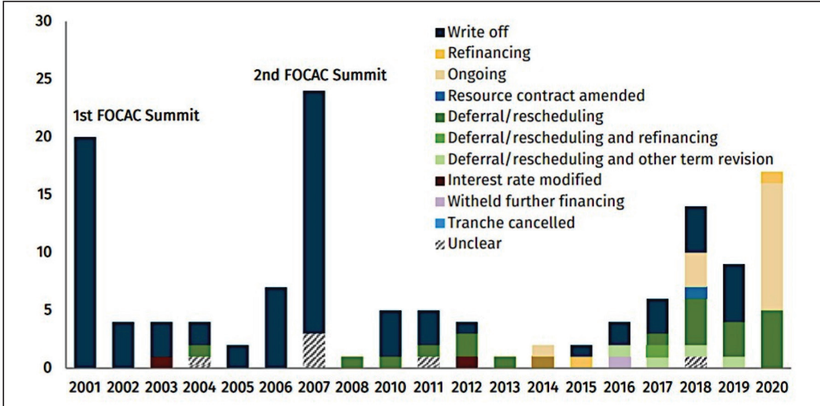
22 Acker et al (n 13).

23 As above.

24 A Kratz, M Mingey & D d'Alelio 'Seeking relief: China's overseas debt after COVID-19' Rhodium Group (8 October 2020), https://rhg.com/research/seeking-relief/ (accessed 19 October 2020).

actors are constrained by the Budget Law, whereas there is no foreign aid law in China.

Figure 5.10: Restructurings of Chinese debt by outcome and year



Source: Kratz et al 2020. Rhodium Group

Note: This does not include recent Chinese claims to have given ten countries debt deferrals through DSSI within the G20 framework.

When considering requests from debt-distressed countries, China's flexibility is based on the fact that China and African countries are partners in climbing the same mountain of structural transformation. Essentially, the Chinese are taking a stake in the development of the host countries in Africa, as reflected in the recent case of Angola.

Recent case of Angola: The country has been hit both by the oil price fall and COVID-19. According to the IMF report released in late September 2020, Angola will receive $6,2 billion in debt relief thanks to agreements lined up with three of its major creditors, among which China is the largest official bilateral creditor. Meanwhile, the country is also busy negotiating with some Chinese banks and government agencies on debt re-profiling deals.[25]

25 For details, see IMF 'Angola: Third review under the extended arrangement under the extended fund facility, requests for augmentation and rephasing of access, waivers of non-observance of performance criterion and applicability of performance criterion, modifications of performance criteria, and completion of financing assurances review' – Press release; staff report; and statement by the executive director for Angola (September 2020) 44-45.

On debt accumulation, China is not the only creditor and is not necessarily the largest bilateral creditor for all the African countries. In fact, other official creditors and the private sector are collectively even more important. Furthermore, 'there are reasons why [developing] countries prefer to borrow from China, given that the private lenders usually provide short-term financing and the traditional Western donors completely forget about the hard infrastructures'.[26] Thus, China's patient capital may be preferred by developing countries, given that they are in great need of real sectoral development.

5.7 What more can be done? Policy options

(1) Support multilateralism and push for the IMF to issue more SDRs, as issuing SDRs is countercyclical and unconditional. In particular, Gallagher et al[27] also suggest putting the funds of the SDRs that are not used by countries, particularly by high-income countries, into trusts of different kinds, which could partly serve the needs of Africa and other developing regions.

(2) Support the IMF, the World Bank Group and regional financial arrangements (RFAs) to issue more emergency liquidity loans and expedite their disbursement. Currently, only about 12 per cent of the IMF and RFAs' resources have been used and only about half of that is disbursed.[28] In addition, the IMF should not resort to its DSF without considering the country's public sector balance sheet and prevent certain countries from borrowing/refinancing. During this pandemic-led global recession, encouraging public investment by allowing continued borrowing and refinancing is critical to maintain economic recovery and to 'build back better'.

(3) Innovative financing and refinancing may be designed, based on already-completed projects that are part of the public assets. Concretely, assume an internationally-financed infrastructure project in country A has been completed and in operation with cash flows,

26 D Dollar 'Seven years into China's Belt and Road' (1 October 2020), https://www.brookings.edu/blog/order-from-chaos/2020/10/01/seven-years-into-chinas-belt-and-road/ (accessed 19 October 2020).

27 KP Gallagher, JA Ocampo & U Volz 'IMF special drawing rights: A key tool for attacking a COVID-19 financial fallout in developing countries' Brookings Blog (26 March 2020), https://www.brookings.edu/blog/future-development/2020/03/26/imf-special-drawing-rights-a-key-tool-for-attacking-a-covid-19-financial-fallout-in-developing-countries/ (accessed 19 October 2020).

28 T Stubbs et al 'Whatever it takes? The global financial safety net, COVID-19, and developing countries' (2020) 137 *World Development* 105171.

and the host country A has repaid a part of the loans, say, 30 per cent, but is now having difficulties in repaying its debts, then if the host country agrees, multilateral or bilateral financial agencies can use the 30 per cent equity share of the cash flows that the government owns as the collateral to issue new finance at a lower interest rate, which may be called ‘asset-based refinance’. Again, if the host government agrees, sovereign wealth funds (SWFs) and green funds can participate in the auction of these shares and bid for these unlisted equity shares. In this way, new liquidity will flow into country A without hurting its credit rating.[29]

(4) The pandemic might be the force that catalyses long-overdue innovation in the sovereign debt market to facilitate less protracted and simpler restructurings and help avoid pitfalls in the future. The ‘state-contingent debt instruments’ have been mentioned again, which link a sovereign’s debt service payments to its capacity to pay, thus could maintain debt relief that a country obtained in a restructuring.[30] One such example is ‘commodity-linked’ bonds (CLBs).[31]

(5) Utilising ‘tailored solutions’ in the ‘debt-distressed’ countries. We have suggested, on various occasions, for the Chinese government to enhance transparency and accountability and expedite the process of enacting a foreign aid law, while continuing to coordinate with G20, the IMF, the Paris Club, and follow international rules of the game. It is possible for the Chinese institutions to ‘find innovative solutions’ for debt restructuring, because they are holders of ‘patient capital’, and they are essentially in the same boat with these African countries where the projects are located.

- China has been acting, and is likely to continue working, within the common framework agreed by G20 countries.[32] China is so far the biggest

29 A recent example is that the USDFC has made a deal with the Ecuadorian government which will privatise the public assets that China helped to build, and USDFC will help repay the Chinese loans. Essentially the Ecuadorian government is auctioning away the public asset. SWFs can do the same, and new finance will flow to this country. See https://www.ft.com/content/affcc432-03c4-459d-a6b8-922ca8346c14 (accessed 19 October 2020)

30 P Breuer & C Cohen ‘Time is ripe for innovation in the world of sovereign debt restructuring’ IMF Blogs (20 November 2020), https://blogs.imf.org/2020/11/19/time-is-ripe-for-innovation-in-the-world-of-sovereign-debt-restructuring/?utm_medium=email&utm_source=govdelivery (accessed 22 November 2020).

31 IMF blog on ‘The role of state-contingent debt instruments in sovereign debt restructurings’ (December 2020).

32 A debt reduction framework will be discussed and agreed in the G20 meeting in November 2020 according to the declaration by G20 finance ministers on 14 October

contributor to the DSSI, suspending at least $1,9 billion in repayment due this year, according to the G20.[33] In addition, Xi Jinping announced additional debt exemption within the framework of the FOCAC.[34] Recently, former Central Bank governor Zhou Xiaochuan also stressed the preference to a 'tailored approach'.[35]

- China's development financing and debt restructuring are driven by requests of host countries. Examples include the TAZARA (Tanzania-Zambia) railways and its maintenance; sugar refineries in Sukala Mali, the Agriculture Technologic Demonstration Stations (which are now commercialised), and the approach used in Angola this year.
- 'Demonstrated willingness to repay' is important for Chinese creditors, as in the cases of Pakistan.[36] However, due to capital flow volatilities of EMDEs, large liquidity injection is not feasible from Chinese creditors, unless capital flight can be stopped through temporary capital controls in these countries. After all, 'liberalising capital account' is not a part of China's experience. Washington-based IFIs need to make good for their own policy conditionalities on liberalising capital accounts and serve as the international lender of last resort.

(6) Debt-for-climate swaps: There is now over 30 years' experience with debt-for-nature swaps whereby countries in debt distress agree to invest a certain percentage of debt relief into natural assets. The most recent case in the SADC region is Seychelles, which had defaulted on its debts in 2008 and had struggled with debt distress thereafter. Seychelles partnered with third parties to buy back US $21,6 million of its sovereign debt at a discount from its creditors. Seychelles now repays these loans into a trust fund called the Seychelles Conservation and Climate Adaptation Trust (SeyCCAT). Then, the trust repays US $15,2 million in loan capital over a ten-year period. Over 20 years, the trust will finance upwards of US $5,6 million of marine conservation

2020.

33 J Wheatley 'African debt to China' Financial Times (26 October 2020), https://www.ft.com/content/bd73a115-1988-43aa-8b2b-40a449da1235 (accessed 30 October 2020).

34 On 17 June 2020 Chinese President Xi Jinping announced that China would exempt the zero-interest loans to 15 African countries under the framework of Forum of China and Africa Cooperation (FOCAC).

35 XC Zhou 'The BRI is not debt trap and China supports G20 proposal to extend debt relief' CF40 (24 October 2020), http://www.xinhuanet.com/english/2019-10/17/c_138480217.htm (accessed 19 October 2020).

36 It is reported that Pakistan received a new loan of $1,3 billion after the country 'made a significantly large foreign debt repayment, resulting in depletion of reserves by $1,71 billion in the week ended on May 26, 2020', https://tribune.com.pk/story/2252732/pakistan-receives-1.3-billion-loan-from-china (accessed 19 October 2020).

> and climate adaptation activities, and transfer US $ 3 million into a long-term endowment that will finance similar activities long into the future.[37]

For SADC countries, and for developing countries in general, it is important to know what the government owns (asset) and owes (liability), to distinguish 'patient capital' from 'footloose' investors, and to separate long-term (structural) and short-term (liquidity) issues. First, to address the immediate health and liquidity crises, African countries need liquidity support from the multilateral financial organisations such as the IMF and the World Bank Group. Debt cancellation will not achieve the goal of liquidity support. The lending of unused SDR and various currency swaps can be used for short-term liquidity purposes. Second, to address the long-term structural issues, African countries need to work with patient capital holders such as multilateral development banks, regional and national development banks. Innovative re-financing arrangements can be explored and designed carefully and worked out, including, but not limited to, 'asset-based refinance', as well as debt-for-climate swaps. The advantage of these approaches is that they provide liquidity without hurting a country's credit rating. In the long term, patient capital is needed to address developing countries' structural issues, such as capacity development for export competitiveness.

37 Economists Group 'Seychelles swaps debt for nature' World Ocean Initiative (8 April 2020), https://www.woi.economist.com/seychelles-swaps-debt-for-nature/ (accessed 19 October 2020).

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6 ASSESSING THE LEGAL OPTIONS OF MANAGING AND RESTRUCTURING SOVEREIGN DEBT IN THE SADC REGION IN THE CONTEXT OF THE COVID-19 PANDEMIC

*Murikuki Muriungi**

6.1 Introduction

The COVID-19 pandemic has only exacerbated what already was a disturbing debt treadmill in the Southern African Development Community (SADC) region. Six of the 16 SADC member states, including Zimbabwe and Angola, had exceeded the public debt to gross national income (GNI) ratio target of 60 per cent in 2019 with some of the countries declared to be in danger of debt distress by the International Monetary Fund (IMF) and the World Bank,[1] Zambia and Mozambique registering a debt to GNI ratio of 119,3 per cent and 135,7 per cent respectively.[2] Further research indicates that the SADC region spends up to US $21,1 billion annually in external public debt repayments, thereby compromising the ability of countries to provide essential public goods such as health care.[3]

A slump in the global economy, low but rising commodity prices,[4] declining exports, increasing public expenditure on social infrastructure, such as health care, and the need to support the vulnerable in the face of a

* The author wishes to thank Prof Daniel Bradlow, Dr Magalie Masamba, Prof Gustav Muller, Dr Celine Tan, Prof Kenneth K Mwenda and Prof Makana Mbengue for their extremely insightful comments and the organisers of and participants in the Sovereign Debt Workshop hosted by the International Development Law Unit of the University of Pretoria for the opportunity to present previous drafts of this paper. All errors remain my own.

1 IMF *World economic and financial surveys: Regional economic outlook: Sub-Saharan Africa domestic revenue mobilisation and private investment* (2018) 12.

2 AFRODAD 'Assessment of national financing and investment policies in the East Africa Community (EAC) and Southern Africa Development Community (SADC) countries against regional protocols' (2019) 17 24-26. Also see World Bank 'International debt statistics' (2021), https://datatopics.worldbank.org/debt/ids/country/mus/counterpartarea/wld (accessed 18 June 2021).

3 ACTSA 'The money drain: How trade misinvoicing and unjust debt undermine economic and social rights in Southern Africa' (2019), https://actsa.org/wp-content/uploads/dlm_uploads/2019/08/ACTSA-The-Money-Drain-FINAL.pdf (accessed 31 October 2020).

4 There has been a marked rise in commodity prices in 2021 which have risen above pre-COVID-19 pandemic levels following an upsurge in economic activity. See AfDB 'African economic outlook 2021: From debt resolution to growth: The road ahead for Africa' (2021).

withering tax base due to the COVID-19 pandemic are sure to increase the public debt burden of SADC countries. This is especially important given the commodity-based nature of a number of economies such as those of Mozambique, Angola, Zambia and South Africa, which are already heavily indebted. There have also been incidences of economic difficulties caused by climate-related disasters among some member states such as Mozambique,[5] which have added to the public debt burden. This impels the need for sovereign debt renegotiation or restructuring that takes care of these considerations.

Unlike in the past under the Heavily-Indebted Poor Countries (HIPC) initiative in which at least three SADC member states were involved,[6] there now is a new creditor landscape with a vastly diversified creditor community comprising official creditors including China as the largest, and private creditors including hedge funds and institutional investors. The different typology of creditors lacking in good communication links, as well as the crisis wrought by the pandemic spanning across all regions will only make debt crisis resolution more difficult to resolve. Yet, there is no overarching international legal framework on sovereign debt restructuring, with most debt restructurings taking place in an *ad hoc* fashion and prompting calls for one suitable to developing economies.[7] Admittedly, however, the G20 countries, at the urging of the IMF and the World Bank, initiated the Debt Service Suspension Initiative (DSSI) which took effect in May 2020 in a bid to temporarily suspend debt repayments for eligible countries. The DSSI has since delivered up to $5 billion in

5 Eg, in 2019 natural disasters claimed more than 1 200 lives in East and Southern Africa with countries such as Mozambique experiencing two severe cyclones in March and April 2019 (Idai and Kenneth) which led to a loss of over US $1 billion in property. There have also been incidences of locust invasions and other climate related disasters including floods and droughts yet most African economic sectors including agriculture are climate-sensitive in nature. See World Meteorological Organisation 'State of the climate in Africa 2019' (2020) 6-8, https://library.wmo.int/doc_num.php?explnum_id=10421 (accessed 4 May 2021).

6 These include Malawi, Mozambique and Zambia, https://www.cadtm.org/Initiative-for-the-heavily?lang=en#:~:text=In per cent201996 per cent20the per cent20IMF per cent20and,of per cent20the per cent20Third per cent20World per cent20Debt (accessed 4 May 2021).

7 M Masamba & F de Bonis 'Towards building a fair and orderly international framework for sovereign debt restructuring: An African perspective' AFRODAD Issues Paper 18, https://media.africaportal.org/documents/SDRM_PAPER_final.pdf (accessed 18 January 2021); also see M Muriungi 'Towards a legal framework on sovereign debt restructuring: A developing countries' perspective' unpublished LLM dissertation, University of Nairobi, 2016, http://erepository.uonbi.ac.ke/bitstream/handle/11295/100281/Muriungi%20Muriuki_Towards%20a%20Legal%20Framework%20on%20Sovereign%20Debt%20Restructuring%20a%20Developing%20Countries%E2%80%99%20Perspective.pdf?sequence=1&isAllo (accessed 18 January 2021).

debt relief to over 40 eligible countries.[8] In November 2020 the G20 also launched the Common Framework for Debt Treatments beyond the Debt Service Suspension initiative aimed at coordinating debt reprofiling and restructuring undertaken by official and private creditors beyond the modest debt relief under the DSSI.[9]

This chapter critically assesses the viability of available legal options for managing and restructuring the SADC region's sovereign debt in the face of the COVID-19 pandemic with a view to exploring the options that SADC countries should consider pursuing. These legal options include arguing that the COVID-19 pandemic is a *force majeure* incident that allows countries to suspend debt repayments; the state of necessity doctrine; debt standstills or moratoriums to stay interest rates and debt repayments from falling due, thus offering relief to debtors; and debt buybacks as well as traditional market-based solutions including collective action clauses and state-contingent debt contracts. The chapter argues that individual SADC debtor countries need to consider making use of the various *ex-ante* contractual mechanisms and *ex-post* legal defences as complements to help manage their debt obligations during the pandemic.

The chapter progresses as follows: Following this introductory part, the second part is a brief summary of the debt situation in the SADC region. The third part considers the legal options for managing and restructuring sovereign debt. In this part, the chapter begins with *ex-ante* contractual mechanisms and *ex-post* mechanisms, beginning with the short-term options and then the long-term options which constitute defences under international law. The final part concludes the chapter.

6.2 Debt situation in the SADC region

Since the year 2012 when debt levels in SADC member countries began to rise following a steady decline in nearly a decade, both the dynamics and composition of sovereign debt in the SADC region have changed significantly.[10] There has been huge borrowing for infrastructural development and to finance budget deficits from both domestic and external sources; a shift from multilateral creditors to bilateral and private creditors; a decline in concessional loans; access to international bond markets and commercial borrowing; and increased external borrowing

8 https://www.worldbank.org/en/topic/debt/brief/covid-19-debt-service-suspension-initiative (accessed 18 June 2021).

9 https://ihsmarkit.com/research-analysis/g20s-common-framework.html (accessed 18 June 2021).

10 AFRODAD (n 2) 9.

from China.[11] This has been on account of many factors, which include the ease in global financing following the 2008 global financial crisis as global capital moved to the Global South in search for yields as the economic recession subsided; the growth of domestic financial markets which enabled increased lending to governments from the domestic market; an increase in lending by non-Paris Club countries such as China;[12] and flexible guidelines on external debt limits set by the IMF and the World Bank.[13] Consequently, the average public debt to gross domestic product (GDP) ratio stood at 47,9 per cent in the year 2017 with the ratio being particularly high for some countries, such as Mozambique and Zambia.[14]

A depreciation in exchange rate following the fall in commodity prices in the year 2015 and the strengthening of the United States dollar contributed to an accumulation of public debt for a number of SADC countries by increasing the foreign currency-denominated external debt

11 AFRODAD (n 2) 8-11. In particular, the loans provided to lower-income economies by China have grown from an average of 4 per cent of total public external debt in 2008 to 17 per cent in 2018; share of bond debt in lower-income economies has been rising by an average of two percentage points of GDP per annum on new entrants and larger issuances with Eurobond issuances almost tripling from an average of $6 billion per annum during 2012 to 2016 to about US $16 billion per annum in 2017 to 2018. See IMF 'IMF policy paper: The evolution of public debt vulnerabilities in lower-income economies' (February 2020) 17. In addition, commercial creditors accounted for 40 per cent of Africa's total external debt at the end of 2019; top five creditors to Africa since 2015 are bondholders accounting for 27 per cent of the continent's external debt at the end of 2019; 21 African countries had issued Eurobond instruments valued at over $155 billion by the end of August 2020, https://www.afdb.org/sites/default/files/2021/03/09/aeo_2021_-_chap2_-_en.pdf (accessed 18 June 2021) 49, 50.

12 China's lending to Africa generally increased tenfold between the years 2012 to 2017 with 40 per cent of Zambia's total debt owing to China. See AL Dahir 'Chinese lending to African countries jumped tenfold in the last five years' *Quartz Africa* (15 November 2018), https://qz.com/africa/1463948/chinese-lending-to-african-countries-jumped-tenfold-in-the-last-five-years/ (accessed 18 January 2021). Also see C van Staden 'China holds all the cards as pandemic pushes African countries to default on loans' *SAIIA* (30 September 2020), https://saiia.org.za/research/china-holds-all-the-cards-as-pandemic-pushes-african-countries-to-default-on-loans/ (accessed 19 January 2021).

13 These Guidelines are the Revised Guidelines on Public Debt Management by the IMF and the World Bank. They have more flexible proposals that allowed for more borrowing by SADC countries, such as excluding debts of state-owned enterprises from the debt sustainability analyses; accounting for remittances when assigning risk ratings of a country; and focusing on lending more for public investment which is key to economic growth. See IMF 'Public information notice: IMF executive board reviews the low-income country debt sustainability framework and adopts a more flexible policy on debt limits in IMF-supported programmes' 09/113 (9 September 2009), https://www.imf.org/en/News/Articles/2015/09/28/04/53/pn09113 (accessed 19 January 2021).

14 AFRODAD (n 2) 9.

when expressed in local currency terms.[15] In particular, external debt in SADC countries rose from 13,7 per cent of the total debt in 2010 to 25,1 per cent in 2018.[16] Further, in terms of debt composition, there has been a shift in borrowing from multilateral creditors toward private creditors and non-Paris Club bilateral creditors such as China as well as a decline in concessional debt. Private debt of SADC countries rose from 3,4 per cent in 2009 to 12 per cent in 2017.[17] In addition, Zambia and Mozambique registered a decline in concessional debt from 80 per cent of total debt in 2009 to 44 per cent in 2017, and 96 per cent of total debt to 76 per cent during the same period, respectively.[18] Basically, the creditor community of the SADC member countries is now significantly diversified comprising multilateral, bilateral and private creditors. This has readily apparent implications in terms of achieving debt workouts given the competing and conflicting interests of these vastly diversified classes of creditors, compared to times past.

Additionally, the COVID-19 pandemic has forced countries to take wide-ranging steps to mitigate the associated social and economic disruptions. Some of these steps have included significant stimulus packages; broad-based tax reliefs; cash transfers to vulnerable groups; increased health expenditures; loans and loan guarantees to businesses; and direct liquidity injections – all of which have had implications on the debt situation of these countries.[19] It is estimated that African countries need an additional US $154 billion in financing for the year 2020/2021 to deal with the pandemic, and this is happening against a withering tax base.[20] While an average debt to GDP ratio had stabilised at around 60 per cent for a number of African countries in 2019, it was estimated that pandemic-related spending had caused increased debt-to-GDP ratio by more than 10 percentage points by the end of 2020.[21] The increasing debt burden as a result of the pandemic thus calls for debt restructuring to offer relief to countries and enable them to deal with the associated consequences.

15 N Mupunga et al 'External debt dynamics and implications for monetary policy in the SADC region' Paper prepared for the SADC Committee of Central Bank Governors (CCBG), RBZ Working Paper Series 1/ 2019 11, 16, https://www.rbz.co.zw/documents/working_papers/External-Debt-SADC-Paper1-Working-Paper-1-2019-.pdf (accessed 19 January 2021).

16 Mupunga et al (n 15) 6.

17 AFRODAD (n 2) 10.

18 As above.

19 https://www.afdb.org/sites/default/files/2021/03/09/aeo_2021_-_chap2_-_en.pdf (accessed 4 May 2021).

20 As above.

21 As above.

6.3 Legal options for managing and restructuring sovereign debt

6.3.1 *Ex ante* contractual mechanisms

Collective action clauses

Collective Action Clauses (CACs) are market-based contractual provisions that enable decision making by a stipulated majority of creditors involved in a debt restructuring process. In the absence of a sovereign bankruptcy law, CACs have proved invaluable in enabling the restructuring of sovereign debt. Usually, CACs allow a qualified majority of creditors or bondholders (say 75 per cent) to change the terms and conditions of the debt contract including a debt standstill and to impose new terms and conditions that apply to all creditors. CACs help prevent holdout creditors, such as vulture funds, from preventing a restructuring by refusing to participate and then suing for their full value of the debt, thus undermining the restructuring process.

CACs are usually contained in various bond contracts. The share of international sovereign bonds incorporating enhanced CACs grew from 27 per cent of total outstanding stock in September 2017 to 39 per cent as of October 2018.[22] Between 2014 and 2018 there have been around 510 sovereign bond issuances for a nominal principal amount of US $620 billion, with 88 per cent of these issuances incorporating enhanced CACs.[23] The uptake of enhanced CACs[24] under New York law and English law have stood at 89 per cent and 90 per cent respectively, with only those issued under Chinese and Japanese law not having enhanced CACs.[25] With respect to sovereign bond issuances in the SADC region, several member countries, including Angola, Mozambique and Zambia,

22 IMF 'Fourth progress report on inclusion of enhanced contractual provisions in international sovereign bond contracts' (March 2019) 4-7.

23 IMF (n 22) 4.

24 Enhanced CACs were introduced by the International Capital Markets Association (ICMA) in 2014 as an improvement to the regular CACs developed in 2003. In the case of enhanced CACs, sovereigns are able to make a single offer to all bondholders subject to the condition that all bondholders receive a uniform offer with a perfect restructuring occurring if there is a 75 per cent threshold of the vote. Accordingly, in enhanced CACs, as opposed to regular CACs, a single vote has the power to bind a sovereign's several series of bonds into a debt restructuring on similar terms. See M Sobel 'Strengthening collective action clauses: Catalysing change – The back story' (2016) 11*Capital Markets Law Journal* 3.

25 IMF (n 22) 4.

have had enhanced CACs in the bond contracts.[26] Consequently, CACs as market-based solution may be useful where they are incorporated in various sovereign debt contracts and this should be complemented with comprehensive debt restructuring (of both official and private class of debt) required for SADC countries and developing economies more generally.

State-contingent debt contracts

Given the inherent uncertainty of life generally, it is usually prudent to provide for any eventualities that may occur. Especially now, with the pandemic that has had enormous impacts on the economic well-being of individuals and sovereigns alike, it would be appropriate if SADC countries' debt contracts were to provide for flexibility that accords with the situations that obtain. State-contingent debt contracts, such as GDP-linked bonds, usually link contractual debt service obligations to a predefined variable state by providing that a sovereign will only pay what it is able to pay in the obtaining circumstances and this may turn out to be smaller or larger payments depending on the variable to which the bonds are linked.[27] Such contracts are usually a recognition of the fact that a sovereign's ability to meet its debt obligations can change significantly almost immediately, as has happened with the pandemic.

The difficulty with crafting a state-contingent debt contract is anticipating the state of the world that would trigger a contingency. SADC countries can predicate their debt agreements on, say, particular commodity prices (for commodity-based economies), export earnings, or the rate of economic growth of a particular sovereign, or even now with the occurrence of a pandemic. Such contracts would also be acceptable to creditors as they would stand to benefit more where the 'state of the world' that obtains turns out better than imagined. Put differently, these state-contingent debt contracts ensure high pay-outs in good states of the world and low pay-outs in bad states of the world, based on the value of a state variable, which variable is linked to the debt-servicing capacity of the particularly sovereign. Accordingly, SADC countries can seek to negotiate state-contingent debt agreements so as to reduce the debt distress that potentially arises when various situations obtain. However, this is an *ex-ante* mechanism that is most useful in contract design when contracting debts. Some of instances where GDP-linked warrants have been featured as part of financial packages issued to creditors in four major debt restructuring cases include Argentina (2005 and 2010); Greece

26 IMF (n 22) 11.

27 ML Anthony et al 'What history tells us about state-contingent debt instruments' *Voxeu* (6 June 2017).

(2012); and Ukraine (2015).[28] In addition, the occurrence of climate events such as hurricanes and floods may found and trigger state-contingent debt contracts especially for SADC countries that frequently experience climate disasters such as Mozambique, as has been the case in the Bahamas.[29]

6.3.2 *Ex-post* mechanisms

Debt Standstills/Moratoriums

The pandemic has had an immediate economic impact on the public finances of SADC member countries with the consequence that these countries are unable or are struggling to meet their obligations. Sovereigns face significant healthcare costs, a withering tax base, frozen debt markets, capital flight, falling export revenues, and a global recession as a consequence of the pandemic.[30] Given the ravages of the pandemic on the economic and social health of member countries, it has become imperative as a matter of urgency for governments to redirect their limited public funds toward alleviation measures of the pandemic as well as to cushion the most vulnerable.[31] For instance, early evidence indicates that up to 113 000 women have died as a result of the cutback in maternal care during the COVID-19 pandemic in low and middle-income nations in sub-Saharan Africa.[32] Governments are reallocating funds that had earlier been earmarked for other purposes, including discharging external debt obligations toward dealing with the pandemic. It is estimated that Africa as a continent requires at least $100 billion in order to resource its health and safety net response as well as a similar amount for economic stimulus.[33] Yet, partly owing to pressure to make debt repayments, SADC countries have limited fiscal space to undertake these important measures. For instance, in 2019 up to 25 countries globally and five SADC member countries (Zimbabwe, Zambia, Congo, Madagascar and Angola) had high

28 C Cohen et al 'IMF staff discussion note: The role of state-contingent debt instruments in sovereign debt restructurings' (November 2020) 9.

29 https://www.iadb.org/en/project/BH-O0003 (accessed 19 June 2021).

30 P Bolton et al 'Born out of necessity: A debt standstill for COVID-19' (2020) *CEPR Policy Insight* 103, https://cepr.org/active/publications/policy_insights/viewpi.php?pino=103 (accessed 31 October 2020).

31 As above.

32 M Gates 'The pandemic's toll on women: COVID-19 is gender-blind, but not gender-neutral' *Foreign Affairs* (15 July 2020).

33 M Sallent 'External debt complicates Africa's COVID-19 recovery, debt relief needed' *Africa Renewal* (30 July 2020), https://www.un.org/africarenewal/magazine/july-2020/external-debt-complicates-africas-post-covid-19-recovery-mitigating-efforts (accessed 20 January 2021).

debt service relative to social spending ratios.[34] As of end of December 2020, the IMF had already categorised three SADC countries, namely, Mozambique, Republic of Congo and Zimbabwe, as being in debt distress and at the same level of risk as they were before the onset of the COVID-19 pandemic.[35]

The immediate challenge, therefore, for countries particularly in the SADC region, nine of which are least-developed countries (LDC),[36] is to assist them in dealing with the significant costs of the pandemic. Besides the official assistance that the SADC countries may have obtained from other countries and international organisations, they still need to suspend their debt repayment obligations in order to redirect these scarce funds to dealing with the pandemic. This will certainly require a co-option of creditors, including private sector creditors, who must commit to such an arrangement, otherwise these sovereigns would be in default, attracting further consequences. In the medium to the long term, however, SADC countries will have to confront the issues that have contributed to their economic situation such as the need to finance budget deficits, finance infrastructural development, and provide essential services in the midst of falling revenues, among other factors,[37] as well as focus on economic recovery and deal with the aftermath of the pandemic so as to repay the debts that may have been suspended.

A debt standstill, at its core, is an agreement among creditors and a debtor that seeks a temporary pause on debt repayments.[38] Therefore, debt standstills are transient in nature and thus more of a short-term remedy as opposed to a long-term option. A temporary debt standstill or moratorium is particularly useful for SADC countries in the midst of the pandemic as it will enable them to finance urgent pandemic responses. It is critical that all creditors, whether official or non-official, agree to a debt standstill to avoid instances where debt repayment reliefs offered by some creditors

34 UNICEF 'Protecting and transforming social spending for inclusive recoveries*:* COVID-19 and the looming debt crisis' (April 2021) 16.

35 UNICEF (n 34) 9.

36 These are Angola, Comoros, Democratic Republic of the Congo, Lesotho, Madagascar, Malawi, Mozambique, Tanzania and Zambia, https://unctad.org/topic/least-developed-countries/list (accessed 4 May 2021).

37 AFRODAD 'An overview of domestic debt in SADC: A synthesis of trends, structure and development impacts' (2014), https://media.africaportal.org/documents/SADC_Debt_Synthesis_Paper_web.pdf (accessed 4 May 2021).

38 A Gelpern et al 'Debt standstills can help vulnerable governments manage the COVID-19 crisis' PIIE Covid-19 Series (7 April 2020), https://www.piie.com/blogs/realtime-economic-issues-watch/debt-standstills-can-help-vulnerable-governments-manage-covid (accessed 31 October 2020).

are applied toward repaying other creditors that have refused a standstill instead of being applied toward crisis response.

Consequently, there would be a need for coordination of the vastly-diversified creditor community, with their varying priorities and constraints, in implementing a standstill. Only such a coordinated mechanism can dissuade creditors from exploitative behaviour where they seek to benefit from concessions made by others or acting in ways that undermine the standstill, such as seeking preferential treatment or seizing assets of the debtor. Yet, it is difficult to have such a mechanism, its lack of legal authority notwithstanding, owing to the lack of any sovereign bankruptcy law or mechanism at the global level. Much would therefore depend on entities such as the G20, the IMF or the World Bank organising creditors so that they can act in a manner that avoids the collective action problem.

Consistent with this view, the G20 established the Debt Service Suspension Initiative (DSSI) in April 2020, which initiative is supported by the World Bank and the IMF.[39] It effectively suspends both principal and interest repayments to official creditors while committing debtors to spending the freed-up resources in social, health and economic spending so as to deal with the pandemic. Under the DSSI, debtors are also required to commit to more debt transparency by disclosing all their public sector financial commitments, which is a useful step in as far as it helps countries to make informed decisions on borrowing and investments and manage debt risks. The DSSI has since been extended in October 2020 to June 2021 and then through to December 2021.[40] Indeed, a number of SADC countries have already benefited from the DSSI, including Angola, Zambia, Comoros, Mozambique, Madagascar, Malawi, Lesotho, Tanzania, Republic of Congo and Democratic Republic of the Congo.[41]

However, the DSSI as currently framed suffers from a number of limitations: Only 47 of the 73 eligible countries have benefited as at the

39 G20 Communiqué by G20 Finance Ministers and Central Bank Governors Meeting (15 April 2020), https://g20.org/en/media/Documents/G20_FMCBG_Communiqu%C3%A9_EN%20(2).pdf (accessed 31 October 2020).

40 Reuters Staff 'Factbox: How the G20's Debt Service Suspension Initiative works' *Reuters* (15 October 2020), https://in.reuters.com/article/us-imf-worldbank-emerging-debtrelief-fac/factbox-how-the-g20s-debt-service-suspension-initiative-works-idUSKBN27021V (accessed 31 October 2020); https://www.worldbank.org/en/topic/debt/brief/covid-19-debt-service-suspension-initiative (accessed 11 November 2021)

41 https://www.worldbank.org/en/topic/debt/brief/covid-19-debt-service-suspension-initiative (accessed 4 May 2021).

time of writing; it has covered only 1,66 per cent of debt payments that fall due in 2020 on the part of developing countries; it has limited impact since multilateral and private creditors are not participants, which means that only 24 per cent of debt payments are subject to potential debt suspension; and it was projected that the extension until June 2021 would only cover 44 per cent of debt payments.[42] In addition, middle-income countries which are also facing the pandemic are not covered by the initiative. The net effect of this is that the DSSI may turn out to be too little to help these SADC countries deal with the pandemic and the funds saved through the debt relief offered under the initiative may actually be expended in repaying other debt payments. A far much more comprehensive debt workout or moratorium that encompasses all creditors is important if the SADC countries are to recover from the pandemic crisis and the resultant economic downturn.

Some countries, such as Kenya, had earlier expressed its intention not to participate in the DSSI for various reasons including the impact on their sovereign ratings and ability to access international financial markets.[43] A downgrade of ratings adds up to the financing costs of a sovereign and also creates barriers to additional financing, yet securing additional financing to retire maturing debt (rolling over debt) is the business model of sovereign borrowing. In effect, initiatives such as the DSSI may not significantly be beneficial to SADC countries as it may have the perverse effect of further increasing their debt vulnerabilities.[44]

42 Eurodad 'The G20 Debt Service Suspension Initiative: Draining out the Titanic with a bucket? Eurodad's shadow report on the limitations of the G20 Debt Service Suspension Initiative (October 2020), https://d3n8a8pro7vhmx.cloudfront.net/eurodad/pages/768/attachments/original/1603714501/DSSIShadowReport_14Oct_%281%29.pdf?1603714501 (accessed 31 October 2020).

43 N Mwangi 'Kenya rejects G20 debt relief initiative over restrictive terms' *CGTN Africa* (16 May 2020), https://africa.cgtn.com/2020/05/16/kenya-rejects-g20-debt-relief-initiative-over-restrictive-terms/ (accessed 31 October 2020). However, the country has since agreed to participate in the DSSI owing to financial difficulties and has been offered a debt repayment reprieve until June 2021 including by its principal lender, China. See D Omondi 'Relief as China grants debt repayment holiday' *The Standard* (20 January 2021), https://www.standardmedia.co.ke/the-standard-insider/article/2001400663/relief-as-china-grants-debt-repayment-holiday (accessed 20 January 2021).

44 M Mutize 'Why African countries are reluctant to take up COVID-19 debt relief' *Quartz Africa* (30 July 2020), https://qz.com/africa/1886916/african-countries-are-reluctant-to-take-up-covid-19-debt-relief/ accessed 31 October 2020.

COVID-19 pandemic as **force majeure**

SADC debtor countries may consider invoking the *force majeure* doctrine[45] as a result of the COVID-19 pandemic that has led to a shrinking of the global economy and a weakening of exports, particularly for commodity-based economies.[46] The economic impacts of the COVID-19 pandemic have seriously jeopardised the ability of SADC member countries to fund essential social and public services as well as to honour their debt repayment obligations with some such as Zambia recently defaulting on its debt repayment.[47] Accordingly, these sovereigns may be at liberty to invoke the *force majeure* doctrine, certainly dependent on the wording of the particular *force majeure* clause, so as to enable them to break their debt repayment obligations. The *force majeure* doctrine usually gives a right to a party to a contract to be relieved from honouring their part of the contractual bargain where unforeseen circumstances arise, which are beyond the control of contracting parties.

The *force majeure* doctrine originated in Roman law and operates to excuse the performance of particular obligations where unforeseen, unforeseeable or uncontrollable extenuating events arise.[48] The doctrine also covers acts of God, frustration, impossibility or impracticability. For the doctrine to be applicable, the occurrence of events must have been beyond the control of the parties.[49] It should be noted, however, that it is not mere difficulties in performing a contractual bargain that suffice in the invocation of the doctrine, but rather, there must have arisen a form of impossibility or impracticability caused by factors beyond the control of the parties.[50] Applying these principles, the COVID-19 pandemic and the associated economic consequences can arguably be said to have been unforeseen and unprecedented and beyond the control of SADC countries

45 *Force majeure* refers to the 'occurrence of an event or circumstance that prevents or impedes a party from performing one or more of its contractual obligations under the contract, if and to the extent that that party proves (a) that such impediment is beyond its reasonable control; (b) that it could not reasonably have been foreseen at the time of the conclusion of the contract; and (c) that the effects of the impediment could not reasonably have been avoided or overcome by the affected party'. See JA Trenor & H-S Lim 'Navigating *force majeure* clauses and related doctrines in light of the COVID-19 pandemic' (2020) 13 *Young Arbitration Review* 15.

46 World Bank Group *Global economic prospects* (2021) 3.

47 SADC 'The impact of COVID-19 pandemic on SADC economy' (May 2020) 3, 103, https://www.sadc.int/files/8015/8988/3255/COVID-19_SADC_Economy_Report.pdf (accessed 19 January 2021).

48 FI Paddeu 'A genealogy of *force majeure* in international law' (2012) 82 *British Yearbook of International Law* 381, 386.

49 Trenor & Lim (n 45) 13, 14-15.

50 As above.

so as to found a basis for the invocation of *force majeure*. In particular, the nature and extent of increased healthcare costs, increased expenditure in social welfare, an increase in unemployment, border closures and falling remittances and exports associated with the pandemic could arguably not have been foreseeable, even where it can be claimed that a pandemic was foreseeable. In addition, the doctrine may be invoked especially because various countries, including those in the SADC region, actually declared states of emergency and imposed extensive lockdowns that significantly affected their economic output.[51] Once these measures came into force and these supervening circumstances obtained, the various SADC debtor countries could have sought to invoke the doctrine.

A number of sovereign debt contracts contain *force majeure* clauses that can be invoked in light of the pandemic. However, some debt contracts contain no such *force majeure* clauses. However, this does not mean that the COVID-19 pandemic cannot qualify as a *force majeure* even in the absence of such a contractual provision. Article 23 of International Law Commission's Articles on the Responsibility of States for Internationally Wrong Acts avails sovereigns of the defence even where there was no such contractual clause. Further, jurisprudence from international tribunals has appeared to chip away at the argument that the *force majeure* doctrine may only be invoked with respect to states or where it is contained in a contract. In an arbitration decision by the Permanent Court of Arbitration in The Hague issued on 11 November 1912 in the 'RIAA, Case of the Russian compensation', the tribunal accepted the defence of *force majeure* as well founded where the Turkish government had gone through a severe financial crisis which made it impossible for it to service its debt owed to Tsarist Russia. The tribunal was emphatic that *force majeure* may apply both in public international law as well as private international law, the latter of which involves a non-state actor as a party. The *force majeure* doctrine is recognised in public international law which regulates relations between states *inter se,* and between states and individuals, especially where the latter happens to be the creditor and the former the debtor.[52]

Accordingly, the *force majeure* doctrine may be invoked in the context of debt owed not only to states, but also to international financial institutions or foreign private sector lenders. This is especially the case when it is considered that article 103 of the United Nations Charter provides for

51 For an overview of global responses to the pandemic, see http://globalresponsescovid19.com/ (accessed 19 January 2021).

52 M Dellinger 'Rethinking *force majeure* in public international law' (2017) 37 *Pace Law Review* 455, 458, https://digitalcommons.pace.edu/cgi/viewcontent.cgi?article=1944&context=plr (accessed 19 January 2021).

the supremacy of the Charter in the event of a conflict between the obligations of members of the United Nations (UN) under the Charter and their obligations under any other international agreement.

The state of necessity doctrine

Sovereigns can also invoke the doctrine of necessity to exempt them from their state responsibility so as to suspend its debt repayments as an emergency response to the pandemic.[53] The state of necessity under public international law is an international customary rule that justifies the breach of an international obligation by a sovereign on the basis that complying with the obligation would be inimical to the essential interests of such sovereign in light of grave circumstances or situations.[54] Economic collapse and the associated potential social and political instability as well as monumental health crisis arguably count as situations of extreme and grave peril that found a basis for the invocation of the doctrine.[55]

By making use of this state of necessity doctrine, sovereigns may suspend currency and capital account convertibility so as to apply to external flows including debt repayments. A temporary moratorium on account of the necessity doctrine would afford the SADC countries an opportunity to reduce the global demand for foreign currency such as the dollar, thereby helping to lower their overall local currency cost of external debt. Restrictions on capital flows subject to article 6 section 3 of the IMF Articles of Agreement may be employed as a matter of necessity, thereby offering a reprieve to distressed sovereigns. In this sense, debt repayments would then be barred from leaving the debtor country owing to the imposed exchange restrictions. Where this counts as an event of default forcing the creditor to seek to enforce the debt contract in court, the sovereign borrower may find a defence under article VIII section 2(b) of the IMF Articles of Agreement which establishes a legally-binding debt standstill mechanism, especially among private creditors who may not be willing to agree to a standstill. The relevant provision

53 For more on the doctrine of state of necessity, see MCH Thjoernelund 'State of necessity as an exemption from state responsibility for investments' in A von Bogdandy & R Wolfrum (eds) *Max Planck yearbook of international law* (2009) 423-480, https://www.mpil.de/files/pdf2/mpunyb_11_llm_thesis.pdf (accessed 31 October 2020).

54 Art 25 of Articles on Responsibility of States for Internationally Wrongful Acts (Articles on State Responsibility) by the International Law Commission (ILC).

55 AO Sykes 'Economic "necessity" in international law' (2015) 109 *American Journal of International Law* 296, 314. The author argues that a public health crisis, say, due to a deadly tropical disease in a developing country, which forces governments to reallocate funds to contain the crisis or to deal with such an emergency, would give rise to the necessity doctrine under international law.

allows the IMF to render certain debt contracts unenforceable in domestic courts of member countries if such contracts violate the exchange control regulations of another IMF member country. The standstill mechanism in effect enables a temporary suspension of enforceability of debt contracts within domestic courts of the 189 IMF member countries and may be invoked by any member country without necessitating a modification of the Articles of Agreement.[56]

The International Centre for Settlement of Investment Disputes (ICSID) has set out circumstances when a country may avail itself of the necessity doctrine. In *LG&E Energy Corp, LG&E Capital Corp and LG&E International Inc v Argentine Republic*[57] a suit was lodged at the ICSID tribunal by three investors who owned local gas distribution companies in Argentina claiming multiple violations of a treaty and sought damages. Argentina had passed a law that guaranteed that tariffs for gas distribution would be calculated in US dollars, besides providing other guarantees under the tariff regime. However, as a result of the economic crisis that the country faced in the 1990s, it abrogated the guarantees given under the law which led to significant reductions of returns for the companies owned by the investors. While the tribunal found that Argentina had breached the standard of fair and equitable treatment by abrogating the guarantees and that the same was discriminatory,[58] it dismissed the claims of expropriation and arbitrariness. Significantly, the tribunal held that Argentina was in a state of necessity between December 2001 and April 2003 and, therefore, was absolved from its international responsibilities during the period under review.[59] Importantly, the tribunal rejected the investors' claims that a state of necessity would only arise in case of military invasion or war, holding that 'when a state's economic foundation is under siege, the severity of the problem can equal that of any military invasion'.[60] Further, while acknowledging that the action of Argentina was not the only means available to them in responding to the economic crisis, the tribunal found that the measures were necessary to maintain public order and protect Argentina's essential security interests under the applicable treaty and under public international law.[61]

56 D Munevar & G Pustovit 'Back to the future: A sovereign debt standstill mechanism IMF Article VIII, Section 2(b)' (2020) SAFE Working Paper 282, Leibniz Institute for Financial Research SAFE, Frankfurt.

57 ICSID Case ARB/02/1; https://www.italaw.com/sites/default/files/case-documents/ita0460.pdf (accessed 31 October 2020).

58 Paras 133-139.

59 Paras 226-261.

60 Para 238.

61 Paras 239, 257.

Consistent with the decision of the ICSID Arbitral Tribunal above, the necessity doctrine as a result of the COVID-19 pandemic may be applied by SADC countries to delay or suspend debt repayments. This is especially the case given that the pandemic has led to stringent lockdown policies that are more extensive than those imposed during World War II; the global economy is facing its worst slump since the Great Depression of the 1930s; and various economies have adopted unprecedented fiscal and monetary policies to ensure economic recovery.

The above notwithstanding, invoking necessity as a doctrine may be difficult for SADC countries since debtor countries must demonstrate that they have not contributed to the debt default.[62] When considered in light of the economic (mis)management of a number of countries, it arguably is difficult to argue that the pandemic is the sole cause of economic difficulties.[63] The pandemic-related elements that may constitute a ground for invocation of the necessity doctrine include the restrictive measures taken to deal with the pandemic, such as social distancing, quarantines, lockdowns, fiscal stimulus packages, the reallocation of funds into public health to deal with the pandemic, among others.

In addition, the necessity doctrine only serves to delay rather than extinguish debt repayment obligations as debtor countries are required to make debt repayments once they regain their financial health.[64] However, even then the necessity doctrine helps debtor countries to subsidise the pandemic crisis response. In addition, the invocation of the doctrine may not accord with the interests of creditors and the objectives of debt restructuring. It, therefore, is not surprising that the necessity doctrine has not yet been invoked successfully by any debtor country in light of the COVID-19 pandemic, given the inherent difficulties. Nonetheless, the doctrine may be employed by SADC countries, where they qualify, to obtain temporary reprieve that enables them to prioritise the welfare of their people as opposed to repaying creditors.

Invoking the necessity doctrine by states may potentially be at odds with some of the respective states' treaty obligations with international financial institutions and the wider creditor community. Article 103 of the UN Charter provides that '[i]n the event of a conflict between the obligations of the members of the United Nations under the present

62 *Gabčíkovo-Nagymaros Project (Hungary v Slovakia*) (Merits), ICJ Rep (1997) 7, 46.

63 M Waibel 'Two worlds of necessity in ICSID arbitration: CMS and LG&E' (2007) 20 *Leiden Journal of International Law* 642.

64 WMC Weidemaier & M Gulati 'Necessity and the COVID-19 pandemic' (2020) 15 *Capital Markets Law Journal* 277, 282-283.

Charter and their obligations under any other international agreement, their obligations under the present Charter shall prevail'.[65] Accordingly, in light of the provisions of article 103 of the UN Charter, which appear to give pre-eminence to the interests of a state in upholding its citizens' living standards, the obligations arising from the respective treaties and agreements with the creditor community may arguably yield to invocation of the necessity doctrine. In addition, given that the UN Charter provides for protection of human rights and the objective of improving peoples' living standards, it may be employed to justify the suspension of debt repayments and moratorium on repayment on the grounds that being forced to repay debts in the context of a pandemic goes against the foregoing rights under the UN Charter.

Debt buy-backs

A sovereign debt buy-back can be useful in overcoming collective action and hold out problems among creditors, thereby avoiding punitive terms associated with debt swaps. A debt buy-back programme essentially is where a sovereign borrower repurchases its own debt from creditors at a discount or at par/face value. Debt buybacks have been employed by various sovereigns in times past, including Bolivia and Greece. For instance, donor countries gave Bolivia a total of $34 million which enabled the country to buy back its debt which were trading for 6 cents on the dollar in the secondary market. Bolivia was able to buy back $302 million of its debt for $40,2 million.[66] The success of the Bolivian experience led other Latin American countries to pursue a similar strategy.

Notably, however, developing countries, including those in the SADC region, are yet to make use of this strategy of debt buy-back, which can be a useful tool of averting a debt crisis. It is indeed the case that debt buy-backs tend to increase the price of the remaining debt by artificially inflating the market price of bonds. However, this concern would be disconcerting in normal times and if credit markets were efficient. This is not usually the case during times of crisis since, for one, credit markets are rarely efficient. Bond prices are not always a reflection of underlying fundamentals as irrationality that characterises financial markets sometimes leads to panic sales that distort market prices.[67] Second, market prices of bonds are also

65 https://legal.un.org/repertory/art103.shtml (accessed 18 June 2021).

66 J Bulow & K Rogoff 'The buyback boondogle' (1988) 2 *Brookings Papers on Economic Activity* 675, https://www.brookings.edu/wp-content/uploads/1988/06/1988b_bpea_bulow_rogoff_dornbusch.pdf (accessed 31 October 2020).

67 J Stiglitz & H Rashid 'Averting catastrophic debt crises in developing countries: Extraordinary challenges call for extraordinary measures' (July 2020) CEPR Policy Insight No 104 19.

partly a function of the subjective judgment or perception of domestic and global politics based on an assessment of how much pressure may be brought to bear on debtors by creditors and the extent to which debtors are willing to comply as well as the ratings accorded by credit rating agencies.

Potentially, debt buy-backs offer an attractive opportunity for sovereigns to obtain significant debt relief at a low cost where such sovereigns' debt is bought back at a steep discount. In addition, they can potentially improve the bargaining power of sovereign borrowers as against creditors. In order to make it possible for SADC countries to engage in debt buy-backs, it is important to enlist the support of donors who will provide the financing necessary for the debt buy-back. This means that SADC countries need to commit to spending the savings to be made from debt buy-backs in creating and supplying essential social services and other public goods. The IMF can manage and coordinate the debt buy-back programme from creditors on behalf of sovereigns, not least because it has the requisite technical capacity. SADC countries would ideally identify the sovereign bonds they would wish the IMF to buy back on their behalf. Nonetheless, SADC countries will find it challenging to obtaining the necessary financing for buying back its debts, and may have to principally rely on donors whose funds will likely be strained given the competing needs as a result of the pandemic.

6.4 Conclusion

This chapter noted that the international financial architecture still suffers from the missing link, one of a statutory sovereign debt restructuring mechanism, which complicates debt restructuring processes. The market-based solutions relied on in the absence of such a statutory mechanism will continue to ensure that debt restructuring happens in a sub-optimal scale and rather late, thereby hurting both debtors and creditors alike. Until there is a statutory global sovereign debt restructuring mechanism, sovereign borrowers in difficulties of debt repayments may consider availing themselves of the various legal options available to them as described in this chapter to deal with the pandemic while avoiding serious debt crises.

In particular, it is important that SADC countries pay much regard to *ex-ante* contractual mechanisms by embedding collective action clauses and designing state-contingent debt instruments. The chapter considered the importance of debt standstills in offering SADC countries immediate debt relief but noted that the current initiatives are too little to suffice. The chapter also noted that there are difficulties fraught with invoking the *force majeure* and necessity doctrines in international law given the stringent

requirements associated with these. It also noted that these twin options, just like the debt standstills, are short term in nature and do not absolve debtor countries from debt repayment obligations. Debt buy-backs offer an attractive option for debtor countries in reducing their debt burden, although this is predicated on their obtaining financing to buy back the debt.

Admittedly, a number of these proposed legal options would be contested by creditors and in courts and may affect relations between the sovereigns and the wider creditor community including international financial institutions. However, it should be noted that such legal options are better taken advantage of, and will not collapse the sovereign debt markets. Creditors usually return to the credit markets almost immediately underlying risks are mitigated. Ultimately, however, the search for a global debt restructuring framework that will enable comprehensive debt workouts must be accelerated.

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7 Sovereign debts under the SADC Model Bilateral Investment Treaty (SADC Model BIT)

*Roselian Jackson**

> In effect, sovereign debt litigation has begun to resemble a chess match: a move by a vulture is blocked or countered, and a new move or theory comes into vogue as another avenue to try to increase the chances of recovery. Unfortunately, for the state defendant, this is not a game; the vulture's portfolio may be diversified, and it may believe that it only needs an occasional big win to recoup its costs of carry-and-litigation expense. For the state however, what is at issue is not a litigation gamble, but the economic and social welfare of its citizens.
>
> *J Blackman & R Mukhi 2010*

7.1 Introduction

This chapter addresses how bilateral investment treaties (BITs) can potentially be used to protect sovereign credits in case of default. The main argument of the chapter is that including sovereign debt within the BIT framework is problematic and defeats the very foundation of sovereign debt restructuring (SDR). States should exclude sovereign debts from the scope of their BITs. This will enable them to fully utilise the important role sovereign debts play in state financing. States should opt to either continue with the existing SDR mechanisms or introduce a new continental framework for SDR.

According to the United Nations Conference on Trade and Development (UNCTAD) database, there currently are more than 2 298 BITs in force around the world.[1] With the progress in global investment law, states have adopted new model BITs to replace the old model BITs. UNCTAD has also advised on the need of modernising the old-generation treaties as part of the international investment treaties reform.[2] The old

* The author wishes to acknowledge Dr Magalie Masamba, Prof Daniel Bradlow, Dr Celine Tan, Prof Makane Moïse Mbengue, Prof Kenneth Mwenda, Adv Othman Omar Othman and all the anonymous reviewers for their comments and guidance.

1 https://investmentpolicy.unctad.org/international-investment-agreements (accessed 1 May 2021).

2 United Nations Conference on Trade and Development (UNCTAD) 2017 World investment report (2017), https://unctad.org/en/PublicationsLibrary/wir2017_en.pdf (accessed 1 May 2021).

regime of investment treaties has been criticised for favouring investors to the detriment of host state policy space and regulatory power. A typical old regime BIT contains a broad definition of investment and investor, a most-favoured-national clause (MFN) without exceptions, fair equitable treatment (FET), full protection and security (FPS) and lack of safeguard provisions for states. On the other hand, the new generation of BITs have tried to limit the definition of investor and investment and provide some clarity on the meaning of FET and FPS clauses.

The Southern African Development Community (SADC) Model BIT is a non-binding model template that contains different alternatives and recommendations for states to adopt when negotiating BITs. The model has been adopted as a means to address the shortcomings emanating from the old regime of investment treaties. It provides alternative provisions to replace and clarify controversial old regime BIT provisions such as the definition provisions, the MFN clause; fair and equitable protection (FEP); FPS; and the investor-state dispute settlement (ISDS) clause.[3] The model has narrowed the definition of investor and investment with an express exclusion of sovereign debt;[4] it has excluded the MFN;[5] replaced the FEP standard treatment clause with a fair administrative treatment clause;[6] it has tried to clarify the scope and meaning of full protection and security; and it has excluded the ISDS mechanism in favour of the domestic and regional dispute settlement framework.[7]

This chapter addresses the provisions of the SADC Model BIT in relation to sovereign debts. The chapter does not intend to provide an analysis of how different BITs have addressed the question of sovereign debts, but only aims to provide insights to states, particularly SADC member states, on the legal implication of SADC Model BIT provisions in relation to sovereign debts. The chapter is divided into three parts. The first part introduces and discusses sovereign debt and BITs as concepts; the second part addresses the interplay of BITs on sovereign debt and how the interplay has been addressed by the SADC Model BIT; the third and last part highlights the general conclusion of the chapter.

3 SADC Model BIT is a non-binding template developed by the SADC Secretariat as assistance for countries when negotiating BIT.

4 South African Development Community Model Bilateral Investment Treaty Template with Commentary (SADC Model BIT) July 2012, art 2.

5 SADC Model BIT (n 4) art 4.

6 SADC Model BIT art 5.

7 SADC Model BIT art 29.

7.2 Introduction to sovereign debt and bilateral investment treaties

7.2.1 Sovereign debt

There has never been an agreed international legal definition on what sovereign debt is. The Vienna Convention on Succession of States in Respect of State Property, Archives and Debt (not yet in force) defines state sovereign debt as 'any financial obligation of a predecessor state arising in conformity with international law towards another state, an international organisation or any other subject of international law'.[8] Despite the fact that the Convention has not entered into force, it remains the only international treaty to try and define sovereign debt. However, the definition under the Convention excludes private lenders as creditors and municipal law as legal framework governing sovereign debt. This chapter adopts the definition of sovereign debt as the debt a state (central government) owes to its creditors.[9]

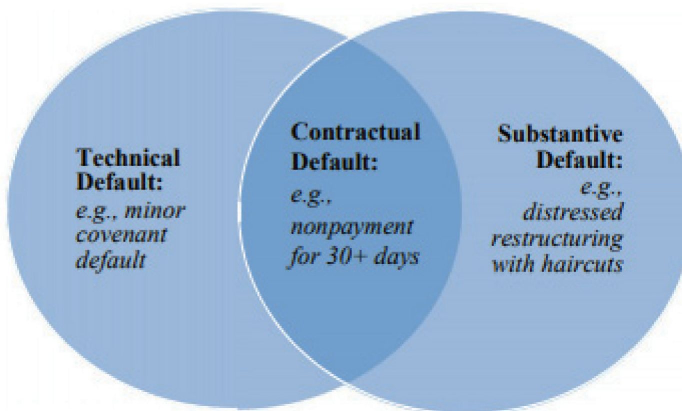
States can, and periodically do, default on their sovereign debt. A sovereign debt default occurs when a state fails to meet its payment obligation to its creditor. Legally speaking, the definition of sovereign debt default should be extracted from the sovereign debt agreement/instrument itself, because the instrument usually provides for factors and incidences of default (events of default). These incidences provide for which obligations, including covenants or warranties in the agreements when breached are considered to lead to default. However, at this point it is imperative to highlight the varying incidences of default. Sometimes default happens when there is a missed interest/principal payment and sometimes only a delay in disbursing payment by the borrower can be considered default. It is mostly the breach of payment obligations and substantive covenants rather than warranties that occasions defaults.

Considering the lack of agreed definition of what default is, some authors have tried to provide different forms of defaults. Ams et al have categorised defaults into three categories based on default as per the underlying contract and default as per credit rating agency such as Moody's, Fitch Group and S&P Global Ratings (S&P). The first category is technical default. This occurs when an event of default in the underlying

8 UN General Assembly Vienna Convention on Succession of States in Respect of State Property, Archives and Debts (8 April 1983) art 33.

9 M Tomz & M Wright 'Empirical research on sovereign debt and default' (2013) 5 *Annual Review of Economics* 247.

debt contract happens, but the credit rating agency does not regard the default as default. The second category is contractual default, which occurs when the event of default arises from the underlying contract. The occurrence will also constitute default under third parties (credit rating agencies) definitions of default. The last category is substantive default; this occurs when an event happens which, according to the credit rating agency, is an event of default, but the default does not constitute an event of default under the underlying debt contracts.[10] Credit rating agency definition of default is worth considering because of the influence of this agency in the financial market when it comes to the rating of government bonds.[11] Of the three categories the second category (contractual default) is the focus of this chapter.



Categories of default by Ams et al (2019)[12]

The causes of default are diverse and not always straightforward. For example, lax fiscal discipline and excessive budget deficits have been attributed as the causes of the Euro area's sovereign debt crisis.[13] However,

10 J Ams et al 'Sovereign default' in SA Abbas, A Pienkowski & K Rogoff (eds) *Sovereign debt: A guide for economists and practitioners* (2019) 3.

11 US Securities and Exchange Commission Report on the Role and Function of Credit Rating Agencies in the Operation of the Securities Markets (2003). Also see the conclusions of the financial crisis inquiry commission.

12 Ams et al (n 10) 4. Also see IMF Conference of 13-14 September 2018 'Sovereign debt: A guide for economists and practitioners', https://www.imf.org/en/News/Seminars/Conferences/2018/05/24/sovereign-debt-a-guide-for-economists-and-practitioners (accessed 20 January 2021).

13 PR Lane 'The European sovereign debt crisis' (2012) 26 *Journal of Economic*

the 2001 Argentine default was not one of excessive budget deficits but more one to do with policy failures, particularly the convertibility plan (*Ley de Convertibilidad del Austral*).[14] In the ten years preceding the default, Argentina's average deficit was 1,2 per cent of gross domestic product (GDP), whereas the debt levels in 2001 stood at 55 per cent of GDP.[15] The recent defaults in the SADC region (Mozambique[16] and Zambia) have been attributed to government fiscal mismanagement. As for Zambia, evidence shows that Zambia was struggling with mounting debt[17] even before the financing gap caused by the COVID-19 pandemic.[18] It has been pointed out that the country's default has more to do with incompetent fiscal management than anything else.[19] Zambia's finance minister Ng'andu noted that the government borrowing was over-ambitious and the debt was unsustainable.[20] This over-borrowing noted by Ng'andu reverberate with the 1980s African countries; sovereign default. Indebtedness was a characteristic feature of post-colonial reconstruction during the 1960s and indebtedness was widely accepted as an unavoidable prerequisite for development. It was the heavy indebtedness that turned countries into insolvency in the early 1980s.[21]

In order to be able to borrow, states avoid defaulting to maintain a good reputation as good borrower.[22] However, sometimes states face

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14 G Nataraj & P Sahoo 'Argentina's crisis: Causes and consequences' (2003) 38 *Economic and Political Weekly* 1641-1644.

15 Y Li & U Panizza 'The economic rationale for the principles on promoting responsible sovereign lending and borrowing' in CD Espósito, Y Li & JP Bohoslavsky (eds) *The UNCTAD principles on responsible sovereign lending and borrowing* (2013).

16 The Mozambique debt crisis was also partially caused by unlawful transactions as per domestic laws and corruption. See A Nuvunga & A Orre 'The 'secret loans affair' and political corruption in Mozambique' in I Amundsen (ed) *Political corruption in Africa. Extraction and power preservation* (2019).

17 C Mfula & K Strohecker K 'UPDATE 6 Zambia will miss Eurobond payment, setting stage for default (13 November 2020), https://www.reuters.com/article/zambia-debt/update-5-zambia-will-miss-eurobond-payment-setting-stage-for-default-idINL1N2HZ0R1 (accessed 20 January 2021).

18 M Hill & TC Mitimingi 'Zambia seeks restructuring after 'over-ambition' on debt' (18 May 2020), https://www.bloomberg.com/news/articles/2020-05-18/zambia-sees-to-restructure-debt-after-over-ambition-on-loans (accessed 20 January 2021).

19 E Olander 'Zambia's Eurobond default – What we have learned' (17 November 2020), https://www.theafricareport.com/50664/zambias-eurobond-default-what-we-have-learned/ (accessed 20 January 2021).

20 Hill & Mitimingi (n 18).

21 W Biermann & J Wagao 'The quest for adjustment: Tanzania and the IMF, 1980-1986' (1986) 29 *African Studies Review* 89.

22 M Tomz *Reputation and international cooperation: Sovereign debt across three centuries*

difficult choices and defaulting becomes necessary. One of these choices is whether to refinance/pay bondholders or to buy medicine and food for the population as pinpointed by Vera Songwe, the executive secretary of the Economic Commission for Africa (ECA).[23] Songwe's concern of choosing whether to provide citizens with essential services or servicing debts is not recent. In 1985, following a heavy burden of debt that trapped most African countries, the then Organisation of Africa Unity (OAU) Chairperson, Mwl Nyerere, said that 'Africa's debt burden is now intolerable. We cannot pay. It is not a rhetorical question when I ask, should we really let our people starve so that we can pay our debts?'[24] In a situation such as this, states sometimes choose to default on their debts.

SADC countries default 1956 – 2020

Country Name	**1956-1965**	**1966-1975**	**1976-1985**	**1986-1994**	**1995-2020**	**Total**
Angola	…	…	…	1	…	1
Malawi	…	…	2	1	…	3
DRC	…	…	8	3	…	11
Mozambique	…	…	1	4	1	6
South Africa	…	…	1	4	…	5
Tanzania	…	…		4	…	4
Zambia	…		2	4	1	7
Total per timeline	**…**	**…**	**14**	**21**	**2**	**37**

Source: from 1956-1994 David F Babbel (1995) and from 1995-2020 by the author

After a state defaults on its debt, creditors find it difficult to enforce their sovereign debt entitlements in courts of law due to sovereign immunity.[25] Even when the bond instruments contain sovereign immunity waivers, courts have been reluctant to enforce these clauses.[26] State immunity in

(2011).

23 A Soto 'The ticking debt bomb in Africa threatens a global explosion' (10 June 2020), https://www.bloomberg.com/news/articles/2020-06-10/africa-will-be-the-next-debt-explosion-after-coronavirus (accessed 20 January 2021); also see J Tim ''Why not default?' The political economy of sovereign debt' (2021) 56 *Community Development Journal* 180-183.

24 RH Green 'Unmanageable: Toward sub-Saharan African debt bargaining' in S Griffith-Jones *Managing world debt* (1988) 245.

25 E Jonathan & F Raquel 'Sovereign debt' in GM Grossman & K Rogoff (eds) (1995*)* *Handbook of international economics* (1995).

26 WM Weidemaier & M Gulati 'Market practice and the evolution of foreign sovereign immunity' (2018) 43 *Law and Social Inquiry* 496; *NML Capital Ltd v po Central de la Republica Argentina* 652 F.3d 172 (2d Cir 2011).

sovereign debt litigation can be categorised into two categories, namely, (i) immunity from suit; and (ii) immunity from execution.[27] Immunity from suit is the bedrock of the international principle that sovereign states should not be taken to foreign courts against their will.[28] On the other hand, immunity from execution stems from the long-standing concerns about disruptions and political ramifications that can result from the seizure of a foreign state's property.[29] A state's immunity from execution is only available for sovereign non-commercial property. This means that sovereign commercial property can be the subject of attachment. In *Connecticut Bank of Commerce v Republic of Congo*[30] the American court was of the view that a sovereign's property could not be attached when there is no evidence of it being used commercially. The court further elaborated that the term 'commercial activity' should be interpreted narrowly. Finding this hurdle of locating commercially-used sovereign property, creditors then turned to the property of state agencies or corporations. This also has been difficult as courts have ruled that these agencies or corporations should have their separate legal personality apart from that of the state respected.[31]

Apart from litigation, the global community has invented different mechanisms to deal with sovereign debt default. These mechanisms include the Debt Service Suspension initiative (DSSI) (although mainly used to temporarily help debtor states preserve resources for other emergencies; it can also be viewed as a mechanism to halt default referring to Nyerere's concerns above); rescheduling and restructuring of debts. Rescheduling or restructuring entails changing the principal amount of the debt, extending maturity time and/or interest payment deferment, and also changing the interest rate on the debt. Restructuring initiatives can be instituted before or after the default. Restructuring before default aims to avoid a total default. For example, when Zambia missed a payment of a $42,5 million coupon on its sovereign bonds in October 2020, the government made a restructuring request to its creditor to defer interest payments for six months. Creditors rejected the request and Zambia remained with a 30-day grace period to make payment or enter a default. The grace period expired and Zambia defaulted, becoming the first pandemic-era African

27 J Blackman & R Mukhi 'The evolution of modern sovereign debt litigation: Vultures, alter egos, and other legal fauna' (2010) 73 *Law and Contemporary Problems* 47, http://www.jstor.org/stable/25800669 (accessed 19 January 2021).

28 *The Schooner Exchange v M'Faddon* 11 US 11, 114 (1812).

29 Blackman & Mukhi (n 27).

30 309 f.3d 240.

31 See *First National City Bank v Banco Para El Comercio Exterior De Cuba (Bancec)* 462 US 611, 626 (1983).

country to default. After a default, states still continue with restructuring initiatives. For example, following a default in 2017, Mozambique in 2019 swapped its debt by exchanging its Euro-denominated bond valued at $726,5 million for a new $900 million bond to cover missed principal and interest payments and extended the maturity time from 2023 to 2031. When bond holders and states do not reach an agreement on restructuring of the debt, bond holders look for other avenues to recover their debts, including the use of bilateral investment treaties (BITs).

7.2.2 Bilateral investment treaties

Bilateral investment treaties (BITs) are treaties between two states for the protection and promotion of investments. BITs have been used by bond holders to initiate arbitration cases under the investor-state dispute settlement (ISDS) mechanism. There currently are 2 298 BITs in force worldwide, and it is not the scope of this chapter to scale how these BITs have addressed sovereign debts. As will be discussed later, a small variation in the BIT provision has far-reaching interpretative and legal implications. An investment tribunal's findings in one case should not be generalised to apply in other cases or BITs. The true implication of a tribunal decision depends on the facts of the case and the exact formulation of the BIT. In one BIT sovereign bonds may qualify as an investment while in other BIT sovereign bonds may not qualify as investments.

To date there have been only four sovereign debt investment cases (SDIC). The first three cases were the results of the Argentina 2000s sovereign debt default (the *Abaclat,*[32] *Ambiente*[33] and *Giovanni*[34] cases). The fourth case was the result of the Greece sovereign default (*Poštová Banka*).[35] In the first three cases which involved the Argentina-Italy BIT, the tribunals accepted that sovereign bonds were investments. In the fourth case which involved the Slovakia-Greece BIT, the tribunal concluded that

32 *Abaclat & Others v Argentina* ICSID Case ARB/ 07/5, Annex A, Settlement Agreement (29 December 2016). The *Abaclat*, *Ambiente* and *Giovanni* cases all concerned claims arising out of Argentina's enactment of legislation concerning the restructuring of its public debt, leading to the government's default in sovereign bonds in late 2001.

33 *Ambiente Ufficio SpA & Others v Argentina* ICSID Case ARB/ 08/9, Order of Discontinuance of the Proceeding (4 May 2015).

34 *Giovanni Alemanni & Others v Argentina* ICSID Case ARB/ 07/8, Order of the Tribunal Discontinuing the Proceeding (14 December 2015).

35 *Poštová banka, as and ISTROKAPITAL SE v Greece* ICSID Case ARB/13/8, Award (9 April 2015). The case concerned claims arising out of the enactment of legislation that amended sovereign bond terms retroactively and unilaterally by the government, allegedly allowing the imposition of new terms upon bond holders against their consent if a supermajority of other bond holders consented, in the context of Greece's 2012 sovereign debt restructuring.

sovereign bonds did not qualify as investments under the Slovakia-Greece BIT. It is important to highlight that none of the above cases reached the merit stage. The *Abaclat* case was settled; the *Ambiente* and *Giovanni* cases were discontinued for non-payment of tribunal's fees; and in the *Poštová Banka* case the tribunal lacked jurisdiction. It therefore is unclear which substantive protection sovereign bonds enjoy under international investment law.[36] Although the cases did not reach to the merit stage, they do raise concerns over the scope and jurisdictional mandate of investment tribunals over investment cases involving sovereign debts.

The major issues of discussion in the *Abaclat* case were (i) how the term 'investment' should be construed and defined; and (ii) whether an investor can bring contract claims (emanating from sovereign bonds) before an investment tribunal. The tribunal ruled that when defining the term 'investment', the focus should be on the contracting parties' agreement and not criteria developed by case law. According to the tribunal, criteria such as the *Salini* case criteria on investment[37] are useful but they cannot be used to create a limit, which neither the ICSID convention's drafters and state parties nor the contracting parties to a specific BIT intended to create.[38] In relation to contract claims, the tribunal held that in this case the arbitral tribunal had no jurisdiction where the claim at stake is a pure contract claim. The tribunal will only have jurisdiction over investment disputes where the acts of a state are purely acts of a sovereign power and not acts of the state as a party to a contract. This means that when the act of the state can be construed as acts that any party to a contract can do, then the dispute is termed a normal contractual dispute to be settled in the normal contractual dispute settlement mechanism. This can further be elaborated by making reference to the *Biwater Gulf (Tanzania) Limited* case against Tanzania.[39] When deciding whether a contract termination by the government of Tanzania amounted to expropriation, the tribunal ruled that the termination in itself did not constitute expropriation. However, the Tanzanian government press release, in which Prime Minister Lowassa announced the termination of the contract, was an unreasonable disruption of the contractual mechanisms existing between the investor and the government, and motivated by political considerations. As such, these actions were inconsistent with the Republic's obligations under the

36 UNCTAD 'Sovereign debt restructuring and international investment agreements 2 IIA Issue Note (2011) 4-5.

37 *Salini Construttori SpA and Italstrade SpA v Kingdom of Morocco* ICSID Case ARB/00/4, Decision on Jurisdiction of 23 July 2001, § 52, 42 ILM 609, 622 (2003) (*Salini*).

38 *Abaclat* (n 32) para 360.

39 *Biwater Gauff (Tanzania) Limited v United Republic of Tanzania* ICSID Case ARB/05/22, Award (24 July 2008).

treaty. Taken alone, they had a concrete effect on the investor's contractual rights, and taken together with the acts that followed (of which it formed part) ultimately contributed to an expropriation.[40] The investor state dispute settlement (ISDS) is not meant to replace contractual remedies.[41]

In the *Ambiente* case the area of contention was whether the term 'investment' encompasses sovereign bonds. The tribunal was of the opinion that the ordinary meaning of the term 'investment' certainly does not restrict the scope of the notion so as to exclude bonds or security entitlements.[42] States have the possibility of restricting economic operations and assets that they consider to constitute investments, by giving or not giving consent or by qualifying their consent with certain restrictions, be it via their domestic investment legislation or via the applicable BIT.[43] According to the tribunal, the definition of the term 'investment' should be a literal meaning plus any restrictions imposed by the host state to the meaning of investment. Such restrictions include (i) notifications under article 25(4); (ii) the definition of investment within the national investment legislations; and (iii) the definition in the applicable BITs.[44]

In the *Postova Banka* case the tribunal considered article 1 of the Slovakia-Greece BIT, which defined 'investment' as 'every kind of asset'. The tribunal concluded that the list of examples provided under article 1 of the Slovakia-Greece BIT must be considered within the context of the treaty. If the interpretation focuses only on the phrase 'every kind of asset' as an investment, the examples in article 1 will be redundant. The tribunal distinguished the Argentina-Italy BIT language because it contained the phrase 'independent of the legal form adopted' which was not equally available in the Slovakia-Greece BIT. It also distinguished the Argentina-Italy BIT because it contained examples of 'obligations' and 'public titles' compared to the Slovakia-Greece BIT reference to 'loans, claims to money or to any performance under contract'. The tribunal's conclusion was that the Argentina-Italy BIT contained a wider definition of investment as compared to that of the Slovakia-Greece BIT. The *Postova Banka* case is a clear illustration of how varying constructions of provisions in BITs can have different interpretations and implications.

The emergence of the sovereign debt investment cases (SDIC) has been the result of a lack of a comprehensive, binding international

40 *Biwater Gauff* (n 39 para 500.

41 As above.

42 *Ambiente* (n 33) para 456.

43 *Ambiente* para 452.

44 *Ambiente* para 453.

legal framework for the resolution of sovereign debt crises.[45] Holdout creditors find investment arbitration advantageous as states usually pay upon award in order to avoid reputational damage.[46] From the four cases above, the substantive standards of sovereign debts under BITs remain at the interpretative mandate of arbitral tribunals. If sovereign debts are not excluded from the BITs legal framework, states are under unpredictable pressure to face SDIC litigation.

Although there have never been SDIC cases in Africa, the possibility cannot be ruled out. The risks of leaving the Pandora's box open are higher. States, in particular SADC member states, should provide a clear stance on the scope of BITs in relation to sovereign debt. The negative implication posed by SDIC is that it hinders the ability of states to solve debt problems. Bond holders are likely to ignore sovereign debt restructuring (SDR) initiatives if they know that they can get even higher compensation by undertaking SDIC. Moreover, the existence of SDIC as an alternative to SDR gives bond holders an upper hand during SDR negotiations. Although the same can be true for waiver of sovereign immunity, SDIC have more effect, because courts have been reluctant to accept sovereignty immunity waivers. This makes it more difficult for states to put forth a successful SDR proposal.

On the other hand, as for the positive aspect of SDIC, it discourages 'opportunistic defaults' of sovereign debt, that is, that states deliberately do not make payment of their debts while they are able to pay. More than half of defaults by middle-income countries occur at levels of external debt relative to GDP below 60 per cent which, under normal circumstances, is usually viewed as an important indicator of debt sustainability.[47] Under opportunistic default, states enjoy the luxury of paying less than the bonds' face value by demanding a haircut. Together with the states' desire to be considered a good borrower, SDIC puts more pressure on states to comply and pay rather than default on their debts. However, this argument should not romanticise SDIC because opportunistic defaults are rare, as explained by the reputational and punishment theories of sovereign debt default. The reputational theory assumes that a debtor's sole incentive to make repayments is to preserve its reputation as a good borrower.[48]

45 G Anna 'Sovereign debt: Now what?' (2016) *Yale Journal of International Law Online* 45.

46 M Waibel 'Opening Pandora's box: Sovereign bonds in international arbitration' (2007) 101 *American Journal of International Law* 711-715.

47 CM Reinhart & KC Rogoff *This time is different: Eight centuries of financial folly* (2009).

48 J Bulow & R Kenneth R 'A constant recontracting model of sovereign debt' (1989) 97 *Journal of Political Economy* 155, also see J Eaton, M Gersovitz & JE Stiglitz 'The pure theory of country risk' (1986) 30 *European Economic Review* 481; H Grossman, H Van & B John B *Sovereign debt as a contingent claim: Excusable default, repudiation, and reputation*

The punishment theory theorises that a country pays their debt to avoid the threat of direct sanctions that lenders can impose which can cost the defaulting debtor's ability to transact freely in the financial and goods markets.[49]

7.3 The interplay between BITs and sovereign debt with particular focus on the SADC Model BIT

The relevance of BITs in sovereign debt default is on (i) the definition of 'investment' in relation to sovereign debt; (ii) the non-discrimination obligation (national treatment (NT) and most-favoured nation (MFN)) and how states can treat different bond holders differently; (iii) the fair and equitable treatment and whether SDRs impairs bond holders' legitimate expectations; and (iv) the utilisation of the investor-state dispute settlement mechanism by bond holders.

7.3.1 The definition of investment in relation to sovereign bonds

It is the definition provision that demarcates the applicability of a treaty. In BITs, the definition section has serious implications for the host state, as it mirrors the host state's exposure to investor-state claims. There are three forms of defining an investment. The first is an enterprise-based definition; the second is a closed-list asset-based definition; and, lastly, an open-list asset-based definition.

An enterprise-based definition is the narrowest option for outlining an investment. It requires the establishment or acquisition of an enterprise for the aim of making a remote investment. The definition then lists the assets of the investor that are covered because they form an element of the enterprise. However, this illustrative list is not the test for investment, but rather an illustration of the styles of assets of the investor that are covered by the treaty. For example, in the Morocco-Nigeria BIT

> investment means an enterprise within the territory of one state established, acquired, expanded or operated, in good faith, by an investor of the other state in accordance with law of the party in whose territory the investment is made

(1987).

49 As above. Also see B Eichengreen *Till debt do us part: The US capital market and foreign lending, I 920-I 955* (1987); PH Lindert & PJ Morton 'How sovereign debt has worked' Working Paper 45 Davis:.

taken together with the asset of the enterprise which contribute sustainable development.[50]

A closed-list asset-based definition is an intermediate approach to defining an investment. This definition is partially analogous to the enterprise-based definition. It provides a closed list which 'starts from an enterprise approach, but expands this to include assets like property rights, whether or not they're associated with an existing enterprise within the host state'. For example, in the Tanzania-Canada BIT '[i]nvestment means (a) an enterprise; (b) shares, stocks and other forms of equity participation in an enterprise; (c) bonds, debentures, and other debt instruments of an enterprise; (d) a loan to an enterprise'.[51]

An open-list asset-based definition provides for the broadest coverage. The definition is characterised by the use of broad language such as 'every kind of asset' or 'every kind of investment', followed by a non-exhaustive list of the investments covered. This approach is more favourable to investors and less predictable for host states. Arbitral tribunals can interpret this definition widely to include assets not usually considered to be investments. The shortage of limitations of this definition therefore is its biggest challenge. This notwithstanding, this has been the foremost widely-adopted definition in the old regime of BITs. For example, in the Germany-Zambia BIT '[t]he term "investment" shall comprise every kind of asset, and more particularly, though not exclusively …'[52]

All four SDICs involved an open-list asset-based definition of investment. Neither BIT (the Argentina-Italy BIT and the Slovakia-Greece BIT) expressly included bonds in the list of qualifying investments. The tribunal in the three Argentina cases held that Argentine sovereign bonds qualified as an 'investment' under the BIT because the BITs defined investment as every kind of asset and the illustrative list of assets contained assets similar to sovereign debt/bonds. However, the tribunal in *Postova Banka* held that the Greece sovereign bonds did not qualify as investments because, although investment was defined to mean every kind of asset, the illustrative list of investments did not contain anything similar to sovereign debt/bond. Whether a sovereign bond falls under the definition of investment depends on the precise wording of the treaty.

50 Reciprocal Investment Promotion and Protection Agreement Between the Government of the Kingdom of Morocco and the Government of the Federal Republic of Nigeria.

51 Art 1, Agreement between the Government of Canada and the Government of the United Republic of Tanzania for the Promotion and Reciprocal Protection of Investments.

52 Art 8, Treaty between the Federal Republic of Germany and the Republic of Zambia Concerning the Encouragement and Reciprocal Protection of Investments.

After considering the most used three options of defining 'investment', the SADC Model BIT recommends the enterprise-based definition and strongly advises against an open-list asset-based definition. The recommended definition reads as follows:

> Investment *means an enterprise within* the territory of one state party established ... An enterprise may possess assets such as ...
>
> For greater certainty, investment does not include:
> (1) debt securities issued by a government or loans to a government.

The SADC model BIT definition of investment specifically excludes sovereign bonds from the scope of the BITs by specifically excluding debt securities issued by the government as investment.

Apart from the three most used forms of defining investment in BITs, some other forms of defining the term 'investment' can be seen in investment treaties involving SADC member states. For example, the Brazilian-Angola Cooperation and Investment Facilitation Agreement (Brazil-Angola CIFA) leaves the definition of investment to be determined under the domestic law of the respective countries. Another is the Brazil-Mozambique CIFA which defines investment as a long-lasting enterprise producing goods and services, with the exclusion of portfolio investments, sovereign debts and money claims.

The discussions above have only addressed the definition of investment under BITs. However, for cases under the ICSID Convention framework,[53] the Convention requires that the transaction or asset should also qualify as investment under the ICSID Convention. The next paragraphs will discuss the relationship between the investment definition in the SADC Model BIT and in the ICSID Convention (Convention).

The ICSID Convention does not define the term 'investment'. The negotiation history reveals diverging views on what investment should be, leading to the non-inclusion of the definition of investment in the Convention. During the negotiations, delegates offered varying views on the inclusion of bonds and loans. Burundi underscored that money lent to a state should not be termed investment.[54] Austria rejected the inclusion of

53 Convention on the Settlement of Investment Disputes Between States and Nationals of Other States (International Centre for Settlement of Investment Disputes (ICSID)) 575 UNTS 159.

54 ICSID *The history of the ICSID Convention: Documents concerning the origin and the formulation of the Convention on the Settlement of Investment Disputes between States and Nationals of Other States* (1970) 261.

public bonds.[55] Australia was of the view that the Convention seemed to include cases where the host country borrows cash from foreign investors.[56]

After having reviewed dozens of cases[57] related to debt instruments and sovereign bonds, Waibel concluded that so far, ICSID tribunals had liberally accepted jurisdiction over debt instruments, despite the ambiguity of article 25.

There have been divergent views on the relationship between the BIT definition of investment and that of the Convention. The first view is to the effect that the ICSID Convention definition of investment takes supremacy over the BIT definition. This position was taken by the annulment committee in the *Mitchell v DRC* case, when it ruled that 'the ICSID Convention may only be applied to the type of investment that the multilateral ICSID Convention envisaged'.[58] This position has been cemented in other legal scholarships and case laws.[59] If this approach is taken, then member states to the ICSID Convention might find it difficult to enjoy the limited scope of the SADC Model BIT definition, in case the definition of investment under the ICSID Convention is found to include sovereign bonds.

The second approach gives the BIT definition supremacy over the ICSID Convention definition. The annulment committee in the *Malaysian Historical Salvors* case ruled that a BIT should be accorded supremacy over

55 ICSID (n 54) 709.

56 ICSID (n 54) 668.

57 The cases reviewed include *Fedax v Venezuela*; *CSOB v Slovakia* (Jurisdiction); *CSOB v Slovakia* (Jurisdiction); *SOABI v Senegal*; *Mytilineos v Serbia & Montenegro* (Jurisdiction); *Globex v Ukraine* (Award); *Joy Mining v Egypt* (Jurisdiction); *CDC v Seychelles* (Jurisdiction); *Booker v Guyana*; *ADC v Hungary* (Award); *OKO Pankki Oyj v Estonia* (Merits); *I&I Beheer v Venezuela*; *Skype v Venzuela* (2009); *Sempra v Argentina* (Award); *Renta 4 v Russian Federation*; *Asian Express v Greater Colombo Economic Commission*; *Mihaly v Sri Lanka* (Jurisdiction).

58 *Mr Patrick Mitchell v Democratic Republic of the Congo* ICSID Case ARB/99/7 (Decision on the Application for Annulment of the Award) para 25.

59 *Mitchell v DRC* (Annulment) para 25; Z Douglas *The international law of investment claims* (2009) 165; CL McLachlan & M Weiniger *International investment arbitration: Substantive principles* (2007) 170; R Dolzer & C Schreuer *Principles of international investment law* (2008) 61-62; *Fakes v Turkey* (Award) para 111; *Globex v Ukraine* (Award) paras 43-44.

the ICSID Convention.'[60] The *Malaysian Historical Salvors* case position echoes the *Biwater Gauff* flexible approach to investment.[61]

The third approach requires that both the BIT and the Convention be given equal weight. The tribunal in the *SGS* case ruled that the jurisdiction of the Centre should be determined by jointly evaluating the BIT and the Convention.[62]

In order to ensure coherence, a two-tier approach is desirable. The tribunal should first evaluate whether the dispute meets the investment criteria under article 25 of the Convention and then undertake a second assessment of whether the investment in dispute is also an investment under the BIT in question.[63] This is so because, first, the question of 'investment definition' is a question of jurisdiction and admissibility of the case. The ICSID tribunal should first assess jurisdiction and admissibility of the case before it starts to deliberate the case. The main or primary document governing the ICSID tribunal jurisdiction and admissibility of case is the ICSID Convention. After the ICSID Convention, the BIT becomes a secondary document for the ICSID tribunal assessment of jurisdiction particularly when answering the question of whether the dispute concerns an investment within the meaning of the BIT under consideration.

It can therefore be concluded that different BITs define investment differently. The variations in the definition of investment are the deciding factors on whether a sovereign debt should be covered as investment or not. The SADC Model BIT defines investment by specifically excluding sovereign debts within the BIT scope of coverage.

7.3.2 Non-discrimination (national treatment and most-favoured nation provision)

Non-discrimination has become the key protection afforded to investors in the treaty system. The thrust of this principle is that states cannot discriminate among investors on the basis of nationality. In international investment law, non-discrimination is exemplified within the national treatment (NT) and the most-favoured nation (MFN) treatment standards.

60 'It is those bilateral and multilateral treaties which today are the engine of ICSID's effective jurisdiction. To ignore or depreciate the importance of the jurisdiction they bestow upon ICSID, and rather embroider upon questionable interpretations of the term 'investment' as found in Article 25(1) of the Convention, risks crippling the institution.' *Malaysian Historical Salvors* (Annulment) para 73.

61 *Malaysian Historical Salvors* para 79.

62 *SGS v Philippines* (Jurisdiction) para 154.

63 M Waibel *Sovereign defaults before international courts and tribunals* (2013).

The NT obligation requires states to treat foreign investors in the same way it treats its own nationals. The problem with this obligation is that debtor states often have a legitimate reason to treat domestic bond holders differently. For example, the insolvency of certain banks or pension funds might hit a country disproportionately hard. However, sovereign bonds nowadays are held by a myriad of creditors, nationals and non-nationals. It therefore seems difficult to discriminate against non-nationals.[64] Therefore, under this sub-part the focus will only be on the MFN standard.

The MFN provisions are designed to prevent trade distortions and promote trade liberalisation.[65] However, the challenges posed by the MFN provisions have led to it being rejected by SADC Model BIT. MFN provisions have been criticised by investment tribunals for their wide interpretation. It has been interpreted as to apply in dispute settlement,[66] and it can also attract a state's obligation from other treaties to be applicable in another treaty which does not contain those obligations.[67] It has allowed investors to free-ride on benefits granted to other investors in other treaties. The MFN clause therefore, as the SADC Model BIT notes, had the unintended consequence of multilateralisation of the international investment regime. In the *Maffezini* case[68] under the Argentine-Spain BIT the tribunal agreed with the investor to import and use the jurisdiction provision available in the Chile-Spain BIT. The Argentine-Spain BIT had a waiting period requirement while it was not the case for the Chile-Spain BIT. The tribunal used the Argentine-Spain BIT's MFN clause to import the ISDS clause from the Chile-Spain BIT. In another case, the *RosInvest Co* case,[69] the tribunal used the MFN clause to broaden claims by incorporating coverage of a wide range of claims available in another BIT.

There was therefore a compelling reason for the SADC Model BIT to omit the MFN clause, irrespective of its benefits. The SADC Model BIT

64 Waibel (n 63) 740.

65 M Ahmad, R Blanpain & B Flodgren *Corporate and employment perspectives in a global business environment* (2006).

66 A Tanzi *International investment law in Latin America: Problems and prospects/Derecho internacional de las inversiones en America Latina: Problemas y perspectivas* (2016).

67 D Collins *An introduction to international investment law* (2017).

68 *Emilio Agustín Maffezini v The Kingdom of Spain* ICSID Case ARB/97/7 (Award) (13 November 2000).

69 *RosInvestCo UK Ltd v The Russian Federation,* Arbitration Institute of the Stockholm Chamber of Commerce Case V079/2005, Final Award (12 September 2010).

recommends that the MFN provision should not be included in a treaty because it has the unintended effect of multilaterisation.

7.3.3 Fair and equitable treatment and the impairment of bond holders' legitimate expectations

While at first glance it seems in order to promise 'fair and equitable treatment' to an investor and his investment, ISDS arbitrators have interpreted this standard of treatment to incorporate as nearly anything negatively impacting investment. The alleged breach of the 'FET provision' remains one of the most used standards of treatment in ISDS cases.[70] It protects legitimate expectations – a notion that has received many, partly diverging interpretations.[71] It will therefore depend on the specific circumstances of a case whether tribunals will recognise a violation of the FET standard. In *CMS* the tribunal held that the host state needed to ensure a stable business environment.[72] It has been ruled that regular insolvency proceedings do not violate the FET standard.[73]

The SADC Model BIT recommends against the inclusion of a provision on fair and equitable treatment and opts instead for an alternate formulation of the availability on fair administrative treatment (FAT), if it is deemed necessary to include this clause. The special note provides that the fair and equitable treatment provision is a highly controversial provision. The drafting committee recommended against its inclusion due to very broad interpretations accorded to it by ISDS tribunals, as explained above. It [FET] has been interpreted to almost include anything negatively impairing an investor's investment. The fair administrative treatment (FAT) provides:

> The State Parties shall ensure that their administrative, legislative, and judicial processes do not operate in a manner that is arbitrary or that denies administrative and procedural [justice][due process] to investors of the

70 J Bonnitcha, LN Poulsen & M Waibel *The political economy of the investment treaty regime* (2017).

71 UNCTAD 'Fair and equitable treatment' UNCTAD Series on Issues in International Investment Agreements (2012) 63.

72 *CMS Gas Transmission Co v Argentina* ICSID Case Arb/01/8 (Award) (12 May 2005) para 274.

73 *Noble Ventures Inc v Romania* ICSID Case ARB/01/11 (Award) (12 October 2005) paras 177-178.

other State Party or their investments [taking into consideration the level of development of the State Party].

According to the commentary the alternative provision seeks to avoid the most controversial elements of FET.[74] However, it is important to note that some of the key words that have been used in the FAT provision have also been interpreted in relation to FET. As Waibel notes, the FET requires governments to act in conformity with the international standards of transparency, non-arbitrariness, due process and proportionality to the policy aims involved.[75] In the same way the FAT provides that 'administrative, legislative, and judicial processes do not operate in a manner that is arbitrary …[76] … improve the transparency, efficiency, independence and accountability'.[77]

Waibel lists five possible claims of FET in relation to sovereign bonds: first, a lack of transparency undermining legitimate expectations;[78] second, a take-it-or-leave-it exchange offer violates due process;[79] third, SDR carried out without good faith; fourth, profound transformation of the business environment; and, fifth, SDR undermines the legal framework of the sovereign bonds.[80]

The first and second forms of possible claims set out by Waibel might equally fall within the ambit of FAT. As for the first possible claim of lack of transparency, the FAT clause requires states to progressively improve transparency. Although progressive sounds like a soft obligation, borrowing from the jurisprudence of the protection of international economic human rights, progressive is an obligation that is capable of being violated if the state does not undertake concrete steps towards the goal.[81] It therefore falls that bond holders can show that the government was not transparent enough and it did not take affirmative steps to achieve that goal to the violation of the FAT obligation. However, in sovereign

74 South African Development Community Model Bilateral Investment Treaty Template with Commentary (SADC Model BIT) (July 2012).

75 Waibel (n 46) 711.

76 SADC Model BIT 5.1.

77 SADC Model BIT 5.5.

78 *Metalclad v Mexico* (Merits) para 76; *Maffezini v Spain* para 83; *CME v Czech Republic* para. 611; *Tecmed v Mexico* (Merits) para 152.

79 Waibel (n 63) 295.

80 Waibel (n 63) 296.

81 S Fukuda-Parr, T Lawson-Remer & S Randolph 'An index of economic and social rights fulfilment: Concept and methodology' (2009) 8 *Journal of Human Rights* 195.

bonds a transparency argument is unlikely to succeed due to the complex nature of the sovereign bonds market and restructuring.[82]

Another form of transparency concern is intrinsic to the sovereign debt management and not necessarily transparency in relation to the legal and regulatory framework. In Mozambique the International Monetary Fund (IMF) had to suspend its cooperation in 2016, after discovering a hidden debt of around $1,2 billion, following its first default in 2013. This raises a concern when it comes to the transparency of the Mozambiquan government.[83]

As to the second possible claim of a lack of due process of law, the SADC FAT provides to the effect that administrative or legislative action should not be operated in a way that denies administrative and procedural [justice][*due process*] to investors. By adopting a take-it-or-leave-it approach, bond holders can argue that the government act is a unilateral confrontational act without regard to due process.[84] To comply with this, the government should at least engage with bond holders in good faith.[85] This mirrors the situation in Zambia. The initiative of the Zambian government to engage with bond holders by requesting a six-month repayment holiday while it drafts its debt-restructuring plan, can be viewed as delaying tactic but it can also be viewed as an initiative of transparency by engaging with bond holders. On the other hand, creditors are raising concerns that the Zambian government is not acting in good faith, and any relief granted by Zambia would be designed to favour Chinese lenders, who account for the utmost amount of debt.[86]

7.3.4 The investor-state dispute settlement

The investor-state dispute settlement (ISDS) is the gateway for the investment arbitration case between an investor and the state. However, this mechanism has been losing its popularity due to concerns over the impartiality of arbitrators and the subjection of a sovereign state on equal footing with an individual person.

82 Fukuda-Parr et al (n 81) 295.

83 'Mozambique: Debt crisis despite Eurobond restructuring', https://www.fxstreet.com/analysis/mozambique-debt-crisis-despite-eurobond-restructuring-202001150911 (accessed 3 November 2020).

84 Waibel (n 63) 295.

85 As above.

86 T Mitimingi 'Zambia's missed Eurobond payment prompts default call by S&P' (23 October 2020), https://www.bloombergquint.com/markets/s-p-cuts-zambia-to-default-after-eurobond-payment-missed (accessed 3 November 2020).

The SADC Model BIT rejects the incorporation of ISDS provisions in BITs and recommends domestic and regional forum frameworks in the settlement of investment disputes. According to the model, investors should vindicate their rights in domestic courts or arbitration within the host country's institutions. However, this option is likely to jeopardise the quality of awards as most SADC countries lack strong arbitration institutions and capacity domestically. The independency of the judiciary remains an issue of concern in most SADC member states.

7.4 Conclusion

SADC Model BIT has significantly succeeded to limit the sovereign debt concept to fall within the BIT legal framework. It has limited the definition of investment to exclude sovereign debt. Hence, for countries adopting the SADC model's investment definition will be under no danger of facing sovereign debt investment cases (SDIC) litigation in case of default.

By excluding the MFN standard, the Model resolves the danger of bond holders importing more favourable terms from other BITs in order to accommodate their interests. For example, if the definition of investment under country A's BIT with country B excludes sovereign debt and country A's BIT with country C does not exclude sovereign debt as investment; then country B's bond holders can demand the definition of investment under country A's BIT with country C be applicable to them if country A's BIT with country B contains a typical old regime MFN clause. This type of importation makes reform useless if they do not address the practical implications of MFN provisions.

However, considering the important role that sovereign debt plays in providing states with needed finance, the global community should undertake coordinated efforts in creating a comprehensive framework to deal with sovereign debt defaults outside the BITs framework.

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8 Sovereign debt restructuring and human rights: Overcoming a false binary

Magalie L Masamba

8.1 Introduction

The COVID-19 pandemic has had an unparalleled impact globally and has resulted in both a health crisis and economic crisis of epic proportions. Further, it has not only refocused the spotlight on sovereign debt related issues, but today it is probably changing the way in which we view debt-related issues that raise complex legal tensions. Sovereign debt restructuring (SoDR) in particular raises many legal questions because, despite decades of discussion, there still is no international mechanism to restructure sovereign debt, especially privately-held sovereign debt. The challenges of SoDR from a global perspective have been extensively discussed in the literature, and an African perspective on these challenges is slowly becoming part of the debate.[1]

The literature on the subject reveals that the governance gap created by an *ad hoc* approach to SoDR presently results in restructurings that are untimely, protracted, disorderly and inefficient. These challenges have arisen for various reasons, including the lack of effective coordination mechanisms, the multiplicity of institutional arrangements dealing with SoDR and the growing and ill-suited gap-filling role that national courts currently play.[2] However, the problems of present-day SoDR go beyond

* I would like to express my gratitude to Prof Daniel D Bradlow for his guidance and commentary on this chapter.

1 UNCTAD 'Sovereign debt workouts: Going forward – Roadmap and guide' (April 2015) 3, http://unctad.org/en/PublicationsLibrary/gdsddf2015misc1_en.pdf (accessed 10 June 2017). Also see ML Masamba 'An African perspective on reforming sovereign debt restructuring of privately held debt' LLD thesis, University of Pretoria, 2020. Also see ML Masamba 'Reflections on the current reality of Africa's debt landscape' AfronomicaLaw (26 January 2021), https://www.afronomicslaw.org/category/african-sovereign-debt-justice-network-afsdjn/reflections-current-reality-africas-debt (accessed 30 April 2021).

2 UNCTAD (n 1) 3.

the procedural issues.[3] The aspect that has been less discussed relates to fairness, or the lack thereof. An ideal approach to SoDR requires addressing the complex web of challenges – both substantive and procedural.[4] Both these dimensions have an impact on fairness, whether relating to fairness in the process or fairness of the outcome of a restructuring. The substantive issues, which are the focus of this chapter, can be grouped into two broad categories, namely, (i) the financial and economic problems required to restore a sovereign debtor to debt sustainability which are the subject of the negotiations between the sovereign debtor and its creditors; and (ii) the social and political concerns that also include human rights concerns, which have generally been seen to be the concern of the debtor.[5]

This chapter focuses on the second point, by addressing the link between sovereign debt and human rights. This chapter, therefore, will answer the question of whether there indeed is a failure of the present SoDR 'non-system' to deal adequately with human rights and

3 The term 'procedural', as Bradlow notes, comprises 'the arrangements for the negotiations between the debtor and creditors in an SODR' and includes, for instance, how to disseminate information to stakeholders in the restructuring process. DD Bradlow 'Can parallel lines ever meet? The strange case of the international standards on sovereign debt and business and human rights' (2016) 41 *Yale Journal of International Law* 201, 235.

4 Traditionally, the problems have mostly revolved around securing sufficient creditor coordination while dealing with numerous and diverse creditors and the high incentives for creditor holdouts. The question of binding minority creditors is among the key challenges in SoDR. This in turn has influenced the types of solutions that have been proposed to date, in particular the use of contractual innovations (CACs, aggregation provisions, etc). In fact, Sedlak has expressed the view that even where agreements are reached with all the major creditors, the question of how to compel minority creditors to accept the restructured deal may still pose a challenge. This challenge becomes ever more acute with restructuring over multiple bond series where there are no provisions for aggregation across multiple bond issues and raises concerns over inter-creditor equity. See J Sedlak 'Sovereign debt restructuring: Statutory reform or contractual solutions' (2004) 152 *Pennsylvania Law Review* 1483, 1493. Since this research in 2004, aggregated CACs have become a more common feature of sovereign bond issuances, including African sovereign bond issuances. However, despite the advancements, not all bonds issued by African countries include CACs and the potential of a collective action problem persists. Eg, in the SADC region, Zambia, the first African country to default during the COVID-19 pandemic, had issued Eurobonds that do not contain CACs, including the 2022 and 2024 bonds, thereby raising major concerns for a potential holdout by minority creditors in 2020. This is only one example of an African bond issuance that does not contain CACs. See Debtwire Republic of Zambia, Special Report (10 August 2020) 2, Governmenthttps://www.mergermarket.com/assets/Zambia%20Sovereign%20Report%20-%20FY19.pdf (accessed 10 April 2021). Further, today the collective action problem that may arise in the context of the current debate on restructuring is not so much that the creditor base is too dispersed, but rather how to get the private sector to agree on a restructuring for poorer and vulnerable countries.

5 Bradlow (n 3) 235.

developmental concerns. In so doing, I argue that not only does sovereign debt raise human rights concerns, but it can and should also be considered a human rights issue. In fact, to me, an analysis of SoDR without the consideration of human rights and developmental concerns would make such an analysis incomplete.

In making the above assessments, the chapter is divided into four parts. The first part briefly highlights the debt landscape in the Southern African Development Community (SADC) region, but does so in an abbreviated manner as other chapters in this book have conducted detailed assessments of the same.[6] The chapter then assesses the link between sovereign debt and human rights in the legal literature and identifies what is a glaring disconnect between these two fields. This leads to the following part, which explores whether there is a place for human rights in the sovereign debt discourse, in particular SoDR, which is one of the emerging issues that is still relatively overlooked. In so doing, this part considers the human rights impact on debtors and creditors and how the adoption of a human rights approach is viewed in present SoDR discourse.

8.2 Africa's sovereign debt landscape and debt restructuring

8.2.1 An overview of SADCs debt landscape

African sovereign debt levels are increasing and the nature of the debts are evolving as African countries turn to the capital markets to raise additional finance for development and to fill their budget deficits.[7] The 2021 statistics for the World Bank Group indicate that sub-Saharan Africa's overall external debt stock has considerably risen from approximately US $266

6 Among the chapters in this publication, see DD Bradlow & ML Masamba, ch 1 'Sovereign debt management and restructuring in SADC: Setting the scene and asking the right questions'; M Kessler, ch 3 'Deferring debt service in times of crisis: Did it matter and what can it lead to?; K Gallagher and Y Wang ch 5 'Sovereign debt via the lens of asset management: Implications for SADC countries'.

7 Among the justifications for the high demand for sovereign borrowing are the high developmental needs of the continent. In particular, the domestic resources of African countries are simply insufficient to meet its needs, including the need to fill the vast infrastructure deficit. At present the public infrastructure deficit is among the leading developmental challenges and is hindering the continent's integration with the global economy. Many countries are now finding their debt at the same levels as pre-HIPC. A case in point is Ghana, which went from being a HIPC success story to again requiring bailouts from the IMF. AfDB African Legal Support Facility 'Vulture funds in the sovereign debt context', http://www.afdb.org/en/topics-and-sectors/initiatives-partnerships/african-legal-support-facility/vulture-funds-in-the-sovereign-debt-context/ (accessed 30 January 2017).

billion in 2009 to approximately US $625 billion in 2019.[8] Furthermore, the external private sector long-term non-guaranteed debt rose from US $203 billion in 2008 to US $535 billion in 2019.[9] On these growing debt levels, the World Bank Group had already raised the concern in 2020 that the region's debt had increased faster than that of other regions with some sub-Saharan African countries more than doubling their debt stocks and with poorer countries that are legible for International Development Association assistance, accumulating an 89 per cent share of the region's then US $116 billion bond debt in 2018.[10] This figure in the most recent statistics is US $109 billion.

While sovereign debt is an important feature of the development process, the increased levels of new private debt bring with it the increased risk of distress or default. Several sub-Saharan African countries that issued Eurobonds in the last decade have at one time or another experienced difficulties with the repayment of their international bonds.[11] Among the experiences of SADC countries, the most recent is Zambia which in November 2020 defaulted on its US $42,5 million Eurobond payment. Previously, in January 2017 Mozambique missed a payment of US $60 million, and defaulted on the interest rate payment due for a US $772 million bond payment and a US $120 million payment due in March

8 World Bank Group 'International debt statistics' (2021), https://openknowledge.worldbank.org/bitstream/handle/10986/34588/9781464816109.pdf (accessed 30 April 2021).

9 World Bank Group (n 8) 31.

10 World Bank Group 'International debt statistics' (2020) vii, https://openknowledge.worldbank.org/bitstream/handle/10986/32382/9781464814617.pdf?sequence=7&isAllowed=y (accessed 1 July 2020).

11 Brooks et al point out that in 2005, most SSA countries had not issued any international bonds. Yet, by 2013 such bonds made up 21% of Zambia's, 27% of Rwanda's and 56% of Namibia's total sovereign debt. S Brooks, D Lombardi & E Suruma 'African perspective on sovereign debt restructuring' Centre for Governance Innovation Issues Paper 47 (September 2014) 6, https://www.cigionline.org/sites/default/files/no43_web.pdf (accessed 1 June 2017).

2017.[12] Additionally, Seychelles defaulted on a US $230 million Eurobond in 2011 following election disputes.[13]

In 2020 in the wake of the COVID-19 pandemic and the ensuing economic crisis, African countries are again in debt distress and payment moratoriums/standstills may be needed.[14] As a response to this need, the G20 has launched the COVID-19 Debt Service Suspension Initiative (DSSI) to temporarily suspend official bilateral debt payments.[15] In this respect, at the World Bank/IMF spring meeting in April 2020, the Development Committee proposed that moratoriums on privately-held sovereign debt apply with terms comparable with those imposed on bilateral debt.[16] The president of the World Bank, David Malpass, in response to this Development Committee proposal, acknowledged the important role that the treatment of privately-held sovereign debt also plays, and noted that '[t]he commercial creditors of governments need to support sovereign debt reduction efforts too – not free ride'. [17] In an effort to provide a more comprehensive option and to tackle the challenge of bringing the private creditors to the table the G20 agreed the Common Framework for Debt Treatments beyond the DSSI. It offers restructuring

12 The case of Mozambique is a very complex one. The bonds in question had been issued to raise finance for the repayment of syndicated loans that were obtained for the alleged purchase of tuna boats by state-owned companies, guaranteed by the government of Mozambique. The Constitutional Council has subsequently held that this government guarantee was provided illegally. See 'Mozambique defaults on repaying fishy debt' *Sunday Times* (29 January 2017), https://www.pressreader.com/south-africa/sunday-times/20170129/282471413582050 (accessed 30 August 2017). Also see 'Mozambique to default again on hidden debt payment due today' *Zitamar News* (21 March 2017), https://zitamar.com/mozambique-default-hidden-debt-payment-due-today/ (accessed 1 December 2017). In this publication, Koen has conducted a detailed case study of Mozambique's debt that has been tainted by corruption. See L Koen ch 10 'The renegotiation of sovereign debt tainted by corruption: Mozambique's "secret" debt in perspective'.

13 Brooks et al (n 11) 6, 7.

14 'Senior Africans propose "standstill" on Eurobond debt payments' *Financial Times* (7 April 2020), https://www.ft.com/content/89c6d60f-5fe9-4b72-b327-4a6eb267a9c9 (accessed 1 July 2020).

15 World Bank Group 'COVID 19: Debt Service Suspension Initiative' (19 February 2021), https://www.worldbank.org/en/topic/debt/brief/covid-19-debt-service-suspen sion-initiative (accessed 3 March 2021).

16 World Bank 'World Bank/IMF spring meetings 2020: Development committee Communiqué' (17 April 2020), https://www.worldbank.org/en/news/press-release/2020/04/17/world-bankimf-spring-meetings-2020-development-committee-communique (accessed 1 July 2020).

17 World Bank Group President 'World Bank Group President Malpass: Remarks to the Development Committee' (17 April 2020), https://www.worldbank.org/en/news/statement/2020/04/17/world-bank-group-president-malpass-remarks-to-the-development-committee (accessed 1 June 2020).

for low-income country debts from a broad array of creditors, including the private creditors.[18]

8.2.2 Why the focus on SADC's debt restructuring experience?

Previous multilateral initiatives on debt relief to African countries focused on official and bilateral debt (which in the past represented the more extensive stock of African debt). These initiatives include the Heavily-Indebted Poor Country programme (HIPC) and Multilateral Debt Relief Initiative (MDRI). Notwithstanding the debt burden reduction achieved, African countries remained vulnerable to predatory litigation by vulture funds that acquired debt that received treatment under the abovementioned debt relief initiatives.[19] These relief initiatives did not alter the legal terms of underlying debt contracts, as such, and, as a result, litigation has still occurred. SADC countries that have had cases brought against them or been threatened with litigation from commercial creditors and vulture funds include Angola, Democratic Republic of the Congo (DRC), Madagascar, Mozambique and Zambia.[20] The vulture fund claims represent a considerable portion of the gross domestic product (GDP) of these and other African debtor countries that have been targeted.[21] It is estimated that the number of sovereign debt claims filed against HIPCs

18 Paris Club 'Common framework for debt treatments beyond the DSSI', https://clubdeparis.org/sites/default/files/annex_common_framework_for_debt_treatments_beyond_the_dssi.pdf (accessed 15 June 2021).

19 According to the AfDB African Legal Support Facility, out of 25 judgments granted in favour of vulture funds (yielding approximately US $1 billion) the majority have been against countries that are regional members of the bank. AfDB African Legal Support Facility (n 7).

20 See AfDB (n 7). Some cases involving African debt pursued by vulture funds in national courts include *Camdex International Ltd v Bank of Zambia* 1996 (3) All ER 431 (CA); *Camdex International Ltd v Bank of Zambia* 1997 CLC 714 (CA); *Lordsvale Finance v Bank of Zambia* 1996 QB 752; and *Donegal International Ltd v Republic of Zambia* 2007 All ER (D) 184, all of which concerned Zambian distressed sovereign debt pursued by vulture funds in national courts of the United Kingdom; the unreported case of *Hamsah Investments Ltd & Another v The Republic of Liberia* Case 2008/587 (High Court of Justice, London), concerning litigation by vulture funds in the national courts of the United States and United Kingdom to recover distressed Liberian debt; and *FG Hemisphere Associates LLC v République du Congo* 455 F.3d 575 (5th Circ 2006); *Democratic Republic of the Congo v FG Hemisphere Associates LLC* [2011] 4 HKC 151, concerning litigation in the national courts of the United States and Hong Kong to recover DRC distressed debt. For a discussion of the case law emanating from the Congolese, Liberian and Zambian case studies, see 'Report of the Independent Expert on the effects of foreign debt and other related international financial obligations of states on the full enjoyment of all human rights, particularly economic, social and cultural rights, Cephas Lumina' Human Rights Council 14th session A/HRC/14/21 (29 April 2010) 7-10, https://www.refworld.org/pdfid/4c29a9f02.pdf (accessed 7 June 2017).

21 AfDB African Legal Support Facility (n 7).

alone has surpassed the volume of debt relief that was provided under this programme.[22] A case in point in the SADC region is the DRC that has debt claims brought against it in foreign courts amounting to approximately 15 per cent of the country's GDP.[23]

More broadly, the focus on the African continent is vital due to the continent's vulnerability. Even though debt crises have a very adverse impact on developed and developing countries alike, this impact is augmented in the case of developing countries and sub-Saharan African countries in particular, due to their vulnerability.[24] In this respect, African countries greatly suffer from the grave human rights and social implications of problematic SoDRs. Further, the SoDR process is less efficient and leads to more negative outcomes in this region, especially for low-income sub-Saharan African countries. On this point, Wright has assessed various outcomes in the SoDR process in the different regions, including the number of years of delay and level of creditor losses.[25] Wright points out that SoDR of privately-held debt 'is time-consuming, expensive, and largely ineffective at preserving the value of creditor claims or reducing the long-term indebtedness of the sovereign debtor', and finds that these outcomes are worse for sub-Saharan Africa.[26] Concerning delays, Wright's research reveals that it generally takes an average of approximately six years for a default to be resolved. More specifically by region, Europe

22 U Das, M Papaioannou & C Trebesch 'Sovereign debt restructurings 1950-2010: Concepts, literature survey and stylised facts' IMF Working Paper 12/203 (August 2012) 50, https://www.imf.org/en/Publications/WP/Issues/2016/12/31/Sovereign-Debt-Restructurings-1950-2010-Literature-Survey-Data-and-Stylized-Facts-26190 (accessed 1 April 2017).

23 As above.

24 Not only does Stichelmans assess the debt vulnerabilities and impact of debt crisis, but he also states that developed and developing countries are increasingly at the risk of debt crisis as debt levels (especially in developed countries) have reached a historical high. Further, these potential crises can undermine the implementation of the Sustainable Development Goals, especially in the case of acute debt crisis. See T Stichelmans 'Why a United Nations sovereign debt restructuring framework is key to implementing the post-2015 sustainable development agenda' European Network on Debt and Development Briefing (May 2015), http://www.eurodad.org/files/pdf/560542f0a6035.pdf (accessed 1 June 2017). Also see N Ellmers & D Hulova 'The new debt vulnerabilities: 10 reasons why the debt crisis is not over' European Network on Debt and Development (November 2013), https://eurodad.org/files/pdf/1546060-the-new-debt-vulnerabilities-10-reasons-why-the-debt-crisis-is-not-over.pdf (accessed 1 June 2017).

25 MLJ Wright 'Sovereign debt restructuring: Problems and prospects' (2012) 2 *Harvard Business Law Review* 153, 156.

26 Wright, however, expresses the view that despite the fact that SoDR leads to worse outcomes in SSA, this region is more reliant on official debt as opposed to private debt owed to commercial creditors. See Wright (n 25) 171.

and Central Asia take about four and a half years; Latin America and the Caribbean take approximately seven and a half years; while for sub-Saharan Africa, the average duration is much longer (approximately eight and a half years).[27]

Finally, commercial debt presents unique and complex problems during and after restructuring, even more so than concessional loan debt. For sub-Saharan African countries, these problems may have additional and even greater implications for a region that is already dealing with the heavy weight of extreme poverty levels and structural weaknesses in public institutional frameworks and good governance.[28] As such, the impact of a gap in the global governance of SoDR is mostly encountered by the citizens of a debtor that is forced to reallocate funds in the national budget that could have been utilised for education, health care and other social services to pay its debts, sometimes to a single creditor.[29] As such, in the absence of an international framework or policy coordination, the future restructurings of sovereign commercial debt owed to private creditors will result in escalated costs, including some unintended human rights, environmental and social costs that are caused by the problems of fragmentation, fairness and procrastination that plague the process. Low-income sub-Saharan African countries are among the most vulnerable to these additional costs which include not only the economic and political costs of SoDR, but also the social costs, including the human rights impact and the environmental costs. This justifies the need to explore the reform of the international sovereign debt landscape.

8.3 Is there a missing link between sovereign debt and human rights in the legal discourse?

The law on human rights and sovereign debt have historically been treated as two distinct fields. This is especially so for foreign sovereign debt. From a historical perspective, after World War II right up to the 1990s, human rights and sovereign debt were not only treated as two unrelated

27 Wright (n 25) 169-170.

28 I Husain & J Underwood 'The debt of sub-Saharan Africa: Problems and solutions' (9 July 1991), http://www.radioradicale.it/exagora/the-debt-of-sub-saharan-africa-problems-and-solutions (accessed 1 August 2017). According to the World Bank, although poverty on the continent has reduced in percentage (from 56% in 1990 to 43% in 2012) these statistics are somewhat misleading as there actually are more poor people today because of increased population growth. Further, out of the world's top 10 most unequal countries, seven are African countries. See World Bank 'While poverty in Africa has declined, number of poor has increased' (March 2016), http://www.worldbank.org/en/region/afr/publication/poverty-rising-africa-poverty-report (accessed 1 August 2017).

29 Bradlow (n 3) 202.

fields but, as Kampel observes, only limited and isolated efforts were made to link them.[30] Despite over-indebtedness in developing countries in the 1970s and 1980s, Kampel opines that the connection between over-indebtedness and human rights was generally overlooked.[31] Instead, the Bretton Woods institutions (the International Monetary Fund (IMF) and World Bank) responded to debt sustainability concerns by introducing structural adjustment programmes (SAPs), which were criticised as not being sufficiently considerate of human rights outcomes.[32] It was only in the mid-1990s that a more explicit link was made between the scale of developing country debt and the impact of debt repayment on human rights, resulting in debt relief programmes. It was then that more focus was given to the human rights impacts of the previous SAPs and conditionality of multilateral lenders such as the IMF. However, there now is a wealth of scholarly works on the human rights impact of SAPs and criticisms of Bretton Wood policies in general.[33] Various authors have likewise now noted the negative and positive human rights impacts and outcomes in different HIPC and MDRI countries.[34]

30 D Kampel & LatMa Research Team 'Sovereign debt restructuring and the right to development' Global Campus of Human Rights Research Programme (2014-2015) 1, https://gchumanrights.org/tl_files/EIUC%20MEDIA/Global%20Campus%20of%20Regional%20Masters/research/2014-15/3.pdf (accessed 1 June 2016).

31 As above. While there indeed is a noticeable gap in the literature on human rights and sovereign debt in the above-mentioned era, there are some important scholarly works that came out in this era that explored the impact of structural adjustment and social welfare. Of note, see GA Cornia, R Jolly & F Stewart (eds) *Adjustment with a human face: Country case studies* (1987).

32 Kampel (n 30) 1.

33 There is a link between the structural adjustment programmes and human rights impact. In some cases these programmes directly cause a negative impact as they aggravate a broad spectrum of rights including economic, social and cultural rights, civil and political rights, environmental rights and the right to self-determination. Negative human rights outcomes of IMF policies have been noted by other authors more recently, including Stubbs and Kentikelenis, who provide an outline of human rights implications of IFI lending conditionality and set out the direct and indirect impacts on the right to health, labour rights, civil and political rights; T Stubbs & A Kentikelenis 'Conditionality and sovereign debt' in I Bantekas & and C Lumina (eds) *Sovereign debt and human rights* (2018) 359-380. Also see AE Kentikelenis & L Seabrooke 'The policies of the world polity: Script-writing in international organisations' (2017) 82 *American Sociological Review*1065; DD Bradlow 'The World Bank, the IMF, and human rights' (1996) 6 *Transactional Law and Contemporary Problems* 47, 72-78; DD Bradlow 'Stuffing new wine into old bottles: The troubling case of the IMF' (2001) 3 *Journal of International Banking Regulation* 3-6; and DB Braaten 'Ambivalent engagement: Human rights and multilateral development banks' in S Park & JR Strand (eds) *Global economic governance and the development practices of the multilateral development banks* (2015) 99-118. Also see M Darrow *Between light and shadow: The World Bank, the International Monetary Fund and international human rights law (Studies in international law)* (2006).

34 Among the articles that discuss the success of the 'aid machinery' are MA Weiss 'The multilateral debt relief initiative' CRS Report for Congress (11 June 2012) 2, https://

The interconnections between the fields of sovereign debt and human rights have become of greater focus in the more recent years. This has, first, been reflected by the work of the UN Independent Expert on the Effects of Foreign Debt and other Related International Financial Obligations of States on the Full Enjoyment of all Human Rights, particularly Economic, Social and Cultural (UN Independent Expert).[35] In addition, scholarly works that explore the interconnection between these two fields have been written in recent years.[36] From the legal literature it is evident that the human rights approach to sovereign debt first requires defining the underlying link between sovereign finance and human rights and, second, it involves a determination of the legal implications flowing therein.[37] Bohoslavsky and Černič acknowledge that the legal theory that links sovereign finance and human rights is both underdeveloped and backward.[38] The authors note, among other observations, this gap exists because of (i) the difficulty in applying a multidisciplinary approach to two fields that have traditionally been treated as separate; (ii) the concern that factoring in human rights considerations when taking on loans will in effect 'politicise' what is viewed to be a purely technical financial issue; (iii) the challenge of tracing the use of borrowed funds and determining and quantifying the human rights obligations of states; and (iv) the fact that legal studies have only recently begun to link sovereign finance and human rights outcomes.[39]

I agree with the idea that there is a need for a stronger link between human rights and sovereign finance. Additionally, I find particular merit

fas.org/sgp/crs/row/RS22534.pdf (accessed 20 June 2016); S Isar 'Was the Highly Indebted Poor Country Initiative (HIPC) a success?' (2012) 9 *Journal of Sustainable Development* 107, 115; S Mustapha & A Prizzon 'Is debt sustainable in the post-HIPC era? A literature review' Overseas Development Institute (February 2014) 3, https://www.odi.org/sites/odi.org.uk/files/odi-assets/publications-opinion-files/9105.pdf (accessed 19 November 2017).

35 The mandate of the Independent Expert was officially set out by the Commission on Human Rights in Resolution 2000/82, and further extended by the Human Rights Council in Resolution 7/4 (2008), which not only renamed the independent expert but also set out key thematic areas of focus to include the impact of debt on human rights and the state's policy-making ability. In addition to the key thematic areas, it also requested the Independent Expert to consider the link between debt and other areas such as trade and HIV, etc. Resolution 16/14 (2001) and Resolution 25/16) which both extended the mandate of the Independent Expert for an additional three years.

36 See JP Bohoslavsky & JL Černič (eds) *Making sovereign debt and human rights and finance work* (2014); Bantekas & Lumina (n 33).

37 JP Bohoslavsky & JL Černič 'Placing human rights at the centre of sovereign financing' in Bohoslavsky & Černič (n 36) 3.

38 As above.

39 Bohoslavsky & Černič (n 37) 4.

in the first, third and fourth arguments by Bohoslavsky and □erni□ listed above. However, I believe that the second observation raises some additional perspectives that should be acknowledged. Of note is that while indeed it is true that the human rights approach has been unpopular with the financial sector, there are noticeable exceptions as some developments have occurred in this space, particularly the fact that several large banks have human rights policies/statements.[40]

In linking human rights and sovereign debt, Bantekas and Lumina not only observe the fragmentation between these disciplines but go as far as noting 'hostility between the "opposing" camps (ie human rights and commercial lawyers)'.[41] Among the reasons Bantekas and Lumina cite for the relatively-independent evolution of the two fields is what they describe, on the one hand, as the 'professionalisation and over-specialisation of human rights' which has culminated in a culture and drafting language that is little understood by those not immersed in human rights.[42] In this respect, they observe that this over-specialisation has resulted in 'a limited understanding of human suffering outside the specific context of existing human rights treaties'.[43] On the other hand, the discipline of human rights

40 As illustrations of the banks with human rights policies or statements, see Standard Bank Group 'Standard Bank Group statement on human rights', https://www.standardbank.com/static_file/StandardBankGroup/Who%20we%20are/Our%20values%20and%20code%20of%20ethics/PDFs/Human%20Rights%20Statement%20PDF.pdf (accessed 2 June 2020); 'Deutsche Bank statement on human rights', https://www.banktrack.org/download/deutsche_bank_human_rights_statement_1_pdf/deutschebankhumanrightsstatement.pdf (accessed 10 May 2020); 'Credit Suisse statement on human rights', https://www.banktrack.org/download/statement_on_human_rights_10/190305humanrightsstatementmarch2019.pdf (accessed 10 May 2020); Bank of America 'Bank of America human rights statement', https://about.bankofamerica.com/assets/pdf/human-rights-statement.pdf (accessed 10 May 2020); 'Citi statement on human rights' (November 2018), https://www.citigroup.com/citi/citizen/data/citi_statement_on_human_rights.pdf (accessed 10 May 2020); Deutsche Bank 'Human rights', https://www.db.com/newsroom/en/human-rights.htm; Lloyds Banking Group 'Human Rights Policy Statement', https://www.lloydsbankinggroup.com/globalassets/our-group/responsible-business/reporting-centre/humanrightspolicystatement-180222.pdf (accessed 2 June 2020). For further discussion on the human rights obligations on international financial institutions, see DD Bradlow 'A human rights-based approach to international financial regulatory standards' (2018) 171 *Articles in Law Reviews and Other Academic Journals* 940, https://digitalcommons.wcl.american.edu/cgi/viewcontent.cgi?article=1948&context=facsch_lawrev (accessed 10 May 2019); and M Aizawa, DD Bradlow & M Wachenfeld 'International financial regulatory standards and human rights: Connecting the dots' (2018) 15 *Manchester Journal of International Economic Law* 2.

41 I Bantekas & C Lumina 'Sovereign debt and human rights: An introduction' in Bantekas & Lumina (n 33) 1.

42 As above.

43 As above.

may be perceived as playing 'a fringed part in this process' by commercial lawyers, who treat sovereign debt as a purely commercial transaction.[44] As a result, commercial lawyers may see no reason to give human rights issues 'professional remit'.[45] Instead, they may find that human rights law opposes the interests of the commercial parties.[46] These factors are said to have limited the link between human rights law and other fields such as debt restructuring, despite what now seems to be a visible link.

In addition to different approaches between 'human rights lawyers' and 'commercial lawyers', there is also a noticeable difference in opinions between developed and developing countries on whether sovereign debt is a human rights issue. Lumina observes that this difference is apparent in the voting patterns of countries participating in the United Nations (UN) Human Rights Council in which two issues stand out, namely, (i) the idea that sovereign debt is not a human rights issue and resultantly is the notion that (ii) debt-related issues should not be discussed at the UN Human Rights Council.[47] For instance, in its vote on the resolution on the mandate on the UN Independent Expert, the US reiterated its concern that debt should not be treated as a human rights issue but rather concerned a commercial relationship between the debtor and creditor.[48] The US felt that the focus on the subject of sovereign debt by the Human Rights Council was not only misplaced, as other financial institutional setups are more suited to deal with sovereign debt.[49] However, the US also unduly side-tracked the Human Rights Council's attention and financial resources from what it described as 'serious human rights issues that more urgently require our attention'.[50] This, in effect, was confirmation of the rejection that sovereign debt is, and at the very least raises human rights implications. Likewise, the US again in 2017 reiterated its view that the Human Rights Council was dealing with subject matters that are both

44 As above.

45 As above.

46 As above.

47 C Lumina 'Sovereign debt and human rights: Making the connection' in Bantekas & Lumina (n 33) 173.

48 Human Rights Council 'US EOV on foreign debt as a human rights problem, explanation of vote of the United States of America, Mandate of the Independent Expert on the Effects of Foreign Debt and other Related International Financial Obligations of States on the Full Enjoyment of all Human Rights, particularly Economic, Social and Cultural' 16th session Human Rights Council (23 March 2011). Also see C Lumina 'Chapter 21: Sovereign debt and human rights' in UN Human Rights Office of High Commissioner *Realising the right to development: Essays in commemoration of 25 years of the United Nations Declaration on the Right to Development* (2013) 291.

49 As above.

50 Human Rights Council (n 48).

too technical and outside its scope, including sovereign debt.[51] The same view has also been expressed by the European Union (EU) member states, which opposed United Nations General Assembly (UNGA) Resolution on Draft Principles on Sovereign Debt Restructuring Process partly on the basis that the IMF was a more appropriate forum to deal with the complex issue of SoDR than the UN.[52] Again, this is confirmation of the rejection by developed countries of the classification of sovereign debt as a human rights issue which, if considered as such, would make it well within the mandate of UN organs. The question that may arise is the following: *If this viewpoint is correct, why have other historical efforts at sovereign workouts in what developed countries consider to be the suitable forums, not resulted in better outcomes, especially for citizens of debtor countries?*

Furthermore, not only has the inadequacy of past approaches been noted in this and other studies, but efforts to develop an SDRM at the IMF was opposed for reasons including the fear of a conflict of interest arising from the Fund's dual role as a lender of last resort and administrator of the SDRM. In exploring this, Lumina points out that despite the view by developed countries that different disciplines and institutional setups should tackle the issues of sovereign debt, from a historical perspective there has thus far been no evidence of better outcomes through any other system.[53] Moreover, the position of developed countries is somewhat alarming because, after the 2008 global financial crisis and even now during the COVID-19 pandemic, it became evident that the challenges of debt and human rights affect developed and developing countries alike. By way of illustration, adjustment programmes that formed part of the Greek

51 This was reiterated in the 34th session Human Rights Council 'Explanation of vote of the United States of America on the Rights Council (n 48).
This was reiterated in the 34th session Human Rights Council 'Explanation of vote of the United States of America on the negative impact of non-repatriation of illicit funds on foreign debt as a human rights problem' delivered by William T Mozdzierz (24 March 2017). See 'The United Nations Human Rights Council: Background and policy issues' Congressional Research Service (20 April 2020), https://fas.org/sgp/crs/row/RL33608.pdf (accessed 10 June 2020).

52 Council of European Union 'EU common position on the UN draft resolution on draft basic principles on sovereign debt restructuring process' A/69/L.84 (2 September 2015) 4, http://data.consilium.europa.eu/doc/document/ST-11705-2015-INIT/en/pdf (accessed 20 November 2016).

53 C Lumina 'Chapter 21: Sovereign debt and human rights' in UN Human Rights Office of High Commissioner (2013) (n 48) 291.

SoDR led to a reduction in social spending and, as a result, impacted the realisation of economic, social and cultural rights in Greece.[54]

Concerning the view of the Global South, both a statutory and human rights-centred approach to the governance of SoDR is a more attractive option, as countries in this region are most affected by vulture

54 According to the UN Independent Expert, these austerity measures after 2010 did little to restore debt sustainability, and instead unemployment levels remained at 25%, while poverty levels increased. While some national efforts were made to enhance social security, the UN Independent Expert called for a 'a more holistic approach' which required the allocation of the 'limited available resources to bolster the real economy and close holes in the social security net and in the system of public health care'. UN Human Rights Office of the High Commissioner 'Greek crisis: Human rights should not stop at doors of international institutions, says UN expert' (2 June 2015), https://www.ohchr.org/EN/NewsEvents/Pages/DisplayNews.aspx?NewsID=16032 (accessed 15 May 2016). Civil society organisations have also pointed out the human rights impact on the 2008 financial crisis on European countries. Amnesty International notes the high costs of debt service that Greece payed (up to 45% of the GDP) and its negative impact on its human rights obligations. Also see S Ambast & K Gogou 'Eurozone governments need to recognise that Greece's debt is a human rights issue' (27 June 2018) Amnesty International, https://www.amnesty.org/en/latest/news/2018/06/eurozone-governments-need-to-recognise-that-greeces-debt-is-a-human-rights-issue/ (accessed 19 July 2018). Also see Amnesty International 'Wrongful prescription: The impact of austerity measures on the right to health in Spain' (2018), https://www.amnesty.org/download/Documents/EUR4181362018ENGLISH.PDF (accessed 1 November 2019). Various cases have arisen flowing from the Greek debt crisis at different fora, including at the European Court of Human Rights on the human rights impact on creditors of Greece's SoDR. Of note in this respect is the case of *Mamatas & Others v Greece* which is important because it will instructive to 'similarly-situated Eurozone sovereign in the future'. The case relates to claims made by creditors on the basis of a violation of the right to property (art 1 of the First Added Protocol to the European Convention on Human Rights) and non-discrimination (art 14 of the European Charter of Human Rights). The case related to the haircut imposed on bonds under the Private Sector Involvement (PSI) Agreement amounting to 53,5% of the nominal value and approximately 75% in net present value. This restructuring was imposed through a voting mechanism by legislative amendments for Greek state bonds. Amongst the issues ruled by the Court in *Mamatas*, it acknowledged the restrictions on the right to property on the basis on 'public emergency threatening the life of the nation' as per art 15 of the European Convention on Human Rights. However, the Court did not carry an assessment on what magnitude of debt crisis constitutes a public emergency and the elements that should be considered. In the case of Greece, the restructuring was seen as unavoidable and considered a public emergency. Additionally, the Court found that investors did not have a legitimate expectation to be paid in full at maturity of the bonds as the possibility of restructuring was made known since 2010. *Mamatas & Others v Hellenic Republic,* Greece App 63066/14 64297/14 66106/14 (ECHR, 21 July 2016). Also see LC Buchheit & MG Gulati 'Sovereign debt restructuring in Europe' Global Policy Special Issue: Ten Years after the Global Financial Crisis: Lessons Learned, Opportunities Missed 9 Vol 1 (2018) 68, https://onlinelibrary.wiley.com/doi/epdf/10.1111/1758-5899.12531 (accessed 15 May 2019). Also see S Grund 'Restructuring government debt under local law: The Greek experience and implications for investor protection in Europe' (2017) 12 *Capital Markets Law Journal* 253.

fund litigation, particularly in Africa and Latin America.[55] One explanation for the preferred approach is that the Global South traditionally tends to mostly be debtor countries, and they feel the implications of sovereign debt in already impoverished communities. In addition, the eradication of poverty in African countries has been elusive in part due to the impact of over-indebtedness, and as such the issues of debt and human rights are not easily separated in the African context.

On the link between sovereign debt and human rights, Bohoslavsky and Černič note that while public debt can facilitate human capital development; infrastructure and social services, it can also enable significant human rights violations.[56] This connection between sovereign debt and human rights can be both direct and indirect. In the first instance of a direct connection, sovereign debt can be used to finance human rights violations such as 'funding death squads and death camps'.[57] In the instance that these violations take place where there is a change in government in the debtor country, this may theoretically make a good case for an odious debt argument to justify cancelling the debt.[58] However, even if this is the case, there may be a preference for arguments arising from the more developed sphere of human rights law, than the less developed odious debt jurisprudence. While the term has been used in various contexts, the main argument behind the legal doctrine of 'odious debt' is that 'sovereign debt incurred without the consent of the people and not benefiting the people is odious and should not be transferable to a successor government, especially if creditors are aware of these facts in advance'.[59]

55 The view of the Global South is evident in the statement made on behalf of the Group of 77 and China by JV Bainimaramam, who noted that with the failings of the contractual approach, as evident through vulture fund litigation, a human rights approach is preferred. He also reiterated the requirement of parties in a restructuring process to respect human rights obligations, as set out in the UN Guiding Principles on Foreign Debt and Human Rights. See 'Lessons learned from debt crisis and ongoing work on sovereign debt restructuring and debt resolution mechanism' Special High Level Meeting of ECOSOC, New York (April 2013), http://www.g77.org/statement/getstatement.php?id=130423 (accessed 15 May 2016).

56 Bohoslavsky & Černič (n 37) 1.

57 Bohoslavsky & Černič (n 37) 2.

58 For an overview of the doctrine of odious debt, see CG Paulus 'The concept of "odious debt": A historical survey' (2007) 179 *Duke Law School Legal Studies Paper*; T Wyler 'Wiping the slate: Maintaining capital markets while addressing the odious debt dilemma' (2008) 29 *University of Pennsylvania Journal of International Law* 947; S Ludington, M Gulati & A L. Brophy 'Applied legal history: Demystifying the doctrine of odious debts' (2010) 11 *Theoretical Inquiries in Law* 247; A Khalfan, J King & B Thomas 'Advancing the odious debt doctrine' Centre for International Sustainable Development Law (11 March 2003).

59 Two examples in the SADC region that may potentially be considered odious debt in the SADC region are (i) the debts accrued on behalf of the DRC by Mobutu

There also is an evident link between sovereign debt and the enjoyment of economic, social and cultural rights when the limited resources of the debtor country, which could have been directed to economic, social and cultural or civil and political rights spending, instead are diverted to debt servicing.[60] The indirect link between sovereign debt and human rights may arise where there is a restructuring that results in 'a factual loss of sovereignty over their [the sovereign debtor's] economic and social policies and in the imposition of policies with potentially negative consequences for the protection of social rights'.[61] In this respect, Bantekas and Lumina correctly note that where the interests of lenders influence debt management, a sovereign borrower will reconfigure its 'revenue-generation power ... in such a way to create annual surplus'.[62] This surplus may be generated in a manner that hampers the delivery of social services through, for instance, social spending cuts and the imposition of retrogressive taxes. The relationship between debt and the enjoyment of human rights is not always clear andless clear at times, is the relationship between SoDR and human rights. The following part attempts to connect the dots.

8.4 Connecting the dots: Assessing the interface between debt restructuring and human rights

8.4.1 The impact of sovereign debt restructuring on the enjoyment of human rights

The previous part of this chapter demonstrated the general missing link between human rights and debt in legal discourse. It also established the notion that sovereign debt indeed is a human rights issue. Flowing from that assessment, the task in this part is to focus on the link between human rights and SoDR of privately-held debt. The starting point of this assessment is the notion that the SoDR process broadly impacts the

Seseseko that was used to personally enrich himself; and (ii) the heavily-criticised debts acquired by the apartheid government of South Africa used to oppress the county's black population. However, the odious debt argument was not raised as a defence for non-repayment of debts in both instances, despite the potential of the argument. See M Kremer & S Jayachandran 'Odious debt' IMF Finance and Development Volume 39, Number 2 (June 2002), https://www.imf.org/external/pubs/ft/fandd/2002/06/kremer.htm (accessed 10 April 2021).

60 Lumina (n 48) 293.

61 S Michalowski 'Sovereign debt and social rights: Legal reflections on a difficult relationship' (2008) 8 *Human Rights Law Review* 35, 39. Also see Lumina (n 48) 293.

62 Bantekas & Lumina (n 41) 4.

different stakeholders (both the debtor and private creditors) in the process in different ways.[63]

The human rights impact within the debtor state

SoDR has an impact on the human rights of citizens of a debtor state because a debtor is in a more vulnerable economic position in a debt crisis. During this period, a debtor is made vulnerable by the contractual obligation to service the debt while it faces economic difficulties. Further vulnerability arises because a failure to meet contractual obligations may result in limitations in market access for additional financing, and even where new funding is possible, this may be at an excessively high cost.[64] During this vulnerable time, there is an inevitably high likelihood that human rights will be negatively impacted. This may manifest in two broad ways:

- First, SoDR may have a direct impact on economic, social and cultural rights in the debtor state. This is mainly through the divergence of resources away from economic, social and cultural spending, to debt service. However, during an economic crisis, I do acknowledge that it is possible that the reduced spending on economic, social and cultural is because of the difficult economic situation in the country and because of choices the government makes in response and not necessarily because of debt service directly. The impact may be felt more by vulnerable groups, such as women and children.[65] In this respect, the broad discussion on economic, social and cultural rights and sovereign debt above also finds relevance in the perspective of SoDR.
- Second, concerning multilateral and bilateral debt, in particular, SoDR may come with structural adjustment and austerity programmes that require policy adjustments. Human rights may be negatively impacted by the introduction of austerity or retrogressive measures, which may decrease or restrict access to essential services such as education, healthcare, judicial systems and employment.

The 'competing' rights of private creditors

The current tension in SoDR may be described as 'how to balance the interests of creditors and debtors in ways that ensure states can respect their

63 Bradlow acknowledges the high probability of a negative human rights impact on different actors in the SoDR process and in particular notes the limited focus on sovereign creditors. Bradlow (n 3) 202.

64 Bradlow (n 3) 202.

65 Lumina (n 48) 295.

obligations in the promotion and protection of rights'.[66] In this respect, the use of privately-held debt raises the need to consider the human rights obligations of creditors, as well as the rights that may be affected, which is an issue that is not generally raised as a concern in the context of debt from multilateral and bilateral lenders.[67] As such, a balanced approach requires consideration not only of the rights of the citizens of the debtor that have been impacted, but also a consideration of the human rights impact on private creditors (individual bondholders). Private creditors are mainly institutional and include insurance funds and pension funds. As such behind these institutions sometimes are the savings of individuals such as pensioners. By way of illustration, Argentina's 2001 default directly affected the rights to social security of hundreds of thousands of Argentinian and Italian retirees.

The complexity that arises, however, is that this enquiry requires answering the question of *how the competing human rights of the populations of the debtor and rights of creditors should be balanced.* This question has thus far not been seen as a critical issue during the acquisition of the debt, less so in the restructuring process.

In SoDR, creditors are adversely affected by the financial losses arising from haircuts to the principal or interest rate, as well as from rescheduling and the costs of delays. From the perspective of private creditors, SoDR may be considered as an attack on their property rights. In some cases, depending on the nature of the creditor, the right to social security may also be impacted.[68] Discussions on the impact of SoDR predominantly revolve around the effect on property rights. Although the right to property is contained in neither the International Covenant on Economic, Social and Cultural Rights (ICESCR) nor the International Covenant on Civil and Political Rights (ICCPR), it features in other international instruments.[69]

66 J Rossi 'Sovereign debt restructuring, national development and human rights' (2016) 13 *SUR International Journal on Human Rights* 185, 189.

67 Bradlow (n 3) 202. A major concern for some authors in the literature is what may be perceived as the limited consideration for creditor rights and SoDR. Porzecanski in particular believes that the limited consideration of property and creditor rights 'has led many contemporary human rights advocates down an infertile, if not inappropriate, intellectual and policy path'. See AC Porzecanski 'Human rights and sovereign debts in the context of property and creditor rights' in Bantekas & Lumina (n 33) 66.

68 Argentina's 2001 default by way of illustration directly affected the rights to social security of hundreds of thousands of Argentinian and Italian retirees. See Porzecanski (n 67) 65.

69 See ICESCR adopted by the UN General Assembly on 16 December 1966 by GA Resolution 2200A (XXI), https://treaties.un.org/doc/treaties/1976/01/19760103%20 09-57%20pm/ch_iv_03.pdf (accessed 10 April 2021). See ICCPR adopted by UN

The Universal Declaration of Human Rights (Universal Declaration), for instance, sets out that '[e]veryone has the right to own property alone as well as in association with others' and 'no one shall be arbitrarily deprived of his property'.[70] The right to property is also contained in the African Charter on Human and Peoples' Rights (African Charter) which in article 14 sets out that 'the right to property shall be guaranteed. It may only be encroached upon in the interest of public need or in the general interest of the community and in accordance with the provisions of appropriate laws.[71]

From the wording of the provisions on the right to property above, it is evident that property rights are not absolute and, in some instances, competing public interests may justify interference with the right to property. The property provision in article 14 of the African Charter has been criticised for having the most far-reaching 'claw-back provisions' that gives the state much more leeway to infringe on property rights while leaving room for weaker safeguards.[72] However, Golay and Cismas note that this far-reaching claw-back provision in the African Charter emanates from the continent's colonial past.[73]

In answering the central question of whether the SoDR process violates the property rights of a creditor, Goldmann observes that where creditors have accepted a restructuring package, there is no violation of rights as this process is both consensual and voluntary.[74] The challenge exists when the creditors do not accept a restructuring or when SoDR is unilateral. In this respect, the case of a unilateral default or restructuring,

General Assembly Resolution 2200A (XXI) on 16 December 1966, https://treaties.un.org/doc/publication/unts/volume%20999/volume-999-i-14668-english.pdf (accessed 10 April 2021).

70 See art 17 of UDHR. Further, the International Convention on the Elimination of All Forms of Racial Discrimination (1965) provides for the right to property as it pertains to racial discrimination in art 5(v). Likewise, the Convention on the Rights of Persons with Disabilities A/RES/61/106 (CRPD, 2006) provides for the right to property in the context of disabled persons in both arts 5(3) and 30(3).

71 African Charter on Human and Peoples' Rights adopted by the Organisation of African Union on 27 June 1981, https://www.achpr.org/legalinstruments/detail?id=49 (accessed 10 April 2021).

72 C Golay & I Cismas 'Legal opinion: The right to property from a human rights' International Centre for Human Rights and Democratic Development & Geneva Academy of International Humanitarian Law and Human Rights (2010) 6, https://dspace.stir.ac.uk/bitstream/1893/21703/1/Golay%20and%20Cismas_Working%20Paper_2010.pdf (accessed 15 May 2016).

73 Golay & Cismas (n 72).

74 M Goldmann 'Human rights and sovereign debt workouts' in Bohoslavsky & Černič (n 33) 86.

in which the debtor in effect has repudiated its debt obligations, raises a different human rights concern. I share the view of Goldmann that a unilateral SoDR raises more of a procedural concern (the issue of due process) and not so much a substantive human rights issue –the violation of property rights.[75]

When it comes to private individuals as creditors, the difficulty is that it appears that there is a tug between the rights within the debtor state and those of creditors, which raises the question of who should assume the weight of over-indebtedness. On this tug, Porzecanski expresses his apprehension for what may be seen as a tendency to take the social and economic rights in the debtor more seriously than creditor rights.[76] Porzecanski harshly criticises the human rights approach that prioritises the human rights of the debtor population. In this respect, the main criticism has been on the position of the former UN Independent Expert, Lumina, who noted that '[i]t may be contended that states' responsibility to ensure the enjoyment of basic human rights may take priority over their debt-service obligations, particularly when such payments further limit the ability of states to fulfil their human rights obligations'.[77]

Moreover, Porzecanski finds fault with the view held by the former UN Independent Expert, Bohoslavsky, whose position is that two factors can limit the principle of the sanctity of contracts (*pacta sunt servanda*) – sovereignty and human rights.[78] In this regard, Bohoslavsky notes that 'under certain circumstances, particularly when economic, social and cultural rights [are] at risk, the operation of contract[s] may not be sufficiently compelling to ask the populations of sovereign states to fully repay their debts in a timely manner'.[79] In response to these views held by the former UN Independent Experts, as set out above, Porzecanski describes these as 'provocative opinions' as they 'lack legal justification', and also are 'counterproductive, especially given the increasingly heavier

75 As above.

76 Porzecanski feels that human rights laws are more honoured in the breach than in the observance in most parts of the world, principally because states accepted international standards governing the treatment of their own nationals in their own territory while reserving to themselves the sovereign right to enforce those rights as they saw fit. See Porzecanski (n 67) 66.

77 Lumina (n 77) 293.

78 UN 'Report of the Independent Expert on the Effects of Foreign Debt and other Related International Financial Obligations of States on the Full Enjoyment of all Human Rights, Particularly Economic, Social and Cultural Rights' (A/70/275 4 August 2015), as set out in Porzecanski (n 67) 63.

79 As above.

reliance, even by low-income countries, on funding from private rather than official (bilateral and multilateral) sources of debt finance'.[80]

Porzecanski opines that, in addition, there is a gap in the human rights literature which, despite being extensive even with economic rights, makes little mention of both creditor and property rights. According to Porzecanski this limited treatment stems from his view that human rights instruments from the past five decades have provided little focus on private property and other creditor rights.[81] He consequently highlights the importance of the enforcement of property and creditor rights for the fulfilment of other human rights, particularly economic rights.[82] Additionally, there is a direct link between broad property rights and various other human rights, and in fact these rights are inseparable. The main view here is what Porzecanski sees as the need, at the minimum, for the acknowledgment by human rights practitioners of the interconnectivity and complementarity between creditor rights and other human rights.[83] As such, for Porzecanski the idea of creditors bearing the burden of the SoDR in favour of welfare spending is 'sheer folly' because, according to him, there is not sufficient financial, economic and legal literature to demonstrate that property rights are a major precondition for a nation's evolution and success.[84] The 'folly', in the view of Porzecanski , arises from the fact that (i) some countries have mismanaged their resources after far-reaching debt relief; (ii) the default results in substantial reputational and economic harm; and (iii) the defaults further weaken already weak legal and regulatory institutions and systems to safeguard private investors.[85]

While to me, Porzecanski does raise concerns that are legitimate to an extent, my point of departure, however, is that they also seem to in effect relieve creditors of any responsibility for the crisis in a debtor. *This raises the complex and still unanswered question of accountability of all actors in the debt landscape and how to share this accountability and what it means in terms of a restructuring.*

80 As above.

81 Porzecanski (n 67) 44.

82 As above.

83 Porzecanski (n 67) 65.

84 Creditor protection emanates from both protections provided in statutes and the accompanying core feature of reliable regulatory and judicial systems to ensure good investor protection. Porzecanski (n 67) 63-64.

85 As above.

8.5 The role of human rights considerations in the sovereign debt restructuring discourse

8.5.1 What are the main considerations in the human rights and sovereign debt restructuring discourse?

Today it seems almost unfathomable why sovereign debt issues could be viewed outside of a human rights paradigm because of what appears to be the prominent human rights impact of a debt crisis. Yet, there seems to be an evident disconnect between the developments in the field of human rights and the field of sovereign debt. This is evidence that from the outset the complexity of SoDR arises from the present conceptualisation of the nature of privately-held sovereign debt. On this note, Goldmann opines that this conceptualisation of SoDR 'demonstrates how global governance blurs the distinction between the public and the private'.[86]

What complicates SoDR is that the distinction between public and private indeed is blurred. Goldmann further correctly notes that the blurring of the public/private divide in turn has had actual repercussions for the protection of human rights, as well as for democracy.[87] Concerning human rights in particular, both debt crises and, inevitably, SoDR tend to favour protecting incomes and profits of foreign creditors, over the human rights of debtor populations.[88] A consideration of the broader human rights impact brings into the spotlight the inadequacy of classifying the restructuring of sovereign bonds as a purely commercial activity. I align myself with the view that *(i) sovereign insolvency is among the risks of investment on the part of private creditors; (ii) the current SoDR regime is highly deficient in the protection of sovereign debtors; and (iii) human rights obligations of citizens of the debtor state should generally be a major consideration in restructuring, versus what may be seen as a very strict application of the sanctity of contracts.*

There is an evident link between human rights and SoDR. Nevertheless, not only is the 'human rights first' approach unpopular with adjudication bodies, but it has also been unpopular in some of the legal literature on the subject. In this regard, an argument that has been put forward in the context of bilateral debt is that if sovereign debtors use social spending as

86 M Goldmann 'Public and private authority in a global setting: The example of sovereign debt restructuring' (2018) 25 *Indiana Journal of Global Legal Studies* 331, 347.

87 Goldmann believes that this impact arises due to 'the insistence on the private law character of sovereign debt instruments serves as a tool for entrenching a neoliberal agenda and for discarding important public interests'. Goldmann (n 86) 347.

88 JP Bohoslavsky & K Raffer (eds) *Sovereign debt crisis: What have we learned*? (2017) 277.

a pretext to evade debt repayment, this will amount to a 'forced transfer of resources from the North to the South'.[89] The basis of this position is that creditors are effectively forced to assume the costs of the debtor's human rights obligations to its citizens and their resources are indirectly transferred when debt obligations are not met.[90] Michalowski, however, observes that the correct position whether or not the loan has enriched the debtor is that the divergence of resources to social spending is not a 'transfer' (even indirectly) of the cost of human rights obligations.[91] Instead, a creditor should accept that human rights obligations trump debt repayment due to the 'overriding importance of human rights'.[92]

8.5.2 What is the treatment of human rights in sovereign debt restructuring standards?

Various human rights soft law instruments have attempted to link human rights and sovereign debt. In 2012 the *United Nations Conference on Trade and Development* (UNCTAD) developed Principles on Promoting Responsible Sovereign Lending and Borrowing.[93] The Principles are relevant to SoDR as they provide that 'lenders should be willing to engage in good faith discussions with the debtor and other creditors' in response to distress.[94] In the event that a SoDR occurs, it should occur 'promptly, efficiently and fairly'.[95] While there is no reference to human rights obligations, it may questionably be inferred that a fair SoDR process is one that takes a balanced approach and not only takes into account human rights obligations but also makes use of shared responsibility. This, however, is not a view shared by all actors in the SoDR process.

Human rights obligations have not been reflected in standards developed by the Institute for International Finance (IIF), for instance. The IIF describes itself as a global association of the financial industry, and its membership includes approximately 450 financial institutions. Consequently, the IIF can be said to represent the views of private

89 Michalowski (n 61) 48.

90 As above.

91 As above.

92 As above.

93 UNCTAD 'Consolidated Principles on Promoting Responsible Sovereign Lending and Borrowing' (10 January 2012), https://unctad.org/en/PublicationsLibrary/gdsddf2012misc1_en.pdf (accessed 11 June 2017).

94 Principle 7 of the Principles on Promoting Responsible Sovereign Lending and Borrowing (n 93).

95 Principle 15 of the Principles on Promoting Responsible Sovereign Lending and Borrowing (n 93).

creditors. In October 2012 the IIF's Principles for Stable Capital Flows and Fair Debt Restructuring in Emerging Markets (Capital Flows Principles) were published.[96] The Capital Flows Principles generally provided for transparency during restructuring (disclosure practice), cooperation between debtors and creditors to avoid SoDR, good faith and fair treatment.[97] However, they made no mention of any human rights obligations in lending activities. In fact, Bradlow notes that instead they 'do not suggest that the creditors have any responsibility to take the likely impact of their actions on these citizens into account in their negotiating and decision-making process'.[98]

In 2012 the UN Independent Expert developed the UN Human Rights Council Guiding Principles on Sovereign Debt and Human Rights (UNHRC Guiding Principles).[99] This soft law instrument requires that lending and borrowing activities refrain from impacting sovereign human rights obligations (Principle 6), and that '[a]ny foreign debt strategy must be designed not to hamper the improvement of conditions guaranteeing the enjoyment of human rights and must be directed, inter alia, to ensuring that debtor states achieve an adequate level of growth to meet their social and economic needs and their development requirements, as well as fulfilment of their human rights obligations'.[100]

The HRC Guiding Principles, however, make no mention of other norms or standards that are relevant to the SoDR process, neither is there a cross-reference to ith the UN Guiding Principles on Business and Human Rights (UNGPs) which is among the leading instruments bridging human rights and business.[101]

96 IIF 'Principles for Stable Capital Flows and Fair Debt Restructuring in Emerging Market' (14 October 2012), https://www.iif.com/Portals/0/Files/content/Regulatory/The%20Principles%20and%20Addendum.pdf (accessed 10 May 2016).

97 Principles for Stable Capital Flows and Fair Debt Restructuring in Emerging Market (n 96).

98 Bradlow (n 3) 211. Similarly, the 2013 report on the Capital Flows Principles make no mention of human rights obligations. See IIF 'Principles for Stable Capital Flows and Fair Debt Restructuring: Report on Implementation by the Principles Consultative Group with Comprehensive Update on Investor Relations Programmes and Data Transparency' (October 2013), https://www.iif.com/portals/0/files/private/2013_IIF_PCG_Report_3.pdf (accessed 10 May 2016).

99 See Annex to the 'Guiding Principles on Foreign Debt and Human Rights' Report of the Independent Expert on the effects of foreign debt and other related international financial obligations of States on the full enjoyment of all human rights, particularly economic, social and cultural rights C Lumina A/HRC/20/23 (10 April 2011), https://undocs.org/en/A/HRC/20/23 (accessed 10 May 2016).

100 See 'Guiding Principles on Foreign Debt and Human Rights' (n 99) Principle 8.

101 Bradlow in his article 'Can parallel lines ever meet? The strange case of the

More recently the UNGA has acknowledged the need for clear principles on 'the management and resolution of financial crises that take into account the obligation of sovereign debtors and their creditors to act in good faith and with a cooperative spirit to reach a consensual rearrangement of the debt of sovereign states'.[102] To fill the normative gap, on 10 September 2015 the UNGA adopted UNGA Resolution 319/69 on Basic Principles on Sovereign Debt Restructuring Processes.[103] The nine basic principles – the right to restructure debt, good faith, transparency, impartiality, equitable treatment, sovereign immunity, legitimacy, sustainability, major restructuring – are intended to be the pillars upon which a multilateral framework is to be established as per UNGA Resolution 69/247.[104] UNGA Resolution 319/69 is a voluntary set of principles. However, some consider them as legally binding because they are seen as a representation of customary law and/or general principles of international law.[105] However, their human rights implications are yet to be determined as there seems to be a weak link expressed.[106]

There is an evident need to consider further developing the normative framework, and the nine basic principles on SoDR have enhanced the normative framework of SoDR, in addition to other voluntary principles and norms. The human rights dimension finds relevance when it comes to the principle of sustainability. The principle of sustainability has shifted the concept of successes in SoDR to go beyond a process which was conducted in a timely and efficient manner, and that stabilised debt levels. A successful SoDR is now also perceived to include a process that

international standards on sovereign debt and business and human rights' questions the developments of soft law principles in the field of human rights and business and explores whether the same can be of use on the subject of SoDR. In addition to the lack of express reference to the UNGPs, Bradlow further finds it peculiar that even the UNCTAD roadmap does not make reference to the UNGPs. Bradlow (n 3) 213-214.

102 UNGA Resolution 'Basic Principles on Sovereign Debt Restructuring Processes' UNGA Resolution A/69/L.84 (2015).

103 As above.

104 For an elaboration of the parameters of each principle, see 'South Africa: Draft Resolution Basic Principles on Sovereign Debt Restructuring Processes' 69 Session of UNGA Session A/69/L.84 (29 July 2015), https://unctad.org/meetings/en/SessionalDocuments/a69L84_en.pdf (accessed 14 May 2016). For a discussion of the principles, also see the discussion by SP Ng'ambi in ch 11 'Sovereign debt: A case study of Zambia'.

105 JP Bohoslavsky 'Why the Addis debt chapter falls short UN Research Institute for Social Development' (15 September 2015), http://www.unrisd.org/road-to-addis-bohoslavsky (accessed 16 May 2019). Also see art 38 of the Rules of the International Court of Justice (adopted on 14 April 1978 and entered into force on 1 July 1978), https://www.icj-cij.org/en/rules (accessed 15 May 2016).

106 Bohoslavsky (n 105).

preserves 'at the outset creditors' rights while promoting sustained and inclusive economic growth and sustainable development, minimising economic and social costs, warranting the stability of the international financial system and respecting human rights'.[107] As a result, the human rights implication of the principle of debt sustainability still is not clear. In fact, while this study sees the Basic Principles as a significant and positive development, human rights treatment still leaves questions.

8.6 Conclusion: SoDR reform requires a human rights-based approach

Flowing from the above-mentioned argument that there is a gap in the human rights treatment of SoDR, this chapter concludes that a significant component to a 'successful' SoDR is the process that preserves 'at the outset creditors' rights while promoting sustained and inclusive economic growth and sustainable development, minimising economic and social costs, warranting the stability of the international financial system and respecting human rights'.[108] As such, the question, therefore, is how to reform SoDR in a manner that both leads to efficiency gains and stabilised debt while also taking into account the human cost and development concerns. In this respect, transforming SoDR as we know it requires developing, among other things, a human rights-based approach (HRBA).

A human rights approach requires the consideration of human rights concerns from the outset. In this respect, a key feature could be the incorporation of human rights in the definition and shared understanding of 'debt sustainability'. Beyond this initial inclusion of human rights considerations, similar considerations should also be made in the SoDR process, including:

(1) Promoting the enjoyment of fundamental human rights by invoking existing human rights obligations in current human rights instruments and their enforcement in SoDR.

A rights-based approach to SoDR is one that will result in normatively basing SoDR on international human rights standards. In particular, the HRBA 'integrates the norms, standards and principles of the international human rights system into the plans, policies and processes of development.

107 Sedlak points out that 'any procedure that focuses on the conflict between the debtor and the creditor will marginalise the interests of the "community" and potentially exacerbate the very problems that caused the sovereign to default in the first place'. Sedlak (n 4) 1514. Also see UNGA Resolution 'Basic Principles on Sovereign Debt Restructuring Processes' (n 102).

108 As above.

The norms and standards are those contained in the wealth of international instruments.'[109]

(2) Developing human rights impact assessment tools and their incorporation in the SoDR process

There is a need for the consistent use of human rights impact assessment tools throughout the lending life cycle. In fact, in 2019 the UN Independent Expert developed the Guiding Principles on Human Rights Impact Assessments of Economic Reforms. Notably, among these, Principle 12 on 'Debt sustainability, debt relief and restructuring' sets out that '[i]ndependent debt sustainability analysis should incorporate human rights impact assessments. Findings of human rights impact assessments should be used to inform debt strategies, debt relief programmes and restructuring negotiations, potentially triggering the latter where actual or potential adverse impacts are identified. Debt audits can contribute valuable information in conducting such assessments.'[110]

(3) Stakeholder engagement and participation, including civil society participation in SoDR

The threats arising from default or even debt distress is even more evident in countries that lack checks and balances such as effective stakeholder engagement and participation, transparency in the law-making processes and institutional mechanisms that hold people accountable. Participation is an integral aspect of a human rights-based approach to SoDR. There is a need for proper engagement and participation in the restructuring debate and the restructuring and dispute resolution process. While the idea of participation in SoDR is not novel, it has fallen into the background. Nevertheless, a HRBA requires the participation of and engagement with citizens, civil society organisations and other stakeholders.

Lessons may be learnt from institutional structures of other organisations such as the International Labour Organisation (ILO) which has gone beyond collaborating with non-governmental organisations (NGOs) and other non-state actors to incorporating them in their institutional framework, by giving NGOs that meet a predetermined criterion a 'consultative status', and not only collaborating with international, regional, national and local NGOs but also integrating them into the structure of the ILO.[111] A similar

109 S Gruskin et al (eds) *Perspectives on health and human rights* (2005) 102.

110 'Guiding principles on human rights impact assessments of economic reforms' Report of the Independent Expert on the effects of foreign debt and other related international financial obligations of States on the full enjoyment of human rights, particularly economic, social and cultural rights, Human Rights Council Fortieth session (25 February-22 March 2019) 13, https://undocs.org/A/HRC/40/57 (accessed 10 April 2019).

111 International Labour Organisation 'Relations with NGOs', https://www.ilo.org/

approach may be incorporated into SoDR if a novel mechanism and a new institutional framework for SoDR are pursued. A new mechanism could go beyond the mere collaboration with NGOs and other non-state actors to actually integrating them in the ILO's institutional framework.

African countries ought to determine and contribute to the approaches that respond to debt-related issues and to design a future for the continent. In line with this view, the development of African regional solutions to SoDR is of value. In an effort to find institutional solutions, regional bodies such as the SADC may potentially be used to create venues and environments for proactive and early dialogue between different stakeholders as sovereign debt challenges arise within the SADC region. Early and ongoing dialogue will reduce the stigma associated with debt distress, which in turn will foster an environment with early and open engagement and a sense of ownership of a restructuring plan by both debtors and creditors. Regional bodies may potentially play a role in this. In conclusion, for African countries there is the need for a system that adequately reflects the developmental, human rights and environmental aspirations of the continent.

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9 Adopting proactive debt management policy strategies to forestall a debt crisis in South Africa

*Marie-Louise F Aren**

9.1 Introduction

South Africa[1] could be heading towards a sovereign debt crisis of huge magnitude if certain decisive actions are not taken to manage rising debt levels. As a result of the national lockdown restrictions, aimed at containing the spread of the COVID-19 pandemic, gross domestic product (GDP) growth per capita[2] moved from 0,2 per cent in 2019 to – 8,3 per cent in 2020. However, it has increased to 1,6 per cent in 2021, owing to the ease of lockdown restrictions. Real GDP per capita (per cent change from previous period) is projected at 0,4 per cent in 2022.[3] In addition, the government's budget deficit and maturing loans increased from ZAR432,7 billion in 2019/2020 to ZAR670,3 billion in 2020/2021. Net government debt figures[4] expected to increase from ZAR3,66 trillion, about 74, 3 per cent of GDP, in 2020/2021 to ZAR5,09 trillion, about 84,9 per cent of GDP in 2023/2024.[5] This does not present a bright economic outlook. Minister Tito Mboweni aptly captures the situation in his supplementary budget speech:[6]

* I wish to express my gratitude to Prof DD Bradlow who gave me the golden opportunity to write on this important topic and to Dr M Masamba who provided support and feedback. Special thanks go to the editor, reviewers, publisher and the International Development Law Unit staff members, Centre for Human Rights, University of Pretoria.

1 'A borrowers' catch-22 African governments face a wall of debt repayments' *The Economist* (6 June 2020), https://www.economist.com/middle-east-and-africa/2020/04/11/africas-debt-crisis-hampers-its-fight-against-covid-19 (accessed 15 October 2020).

2 As percentage change from previous period. See https://data.imf.org/?sk=5778F645-51FB-4F37-A775-B8FECD6BC69B&sId=1461703256968 (accessed 9 June 2021).

3 As above.

4 Gross loan debt less cash balances.

5 Department of National Treasury Republic of South Africa Budget Review 2021 80.

6 Supplementary Budget Speech 2020, https://www.gov.za/speeches/minister-tito-mboweni-2020-supplementary-budget-speech-24-jun-2020-0000 (accessed 15 October 2020).

> We have many strengths. These include our young and ambitious people; our institutions, a robust and vibrant democracy, independent judiciary and our commitment to social justice progress; and our economic strengths: a diverse industrial base, a flexible exchange rate, stable inflation, and deep domestic capital markets that allow us to borrow mainly in rand. But debt is our weakness. We have accumulated far too much debt; this downturn will add more. This year, out of every rand that we pay in tax, 21 cents goes to paying the interest on our past debts. This indebtedness condemns us to ever higher interest rates. If we reduce debt, we will reduce interest rates for everyone, and we will unleash investment and growth. So today, with an eye on the future, we set out a strategy to build a bridge to recovery. Our Herculean task is to close the mouth of the hippopotamus! It is eating our children's inheritance. We need to stop it now! Our Herculean task is to stabilise debt.

Leaving this rising debt unattended may give rise to hyperinflation such as that experienced in other countries such as Zimbabwe in the early 2000s.[7] South Africa's budget deficit has already been revised to 14 per cent of GDP in 2020/21 in response to the spending demands and economic pressures of the COVID-19 pandemic.[8] Also, reduced tax revenue in the early parts of the pandemic contributed to a relatively high budget deficit arising from limited economic activities from which taxes are generated and a retraction of the previously-announced tax increases of ZAR40 billion.[9] A decline in government revenue and economic activities affects the unemployment rate. South Africa's unemployment rate is at 32,6 per cent in the first quarter of 2021 compared to 30,1 per cent in the first quarter of 2020, with a year-on-year percentage change of 2,5 per cent.[10]

The response to the crisis has been to access new sources of funding. The International Monetary Fund (IMF) in July 2020 approved over ZAR70 billion emergency loan[11] from the rapid financing instrument. In addition to this, the African Development Bank (AfDB)[12] and the

7 Zimbabwe's monthly inflation rate reached the 50% mark in February 1999 and gradually increased, reaching its peak at 2200,2% in March 2007. See A Makochekanwa 'A dynamic enquiry into the causes of hyperinflation in Zimbabwe' (2007) 10 University of Pretoria Department of Economics Working Paper 12 4.

8 Budget Review (n 5) 1-2. Tax revenue was R213,2 billion lower than projected in the 2020 budget.

9 As above.

10 Statistics South Africa Quarterly Labour Force Survey Report Quarter 1 2021 13.

11 SABC News 'IMF grants SA more than R70 billion loan to mitigate COVID-19 impact' (27 July 2020), https://www.sabcnews.com/sabcnews/imf-grants-sa-more-than-r70-billion-loan-to-mitigate-covid-19-impact/ (accessed 15 October 2020).

12 'South Africa: African Development Bank approves first ever crisis response budget support of R5 billion to fight COVID-19' *AfDB News* (22 July 2020).

New Development Bank approved emergency loans of US $1 billion to South Africa to tackle the socio-economic impacts of the COVID-19 pandemic.[13] Altogether, South Africa has borrowed over ZAR80 billion more to its already enormous debt and recessed economy.[14] There is scepticism from some political parties[15] such as the Democratic Alliance, who have expressed some reservation about government IMF COVID-19 relief funds. There is doubt that the emergency funds may end up being poorly managed, which could end up affecting South Africa's economic independence, especially if a default in payment occurs.[16] This fear is strongly held because of the IMF's previous track record of conditionalities that have resulted in restrictive monetary and fiscal policies especially in developing countries, with an accompanying negative impact on growth and social spending.[17]

9.2 The growth of sovereign debt post-1994 in South Africa

South Africa's government debt stands at 77 per cent of the nominal GDP in June 2020,[18] compared to about 62 per cent of its GDP in 2019.[19] It is expected to rise to 80 per cent and 84 per cent for 2021 and 2022 respectively.[20] At this stage, it is important to delve back to the post-

13 Reuters News 'New development bank provides South Africa with $1 billion COVID-19 loan' (June 2020), https://www.reuters.com/article/us-health-coronavirus-safrica-ndb-idUSKBN23R09I (accessed 15 October 2020).

14 Statistics for Business February 2020 report 3, http://www.statssa.gov.za/?p=13062 (accessed 15 October 2020).

15 N Mokobo 'Political parties concerned about impact of IMF loan on SA's sovereignty' *SABC News* (28 July 2020), https://www.sabcnews.com/sabcnews/political-parties-concerned-about-impact-of-imf-loan-on-sas-sovereignty/ (accessed 6 June 2021).

16 E Naki 'Fears over IMF loan conditions' *The Citizen Online* (7 August 2020), https://citizen.co.za/news/south-africa/government/2336932/fears-over-imf-loan-conditions/ (accessed 15 October 2020).

17 A Buira 'An analysis of IMF conditionality' (2002) 104 Oxford University Department of Economics Discussion Paper, https://ora.ox.ac.uk/objects/uuid:de9f4d70-c402-42aa-8031-032b89ec0a7b/download_file?file_format=pdf&safe_filename=JOURNAL&type_of_work=Working+paper (accessed 20 December 2020).

18 'South Africa government debt: % of GDP 1960 – 2020' Quarterly CEIC Quarterly Data (September 2020), https://www.ceicdata.com/en/indicator/south-africa/government-debt--of-nominal-gdp#:~:text=South%20Africa's%20Government%20debt%20accounted,63.3%20%25%20in%20the%20previous%20quarter (accessed 15 October 2020).

19 Budget Review of South Africa (2020) 10.

20 As above. Compare with projection at 91% of GDP including debt owed to state-owned enterprises. See 'Moody's downgrades South Africa's ratings to Ba1, maintains negative outlook' Moody Rating Action (27 March 2020), https://www.moodys.com/research/Moodys-downgrades-South-Africas-ratings-to-Ba1-maintains-negative-

democratic history to follow the evolution of South Africa's debt to its present figures, to finding a way out of this quagmire.

From the late apartheid era, it is believed that macro-economic policy and monetarism contributed to the debt build-up,[21] and continued into the post-apartheid era.[22] With the end of the former apartheid regime, the democratic government inherited a large public debt of over US $13 billion, mainly from widespread borrowing and a foreign debt standstill imposed against South Africa.[23] A tight monetary policy was adopted, premised on the belief that a coherent, strict, and effective monetary and fiscal policies will be a basis of the reconstruction and development programme (RDP).[24] Public debt rose to above 48 per cent in 1995. From 1996 the government took measures that prevented further increases in the debt level and by 2000 had reduced the debt level as a percentage of GDP to about 44 per cent.[25]

Debt repayments required under the 1986 plan continued. This is because economists believed that reneging on the debt by declaring it an odious debt[26] would affect the country's credit outlook,[27] especially by rating agencies such as Standards and Poors and Moody. South Africa

outlook--PR_420630 (accessed 17 October 2020). See also Statista 'South Africa: National debt in relation to gross domestic product (GDP) from 2016 to 2026' Data, https://www.statista.com/statistics/578887/national-debt-of-south-africa-in-relation-to-gross-domestic-product-gdp/ (accessed 14 June 2021).

21 A result of the high-interest, tight-money policies to maintain the value of the rand and keep interest rate low. See C Stals 'South African exchange rate policy: A Reserve Bank perspective' in PH Baker (ed) *South Africa and the World Economy in the 1990s* (1993) 148.

22 C Bassett 'The spectre of debt in South Africa' (2008) 41 *Labour, Capital and Society/ Travail, Capital Et Société* 70.

23 N Mhlaba & A Phiri 'Is public debt harmful towards economic growth? New evidence from South Africa' (2019) 7 *Cogent Economics and Finance* 3. See also 'Apartheid debt resettled' *Fin24 Online* (3 September 2001), https://www.news24.com/Fin24/ Apartheid-debt-settled-20010903 (accessed 12 June 2021).

24 G Gotz 'Shoot anything that flies, claim anything that falls' in G Adler & E Webster (eds) *Trade unions and democratisation in South Africa*, *1985-1997* (2000) 172-173.

25 By cutting on public spending. See South African Reserve Bank Statistical Tables, Public Finance 1997 69, https://www.resbank.co.za/content/dam/sarb/publications/ quarterly-bulletins/quarterly-bulletin-publications/1997/4752/Statistical-tables---Public-finance.pdf (accessed 13 June 2021). See also World Bank Central Government Debt Total (% of GDP) South Africa, https://data.worldbank.org/indicator/ GC.DOD.TOTL.GD.ZS?view=chart&locations= (accessed 13 June 2021).

26 Many activists suggested this route. See J Rubin 'Challenging apartheid's foreign debt', http://probeinternational.org/library/wp-content/uploads/2011/02/RUBIN.pdf (accessed 27 April 2021).

27 Fin 24 'Apartheid debt settled' (3 September 2001), https://www.news24.com/Fin24/ apartheid-debt-settled-20010903 (accessed 27 April 2021).

was also wary of a financial imbalance that could produce a debt crisis and compromise its sovereignty with an adverse effect on its economy.[28] Eventually, South Africa repaid the affected debt in full in August 2001 and the debt standstill regulations were repealed in November 2001.[29]

From 2002 to 2004, South Africa committed to a moderately expansionary fiscal regime, beginning roughly with the 2002-2003 government budget.[30] There was more spending on social and capital infrastructure and tax cuts, especially for small businesses.[31] The years 2002 to 2007 were good years.[32]

Arising from a period of prudent fiscal policy management, South Africa used the considerable fiscal space it had created from years of running a budget surplus to carry out strong government spending. Government surpluses and low deficits helped to bring the debt level down, to less than 24 per cent in 2008.[33] Sadly, the global financial crisis of 2008 to 2009 happened, and an economic recession soon followed. The recession led to a fall in tax collection from businesses, contributing to a reduction in government revenue. Spending continued,[34] however, and in time overtook revenue, causing the fiscal balance to turn to a deficit. The discrepancy between spending and revenue was financed by the accumulation of public debt from the capital markets causing South Africa's public debt level to escalate to 43,9 per cent of GDP by 2014.[35]

From 2014 onward, following the downgrading of South Africa's sovereign risk rating and the fiscal response it prompted, the fall in world

28 African National Congress 'Forward to a democratic economy' (1990) Discussion Document, Department of Economic Planning 13. See also Bassett (n 22) 77-79.

29 VB Shayanewako 'The impact of foreign debt on economic growth in South Africa' MComm dissertation, University of Fort Hare, 2013 10, 11.

30 AfDB/OECD 'African economic outlook' (2003) 283.

31 Bassett (n 22) 79. It was the Reserve Bank's policy commitments that kept the interest rates high to maintain the value of the rand that contributed substantially to the debt build-up.

32 L Kganyago 'Fiscal policy, public debt management and government bond markets: Issues for central banks' (2012) 67 BIS Paper 315. Until 2008 South Africa operated a budget surplus and prudent fiscal policy.

33 M Schoeman & K Creamer 'Public debt in post-crisis South Africa' (2015) 1-3, http://2015.essa.org.za/fullpaper/essa_2813.pdf (accessed 18 October 2020).

34 This continued because of the pre-recession spending obligations of the government related to the economic recovery plan. See Oxford Business Group South Africa Economy Outlook 'External factors challenge South Africa's record of strong economic growth', https://oxfordbusinessgroup.com/overview/mixed-review-external-factors-are-making-challenging-period (accessed 28 April 2021).

35 South African Reserve Bank 2014.

commodity prices, the severe recession hitting some of the country's trading partners, uncertain government policies, structural challenges, and the impact of state capture and corruption,[36] created negative GDP growth, causing massive job losses, and increasing the strain on public finances.[37] Deficit financing continued to increase moderately over the next few years, from 43, 9 per cent of GDP in 2014 to 62, 2 per cent of GDP in 2019.

In 2020 the COVID-19 pandemic forced the government to increase its debt with debt financing, to mitigate the effect of the COVID-19 pandemic control measures, such as the national lockdown on the economy. This is in addition to a tax revenue underperformance and an increasing expenditure from fund allocations for containing the COVID-19 effect. The result is a further increase in the debt to GDP figures. Moody estimates that the debt burden will reach 91 per cent of GDP by fiscal year 2023, inclusive of the guarantees to state-owned enterprises (SOEs).[38]

9.3 Implication of rising debt for South Africa

In a study investigating the dynamic relationship between accumulated public debt ratio and real GDP growth in the South African economy over the period from 1980 to 2014, it was concluded that the estimated threshold level that makes the positive correlation between public debt and growth turns negative at 31,37 per cent and above.[39] Against this backdrop, the implication of South Africa's rising debt profile is glaring.

9.3.1 Very high debt levels are accompanied by stiffer austerity budgets

Austerity measures are adopted when governments need to aggressively reduce their budget deficits. In emerging markets, it has been shown that the government starts implementing austerity measures when the debt to

36 J Rossouw & F Joubert 'Warnings about SA's push towards the fiscal cliff went unheeded for years' *Business Day online* (3 September 2020), https://www.businesslive.co.za/bd/opinion/2020-09-06-warnings-about-sas-push-towards-the-fiscal-cliff-went-unheeded-for-years/ (accessed 29 April 2021).

37 Schoeman & Creamer (n 33) 2.

38 M Mkhabela 'South African debt burden will reach 90% of GDP by 2021' IOL Business Report Opinion/ (27 April 2020), https://www.iol.co.za/business-report/opinion/south-african-debt-burden-will-reach-90-of-gdp-by-202 47236765#:~:text=South%20Africa%20recorded%20a%20government,the%20end%20of%20fiscal%202019. (accessed 18 October 2020).

39 Y Baaziz et al 'Does public debt matter for economic growth? Evidence from South Africa' (2015) 31 *Journal of Applied Business Research* 2187, 2194.

GDP ratio exceeds 64 per cent.[40] Austerity budgeting is commonly adopted to show fiscal discipline, especially when creditors become concerned that sovereign states are likely to default on their debts. Austerity measures are implemented through spending cuts, regressive tax increases, or both.

South Africa has gradually adopted austerity measures in response to rising debt levels over the years despite its commitment to the counter-cyclical policies in the 2014-2019 Medium Term Strategic Framework (MTSF). This is evidenced, for example, by the increase in the value-added tax (VAT) rate from 14 to 15 per cent as of April 2018[41] and the steady declining spending allocation per learner in real terms from ZAR17 822 in 2010 to ZAR16 435 in 2017.[42] The presence of austerity budgets has been justified by national treasury to curtail debt levels even though there is strong evidence that austerity fails to achieve this objective.[43] Given South Africa's historical economic injustices of the past and the widening global inequality trends, introducing austerity measures and social spending cuts may delay the emergence of a strong state, capable of meeting its developmental objectives. For example, in the education sector there have been reports on the declining quality of education from learner spending cuts.[44] In 2021 there is more allocation to economic development, but some of the key components of economic development have received cuts as well. For instance, industrialization and exports expenditure allocation is ZAR 36 billion.[45] This is about ZAR 3 billion less than the 2020 budget expenditure allocation of ZAR 39 billion. In contrast, debt service cost rose from ZAR 229 billion to ZAR 269 billion, with a ZAR 40 billion difference.[46] This implies that reducing productive spending in key sectors of the economy or key sub-divisions within a sector does not necessarily translate into reduced debt levels or debt servicing costs.

Studies on Greece show the negative effect from the imposition of austerity. Due to the austerity measures imposed in Greece, public employees' wages reduced by 17 per cent, followed by a reduction in

40 T Grennes 'Finding the tipping point: When sovereign debt turns bad' (2010) WBG Policy Research Working Papers.

41 National Treasury of the Republic of South Africa, Budget Review 2019.

42 B Sibeko 'The cost of austerity: Lessons for South Africa' (2019) 2 Institute for Economic Justice Working Paper Series 29.

43 As above.

44 National Treasury of the Republic of South Africa Budget Review 2019. Eg, learner spending fell by 8% in real terms from R17 822 in 2010 to R16 435 in 2017. See also Sibeko (n 42).

45 National Treasury of the Republic of South Africa Budget Review 2020 and National Treasury of the Republic of South Africa Budget Review 2021.

46 As above.

pension benefits. By 2012 Greece's debt-to-GDP ratio had increased to 175 per cent, one of the highest in the world.[47] Despite Greece implementing one of the most extensive fiscal consolidation programmes, Greece continued to experience a prolonged recession.

In the case of Zambia, austerity measures introduced in 1991 resulted in drastic cuts in Zambia's budget allocations for education, health and social welfare. This is because interest payments on debt accounted for over 50 per cent of government spending in 1991,[48] making it difficult for the Zambian government to spend on its citizens' welfare.

9.3.2 Unchecked rising debt profile affects credit ratings and consequently foreign investment levels

With increasing debt levels, the South African state stands to witness a further deterioration in its credit rating. Although most of South Africa's sovereign debt is denominated in Rands and protects the fiscus from currency exchange fluctuations, especially from trade imbalances, this does not reduce rising borrowing costs which increases debt level. This is because long-term domestic bonds attract higher interest rates on repayment and contributes to debt costs, in addition to a slow growing economy, as seen from the GDP projections and reduced tax income to buffer the rising debt cost. This is an unsustainable debt position to be in and presents a huge risk to South Africa's investment-grade credit ratings.

In January 2020 foreign holding of domestic bonds was at 37 per cent. However, owing to the Moody assessment downgrade from Baa3 to Ba1, foreign investors reacted to the downgrade by disinvesting out of the domestic bond market to the tune of ZAR 54 billion bringing foreign bond holding of domestic bonds to 30 per cent in July 2020.[49]

For 2021, the outlook on South Africa's rating is quite negative even though there are prospects for growth. While S&P maintains a stable outlook on South Africa, Fitch sovereign credit rating (SCR) outlook remains quite gloomy as Fitch bases its SCR at 'BB' status on South Africa's rising government debt, low economic growth and high level

47 Sibeko (n 42).

48 MS Grindle *Challenging the state: Crisis and innovation in Latin America and Africa* (1996) 25.

49 Bloomberg 'Foreign investors lose interest in South African bonds' *Business Tech* (4 August 2020), https://businesstech.co.za/news/finance/422616/foreign-investors-lose-interest-in-south-african-bonds/ (accessed 14 June 2021).

of inequality that could affect consolidation efforts.[50] This presents a challenge to the stabilisation of debt level because sovereign credit ratings influence foreign investors' investment decisions.[51] South Africa's reduced SCR could signal to investors the high-risk potential of investing in the domestic bond market, which could lead to reduced foreign investment inflow into South Africa and act as a setback to economic recovery in COVID-19 times.

Furthermore, unchecked debt levels may lure the government into seeking more foreign loans/credit than it can sustainably manage and gain positive returns on. According to Devarajan et al,[52] rising sovereign debt profiles may result in increased pressure from foreign creditors and international financial institutions (IFIs) on a debtor country to honour its debt repayments or carry out reforms to ensure reliable debt servicing. In addition, the promise of the provision of future credit on domestic structural reform could be used by IFIs and foreign investors to influence reforms that conflict with a country's developmental plans.

9.3.3 Increasing level of state capture, corruption, and interest rates

A high-level accumulation of public debt may provide fertile ground for increased corruption in a nation. This is due to a distortionary effect of the misallocation of resources in unproductive spending with little growth effect on the economy, such as national defence spending.[53] Increased corruption also increases public debt in a vicious cycle, creating a shadow economy that affects the ability of the government to raise taxes. This in turn leads to more borrowing to be used in financing bribes (in addition to tax revenues raised).[54] Poorly-managed debt levels in South Africa are likely to have a negative impact on the sincere fight against state capture and increase corruption levels, creating a vicious cycle of higher debts levels and undelivered developmental goals.

50 S Naidoo 'S&P and Fitch affirm SA's sovereign credit rating and outlooks' (21 May 2021) Money Web Budget, https://www.moneyweb.co.za/news/economy/sp-and-fitch-affirm-sas-sovereign-credit-rating-and-outlooks/ (accessed 14 June 2021).

51 G Kaminsky & SL Schmukler 'Emerging market instability: Do sovereign ratings affect country risk and stock returns?' (2002) 16 *The World Bank Economic Review* 171.

52 S Deverajan, D Dollar & T Holmgren *Aid and reform in Africa* (2001) 21.

53 E Kim, Y Ha & S Kim 'Public debt, corruption and sustainable economic growth' (2017) *MDPI Journal* 4, file:///C:/Users/Marie-Louise/Downloads/Public_Debt_Corruption_and_Sustainable_Economic_Gr.pdf (accessed 20 December 2020).

54 D Kaufmann, A Kraay & M Mastruzzi *World governance indicators project* (2013).

Unchecked government debt from large private sector borrowing for unproductive purposes poses another problem, especially when foreign debt holders decide to sell bonds. There might be difficulties in obtaining buyers willing to take a risk to hold government bonds when debt levels are very high. This could cause interest rates to rise sharply, push the government budget further into deficit and tilt the economy further into recession. An economy operating on a budget deficit causes interest rates to rise. This will be seen through a high inflation, and a stagnant local and regional market. The overall implication is that very high external debt levels may lead to economic inertia and growth depression, according to Schclarek,[55] especially in developing countries, due to a spill-over effect from the private sector hit by the high cost of debt. This in turn undermines foreign investor confidence and stalls the possibility of equity funds injection into the economy leading to more depression.

COVID-19 debt is a unique situation. This is because it comes from a sudden global pandemic, unlike the global financial crisis of 2008. The final part of this chapter provides some recommendations on the way forward.

9.4 Policy recommendations

The necessity of taking proactive steps and corrective policy measures to stabilise sovereign debt cannot be overemphasised. Debt, while useful in an economy, depends on prudent management to deliver its benefits. South Africa's rising debt profile, though disturbing, should not be used as a justification for hastily-reactive fiscal decisions. To this end, the debt management approaches adopted in this chapter would be centred on two major themes – closing the drainage channels and charting new courses.

9.4.1 Replace austerity budgeting with inclusive GDP growth spending

Austerity policies are expected to free up resources not only to meet debt obligations, but can be used to promote a growing economy. However, empirical evidence shows that this does not always happen. Instead, social services decline, employment and wages do not grow and, in the long run, austerity policies eventually harm the economy.[56] While imposing stiff austerity measures may reduce debt in the short term, it leaves a trail

55 A Schclarek *Debt and economic growth in developing and industrial countries* (2004).

56 OXFAM 'A cautionary tale: The true cost of austerity and inequality in Europe' (2013) 174 Oxfam Briefing Paper.

of long-term negative impacts,[57] such as a decline in wages, an increase in unemployment levels, and depressed growth, social unrest which could further exacerbate current sovereign debt levels,[58] as noticed in Greece.[59] This should be avoided. First, South Africa can look inward by adopting inclusive growth policies and mobilising domestic sources of finance that are sustainable, such as adopting policies geared towards a stronger reliance on domestic financial markets and domestic savings, to avoid relying heavily on short-term external finance.

Also, government spending budgets should be reasonable, purposeful, and aimed at productive sectors/activities of the economy that can pull in private sector investment such as digital trade, innovation in fin-tech, and agro-based SMEs. Also, there should be limited cuts to programmes and expenditure that do not harm essential services or economic activities, while channelling funds realised towards areas that have a direct and strong potential for positive impact on the GDP and spur economic growth. Funds so channelled should be constantly monitored and evaluated for performance. For example, government departments/parastatals performing similar functions could be merged, and over-bloated expenses such as 'foreign training expenses' could be trimmed. Funds realised from non-essential cuts could be channelled into strategic educational programmes such as investment in STEM and entrepreneurship. This would empower a generation of new economic growth drivers through continuous product and business innovation. As the GDP grows, debt levels would eventually reduce from a stable moving economy, investor confidence (for investment into the economy) would

57 IC Amakor & P Ndubuisi-Okolo *Austerity measures and its effect on net investment and export capacity of Tanzania (1986-2018)* (2019) 8 *Journal of Social Development* 6. Tanzania's government austerity measure toward export sustainability did not yield any positive result.

58 Notably, 'the interaction between the austerity measures and structural reforms generated a downward spiral of shrinking GDP and continued increases in sovereign debt'. See P Engler & M Klein 'Austerity measures amplified crisis in Spain, Portugal, and Italy' (2017) 7 *DIW Economic Bulletin*, DIW Berlin, German Institute for Economic Research 89-93, https://ideas.repec.org/a/diw/diwdeb/2017-8-1.html (accessed 27 October 2020).

59 FIDH/HLHR Report on downgrading rights: The cost of austerity in Greece 3, 9-12, https://www.fidh.org/IMG/pdf/downgrading_rights_the_cost_of_austerity_in_greece.pdf (accessed 29 April 2021).

be strengthened, producing a strong multiplying effect. In addition, GDP growth expenditure will fund itself over time, if properly managed.

9.4.2 Multilateral calls for partial debt forgiveness and renegotiated debt repayment to private creditors

Corrupt activities negatively impact a state's decision-making and service delivery processes that drive economic growth. It is recommended that the state impose strict consequences for deliberate fiscal corrupt activities.

According to the International Debt Statistics,[60] South Africa, like most other middle-income countries, owes a large chunk of its long-term (public and publicly-guaranteed) external debt stock to private creditors.[61] Private creditors own about 9 per cent of the external public debt of low-income countries, but 63 per cent of that of middle-income countries,[62] through their ownership of emerging market bonds, with interest payments made on these bonds. High debt figures may act as a constraint to more borrowing because of falling credit ratings.[63] This in turn affects creditors' desire to lend.

A policy recommendation would be for South Africa to reach an agreement with other middle-income countries such as Nigeria and Kenya, to multilaterally approach these private creditors (instead of unilaterally) and collectively renegotiate the terms of debt servicing. Also, in renegotiating debt terms, a proposal that balances partial debt servicing and partial debt forgiveness on grounds that funds released from 'partial debt interest payment' be channelled to economic recovery could be put forward. The proposal could rely on the unforeseen economic consequences of the COVID-19 pandemic as a '*force majeure* of sorts' that had upset the economic *status quo* and agreed payment plans.

Similarly, massive capital flight from large-scale tax evasion and accumulation of offshore wealth flow out of South Africa should be examined and addressed. This deprives the fiscus of necessary resources for development through reduced taxes from private sector investment, contributing to an underactive economy. An estimate of accumulated

60 World Bank Group International Debt Statistics (2021) 128.

61 As above. Total long-term (public and publicly guaranteed) external debt stock is about US $151 million with private creditor total figure share at US $78,523 million.

62 P Bolton et al 'Born out of necessity: A debt standstill for COVID-19' (2020) *CEPR Policy Insight* 103.

63 One of the reasons provided by Fitch in downgrading South Africa's SCR is its high debt levels. See Naidoo (n 50).

capital flight out of South Africa in 2017 amounted to over US $290 billion.[64] Capital flight of such magnitude will persist in delaying South Africa's development and adversely impact the economy through foregone private investment, tax revenue and potential funds for public investment. In addition, the use of cross-border tax planning and transfer pricing manipulations by businesses to reduce their local tax liabilities should be curbed. Although there are laws addressing illicit flows, proper execution remains a challenge especially because the effective tax collection abilities of the South African Revenue Service (SARS) have been steadily undermined by corruption.[65] Therefore, the government must focus on restoring capacity of revenue administration and encourage inter-departmental cooperation and swift communication as a short to long-term strategy to blocking this drainage channel.

9.4.3 More focus on resource mobilisation through minute taxing of domestic and cross-border digital transactions

Owing to the national lockdown imposed by the South African government in curbing the spread of the pandemic, businesses have had to find creative ways in adapting to the new situation. This has led to a growing preference for digital business platforms to physical business locations for transactions by consumers. On the other hand, businesses, including SMEs, are adapting to the new situation through integrating digital processes into their physical business model.[66] This is a catalyst for developing the digital economy alongside the physical economy through the creation of digital monetary value that can be taxed. The government could develop a policy in cooperation with the commercial banks to include a tiny digital platform levy on payment platforms, perhaps at 0,05 per cent of digital transaction cost. With regard to cross-border digital transactions, perhaps it is time for South Africa to cooperate with other Southern African countries on reviewing and reforming the Draft SADC Model Multilateral Tax Agreement, to capture cross-border digital transaction taxation, especially

64 Calculated and capitalised as the capital flight in present year plus the stock of wealth in the previous year capitalised at the Treasury bill rate. See L Ndikumana, K Naidoo & A Aboobaker 'Capital flight from South Africa: A case study' (2020) PERI Working Paper 11, https://www.peri.umass.edu/economists/leonce-ndikumana/item/1323-capital-flight-from-south-africa-a-case-study (accessed 14 June 2021).

65 S Gebrekidan & N Onishi 'Corruption gutted South Africa's tax agency. Now the nation is paying the price' *The New York Times* (10 June 2018), https://www.nytimes.com/2018/06/10/world/africa/south-africa-corruption-taxes.html (accessed 29 April 2021).

66 K Thompson Davy 'How COVID sped up SA's digital transformation' *Financial Mail Digital* (21 April 2021), https://www.businesslive.co.za/fm/fm-fox/digital/2021-04-08-how-covid-sped-up-sas-digital-transformation/ (accessed 8 June 2021).

by SMEs. This could be achieved by creating a nexus between the transaction parties and the income without the use of a physical presence or an effective place of management as is found in most tax treaties.[67] Furthermore, with regard to capturing cross-border digital transactions, there would be a need for stronger cooperation between SARS and other revenue administration authorities, starting regionally within the SADC for cross-border digital transaction information sharing before extending it to a continental and global level in time.

9.5 Conclusion

An unsustainably high debt level is fiscally unhealthy for an emerging market economy such as South Africa. Funds for development are unproductively channelled into debt servicing, contributing to a vicious debt cycle. Despite the challenges, a near sovereign debt crisis often provides a golden opportunity to 'never let a good crisis go to waste' while serving as a wake-up call for addressing weak policy decisions. There may not be a one-size-fits-all solution to forestalling a crisis, but one thing is clear: Fiscal resource drainage must be contained, while ensuring that a transparent, well-monitored GDP growth expenditure path is followed. It is hoped that the recommendations proposed in this study contribute to managing South Africa's rising sovereign debt.

67 Art 5 SADC Draft Model Multilateral Tax Agreement.

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10 The renegotiation of sovereign debt tainted by corruption: Mozambique's 'secret' debt in perspective

Louis Koen

10.1 Introduction

Significant international efforts have been made to raise awareness of corruption and its harmful effects on the welfare and development of countries and their peoples.[1] The international community has increasingly acknowledged corruption as a serious obstacle to effective government, economic growth and stability.[2] This recognition has also contributed to an increasing scholarly focus on the effect of corruption on public debt.[3] This chapter aims to build on these scholarly contributions by analysing the validity of certain Mozambican sovereign debt obligations tainted by corruption.[4]

The Mozambican case is also not the first, nor is it likely to be the last, instance in the Southern African Development Community (SADC) where sovereign debt has allegedly been tainted with corruption.[5] In the case of *Donegal International Ltd v Republic of Zambia*, for example, it was alleged that a settlement agreement on certain Zambian debt obligations had been procured through bribery.[6] Despite the Mozambican case not

1 UN Office on Drugs and Crime *The global programme against corruption: UN anti-corruption tool kit* (2004) 5.

2 As above; United Nations Convention against Corruption; OECD *Managing conflict of interest in the public sector* (2005) 3.

3 See in this respect NN Henri 'Impact of corruption on public debt: Evidence from sub-Saharan African countries' (2018) 8 *American Journal of Economics* 14-17; L Benfratello et al 'Corruption and public debt: A cross-country analysis' (2017) 25 *Applied Economics Letters* (2017) 340-344; E Kim, Y Ha & S Kim 'Public debt, corruption and sustainable economic growth' (2017) 9 *Sustainability* 433; K Omoteso & H Mobolaji 'Corruption, governance and economic growth in sub-Saharan Africa: A need for the prioritisation of reform policies' (2014) 10 *Social Responsibility Journal* 316.

4 For purposes of this contribution it will be assumed that the allegations of corruption in this case are true. This is done for discussion purposes and this contribution does not purport to make a determination on the culpability of any specific individual or entity.

5 See, eg, *Donegal International Ltd v Republic of Zambia* [2007] EWHC 197 (Comm), a case involving a settlement agreement concluded by the Zambian government which had allegedly been tainted with corruption and which was also decided in the English courts.

6 *Donegal* (n 5).

being the first case in the SADC where debt has allegedly been tainted with corruption, it is one of the most prominent cases for the sheer scale of the corruption involved. The case also offers the clearest guidelines to date on how rating agencies will treat non-payment on sovereign debt allegedly tainted with corruption.[7] SADC countries, therefore, could draw important lessons from the Mozambican case on dealing with sovereign debt that may be tainted with corruption.

In pursuit of these aims this chapter will, first, provide a brief background on how the Mozambican debt was incurred before, second, proceeding to consider the legality of the debt under Mozambican law. Third, the validity of the debt is analysed in terms of English law.[8] This contribution will lastly analyse the enforceability of the debt through investor-state arbitration.

10.2 Background to the disputed debt

In 2013 and 2014 the government of Mozambique launched a series of maritime projects to 'furnish Mozambique with the means to assert sovereignty over its Exclusive Economic Zone and exploit the natural resources within it'.[9] Three companies were formed in pursuit of this objective, namely, ProIndicus SA (ProIndicus); Empresa Moçambicana de Atum SA (EMATUM); and Mozambique Asset Management SA (MAM).[10] These companies were all owned, directly or indirectly,[11] by the Mozambican state and incurred almost US $2 billion in debt guaranteed by the state.[12] Only the EMATUM loan was initially disclosed to the

7 The term 'non-payment' is used here rather than 'default'. This is a deliberate terminological choice in light thereof that such non-payment will seemingly not be regarded as a default if the state institutes judicial proceedings challenging the validity of the debt. See in this respect Fitch Rating 'Fitch affirms Mozambique at "CCC"' (9 July 2020), https://www.fitchratings.com/research/sovereigns/fitch-affirms-mozambique-at-ccc-09-07-2020#:~:text=We%20expect%20growth%20to%20rebound,a%200.2%25%20surplus%20in%202019 (accessed 20 January 2021).

8 In this contribution any reference to 'English law' should be construed as a reference to the law of England and Wales.

9 Kroll 'Independent audit related to loans contracted by ProIndicus SA, EMATUM SA, and Mozambique Asset Management SA' (2017) 12.

10 As above.

11 In *Republic of Mozambique v Credit Suisse International* [2021] EWCA Civ 329 the English Court of Appeal explained all entities as being 'wholly owned by the Republic'. Although some entities were partially owned by other state-owned enterprises and various different organs of state, all entities were ultimately wholly owned by the Mozambican government.

12 Kroll (n 9) 12.

public.[13] The disclosure of the balance of this debt, in 2016, following revelations by investigative journalists, resulted in an economic crisis as Mozambique defaulted on all of its external commercial debt obligations and the International Monetary Fund (IMF) withdrew all support.[14] In response thereto, foreign governments also ceased providing aid conditional upon IMF support and Mozambique's currency plunged.[15] These debt obligations have since been linked to widespread corruption involving high-level Mozambican government officials, including its former Minister of Finance.[16]

10.2.1 The ProIndicus debt

Privinvest Group, an Abu Dhabi-based holding company, had initiated discussions with Mozambican government officials in 2011 ostensibly aimed at establishing a coastal monitoring system through a contract with the company.[17] The Mozambican government incorporated ProIndicus to perform these activities on behalf of it.[18] It is alleged that Privinvest later approached Credit Suisse, intending to secure financing for the project.[19] Credit Suisse is said to have made it clear that it would only provide financing at market rates and subject to it being guaranteed by the government of Mozambique.[20]

13 C Reid 'Mozambique: The anatomy of corruption' (26 June 2018), https://www.theafricareport.com/607/mozambique-the-anatomy-of-corruption/ (accessed 26 October 2020).

14 IMF 'IMF executive board considers Mozambique's misreporting under the policy support instrument and breach of obligation under Article VIII, Section 5' (21 November 2016), https://www.imf.org/en/News/Articles/2016/11/21/PR16521-IMF-Executive-Board-Considers-Mozambiques-Misreporting-Under-the-Policy-Support-Instrument (accessed 17 April 2021).

15 Economist Intelligence Unit 'Undisclosed debts push Mozambique towards crisis' (26 April 2016), http://country.eiu.com/article.aspx?articleid=1494162133&Country=Mozambique&topic=Economy (accessed 20 October 2020). A group of donor nations and international organisations known as the Group of 14 (G14) collectively agreed to suspend all direct budgetary support to the government of Mozambique. The collective amount that Mozambique was set to receive from this group exceeded US $280 million. The G14 is composed of Austria, the African Development Bank, the World Bank, Canada, Spain, Finland, France, Ireland, Italy, Portugal, United Kingdom, Sweden, Switzerland and the European Union.

16 Reid (n 13).

17 Indictment, *United States v Boustani & Others* Case CR 18 681 para 31.

18 Kroll (n 9) 22.

19 *United States v Boustani* (n 17) para 34.

20 As above.

ProIndicus and Credit Suisse agreed upon a US $372 million loan facility on 28 February 2013.[21] The maximum amount available under this credit facility was subsequently increased to US $900 million of which ProIndicus utilised around US $622 million to purchase ships from PrivInvest.[22] The initial agreement and the subsequent agreements, increasing the amount available under the credit facility, were all guaranteed by the government of Mozambique acting through the Minister of Finance.[23] It has since transpired that PrivInvest has allegedly paid bribes of up to US $5 million to the Minister of Finance to secure his signature on the guarantees.[24] The vessels purchased with these funds have also remained largely unused and provide little to no benefits to the Mozambican people.[25]

10.2.2 The EMATUM and EMATUM-related debt

EMATUM was formed to develop a 'home-grown and self-sustaining fishing industry in Mozambique'.[26] To achieve these objectives, EMATUM was to acquire a fleet of vessels from the Privinvest Group.[27] EMATUM concluded a loan agreement with Credit Suisse for an amount not exceeding US $850 million on 30 August 2013.[28] Like the ProIndicus agreement, this agreement was accompanied by a government guarantee signed by the Minister of Finance on Mozambique's behalf.[29]

EMATUM initially drew US $500 million from the credit facility on 5 September 2013 and later drew a further US $350 million provided by VTB Capital, a subsidiary of the Russian state-owned bank VTB.[30] The

21 Kroll (n 9) 22.

22 As above.

23 As above.

24 *United States v Boustani* (n 17) para 38.

25 B Ballard 'Mozambique's dramatic economic reversal' (11 July 2018), https://www.worldfinance.com/special-reports/the-mozambique-debt-crisis (accessed 28 October 2020). These ships have remained largely unused because the vessels purchased were not suited for the purpose for which they were acquired.

26 F Guilenge 'Three layers of uncertainty in Mozambique: What's happening and why does It matter?' (date unknown), https://www.rosalux.de/en/publication/id/38966/three-layers-of-uncertainty-in-mozambique (accessed 30 October 2020). EMATUM was co-owned by the state holding company (IGEPE), the state fishing company (Emopesca) and the Mozambican Intelligence Service, SISE (Servico de Informacao e Seguranca do Estado).

27 Kroll (n 9) 12.

28 Kroll (n 9) 29.

29 As above.

30 As above.

existence of the EMATUM debt was disclosed to the IMF in 2014.[31] The government of Mozambique later restructured the EMATUM loan.[32] In the restructuring process holders of the EMATUM loan participation notes (LPNs) were to exchange these notes for sovereign Eurobonds issued by the government of Mozambique.[33] Mozambique defaulted on these Eurobonds shortly thereafter as the economic crises resulting from the disclosure of the ProIndicus and MAM debts severely curtailed Mozambique's ability to honour its obligations under the Eurobonds.[34] With more than US $200 million in direct foreign aid to Mozambique's budget suspended, the country could not afford to make timeous payment on these bonds.[35]

The Eurobonds were in turn again restructured in 2019.[36] In terms of this restructuring arrangement, holders of the previous Eurobond valued at US $726,5 million were to exchange these for new Eurobonds valued at US $900 million.[37] The higher debt value is said to cover missed principal and interest payments under the previous issue of Eurobonds.[38] These restructured debts will be collectively referred to as the EMATUM-related debt in this chapter.

10.2.3 The MAM debt

MAM concluded a loan agreement for US $540 million with VTB on 20 May 2014.[39] This agreement was also accompanied by a guarantee

31 IMF 'Mozambique Country Report 18/66' (21 February 2018) 36.

32 As above. The restructuring of the loan occurred as EMATUM could not meet its obligations. The Mozambican government then agreed to step in and assist EMATUM. Importantly, unlike the ProIndicus and MAM debt, Mozambique benefited, at least partially, from the EMATUM loan. US $500 million had been transferred to the Mozambican general budget by EMATUM.

33 As above.

34 Capital Markets in Africa 'Mozambique to miss coupon payment on Eurobond, ministry says' (date unknown), https://www.capitalmarketsinafrica.com/mozambique-to-miss-coupon-payment-on-eurobond-ministry-says/ (accessed 30 October 2020).

35 See para 2 of the contribution with respect to the economic crises resulting from the IMF's suspension of support and the withdrawal of foreign aid.

36 IMF 'Republic of Mozambique: Request for disbursement under the rapid credit facility-debt sustainability analysis' (17 April 2020) 3.

37 T Roca 'Fitch upgrades Mozambique to CCC after debt restructuring' 7 (November 2019), https://www.spglobal.com/marketintelligence/en/news-insights/trending/xku6e3ietvexzlqtsj6hkg2 (accessed 20 October 2020).

38 As above.

39 Kroll (n 9) 38. MAM was almost entirely owned by SISE other than the shares held by EMATUM and ProIndicus, who each held 1%.

provided by the government and signed by the Minister of Finance.[40] The MAM debt involved many of the same parties who had arranged the other unlawful debts. However, thus far no evidence has emerged indicating any participation by VTB and/or its employees in the corrupt scheme.[41]

10.3 The (in)validity of the guarantees under Mozambican law

The Constitutional Council of the Republic of Mozambique has declared all of the secret debt unlawful in terms of the law of Mozambique.[42] In all instances, the value of the guarantees provided exceeded the annual limit on the value of state guarantees authorised.[43] The 2013 and 2014 budget laws provided for a limit to state guarantees of 183,5 million Meticals (approximately US $5 million) and 15,7835 billion Meticals (approximately US $375 million) respectively.[44] In 2013 each guarantee provided in relation to the various 'secret debts' exceeded the annual limit on its own not even accounting for the combined effect of these guarantees.

The debts were also declared unlawful in light of the market rate of interest attached to these loans.[45] In terms of Mozambican law, the state cannot incur a debt obligation unless the interest rate it obtains is at least 35 per cent below the market rate.[46] The Court held that although the companies were essentially incorporated as private entities they remained bound by these laws in light of the significant state control and public functions performed by these entities.[47] The illegality of the loans and guarantees is further founded upon article 179(1)(p) of the Mozambican Constitution which provides that parliamentary approval must be obtained for debts with a maturity exceeding one year and that Parliament has the

40 As above.

41 M Goldmann 'The law and political economy of Mozambique's odious debt' Keynote address delivered at *Centro de Integridade Pública Conference* (Maputo 15 March 2019) 10.

42 Constitutional Council of Mozambique Judgment 5/CC/2019 of 3 June 2019; Constitutional Council of Mozambique Judgment 7/CC / 2020 of 8 May. In terms of art 241 of the Constitution of Mozambique the Constitutional Council is the highest judicial authority with respect to constitutional matters. It is afforded with broad authority to 'evaluate and declare the unconstitutionality of laws and the illegality of normative acts of state offices'.

43 Judgment 7/CC / 2020 (n 42) 7.

44 Judgment 7/CC / 2020 (n 42) 7, in reference to Law 1/2013 of 7 January and Law 1/2014 of 24 January.

45 Judgment 7/CC / 2020 (n 42) 7.

46 Art 9(2) of Law 1/2013 of 7 January, in reference to art 179(1) of the Constitution of Mozambique, 2004.

47 Judgment 7/CC / 2020 (n 42) 7.

exclusive competence to set the upper limit for guarantees that may be given by the state.[48]

The Constitutional Council also held Assembly Resolution 11/2016 to be void for illegality.[49] In this Resolution the assembly purportedly recognised the EMATUM debt in an attempt to cloak an otherwise void act with validity. The Constitutional Council found that the assembly had no power to recognise an invalid and unconstitutional act.[50] It went on to explain that in terms of Mozambican law 'expenditure may only be assumed during the economic year for which it has been budgeted'.[51] It is accordingly beyond dispute that as a matter of Mozambican law the guarantees and the Eurobonds emerging from the first restructuring are invalid.

10.4 The validity/invalidity of the debts under the law of England and Wales

The invalidity of the guarantees per Mozambican law would not automatically render them invalid under English law.[52] The debts are ultimately governed by English law and not Mozambican law.[53] This part, therefore, will briefly consider the validity of the guarantees in terms of

48 Judgment 5/CC/2019 of 3 June 2019 (n 42) 12.

49 As above.

50 As above.

51 Judgment 5/CC/2019 of 3 June 2019 (n 42) 11 in reference to Law 9/2002 of 12 February.

52 The principles of international comity have formed part of English law since the 18th century. It permits the English courts to give effect to decisions made by foreign courts. Mozambique may potentially argue that the English courts should, on the basis of comity, follow the decision of the Constitutional Council and hold the debts to be invalid. However, the author could not find any case law where the English courts have ever dismissed a sovereign debt claim, governed by English law, on the basis of comity. As seen in *Ukraine v Law Debentures Trust Corporation PLC* [2018] EWCA Civ 2026 (Ukraine appeal case) the English courts have generally limited deference to accepting that the debt is invalid in terms of the law of the state concerned. Questions such as ostensible or usual authority were still determined with reference to English law. See para 4.1.3 of this contribution in this respect. The extent to which Mozambique could raise this argument, therefore, is uncertain and a full discussion thereof falls outside of the scope of this contribution.

53 The Mozambican judgments also only dealt with a lack of actual authority and the breaches of the budget law. These grounds on their own may be insufficient for invalidity in terms of English law. Importantly, the Mozambican courts also did not make any findings regarding the culpability of any of the banks concerned.

English law. In this part, the validity of the EMATUM-related debt is addressed separately from the guarantees.

10.4.1 The invalidity of the guarantees

In terms of English law, it is unlawful to bribe a foreign public official.[54] The Bribery Act also provides that a failure by a commercial organisation to prevent bribery is a criminal offence.[55] However, as Goldmann correctly notes, the Bribery Act does not in itself render a contract void in instances where bribery has occurred.[56] He instead argues that the ProIndicus and EMATUM debts are invalid under the common law doctrine of illegality.[57] In this contribution, the author largely agrees with the conclusion reached by Goldmann. However, this contribution disagrees with him on the manner in which he arrived at the conclusion.

In this part it is argued that Goldmann is incorrect in suggesting that a claim would be barred by the doctrine of illegality as a result of the guarantees being procured through bribery. This contribution instead considers the distinction in English law between contracts to bribe and contracts procured through bribery.[58] The former has been held to be unenforceable under the illegality doctrine while the latter is not.[59] This contribution also disagrees with Goldmann to the extent that he implies the agreements are void, rather than voidable, by virtue of the bribery.[60] In this part it will instead be argued that the agreements are voidable at the instance of Mozambique as the innocent party.

The doctrine of illegality in English law

It is a well-established principle of English law that a contractual claim can be defeated by illegality.[61] This principle, arising from the Roman law principle of *ex turpi causa non oritur actio*, provides that a court will not aid

54 UK Bribery Act 2010 sec 6.

55 UK Bribery Act 2010 sec 7.

56 Goldmann (n 41) 5.

57 As above.

58 *National Iranian Oil Company v Crescent Petroleum Company International Ltd & Crescent Gas Corporation Ltd* [2016] EWHC 510 (Comm) para 49; *Honeywell International Middle East Ltd v Meydan Group* LLC [2014] EWHC 1344 (TCC) para 184.

59 See part 10.4.1of this contribution and the authorities cited there in this respect.

60 In his paper Goldmann states that '[t]he loan agreement is therefore void'. Goldmann (n 41) 5.

61 *Hall v Woolston Hall Leisure Ltd* [2001] 1 WLR 225 para 28.

a party whose cause of action is founded upon an immoral or illegal act.[62] Despite its relatively simplistic formulation, the operation of illegality in the law of obligations has given rise to much controversy and at times contradictory case law.[63] However, the English courts have been quite clear on the difference between contracts procured by bribery and a contract illegal in itself such as an agreement to pay a bribe.[64]

Concerning the loan guarantees provided by the Mozambican government in connection with the hidden loans, it can be said that these agreements were likely procured through the bribery of the Minister of Finance.[65] However, the Court in *Honeywell International Middle East Ltd v Meydan Group LLC* (*Honeywell* case) held that 'whilst bribery is clearly contrary to English public policy and contracts to bribe are unenforceable, as a matter of English public policy, contracts which have been procured by bribes are not unenforceable'.[66] The effect of this decision is that the enforcement of the ProIndicus and EMATUM guarantees are not prohibited by the *ex turpi causa* rule as Goldmann suggests.[67]

The voidability of a contract procured through bribery

The mere fact that a claim is not barred by the *ex turpi causa* rule nevertheless does not mean that Mozambique is without recourse. In *Wilson v Hurstanger* the Court held that where there had been bribery involved in the procurement of the contract such agreement would be voidable at the

62 *Holman v Johnson* (1775) 1 Cowp. 341, 343; *Hall v Woolston* (n 61) para 28.

63 A Burrows 'A new dawn for the law of illegality' in S Green & A Bogg (eds) *Illegality after* Patel v Mirza (2018).

64 *Honeywell* case (n 58) para 185.

65 *United States v Boustani* (n 17) para 38.

66 *Honeywell* case (n 58) para 185. This position was also reaffirmed in *National Iranian Oil Company v Crescent Petroleum Company International Ltd & Crescent Gas Corporation Ltd* [2016] EWHC 510 (Comm) para 49.

67 It is not clear on what basis Goldmann proceeds to apply the illegality doctrine directly to the guarantees. Goldmann does not mention any of the cases that treats contracts procured by bribery differently than contracts to bribe. His reliance on *Patel v Mirza* [2016] UKSC 42 might suggest that, in his view, the distinction between illegal contracts themselves and contracts procured through bribery is no longer applicable. The author disagrees to the extent that this is his argument as the effect of Patel is that even contracts illegal in themselves would no longer per se be unenforceable. These contracts would only be unenforceable if they have the potential to bring the legal system into disrepute. *Post-Patel* cases, such as *UBS AG (London Branch) v Kommunale Wasserwerke Leipzig GmbH* [2017] EWCA (Civ) 1567, have also continued to address contracts procured through bribery as voidable rather than unenforceable under the illegality doctrine.

instance of the innocent party.[68] The Court in the *Honeywell* case agreed with this finding and indicated that bribery allows the innocent party to avoid the contract, at its election, provided counter-restitution can be made.[69] The guarantees procured through bribery, therefore, is voidable at the election of Mozambique.[70]

Article 34 of the UN Convention Against Corruption requires state parties to ensure that no person benefits from contracts, concessions or similar advantages obtained through corrupt means.[71] The UN Office on Drugs and Crime has also noted that it is common practice in many states to provide that agreements procured through bribery are voidable.[72] There are certain instances where holding such contracts as void, rather than voidable, may benefit the corrupt party.[73] It is for this reason that English law provides the innocent party with a right of election to seek rescission or to continue with the contract.[74] Therefore, it is submitted that this approach is not in conflict with the UN Convention Against Corruption.

In his analysis Goldmann also suggests that Mozambique would not need to make counter-restitution in light of the doctrine of illegality.[75] In reaching this conclusion he relies on the limited discretion conferred upon English courts to deny a claim based on unjustified enrichment where the enforcement of the claim would be contrary to the public interest or harmful to the integrity of the legal system having regard to a range of factors.[76] The author agrees with Goldmann that an English court is likely

68 *Wilson & Another v Hurstanger Ltd* [2007] EWCA Civ 299 para 39.

69 *Honeywell* case (n 58) para 184.

70 This contribution does not address the extent to which the banks were aware of the corruption. In English law it is not necessary to prove that the bank itself authorised the bribe, or even knew about it, for the contract to be voidable. Participation by some of the bank's employees in the corrupt scheme will generally suffice. See *UBS AGv Kommunale Wasserwerke* (n 67). It is known that certain CreditSuisse employees had pleaded guilty to bribery in this case (B Pierson 'Second ex-Credit Suisse banker pleads guilty in Mozambique loan scheme' (20 July 2019), https://www.reuters.com/article/us-mozambique-credit-suisse-gp-charges-idUKKCN1UE2OJ (accessed 20 October 2020).

71 UN Office on Drugs and Crime *State of implementation of the United Nations Convention against Corruption* (2017) 157.

72 As above.

73 UN Office on Drugs and Crime (n 71) 158. This would, eg, arise in instances where the innocent party has performed but the briber has yet to deliver its counter performance. In such instances the innocent party may elect to continue with the contract in addition to claiming damages.

74 *Honeywell* case (n 58) para 185.

75 Goldmann (n 41) 5.

76 Goldmann (n 41) 6; *Patel v Mirza* [2016] UKSC 42 para 120.

to decline an award against Mozambique based on unjustified enrichment considering the illegalities.[77]

In this contribution it is additionally argued that at least in as far as the Mozambican government is concerned, there has been no enrichment and, therefore, the issue of counter-restitution does not arise. In *National Commercial Bank (Jamaica) Ltd v Hew* the Privy Council held that 'with a guarantee, the surety incurs a liability but obtains no benefit, so there is nothing to disgorge by way of counter-restitution if the guarantee is set aside'.[78] It is therefore submitted that Mozambique need not make any counter-restitution as it did not directly obtain any benefit through the provision of the guarantee.[79]

The Minister of Finance's capacity to bind Mozambique to the guarantees

For purposes of this contribution, the discussion is primarily concerned with the effect of corruption on the validity of the debt or debt guarantees. However, the question of the capacity of the Minister of Finance is briefly considered as a lack of capacity has been advanced as a key reason for the invalidity of the MAM guarantee.[80] Goldmann argues that the MAM guarantee is unlawful as the Minister of Finance, who signed the guarantee, did not have the authority to do so.[81] This argument relies upon the Minister's lack of actual authority to bind Mozambique in terms of its domestic law.[82] The English courts will generally defer to the Mozambican

77 Goldmann (n 41) 6.

78 *National Commercial Bank (Jamaica) Ltd v Hew* [2003] UKPC 51 para 43. This position has also been followed in several other cases, be it explicitly or implicitly. See among others *Eastern Shipping Co v Scales Trading Ltd* [2000] UKPC 44; *TSB Bank plc v Camfield* [1995] 1 WLR 430.

79 It is important to distinguish between the parties before the court. Where ProIndicus or MAM are the parties they would need to make counter-restitution as they have received assets. However, these assets do not belong to the Mozambican government directly. The ships supplied continue to be owned by these companies and have largely been left unused. See B Aris 'Debt deals in Mozambique that go wrong' (28 November 2019), https://www.intellinews.com/long-read-debt-deals-in-mozambique-that-go-wrong-172448/ (accessed 15 January 2021). The military equipped ships that ere was to be supplied saw the order changed and was also supplied to ProIndicus rather than directly to the Mozambican government. If any of these assets have since been transferred to the Mozambican government it may need to make counter-restitution unless the court's limited discretion to refuse enforcement is exercised in its favour.

80 Goldmann (n 41) 10.

81 As above.

82 In this argument Goldmann specifically refers to art 179(1)(p) of the Constitution of Mozambique as well as the ceiling placed on debt guarantees by the 2013 and 2014 budget laws. In this contribution, these provisions are not considered to be the basis for invalidity. However, they are considered as the sources placing the banks on notice

courts and accept their findings that the Minister lacked actual authority in terms of Mozambican law.[83] However, in English law liability may in some instances be established based on usual or ostensible authority.[84]

In *Law Debentures v Ukraine* (*Ukraine* case) the Court reiterated that 'questions of ostensible authority or usual authority are to be determined by the putative applicable law of the contract'.[85] Where VTB relies upon usual or ostensible authority, the question will therefore be determined by English law, as the law governing the agreement, and not Mozambique's domestic law. In the *Ukraine* case the Court held that in English law the usual authority of a minister of finance to enter into a guarantee needs to be determined with reference to the role of the finance minister within that particular state and the particular borrowing.[86] In that case, Ukraine argued that the plaintiff should have been aware that in incurring the debt in question the minister would breach the debt limit set out in its budget law which had been public information.[87] The Court ultimately rejected this argument by Ukraine.[88]

If this approach were correct, it seems unlikely that Mozambique would succeed in similarly arguing that VTB ought to have been aware of the upper limit on the value of state guarantees provided for in the 2013 and 2014 budget laws. This approach would also contrast sharply with the United Nations Conference on Trade and Development (UNCTAD) Principles on Responsible Sovereign Lending which provides for a duty of due diligence on creditors to verify that the debt would comply with the host states law.[89] Although the Court of Appeal upheld the finding by the High Court in this respect, it also warned that where legislation was publicly available anyone lending to the country must be 'taken to know of its effects'.[90] The Court of Appeal only dismissed Ukraine's argument on this point because of its own conduct that induced the belief that it would not breach the limit.[91]

with respect to the minister's lack of capacity.

83 *Law Debentures Trust Corporation PLC v Ukraine, represented by the Minister of Finance of Ukraine acting upon the instructions of the Cabinet of Ministers of Ukraine* [2017] EWHC 655 (Comm) para 154; *Ukraine* appeal case (n 52) para 36.

84 *Marubeni Hong Kong and South China Ltd v Mongolia* [2005] EWCA Civ 395 para 46.

85 *Ukraine* case (n 52) para 154.

86 *Ukraine* case (n 83) para 160.

87 *Ukraine* case (n 83) para 96.

88 *Ukraine* case (n 83) para 164.

89 Principle 3 of the UNCTAD Principles on Responsible Sovereign Lending.

90 *Ukraine* appeal case (n 52) para 121.

91 *Ukraine* appeal case (n 52) para 125.

In the *Ukraine* case the Court was also confronted with a resolution purportedly passed by the Cabinet of Ministers of Ukraine (CMU) in which authority was conferred upon the Minister of Finance to enter into debt transactions. The Court accepted that the resolution breached Ukraine's internal law as the CMU lacked the authority to authorise the Minister of Finance to do something beyond his actual authority.[92] However, the Court held that even if the CMU 'had no actual authority to hold out the Minister of Finance as Ukraine's representative in the transaction, it did have usual authority to do so as the state's cabinet'.[93]

If this position were correct, Presidential Decree 2/2010 would have posed a substantial obstacle to any defence raised by Mozambique based on a lack of capacity by the Minister of Finance. The Decree provided that the Minister of Finance has the competency to enter into and implement agreements for the contracting of internal and external public debt, to enter into and implement agreements with international financial institutions, and to enter into contracts or agreements that entailed the assumption of financial liabilities or involved fiscal matters.[94] However, the Court of Appeals rejected this finding to the extent that the resolution violates express provisions of the Ukrainian Budget Code.[95] Similarly, although Presidential Decree 2/2010 conferred authority upon the Minister of Finance to contract debts, it did not, nor did it purport to, authorise the Minister to exceed the limit on state guarantees.

In conclusion, although English law distinguishes between actual authority and usual or ostensible authority, a party cannot rely on the latter where it has been placed on notice that the Minister lacks actual authority.[96] Publicly available legislation setting out limitations on the Minister's competence may be sufficient to serve as notice unless the state induces a belief to the contrary.[97] The courts will regard VTB as having been aware of the upper limit on state guarantees in the present case. This ought to be sufficient to defeat any reliance by VTB upon usual or ostensible authority by the Minister of Finance. This may differ if Mozambique had

92 *Ukraine* case (n 83) para 167.

93 As above.

94 Presidential Decree 2/2010 art 3.

95 *Ukraine* appeal case (n 52) para 131. The Court of Appeals went on to explain that '[t]he person holding out an "agent" so as to give them ostensible authority must have actual (express or implied) authority to do so on behalf of the principal, or ostensible authority derived from someone with actual authority. Ostensible authority is not otherwise sufficient.'

96 *Ukraine* appeal case (n 52) para 121.

97 *Ukraine* appeal case (n 52) paras 121-125.

taken some action to induce the belief that the upper limit would not be breached. However, it is submitted that such an argument would, in either event, be untenable in this case as the individual guarantee provided to VTB on its own exceeded the upper limit on state guarantees.[98]

10.5 The validity of the EMATUM-related debt

10.5.1 The Eurobonds as a new debt obligation independent from the initial guarantee

In terms of English law, a substitution of one lender for another is usually regarded as a novation.[99] Novation has the effect of terminating the initial agreement and replacing it with a new agreement independent from the previous agreement.[100] Olivares-Caminal has persuasively argued that the LPN's issued by EMMATUM were novated when Mozambique exchanged these notes for the sovereign Eurobonds issued directly by the government of Mozambique.[101] The government of Mozambique had replaced EMATUM as the principal debtor and had assumed liability separate from the initial guarantee.[102]

Importantly a transfer by way of novation is not subject to equities in terms of English law.[103] Accordingly, any right to rescind, which a party might have had concerning the original agreement, is lost upon the extinguishment and replacement thereof by the new, novated, agreement.[104] Effectively this means that the novated agreement would not be affected by any potential invalidity of the previous agreement. Mozambique would accordingly be liable to pay the EMATUM-related debt even though the original guarantee had been procured through corruption.

Goldmann, however, raises an interesting argument wherein he opines that a novated agreement may itself be invalid where it too has

98 If, eg, the VTB guarantee had been below the annual limit and Mozambique had failed to disclose the existence of other guarantees, VTB would have been able to rely on Mozambique's own conduct as inducing this belief.

99 R Gray et al 'Transfer of syndicated loans: Similar objectives, subtle differences' (2010) *International Financial Law Review* 63.

100 As above.

101 R Olivares-Caminal 'Mozambique policymakers need to act now!' (4 April 2019), https://www.linkedin.com/pulse/mozambique-policymakers-need-act-now-rodrigo-olivares-caminal/ (accessed 25 October 2020).

102 As above.

103 A Burrows *A restatement of the English law of contract* (2016).

104 *Deutsche Bank AG & Others v Unitech Global Ltd & Others* [2013] EWHC 471 (Comm) para 50.

been obtained through corruption.[105] Although this may be correct, as Goldmann himself acknowledges, mere involvement of some of the parties to the initial corruption in the restructuring would not be sufficient to prove that the restructuring itself has been affected by corruption.[106] The point has in either event also become moot as those Eurobonds have again been restructured, potentially resulting in yet another novation.

It may seem unjust to expect Mozambique to repay debts from which it has received little to no benefit.[107] In this regard, some have suggested that Mozambique ought to declare the debt as odious and refuse repayment on this basis.[108] The validity of the doctrine of odious debts is heavily disputed in international law.[109] Additionally, even if Mozambique were to satisfy a court that the doctrine is a valid norm of public international law, this would not assist it in a case before the English courts. It is well established in terms of English law that unless international norms have been incorporated into domestic law, these norms 'cannot be the source of domestic rights or duties and will not be interpreted by' the courts.[110] While it may, therefore, be tempting to seek non-repayment of the Eurobonds from a moral perspective, it is submitted that the debt remains legally valid under English law.

10.6 Investor corruption as a jurisdictional bar to international investor-state arbitration

Mozambique is a party to several bilateral investment treaties (BITs) in which jurisdiction is conferred upon the International Centre for the Settlement of Investment Disputes (ICSID).[111] The ICSID has long held that the holders of sovereign debt may be considered investors for

105 Goldmann (n 41) 8.

106 As above.

107 D Williams & J Isaksen 'Corruption and state-backed debts in Mozambique: What can external actors do?' (2016), https://www.cmi.no/publications/6024-corruption-and-state-backed-debts-in-mozambique (accessed 30 October 2020).

108 As above. It has been said that '[a]ccording to the doctrine of odious debt, loans which are knowingly provided to subjugate or defraud the population of a debtor state are not legally binding against that state under international law'; see J King *The doctrine of odious debt in international law: A restatement* (2016) 1.

109 See among others King (n 108) 62.

110 *Belhaj & Others v Straw & Others* [2017] UKSC 3 para 123.

111 See art 8 Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Mozambique for the Promotion and Protection of Investments (UK-Mozambique BIT); art 10(2) Agreement between the Belgium-Luxembourg Economic Union and The Government of the Republic of Mozambique on the Promotion and Protection of Investments.

purposes of establishing its jurisdiction.[112] Investors in the debt from any of these countries may potentially lodge a claim against Mozambique at the ICSID. This contribution will, therefore, briefly consider the ICSID's approach to investor corruption as a jurisdictional bar.[113]

States have long argued that international investment protection does not extend to investments tainted with illegality.[114] The ICSID decision in *Metal-Tech Ltd v Uzbekistan* (*Metal-Tech* case) gave recognition to these assertions by states.[115] In this case serious concerns arose over large sums paid in the form of 'consulting fees' to individuals closely connected to high-ranking government officials in Uzbekistan.[116] The tribunal in the *Metal-Tech* case explained that an investor may only claim under a BIT if it had established an investment under the BIT.[117] In that case, the tribunal concluded that the investor had been unable to rebut the suspicion of illicit activities established by Uzbekistan and, accordingly, it could not be said that the investment had been implemented in terms of the law of the host state as required by the BIT.[118] It is on this basis that the tribunal declined jurisdiction over the matter.

From the *Metal-Tech* case, it would seemingly be enough for Mozambique to establish a *prima facie* case of corruption upon which the burden would shift to the investor to rebut the 'suspicion of illicit activities'. However, to defeat a claim at the jurisdictional stage the BIT in question would need to contain a so-called 'in-accordance with its laws'

112 *Fedax NV v The Republic of Venezuela*, ICSID Decision Objections to Jurisdiction (11 July 1997) ICSID Case ARB/96/3 para 43. In a recent article Pahis criticises investment tribunals' assertion of jurisdiction over sovereign debt as investments. He argues that it undermines the core purpose of bilateral investment treaties and raises the cost of sovereign debt. This contribution agrees with the arguments raised. However, as Pahis also notes, 'recent jurisdictional decisions suggest that sovereign debt will be subject to' investment arbitration for the foreseeable future. See S Pahis 'BITs & bonds: The international law and economics of sovereign debt' (2021) 115 *American Journal of International Law* 242.

113 It is important to note that this contribution does not consider the substantive validity of debt tainted by corruption before the ICSID. This is because if corruption acts as a jurisdictional bar the tribunal would not consider the matter beyond this jurisdictional phase.

114 A Bulovsky 'Promises unfulfilled: How investment arbitration tribunals mishandle corruption claims and undermine international development' (2019) 118 *Michigan Law Review* 117 119.

115 *Metal-Tech Ltd v Republic of Uzbekistan*, ICSID Award (4 October 2013) ICSID Case ARB/10/3.

116 *Metal-Tech* case (n 115) para 279.

117 *Metal-Tech* case (n 115) para 145.

118 *Metal-Tech* case (n 115) para 373.

clause.[119] Certain Mozambican BITs contain such a clause while others do not.[120] Mozambique's ability to defeat an ICSID claim at the jurisdictional stage may thus be dependent on the nationality of the claimant.

Importantly, the principles above would only apply before the ICSID where corruption or a reasonable suspicion of investor corruption has been proven.[121] The ICSID will also not find every investment in breach of the host state's law to be a jurisdictional bar. This is so particularly where the breach of domestic law occurred through no fault of the investor and government officials of the host state had created the impression that the investment would be lawful.[122]

It is accordingly submitted that investors who subsequently purchased the EMMATUM-related Eurobonds could, therefore, potentially invoke the jurisdiction of the ICSID should Mozambique repudiate the restructured debt. These investors' claims would not be barred by the corruption of other parties involved in the proceedings unless they were aware or ought to have been aware of the corruption.[123]

10.7 Conclusion and recommendations

From the foregoing analysis it becomes clear that Mozambique finds itself in a precarious position where it may be liable for the Eurobonds in terms of English law. Mozambique is simultaneously facing significant pressure from civil society groups not to pay any of the debt including the Eurobonds.[124] The international investment community in turn expects Mozambique to honour its obligations arising from the Eurobonds. This is so particularly considering that the Eurobonds are, as argued in this contribution, valid in terms of its governing law. Were Mozambique to renege on its obligations arising from the restructured Eurobonds again, it could significantly impair investor confidence in the country. The

119 As above. The so-called 'in accordance with its laws' clause is a clause in a bilateral investment treaty indicating that all investments are to be made in accordance with the law of the host state.

120 See eg art 2 of the Agreement between the Swiss Confederation and the Republic of Mozambique Concerning the Promotion and Reciprocal Protection of Investments which contains such a clause while the UK-Mozambique BIT (n 111) does not.

121 *Tethyan Copper Company Pty Limited v Islamic Republic of Pakistan* ICSID Decision on Jurisdiction and Liability (10 November 2017) ICSID Case ARB/12/1 para 684.

122 As above.

123 As above.

124 Club of Mozambique 'Hidden debts: Civil society wants to sue government' (1 November 2019), https://clubofmozambique.com/news/hidden-debts-civil-society-wants-to-sue-government-dw-146045/ (accessed 30 October 2020).

Mozambican government has itself acknowledged that it will require significant private investment capital in the coming years, making it imperative for the government to boost investor confidence rather than undermining it.[125]

Yet, in honouring the debt obligations arising from the Eurobonds, Mozambique may breach the ruling of its Constitutional Council. It has been argued that the latest restructuring has so breached this ruling in light thereof that the Constitutional Council held the original EMATUM debt and all related transactions to be void.[126] Should the Constitutional Council find that the latest restructuring is void, it would impair Mozambique's ability to make payment without breaching its domestic law. As established in this contribution, it additionally seems unlikely that Mozambique would succeed in resisting a claim based on the Eurobonds in ICSID arbitration. Holding the latest restructuring invalid would thus leave Mozambique with the equally undesirable options of either (i) breaching its domestic law or (ii) defaulting upon valid debt obligations.

Mozambique's decision to honour the Eurobonds is prudent. The mere fact that Mozambique is honouring the Eurobonds also does not automatically result in the Mozambican people being unfairly burdened with the cost of debts from which they have not benefited.[127] Mozambique is seeking damages in tort against the parties who had been involved in the alleged corrupt scheme.[128] This allows Mozambique to try and recover losses suffered as a result of the corruption without defaulting upon valid debt obligations.

125 Club of Mozambique 'Mozambique Eurobonds out of debt relief to build up investors' confidence' (15 October 2020), https://furtherafrica.com/2020/10/15/mozambique-eurobonds-out-of-debt-relief-to-build-up-investors-confidence/ (accessed 30 October 2020).

126 AIM 'Mozambique: Finance Ministry defies Constitutional Council over Ematum' (1 November 2019), https://clubofmozambique.com/news/mozambique-finance-ministry-defies-constitutional-council-over-ematum-aim-report-145951/ (accessed 31 October 2020).

127 English law recognises a claim in tort against any person who had participated in bribery where rescission may not be available. See eg *Chancery Client Partners Ltd & Others v MRC 957 Ltd & Others* [2016] EWHC 2142 (Ch) paras 23-24. Importantly, this does not affect the validity of the debt but merely provides an avenue for Mozambique to obtain some form of redress. A full discussion of tort law falls outside the scope of this contribution.

128 The English Court of Appeal in *The Republic of Mozambique v Credit Suisse International & Others* [2021] EWCA Civ 329 recently held that part of Mozambique's claim is closely connected to an arbitration clause and a stay of proceedings may be warranted. The arbitral case is *PrivInvest v Mozambique* ICC Case 24325. A full commentary on those proceedings fall outside the scope of this contribution.

The Mozambican case highlights the importance for SADC states to obtain appropriate advice prior to embarking upon the restructuring of sovereign debt. Had Mozambique not restructured the EMATUM debt, the obligations may well have been invalid and unenforceable. Additionally, the treatment of the ProIndicus and MAM loans makes it clear that rating agencies do not regard a state to be in default where the debt is potentially invalid as a result of corruption provided that judicial proceedings are instituted.[129] The reprieve offered by rating agencies and international financial institutions such as the IMF in these cases should assist states to avoid rushing towards the restructuring of debts that may be invalid.[130]

129 Fitch Rating (n 7).

130 Postscript: A settlement agreement had been reached between Credit Suisse and regulatory authorities in Switzerland, the United Kingdom and the United States after this contribution had been finalized. In terms of the settlement agreement, Credit Suisse will pay large fines to these regulators and also forgive debts owed by Mozambique in the amount of $200 million. However, this settlement agreement was aimed at avoiding criminal liability on the part of Credit Suisse and does not resolve the ongoing civil litigation in the UK courts or the arbitral proceedings in Switzerland.

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11 Sovereign debt restructuring in Zambia: A United Nations principles-based approach?

Sangwani Patrick Ng'ambi

11.1 Introduction

Zambia's debt has risen dramatically over the past decade.[1] Whereas Zambia's total debt stood at US $3,5 billion in 2011, it rose considerably to US $14,4 billion in March 2018. These alarming debt levels led to a declaration by the International Monetary Fund (IMF) to the effect that Zambia was at high risk of debt distress.[2]

Zambia had previously benefited from the heavily indebted poor countries (HIPC) debt relief in 2005, which cancelled virtually all external debt.[3] For a time, debt remained low and government spending was relatively conservative. However, it has borrowed heavily since 2012 for important infrastructure in roads, energy, railways and telecommunications.[4] It also used other loans to cover budget deficits.[5] Although some of the loans for infrastructure had significant socio-economic benefits, others generated very few.[6]

China is the single biggest creditor.[7] However, Zambia has borrowed from others. These include development banks and the commercial Eurobond market. The loans obtained for projects from China are

1 See PA Ayinla & SF Folarin 'The politics of foreign aid: A study of China-Zambia economic relations' (2019) 7 *Covenant University Journal of Politics and International Affair* 76.

2 2019 Article IV Consultation – Press release; staff report; and statement by the executive director for Zambia (August 2019) IMF Country Report 19/263.

3 T Saungweme & NM Odhiambo 'The dynamics of public debt in Zambia: A critical review' (2018) 3 *Euro Economics* 47.

4 JC Servant 'China steps in as Zambia runs out of loan options' *The Guardian* (11 December 2019).

5 As above.

6 L Daka et al 'The impact of external debt on Zambia's economic growth: An ARDL approach' (2017) 8 *Journal of Economics and Sustainable Development* 55.

7 W Orr 'The curse of the white elephant: The pitfalls of Zambia's dependence on China' global risk insights' (1 December 2020), https://globalriskinsights.com/2020/12/the-curse-of-the-white-elephant-the-pitfalls-of-zambias-dependence-on-china/ (accessed 28 November 2021).

typically on a build-operate-transfer (BOT) basis. This essentially means that there is Chinese or joint management on specific models for specific projects. Examples of these include hydropower projects for the Zambia Electricity Supply Company (ZESCO), the digitalisation of the Zambia National Broadcasting Company (ZNBC) and two airports.[8]

The difficulty with this debt is that it has become a burden on the economy, with interest payments alone consuming a significant proportion of the national budget.[9] To contextualise this assertion, total domestic government revenue from taxes, fees and levies amounted to K39,2 billion in 2017. The interest payments rendered that year amounted to K9,8 billion.[10] Therefore, interest payments amounted to 25 per cent of the government's revenue.

Because there is limited transparency in Chinese lending and financial flows to Zambia, there is very little accurate data on the loan conditions as such. This is further compounded by the fact that the Chinese approach to finance creates incentives for kickbacks and inflated project costs, in turn leading to rent-seeking and cronyism. As pointed out by Foreign Policy Magazine: 'Opaque deals, reports of large-scale corruption and mismanagement, doubts about project feasibility, and a stark trade imbalance raise serious questions about how well African leaders are managing the opportunities they receive.'[11]

Zambia must take full responsibility for this debt crisis. This is owing to the fact that the Zambian government received ample warnings against the increasing debt burden from its own economists, the opposition and the external actors, such as the IMF and the World Bank.[12]

There are concerns about the levels of debt that Zambia has accumulated. Thus, it comes as no surprise that there is increasing attention on debt sustainability. The aim of this chapter is to give an overview of

8 A Ofstad & E Tjønneland 'Zambia's looming debt crisis – Is China to blame?' (2019) 1 *CMI Insight* 6-7.

9 See eg 2021 Budget Address by Dr Bwalya KE Ng'andu, MP, Minister of Finance, delivered to the National Assembly on Friday 25 September 2020 22, http://www.parliament.gov.zm/sites/default/files/images/publication_docs/2021_National_Budget_Speech.pdf (accessed 28 November 2021).

10 CUTS International *#DebtConcernsMe: Understanding the impact of Zambia's growing debt on different stakeholders* (2019) 5.

11 S Solomon & C Frechette 'Corruption is wasting Chinese money in Africa, foreign policy', https://foreignpolicy.com/2018/09/13/corruption-is-wasting-chinese-money-in-africa/ (accessed 28 November 2021).

12 See generally Ofstad & Tjønneland (n 8) 5.

the debt acquired by the Republic of Zambia and its impact. It advocates the restructuring of Zambian debt and examines the principles upon which such debt restructuring would be based. Part two of the chapter looks at the impact of the debt crisis on the Republic of Zambia. It is against this backdrop that debt restructuring would be necessitated. Part three then looks at the principles to be observed in accordance with the Basic Principles on Sovereign Debt Restructuring Processes, should the government of the Republic of Zambia elect to have its debt restructured.[13]

11.2 The impact of Zambia's debt crisis

Zambia's macro-economic position was a relatively healthy one in 2011. This was as a consequence of the high economic growth it had enjoyed since 2002 and a sound government budget. Regrettably, this economic growth did not translate to alleviating poverty and changing the lives of the majority. The Patriotic Front (PF) took over power from the Movement for Multiparty Democracy in 2011.[14] Their victory elicited high expectations of broader growth. As such, the PF responded to this by initiating a high number of infrastructure projects, including roads, airports in Lusaka and Ndola and hydropower plants.

Such ambitious plans necessitated the high levels of borrowing from the Eurobond market, multilateral banks and China, as well as other untraditional sources.[15] Cumulatively, the Eurobond amounts to US $3 billion and was borrowed at commercial rates. The government is due to commence with repayments in 2022.[16] The government of Zambia had also borrowed US $1,6 billion from multilateral banks such as the World Bank, the IMF and the African Development Fund.[17] It is estimated by the China Africa Research Initiative (CARI) at Johns Hopkins University that Zambia had accumulated loans totalling US $6,4 billion from China.[18] The Zambian government also borrowed from several non-Chinese sources. These included bilateral government loans, loans from fuel suppliers, the Arab Development Bank, Israeli sources and from commercial banks in the United Kingdom, Nigeria and South Africa. It is highly likely that

13 See United Nations General Assembly Resolution 69/319.

14 M Hinfelaar, O Kaaba & M Wahman 'Electoral turnovers and the disappointment of enduring presidential power: Constitution making in Zambia' (2020) 15 *Journal of Eastern African Studies* 63.

15 Ofstad and Tjønneland (n 8) 5.

16 As above.

17 As above.

18 China Africa Research Initiative (CARI) Loan Data, http://www.sais-cari.org/data (accessed 28 November 2021).

these loans have commercial market conditions attached to them.[19] This essentially means that they have higher interest rates and shorter time frames.[20]

Critics also contend that there may be hidden loans.[21] The lack of transparency around the accumulation of loans in general does little to abate this assertion. What we do know is that the high levels of debt have left Zambia in a rather precarious situation. The aim of this part is to examine some of the challenges emanating from Zambia's debt crisis. It is on this basis that debt restructuring is recommended.

11.2.1 National budget

It is evident that the high levels of debt have had an impact on the national budget. In September 2018 the Minister of Finance announced the national budget. External debt repayments amounted to K14,9 billion, while domestic debt repayment was K8,6 billion. Combined, this amounts to 27 per cent of the national budget. As such, debt repayments took up the largest portion of the national budget. To contextualise it, the amount allocated to debt servicing was equivalent to the total combined amount allocated for health, education and social protection.[22]

Debt repayments have since continued to increase. For example, in the 2020 national budget, external debt repayments increased to K21 billion, while domestic debt repayments amounted to K12,6 billion.[23] Furthermore, in the 2021 national budget it was announced that the government is to spend K18,3 billion on domestic debt interest and K27,7billion on external debt.[24]

Debt servicing has inevitably meant that there has been an attempt to broaden the tax base, introducing compliance initiatives and imposing new taxes. This is in order to ensure that the government increases its revenue

19 Ofstad & Tjønneland (n 8) 5.

20 As above.

21 As above.

22 2019 Budget Address by Margaret D Mwanakatwe, MP, Minister of Finance, delivered to the National Assembly on 28 September 2018 17, http://www.parliament.gov.zm/sites/default/files/images/publication_docs/Budget%20Speech%202019.pdf (accessed 28 November 2021).

23 2020 Budget Address by Dr Bwalya KE Ng'andu, MP, Minister of Finance, delivered to the National Assembly on 27 September 2019 17, http://www.parliament.gov.zm/sites/default/files/images/publication_docs/2020BUDGET-SPEECH.pdf (accessed November 28. 2021)

24 2021 Budget Address (n 9) 22.

to pay for public services and pay back its debt. The new initiatives include innovative ways of raising taxes and also the imposition of fees to raise revenues domestically and reduce its reliance on borrowing.

A number of taxes have been imposed. These include borehole tax and increased toll gate fees. In addition to this, there is also a proposed internet calling tax. Moreover, the government introduced a K0,30 excise duty on non-alcoholic drinks, increased the carbon emission surtax on vehicles and increased the charge on fees and fines. A national health insurance scheme has also been implemented, which is to be deducted as a percentage from citizens' income. This adds considerable financial pressure on Zambians.[25]

Most new fundraising initiatives have been targeted at the corporate sector and the mines in particular. However, it has been seen that taxes have also been targeted at ordinary Zambians. However, the timing could not be worse. This is owing to the fact that Zambians are already experiencing high inflation due to a depreciation of the kwacha. Higher taxes mean an increase in the cost of living. This in turn will push low-income earners further into poverty. Furthermore, aggregate economic growth will be reduced, as individuals will have less money for the consumption of goods and services.

11.2.2 Social spending

The fact that the Zambian government has to spend so much on debt servicing means that there is less money to invest in public services and in poverty-reduction initiatives. For example, education has suffered from a lack of funding. As it is, the teacher to pupil ratio in Zambia remains high. There is one teacher to every 60 pupils. Moreover, there is a lack of access to teaching aids and support infrastructure such as desks. In 2018, 29 per cent of domestic revenues went towards debt servicing, 42 per cent went to wages and salaries, while only 30 per cent of government revenues were spent on programmes that drive the country's development, such as health, education and agriculture.[26]

The health sector suffers from a lack of resources. For example, most rural clinics do not have medical doctors or support staff such as technologists, laboratory technicians and midwives. Moreover, support for farmers has fallen. This is due to a lack of extension officers. In some

25 CUTS International (n 10) 11.

26 CUTS International (n 10) 9.

areas the ratio of extension officers to farmers is as high as 1 to 1 200. This is three times the ideal ratio, which should be 1 to 400.[27]

A lack of investment in these areas consequently hinders development. This is owing to the fact that if Zambia is to prosper, the country needs a well-educated, healthy and productive populace. Without a good education system and quality health care, it means that the work force needed to develop the country will be less productive. It is thus evident that the lack of investment in these areas, caused by high debt servicing, is having an adverse effect on the development of the country.[28]

Consumers and businesses

The accumulation of debt has also had an adverse effect on the average Zambian consumer. Prices in Zambia are impacted by a plethora of factors. These include the cost of labour, the exchange rate and, indeed, taxes. There have been increases in the price of fuel and food. Although the country's debt levels are not the only driver behind these price increases, they certainly are a factor.[29]

There is a correlation between high debt levels and the stability of the Zambian kwacha.[30] As such, this will have an impact on the lives of consumers, through aspects such as inflation. Over the past few years the Zambian government has been issuing bonds. This essentially means that the government has been accepting loans in order to finance certain activities; while foreign investors expect to profit from this investment through interest repayments. Such investors base their decision to invest in a country upon several factors, including the host state's likelihood of defaulting on debt repayments. As such, foreign investors will look at the economy's immediate and long-term performance. Thus, they will look at the state's financial position, plans for managing debt and 'prospects for growth through documents such as the medium-term expenditure framework and budget'.[31]

Zambia's unsustainable debt levels have certainly been of concern to investors. This is evinced in the fact that Zambia's debt carries high interest rates and the fact that in September 2018 there was a drastic

27 As above.

28 As above.

29 CUTS International (n 10) 5.

30 See generally C Cheelo & T Banda 'A tightening balancing act: Economic implications of Zambia's balance of payments performance' Working Paper 24 (June 2017) 2.

31 CUTS International (n 10) 13.

reduction in investment in Zambian government bonds. The purchase of bonds by foreign investors typically involves converting foreign currency into Zambian kwacha. A drastic decrease in the purchase of bonds meant a decrease in demand for Zambian kwacha. Thus, it contributed to a depreciation of the kwacha by 20 per cent from K9 to K12 per dollar in the month of September 2018.[32]

Zambia relies rather heavily on imported goods. With a weakened currency, this meant that importing goods became expensive. Given this fact, all imported goods became more expensive. Moreover, the increase in the price of fuel, driven primarily by an increase in world oil prices, was further exacerbated by the weakened currency. The fact that there have been tax increases, and a weakened currency, means that businesses will have to pass on any additional costs of doing business to the consumer. As such, it is evident that Zambia's debt situation has had an adverse impact on the everyday lives of consumers.

This is further compounded by the fact that the debt levels have created a difficult environment for business to operate in. The depreciation of the kwacha means that businesses suffer from higher costs of inputs such as fuel and other imported goods. This means that running a business becomes more expensive. In addition to this, inflation reduces the demand for goods and services, in an economy where the incomes of ordinary Zambian citizens are already strained. This is further compounded by a generally weak economy, which leads to reduced profits. Consequently, this could lead to job losses. This could lead to disastrous consequences as 90 per cent of employment in Zambia is generated by the private sector.[33]

It has been seen that Zambia's high accumulation of debt is not only unsustainable, but also has a huge impact on the growth of the economy in the immediate term. Debt servicing takes up a large part of the national budget. This essentially means that there is no money left for spending on sectors that contribute to the development of the country, including education, health care and agriculture. In addition to this, it has been seen that debt servicing has an impact on the national currency, which in turn leads to inflation. Such inflation also means that doing business in Zambia is rendered more onerous, which in turn leads to job losses. This is exacerbated by the fact that the government has to raise taxes not only to service debts but also to finance public services. These circumstances necessitate drastic measures on the part of the Zambian government. Such measures include debt restructuring. This is discussed in the next part.

32 As above.

33 As above.

11.3 The Basic Principles of Sovereign Debt Restructuring

The purpose behind sovereign debt restructuring is to 'restore the sustainability of public debt with high probability'.[34] During the nineteenth and early twentieth centuries sovereign debt restructuring relied mainly on consent-based negotiations.[35] Indeed, this was also the era of gunboat diplomacy.

At present there is no international mechanism on how sovereign debt restructuring is conducted *per se*. There were attempts by the IMF to establish a sovereign debt restructuring mechanism (SDRM).[36] However, this was opposed by the United States. It was also opposed by emerging market nations such as Turkey, Mexico and Brazil on the basis that it may raise interest rates on sovereign bonds.[37] There have since been further calls for some form of sovereign debt restructuring mechanism through various frameworks.[38] An example of this is the Basic Principles on Sovereign Debt Restructuring Processes propounded in General Assembly Resolution 69/319, adopted on 10 September 2015.[39] Indeed, even a model law has been proposed.[40]

Thus, for the time being at least, a multilateral statutory framework for the resolution of debt crises is not feasible. However, the United Nations Basic Principles of Sovereign Debt Restructuring may provide a valuable basis for the stages of the debt-restructuring process.[41] This part looks at

34 M Guzman & JE Stiglitz *A soft law mechanism of sovereign debt restructuring: Based on the UN Principles* (2015) 3.

35 M Goldman 'Public and private authority in a global setting: The example of sovereign debt restructuring' (2019) 25 *Indiana Journal of Global Legal Studies* 341.

36 SL Schwarcz 'Sovereign debt restructuring: A model-law approach' (2016) *Journal of Globalization and Development* 9, https://scholarship.law.duke.edu/faculty_scholarship/3492 (accessed November 28. 2021)

37 As above.

38 M Guzman & JE Stiglitz 'Creating a framework for sovereign debt restructuring that works' in M Guzman, JA Ocampo & JE Stiglitz (eds) *Too little, too late: The quest to resolve sovereign debt crises* (2016) 3. See also SL Schwarcz, '"Idiot's guide" to sovereign debt restructuring' (2004) 53 *Emory Law Journal* 1215.

39 A/69/L.84.

40 See eg SL Schwarcz 'Sovereign debt restructuring and English governing law' (2017) 12 *Brooklyn Journal of Corporate, Financial and Commercial Law* 73.

41 See also J Rossi 'Sovereign debt restructuring, national development and human rights' (2016) 13 *SUR* 192, https://ssrn.com/abstract=2838329 (accessed 28 November 2021)..

these principles and their status under international law. Thereafter, we look at their potential application in the case of Zambia.

11.3.1 The Basic Principles of Sovereign Debt Restructuring

The Basic Principles on Sovereign Debt Restructuring processes consist of nine principles by which sovereign debt restructurings should be guided.[42] These are sovereignty; good faith; transparency; impartiality; equitable treatment; sovereign immunity; legitimacy; sustainability; and majority restructuring. These are looked at in turn below and can certainly be the basis of a Zambian debt restructuring.

Sovereignty

One of the first principles espoused under the Basic Principles on Sovereign Debt Restructuring processes is that of sovereignty. As such, GA Resolution 69/319 provides that a state has the right to design its macro-economic policy. This includes the qualified right to restructure its sovereign debt.[43] Such a right should not be frustrated or impeded by any abusive measures. It further provides that restructuring 'should be done as the last resort and preserving at the outset creditors' rights'. Therefore, it is to be a measure of last resort and states must conduct the restructuring process, with an eye to preserving creditors' rights.

Good faith

The second principle is that of good faith. Therefore, good faith must be observed by both the sovereign state and all its creditors. Debtors who initiate the negotiation process have a duty to do so in good faith. A question that may arise is whether the repudiation of a debt or debt payment suspension would violate the good faith principle. The Resolution provides:

> Good faith by both the sovereign debtor and all its creditors would entail their engagement in constructive sovereign debt restructuring workout negotiations and other stages of the process with the aim of a prompt and durable re-establishment of debt sustainability and debt servicing, as well as achieving

42 V Paliouras 'The right to restructure sovereign debt' (2017) 20 *Journal of International Economic Law* 120.

43 See generally Paliouras (n 42) 115-136.

the support of a critical mass of creditors through a constructive dialogue regarding the restructuring terms.

The conclusion of Argentina's 15-year stand-off with the majority of its holdout creditors in April 2015 has largely been attributed to the fact that negotiations were conducted in good faith.[44] Negotiations conducted in good faith by both the Zambian government and its creditors can certainly be a factor that will contribute to the steady conclusion of a potential debt restructuring process.

Transparency

The Resolution further provides that transparency between the debtor, creditor and other stakeholders should be promoted. This is in order to enhance the accountability of the actors concerned. The Resolution provides that this can be accomplished through the timely sharing of information related to the process of sovereign debt restructuring with interested stakeholders, including the public at large. This is particularly critical for a country such as Zambia, where the process of debt acquisition has sometimes been criticised as opaque. It thus is important that the process of debt restructuring is undertaken in a manner that ensures that the public is kept well informed.

Impartiality

Yet another principle espoused under the GA Resolution is that of impartiality. In general terms impartiality is defined as 'a way of thinking, decision-making or acting that is free of bias or preference and that is grounded in independence and objectivity'.[45] Not only should actors conduct themselves in a manner that is objective and independent, but they should also be seen to do so.[46]

All institutions and actors involved in the sovereign debt restructuring process are to 'enjoy independence and refrain from exercising any undue influence over the process and other stakeholder'. They should further refrain from engaging in actions that would lead to a conflict of interest or corruption, or indeed both.

44 K Erichsen & A Wilkinson 'Sovereign debt restructuring: What can we learn from Argentina, Greece and Ukraine?' (2016) 7 *Journal of International Banking and Financial Law* 1.

45 O Lienau 'Legitimacy and impartiality as basic principles for debt restructuring' (2016) 41 *Yale Journal of International Law Online* 107.

46 Lienau (n 45) 108.

Thus, in order to maximise institutional impartiality, actors must allow institutional independence. This is even more important, given the fact that debtors and creditors are clearly interested parties. Therefore, organisations and mechanisms involved must minimise their affiliation with groups or actors that might be affected by the process of restructuring. As such, there must be attentiveness to financial independence, personnel independence and physical independence, which can be accomplished through geographic location in a neutral setting.[47] Decision makers must also remain independent of the negotiating parties

Equitable treatment

States are also required to observe the tenets of equitable treatment. Therefore, states must refrain from arbitrarily discriminating against creditors. The only exception to this rule is if different treatment is justified under the law, is reasonable and is 'correlated to the characteristics of the credit, guaranteeing inter-creditor equality, discussed among creditors'. Under this principle, creditors have the right to receive treatment that is commensurate to their credit and its characteristics. Moreover, it provides that no creditors are to be excluded *ex ante* from the sovereign debt restructuring process.

Sovereign immunity

One of the most critical principles espoused is that of sovereign immunity. This implies that the validity of any sovereign debt contract is subject to the very fundamental principle under international law, namely, that no nation can renounce its sovereign immunity.[48] The principles provide that sovereign immunity from jurisdiction and execution regarding sovereign debt restructuring is a right of states. Any exceptions to this rule are to be applied restrictively.

Under the principle of sovereign immunity, there is also a limit as to the extent to which a democratic government can bind its successors.[49] Although the principle does not rule out the possibility of the issuing of debt under foreign law, there is a limit on the reach of foreign law. This limits the reach of foreign jurisdictions during the process of restructuring sovereign debt.[50] Therefore, it reaffirms the limitations of foreign jurisdictions in the process of debt restructuring.

47 As above.

48 Guzman and Stiglitz (n 34) 6.

49 As above.

50 As above.

Legitimacy

Legitimacy is also important. This is due to the fact that if a rule or mechanism is perceived as legitimate, then parties are more likely to approve or comply with it on that basis, rather than other reasons such as coercion or self-interest.[51] The principles thus provide that

> [l]egitimacy entails that the establishment of institutions and the operations related to sovereign debt restructuring workouts respect requirements of inclusiveness and the rule of law, at all levels. The terms and conditions of the original contracts should remain valid until such time as they are modified by a restructuring agreement.

There are circumstances under which a debt restructuring will lack legitimacy. For example, a debt restructuring under force of arms would lack legitimacy. So would one conducted under the threat of economic sanctions. It is argued, for example, that Argentina's 2016 debt restructuring arguably lacks legitimacy, because of Judge Griesa's ruling which effectively precluded Argentina from accessing international credit markets.[52] Furthermore, any debt restructuring that results in a country violating its own constitution or the UN Declaration of Human Rights would also lack legitimacy.[53] Thus, any economic or military threats on Zambia may negate the debt restructuring process. This may also apply in the event that Zambia violates its own Constitution. Therefore, the government would have an obligation to engage the national assembly in any debt-restructuring process, as it is their constitutional prerogative to oversee executive functions in this respect.[54]

Sustainability

Sustainability is another principle emanating from GA Resolution 69/319. This entails that the process of sovereign debt restructuring is completed in a timely and efficient manner. It should also lead to a stable debt situation in the debtor state. There must also be a balance between preserving creditors' rights, while promoting sustained and economic growth and development. Furthermore, sustainability entails 'minimising economic and social costs, warranting the stability of the international

51 CA Thomas 'The uses and abuses of legitimacy in international law' (2014) 34 *Oxford Journal of Legal Studies* 729.

52 Guzman & Stiglitz (n 34) 7.

53 As above.

54 See art 63(2) of the Constitution of Zambia (as amended by Act 2 of 2016).

financial system and respecting human rights'. Indeed, this is easy to assert but difficult to apply.

Sustainability is one of the most emphasised principles of these resolutions.[55] Not only is this Resolution concerned with debt sustainability but with issues such as inclusive economic growth, sustainable development and respect for human rights. In this sense, the Resolution is holistic and considers the long-term impact on social and economic welfare of those in the debtor state.[56]

The IMF's definition of sustainability certainly is compatible with this provision of the Basic Principles, even though it has been described as being 'in purely financial terms'.[57] The IMF defines debt sustainability as 'a situation in which the borrower is expected to be able to continue servicing its debts without unrealistically large future correction to the balance of income and expenditure'.[58] The IMF has also developed a formal framework for conducting public and external debt sustainability analyses (DSAs) as a means through which to detect, prevent, and resolve potential crises.[59]

The IMF's definition of sustainability has two components. The first is that a debtor state cannot indefinitely accumulate debts faster than its capacity to service them.[60] A state should thus be prevented from accumulating more debt than it is able to pay. The second element is that the servicing of debts should not be contingent upon an 'unrealistically large future correction to the balance of income and expenditure'.[61] This would imply that there are indeed social and political limits to debt adjustments.[62] Given the fact that the IMF recognises the social

55 See also Rossi (n 41) 192.

56 MPT Sison 'Sustainability in indebtedness: A proposal for a treaty-based framework in sovereign debt restructuring, accounting and finance – New perspectives on banking, financial statements and reporting, Reza Gharoie Ahangar & Can Öztürk, IntechOpen, DOI: 10.5772/intechopen.82470.

57 JP Bohoslavsky & M Goldmann 'An incremental approach to sovereign debt restructuring: Sovereign debt sustainability as a principle of public international law' (2016) 41 *Yale Journal of International Law Online* 25.

58 IMF 'Assessing sustainability' IMF Policy Paper (28 May 2002).

59 Debt Sustainability Analysis, https://www.imf.org/external/pubs/ft/dsa/ (accessed 28 November 2021).

60 U Das, M Papaioannou M & C Trebesch 'Sovereign debt restructurings: Concepts, literature survey, and stylised facts' IMF Working Paper WP/12/203 (August 2012) 71.

61 IMF (n 58).

62 Das et al (n 60) 71.

and political limits to adjustment policies, it could be argued that this definition is congruous with that of the UN Basic Principles, in that the latter emphasises economic growth and sustainable development.

Sustainability will be a key principle to be observed in the event that Zambia elects to restructure its debt. Not only is it a key feature of the UN Basic Principles, but it is also compatible with the IMF's definition, in that the latter certainly acknowledges that there are social and political limits to debt adjustment. Thus, debt restructuring will have to be conducted with an eye to its impact on socio-economic and human rights aspects while, of course, balancing that with the rights of creditors.

Majority structuring

Another principle espoused under the UN Basic Principles is that of majority structuring. This is one of the elementary principles of any insolvency or bankruptcy procedure, which entails that if the results of a sovereign debt renegotiation is approved by 'a qualified majority', the rest of the bondholders must acquiesce.[63] As such, the UN Basic Principles state:

> Majority restructuring implies that sovereign debt restructuring agreements that are approved by a qualified majority of the creditors of a state are not to be affected, jeopardised or otherwise impeded by other states or a non-representative minority of creditors, who must respect the decisions adopted by the majority of the creditors. States should be encouraged to include collective action clauses in their sovereign debt to be issued.

This principle will be advantageous to a country such as the Republic of Zambia, as it effectively operates as a shield against hold-out strategies, such as those that have been successfully pursued by vulture funds. Once there is a qualified majority that has made a decision, minority creditors will be bound by it.

11.3.2 Status of General Assembly Resolutions

The Basic Principles on Sovereign Debt Restructuring processes stem from a General Assembly resolution. Therefore, there may be questions as to whether the principles espoused therein are binding. On the one hand, it is contended that General Assembly resolutions are not binding and are simply a form of soft law that expresses the view of the majority of UN

63 See also Rossi (n 41) 192.

member states.[64] Under this school of thought, it certainly is recognised that the General Assembly of the UN possesses quasi-legislative functions.[65] Despite this fact, the General Assembly is not actually a legislative organ.[66] This is so, first, because there is an objection to a two-thirds majority binding the minority. Second, binding states under General Assembly resolutions may circumvent the traditional treaty-making process which requires ratification in order for the state to be bound, under some national constitutions.[67]

However, completely disregarding the principles espoused under General Assembly resolutions would be erroneous. This is due to the fact that there are general procedures that lead to the vote and adoption of a resolution, which in turn constitute evidence of customary international law.[68] A customary rule 'comes into existence only where there are acts of state in conformity with it, coupled with the belief that those acts are required by international law'.[69]

The General Assembly itself is a vehicle through which states form and express the practice of international law. As such, the resolutions emanating therefrom become customary norms.[70] Resolutions are drafted in a manner that ensures that they can win the support of the majority of the Assembly. Prior to a vote being called, more than a bare majority must typically be ensured.[71] Such a resolution will typically represent a harmonisation of the conflicting views that might have been expressed, before the vote is called.[72] Thus, by the time a General Assembly resolution is adopted, it represents an expression of the views of the general consensus. This in turn may be construed as the formulation of a norm under customary international law.[73]

64 See generally J Crawford *The creation of states in international law* (2006) 113; A Boyle & C Chinkin *The making of international law* (2007) 116; GJ Kerwin 'The role of United Nations General Assembly resolutions in determining principles of international law in United States courts' (1983) 4 *Duke Law Journal* 876.

65 P Sands & P Klein *Bowett's law of international institutions* (2009) 28.

66 As above.

67 As above.

68 Sands & Klein (n 65) 27-28.

69 SA Bleicher 'The legal significance of re-citation of General Assembly resolutions' (1969) 63 *American Journal of International Law* 449.

70 M Sornarajah *The international law on foreign investment* (2010) 446.

71 Bleicher (n 69) 451.

72 As above..

73 As above.

As such, this chapter advances that the Basic Principles on Sovereign Debt Restructuring processes is an expression of the general consensus. This is due to the process involved in drafting the resolution, and the harmonisation of conflicting views that might be expressed before the vote is called. Given this fact, it is contended that the Basic Principles on Sovereign Debt Restructuring processes, just like previous United Nations General Assembly resolutions, may be construed as part of customary international law.

11.4 Conclusion

It could thus be concluded that Zambia's debt has indeed radically increased in the past ten years. The failure to sustain this debt has inevitably had an adverse effect on the Zambian economy. This is particularly evident in the areas of social spending, the national budget, the rise in prices, and business and employment. This chapter has advocated that sovereign debt restructuring be the avenue adopted by the government of Zambia.

One key international instrument governing sovereign debt restructuring is the Basic Principles on Sovereign Debt Restructuring processes, which emanate from General Assembly Resolution 69/319. There is debate surrounding the binding nature of a General Assembly resolution under international law. This chapter advances the view that General Assembly resolutions are evidence of state practice. For this reason, General Assembly Resolution 69 becomes a part of customary international law. As such, these principles are legitimate principles under international law and, therefore, are principles to be observed, in the event that the Republic of Zambia chooses to exercise its sovereign right to restructure its debt.

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12 Steeling for the next pandemic through fiscal responsibility: The Bank of Namibia as fiscal council

*Dunia P Zongwe**

12.1 Introduction

If you are tempted to think that nothing could be worse than the unfolding COVID-19 pandemic, think again. Even before the COVID-19 pandemic broke out, some experts had predicted that the future has several global pandemics in store.[1] The fact that 25 heads of state clamoured for a multilateral treaty for 'pandemic preparedness and response'[2] reveals that some leaders are now making the same predictions.

Similarly, in light of the ongoing COVID-19 pandemic and those in the future, this chapter mounts a fiscal responsibility framework to enable developing countries, Namibia in particular, to strike the delicate balance between easing short-term liquidity crises and preserving their country's long-term development. This pandemic has created manifold pandemonium, affecting the economy, the healthcare system, and state finances. Hence, this public health nightmare has set the stage for upheaval and bitter strife within society.

* I owe deep gratitude to Daniel Bradlow, Magalie Masamba, Walter Ochieng, and anonymous reviewers for commenting on drafts of my chapter. I am also hugely indebted to James T Gathii and Barry Herman for sharing their time and thoughts on my research on 19 November 2020 during the Interdisciplinary Virtual Conference entitled 'Sovereign Debt Management and Renegotiation in Africa: A SADC Perspective', hosted by the University of Pretoria. Errors are mine, so is the responsibility – fiscal and otherwise – for these.

1 See R Preston *Crisis in the red zone: The story of the deadliest Ebola outbreak in history, and of the outbreaks to come* (2019); S Shah *Pandemic: Tracking contagions, from cholera to Ebola and beyond* (2016) (submitting that civilisation has carried along many new pathogens – a situation that has led many researchers to predict a new pandemic); D Quammen *Spillover: Animal infections and the next human pandemic* (2012).

2 World Health Organisation 'Global leaders unite in urgent call for international pandemic treaty' (30 March 2021), https://www.who.int/news/item/30-03-2021-global-leaders-unite-in-urgent-call-for-international-pandemic-treaty (accessed 30 April 2021).

Inexorably, most governments will have to borrow money if they genuinely wish to pull through COVID-19, the world's worst economic crisis since the Great Depression. On the African continent, the most industrialised nation, South Africa, had to resort to emergency funding from the International Monetary Fund (IMF),[3] and so did its western neighbour, Namibia.[4] In fact, several affected countries have received funds from the IMF.[5]

Disasters such as the latest coronavirus cause government spending to shoot up. The authorities need to spend huge sums to engage in relief activities, recover losses suffered or repair damage caused, and shore up the economy. Crucially, however, disasters tend to push up public debt to unsustainable levels.[6]

While economists and economically-oriented lawyers spoke about this thorny dilemma, the legal literature has remained silent as to how developing countries could use or tweak their laws to tackle this singular and multi-faceted crisis. In a related vein, no one seems to have studied the possibility of modifying budget system laws in order to face the crisis.

The time is opportune to ponder on budget system laws in developing countries and reflect on how governments can adapt to suit the unique and uncertain circumstances brought about by the COVID-19 pandemic and the ensuing Great Lockdown. This holds especially true given the evidence that this pandemic may be one only of several pandemics to come.

Accordingly, this chapter seeks to resolve this trade-off between emergency liquidity and long-term solvency by exploring the possibility of

3 International Monetary Fund 'IMF executive board approves US $4,3 billion in emergency support to South Africa to address the COVID-19 pandemic' (27 July 2020), https://www.imf.org/en/News/Articles/2020/07/27/pr20271-south-africa-imf-executive-board-approves-us-billion-emergency-support-covid-19-pandemic (accessed 15 June 2021).

4 International Monetary Fund 'IMF executive board approves US $270,83 million disbursement to Namibia to address the COVID-19 pandemic' (31 March 2021), https://www.imf.org/en/News/Articles/2021/04/01/pr2195-namibia-imf-executive-board-approves-disbursement-to-address-covid-19-pandemic (accessed 15 June 2021).

5 For an overview of the lending and debt service relief financed by the International Monetary Fund (IMF), see International Monetary Fund 'COVID-19 financial assistance and debt service relief' (27 May 2021), https://www.imf.org/en/Topics/imf-and-covid19/COVID-Lending-Tracker (accessed 15 June 2021).

6 See E Borensztein et al 'Debt sustainability under catastrophic risk: The case for government budget insurance' (2007) Inter-American Development Bank Working Paper 607 4 (observing that disasters increase government debt and the risk that the debt reaches unsustainable levels).

enacting fiscal responsibility laws. To help policy makers juggle between these two diametrically-opposed poles, I have divided the substance of this chapter in five parts. The first part looks at the COVID-19 pandemic that forms the context of this chapter, focusing on its effects on Namibia's fiscus. The second part presents the core dilemma that has ensnared developing countries, namely, the uneasy balancing act that consists in defusing the present liquidity crises while ensuring long-term growth and development.

Third, the chapter analyses best practices around the globe in budget system laws to gain insights about the broad policy directions that responsible governments take when facing major economic shocks, such as the Great Depression in the 1930s,[7] the Great Recession in 2007-2009, and the unfolding Great Lockdown. In this part I also sketch Namibia's budget system laws before affirming that Namibia lacks any legal framework for fiscal responsibility. Next, by relying on those best practices, the chapter outlines the framework for a fiscal responsibility law (FRL) that a developing country such as Namibia could pass to safeguard debt sustainability.

Subsequently, the chapter assesses the FRL outlined in the previous part. I advance the thesis that, as it currently stands, Namibia's legal system can most effectively balance the liquidity-strategy dilemma by enabling the Bank of Namibia, the central bank, to act as a fiscal council. The Southern African Development Community (SADC) appears to have carved out that role for central banks in the region. In 2009 SADC adopted a model law[8] that Namibia utilised to enact a new law in 2020 which makes it possible for the central bank to act as a fiscal council.[9] In that capacity, the Bank of Namibia can guide the government in fixing the appropriate level of public debt that Namibia can take on. This level strikes a balance between the two poles of the dilemma mentioned above – a dilemma that pits short-term emergency against long-term strategy. I round off this chapter with brief remarks.

12.2 The context of the (next) global pandemic(s)

The latest coronavirus pandemic is not the first outbreak of this kind. For example, the SARS preceded COVID-19. From 2002 to 2004, that severe acute respiratory syndrome (SARS) pandemic erupted in China, spread to other Asian countries and to several other countries (including Canada

7 The Great Depression lasted from 1929 to 1939.

8 See SADC Central Bank Model Law 2009.

9 See Bank of Namibia Act 1 of 2020.

and the United Kingdom), claiming the lives of 774 people.[10] However, what sets this latest coronavirus outbreak miles away from its predecessors relates to its wide sweep. None of the earlier coronavirus outbreaks[11] had led to both contagion and economic recession worldwide. Fortunately, COVID-19 remains far behind the devastating toll of the Black Death, which broke out in the fourteenth century and killed at least 75 million people.[12]

The COVID-19 pandemic has given headaches not only to the peoples it infected, but also to the policy makers and the governments tasked with protecting those peoples. The proper policy response calls for targeted measures in matters concerning the country's constitution, the economy, the budget, public health systems, society, and the security apparatus.[13] However, even if it touches on how COVID-19 has affected some of these facets of national life, this chapter mostly focuses on the budgetary policy responses that the government can or should mount against this global pandemic.

12.2.1 Pandemics and pandemonium

Like SARS or the avian flu, global pandemics drastically disrupt international trade, and severely affect the world economy and the national budgets of individual countries. In Namibia the government announced that it would borrow an extra 40 billion Namibian dollars (that is, ZAR 40 billion) over three years to deal with the liquidity and monetary crises brought about by the COVID-19 pandemic.[14] Borrowing such a huge amount would push up the country's public debt to its highest level since Namibia achieved statehood in March 1990.

10 NHS 'SARS (severe acute respiratory syndrome)' (24 October 2019), https://www.nhs.uk/conditions/sars/ (accessed 24 January 2021).

11 Note that although the Spanish flu caused a pandemic in 1918 that spread around the globe, the 1918 virus (ie, Influenza A Subtype H1N1) differs from coronaviruses generally and the latest coronavirus (ie, SARS-CoV-2). Furthermore, the 1918 virus descends from a family of viruses that differs from the family to which SARS-CoV-2 belongs.

12 See MS Rosenwald 'History's deadliest pandemics, from ancient Rome to modern America' *The Washington Post* (7 April 2020), https://www.washingtonpost.com/graphics/2020/local/retropolis/coronavirus-deadliest-pandemics/ (accessed 24 January 2021).

13 For a rundown of anti-COVID-19 policy responses around the globe, see the IMF policy tracker: International Monetary Fund 'Policy responses to COVID-19', https://www.imf.org/en/Topics/imf-and-covid19/Policy-Responses-to-COVID-19 (accessed 29 April 2021).

14 See L Amukeshe 'Govt in deeper debt ditch' *The Namibian* (21 October 2020) 1.

COVID-19 represents an elusive worst-case scenario: The fiscal position of the government worsens as revenue drops and as the crisis induces the government to spend more to assist citizens and businesses; inflation then edges up;[15] and the trade balance deteriorates as the crisis hampers exporting capacity while imports go up, which exerts pressure on the exchange rate, prompting investors' concerns about the government's ability to repay public debt.[16] In Namibia the COVID-19 pandemic added to the pre-existing worst economic recession since independence and to revelations about the 'Fishrot Files',[17] arguably the country's ugliest corruption scandal.

As this nightmare scenario unfolds, many businesses, such as the state-owned national carrier Air Namibia, close down and lay off workers, resulting in the government losing substantial tax revenue. These losses leave the government with little to no room for manoeuvre through the budget. This reduced fiscal space leads to far-reaching consequences, as governments run short of money to spend on social services, among others, which often sparks disenchantment, discontent, upheaval and pandemonium.

Repairing or reconstructing what disasters have damaged or destroyed widen budget deficits over several budget cycles.[18] Similarly, experts fear that this global pandemic will dim the growth prospects of developing countries for several years to come, as they crumble under the weight of much heavier debt burdens. For instance, Namibia is expected to pay at

15 See MB Reinsdorf 'COVID-19 and the CPI: Is inflation underestimated?' (2020) International Monetary Fund Working Paper WP/10/248 13 (showing that, during the height of the pandemic, true inflation rose higher than what the consumer price index recorded in almost all regions). See also C Öner 'Inflation: Prices on the rise' (2017) *Finance and Development* 31 (explaining that inflation results when, among others, the government raises spending and the ensuing rise in demand outstrips an economy's production capacity).

16 Borensztein et al (n 6) 6.

17 The ongoing 'Fishrot' scandal is a kickback scheme that implicates prominent ministers (ie, the Justice Minister and the Fisheries Minister), business people, lawyers and their firms, and senior members of government and the ruling SWAPO party in Namibia as well as powerful fishing interests in Iceland. The scandal broke on the front pages of newspapers in November 2019 before the general and legislative elections took place in Namibia that same month. See eg J Kleinfeld 'Namibian president caught in new fishing corruption allegations' *Al Jazeera* (2 April 2021), https://www.aljazeera.com/news/2021/4/2/namibian-president-caught-in-new-fishing-corruption-allegations (accessed 29 April 2021).

18 See Borensztein et al (n 6) 5 (explaining that expenditures associated with those storms that hit Belize in 2000 and 2001 increased budget deficits and took three fiscal cycles).

least 35 billion Namibian dollars over the next three years only to cover debt interest.[19]

The consequences of a global pandemic for the economy and state finances can span an entire decade. In the Global South, like the Global North, the COVID-19 pandemic has decimated public finances; the pandemic's fiscal fallout and the ensuing chaos will be keenly felt in the next decade, whether or not medical researchers or pharmaceutical companies develop effective vaccines or start more effective treatments for the disease. Developing countries, in particular, will struggle to recover from the deterioration of their finances and may watch powerlessly as their population, especially the youth, live through a 'lost decade' – a long period of mass unemployment and low growth caused by duties to repay the large debts at the detriment of spending in key sectors, such as social services, health and education.

12.2.2 The fiscal fallout of COVID-19: The Namibian experience

According to Mwinga et al, Namibia has been 'sleepwalking its way into troublesome debt-to-gross domestic product (GDP) ratios'.[20] Since independence the debt-to-GDP ratio shot up, from 7 per cent in 1990/91 to 45 per cent in 2018/2019.[21] Even before the onset of the COVID-19 pandemic, the IMF had projected that Namibia's debt-to-GDP ratio would jump from 39,9 per cent in 2015 to 56 per cent in 2024. Now, with the emergency borrowing necessitated by the pandemic, Namibia has already surpassed the projected 2024 ratio.[22] In October 2020 the Finance Minister estimated public debt at 68,8 per cent of GDP.[23] Running parallel, the cost of servicing this public debt has ballooned from 2 per cent of government revenue (that is, 200 million N$/Rand) in 1990/1991 to 11 per cent of revenue (that is, 6,5 billion N$/Rand).[24]

19 Amukeshe (n 14) 1.

20 M Mwinga et al *Namibia: Fiscal policy analysis* (2019) 22.

21 As above.

22 International Monetary Fund *Namibia: Staff report for the 2019 Article IV consultation* (2019) 31.

23 Ipumbu Shiimi, Minister of Finance 'FY2020/2021 Mid-Year Budget Review and Medium Term Budget Policy Statement', https://mof.gov.na/documents/35641/36583/2020_21+Mid-Year+Budget+Review+and+Medium-Term+Policy+Statement+.pdf/7bade6a3-7108-f792-d0f2-6a534fda937c (accessed 8 March 2021).

24 Mwinga et al (n 20) 25.

That said, Namibia's debt-to-GDP ratio of 45 per cent compares favourably with the ratios of most African countries. In 2019 the debt-to-GDP ratio averaged 48,2 per cent in sub-Saharan Africa, 56,3 per cent in SADC, and 54,9 per cent in the Southern African Customs Union (SACU).[25]

In July 2020 Namibia approached the IMF for a loan of 4,5 billion N$/Rand (about 273 million US dollars). In requesting the IMF for a loan, the Namibian government sought to fund heightened spending due to the COVID-19 pandemic.[26] In the 2020/2021 mid-term budget review tabled in Parliament by Finance Minister Iipumbu Shiimi, the government plans to borrow 40 billion N$/Rand in the next three years, pushing up the country's debt burden to 158 billion N$/Rand.[27] Over the same period, the government will pay at least 35 billion N$/Rand in interest payments only.[28]

The pandemic leaves the Namibian government with no choice than to borrow. The government must now trade off a long-term strategy against short-term stability. The next part shows how this dilemma plays out.

12.3 Short-term liquidity versus debt sustainability

Policy experts can barely imagine a central bank doubling as a fiscal council, even if the existing economic and legal literature on fiscal responsibility, debt sustainability, and catastrophes opens up vistas of possibilities and worlds of alternative policy responses. That literature has not yet seriously mooted the possibility of a 'fiscal' central bank, but I hope that this chapter will allow policy makers to start imagining such a central bank – a bank that enables the government that it advises to become much better at managing the core issue: the delicate balance between short-term liquidity and long-term development strategy.

12.3.1 A delicate balance

Seemingly, to come to grips with the COVID-19 pandemic, governments in Africa and the rest of the planet will not avoid contracting heavier debt burdens. Müller et al predict that during downturns, both left-leaning and

25 Mwinga et al (n 20) 26.

26 L Amukeshe 'IMF still sitting on N$ 4,5 billion loan request' *The Namibian* (2 December 2020) 13.

27 Amukeshe (n 14) 1.

28 As above.

right-leaning governments will take on more debt.[29] Using a dynamic stochastic general equilibrium (DSGE) model, they show that fiscal policy swings between left-leaning governments (which favour public goods) and right-leaning governments (which favour private consumption). They also predict and test their predictions that left-leaning governments will increase taxation and government expenditures, and decrease debt, except during downturns.[30] Conversely, right-leaning governments will decrease taxation and expenditures, and increase debt.[31] These tested predictions contradict the rhetoric of recent debates which typically present left-leaning governments as caring less for fiscal responsibility.[32]

These findings, though they relied on data from the United States (US) and countries belonging to the Organisation for Economic Cooperation and Development (OECD), predict that the left-leaning SWAPO-led[33] government or any right-leaning government would increase Namibia's debt burden.

In sum, governments should not sacrifice tomorrow for today, and to do so, they must maintain a certain balance. That balance proves delicate because it carries the risk of default. Along with default comes the risk of debt restructuring. Indeed, if a government borrows money beyond a certain threshold, it shortens the odds that the government will default on its debt.

12.3.2 Easing short-term liquidity crises

The COVID-19 pandemic brings about crises of several sorts. Crucially, liquidity shortfalls count among the series of crises that the government has to handle. These cash flow problems require rapid relief, typically in the form of debt. This is precisely what led the government of Namibia to decide last year that, for the first time in its history as an independent state, it will borrow money from the IMF. Criticisms stung scathingly.[34]

29 A Müller, K Storesletten & F Zilibotti 'The political colour of fiscal responsibility' (2015) 14 *Journal of the European Economic Association* 252.

30 Müller (n 29) 288-289.

31 As above.

32 Müller et al (n 29) 289.

33 Since independence the South West Africa People's Organisation (SWAPO) has been the ruling political party in Namibia.

34 E Brandt 'PDM labels IMF loan as "rent-seeking"… Says money will disappear in bottomless pit' *New Era* (4 August 2020), https://neweralive.na/posts/pdm-labels-imf-loan-as-rent-seekingsays-money-will-disappear-in-bottomless-pit (accessed 25 August 2020); J Heita 'We don't need an IMF loan – Nico Smit' *Eagle FM* (3 August 2020), https://www.eaglefm.com.na/news/we-dont-need-an-imf-loan-nico-smit/ (accessed

A prominent member of the ruling party and a former Prime Minister, Nahas Angula, argued that Namibia can simply not afford the IMF loan worth US $273 million(about ZAR 4,5 billion).[35]

On 31 March 2021 the IMF approved the "outright purchase" of special drawing rights (SDR) 191,1 million (about US $270,83 million and about ZAR 4,062 billion) to Namibia under the rapid financing instrument (RFI).[36] The IMF declared that it lent that financial assistance to Namibia to address 'urgent balance of payment and fiscal financing needs stemming from the COVID-19 pandemic' and to 'mitigate the severe socio-economic impact of the pandemic'.[37] For the international lender, disbursing this finance enables Namibia to respond to the pandemic, including the purchase of vaccines and the deployment of the vaccine campaign.[38]

The RFI has a maturity of five years.[39] Over this period the interest rate that the IMF is charging Namibia for the RFI will vary.[40] The rate starts at 1,04 per cent for the year 2021, continues at 2,07 per cent for 2022 and 2023, drops to 1,97 per cent for 2024, and ends at 1,12 per cent for 2025.[41]

Nonetheless, the dire peril when addressing these liquidity emergencies is their short-termism. Indeed, governments factor electoral cycles in their decision making, and this way of thinking does not always advance the best interests of the country over the long haul. Their focused attention to the 'now' may make them lose sight of the 'after' and the bigger picture.

So how can governments deal with or alleviate these short-term liquidity crises? This chapter now turns to this question.

12.3.3 The imperative of preserving long-term development

The urgency of the short-term liquidity challenges must be tempered with the necessity to preserve future development. Although this way of easing

25 August 2020).

35 N Angula 'Can Namibia afford an IMF loan?' *The Namibian* (7 August 2020) 11.

36 International Monetary Fund (n 5).

37 As above.

38 As above.

39 International Monetary Fund 'Financial position in the Fund for Namibia as of June 30, 2021' (30 June 2021), https://www.imf.org/external/np/fin/tad/exfin2.aspx?memberKey1=689&date1key=2099-12-31 (accessed 12 July 2021).

40 As above.

41 As above.

liquidity crises may at first come across as insensitive to the people's or the citizens' plight, in reality this tempering demonstrates real leadership. It recognises that, in a situation such as the one with which countries in every corner of the globe grapple, governments must act (or react) swiftly but, at the same time, it reckons that, precisely because they have to act swiftly and decisively, governments tend to make ghastly and irreversible mistakes.

New Zealand's Fiscal Responsibility Act of 1994,[42] which pioneered FRLs, also aimed to tilt the balance of fiscal decision making towards strategic and long-term objectives.[43] In that regard, the Act departed from the former position, which attached great weight to short-term policies and economics.[44]

What does the imperative of 'long-term development' entail? Scholars define and understand 'development' differently, and this chapter does not seek to define this idea holistically. Rather, the notion of development employed in this chapter simply refers to the ability of the state to use the budget to make targeted expenditures. Thus, when I say that the COVID-19 pandemic hinders development, I merely intend to say that it adversely affects the ability of the state to use the budget to grow the economy, achieve welfare, and fulfil its policy goals.

By 'long term' I mean any period beyond the medium term, to wit, any period extending beyond three years from now. Strictly speaking, my rendering of 'development' in this chapter does not require the time element conveyed by the expressions 'long term' and 'short term', but discussing the sustainability of public debt without that element would not make sense. Likewise, discussing fiscal discipline or FRLs without focusing on debt sustainability would lead nowhere.

Prioritising long-term development calls for hard choices that, if implemented, may motivate citizens to vote out of power the courageous governments that made those hard yet necessary choices. Seen like this, the challenge for governments consists in summoning up the courage to make those hard choices without compromising their electability.

42 Fiscal Responsibility Act 1994 (1994 No 17) (New Zealand). The Act no longer applies in its initial form in New Zealand. In 2004 the New Zealand Parliament incorporated the Fiscal Responsibility Act into the Public Finance Act as Chapter 2. Then, in 2013, Parliament amended Chapter 2 of the Public Finance Act substantially. See The Treasury [New Zealand] *An introduction to New Zealand's fiscal policy framework* (2015) 8.

43 G Scott 'New Zealand's Fiscal Responsibility Act' (1995) 2 *Agenda: A Journal of Policy Analysis and Reform* 3.

44 As above.

12.4 Fiscal responsibility and budget system laws

In the face of a fiscally crippling pandemic, a FRL could assist a government in preserving long-term development. Namibia has neither a FRL nor an explicit fiscal responsibility framework. Considering the grim statistics that Namibia is staring at (see part 2.2 above) the absence of any FRL does not bode well. Accordingly, this part proceeds to outline a fiscal responsibility framework.

12.4.1 The role played by the law

Governments cannot dispense with the law as they fight the COVID-19 pandemic. The laws in question do not merely comprise those that regulate the lockdown, social distancing, the closing of businesses or schools, and so forth. They also pertain to the budget and its system.

These budget system laws include the Constitution, public finance laws, and the budget document itself, also known as the 'Appropriation Act' in common law jurisdictions such as Kenya, South Africa and Namibia.

Sceptics could retort that I place too much faith in the capacity of the law to bring about change and raise living standards. Increasingly, states legislate fiscal policy, yet this trend has not yielded the intended outcomes.[45] The inconclusive nature of the evidence on how FRLs impacted economies[46] seems to support their scepticism. While I agree that it cannot easily legislate away its debt woes, the Namibian government has a good track record of executing the laws that Parliament has passed.[47] I would therefore not be foolish to suggest that, by adopting a FRL, the country with Africa's strongest adherence to the rule of law[48] could restrain the government's fiscal policy. Thus, when Namibia enacts laws,

45 See G Kopits 'Overview of fiscal policy rules in emerging markets' in G Kopits (ed) *Rules-based fiscal policy in emerging markets. Procyclicality of financial systems in Asia* (2004) 1; G Kopits 'Fiscal rules: Useful policy framework or unnecessary ornament?' (2001) International Monetary Fund Working Paper 1/145.

46 See eg L Aaskoven 'Do fiscal rules reduce political polarisation' (2019) 18 *Comparative European Politics* 630 (finding that little evidence that fiscal rules independently depoliticise fiscal rules by forcing political parties to adopt similar stances on fiscal policy).

47 See World Justice Project *Rule of Law Index 2020* (2020) 16-17 (giving Namibia a score of 0,63 out of 1,0 (ie, 63 per cent) and ranking it 35th best in the world (out of 128 countries)).

48 As above (indicating that Namibia has the strongest adherence to the rule of law in Africa).

it routinely implements them and, if it promulgates a FRL, the Namibian government will most likely apply it.

12.4.2 In Namibia, no framework for fiscal responsibility

Overall and, quite disturbingly, Namibia lacks any fiscal responsibility framework, let alone a law that disciplines the fiscus. The existing legal framework comprises the Constitution, the State Finance Act 31 of 1991, the freshly-adopted Bank of Namibia Act 1 of 2020, and the Appropriation Acts.

The Constitution

The Constitution, Namibia's supreme law,[49] does not expressly encourage the state or its organs to uphold fiscal discipline. Article 95, which falls under Chapter 11 (principles of state policy), urges the state to 'actively promote and maintain the welfare of the people'. However, the Constitution waters down this overarching welfarist principle by providing that the courts have no duty to enforce the principles spelled out in Chapter 11, although they may resort to those principles when interpreting laws based on them.[50] Hence, a concerned citizen cannot prompt the government to spend responsibly by invoking article 95.

Despite the absence of express provisions on fiscal responsibility, the Constitution sets up structures that deal with state finances, including notably the Auditor-General and the State Revenue Fund. The Constitution lays down that the pre-independence Central Revenue Fund of the mandate territory of South West Africa/Namibia must continue as the State Revenue Fund.[51] The Fund's mission consists in receiving all income accruing to the central government.[52] The Constitution vests the government with the sole authority to dispose of the income deposited in the Fund,[53] but it does not say how responsibly or prudently the government should dispose of that money.

In addition to the State Revenue Fund, the Constitution establishes the office of the Auditor-General. It empowers the President to appoint an Auditor-General after the Public Service Commission recommends it and

49 Constitution of Namibia art 1(6).

50 Constitution of Namibia art 101.

51 Constitution of Namibia art 125(1).

52 Constitution of Namibia art 125(2).

53 As above.

the National Assembly approves it.[54] The Constitution hands the Auditor-General the mandate to audit the State Revenue Fund and entrenches that office.[55] Although the Auditor-General's role involves detecting, disclosing and reporting irregularities, it does not imply stopping the government from incurring huge debts that it will probably fail to repay.

The Constitution provides for annual budgets or 'Appropriation Acts'. In a vibrant democracy, the process of approving budgets proposed by the government affords elected representatives a golden opportunity to warn the government and the Finance Minister against profligacy.

The Constitution obliges the Finance Minister to table in the National Assembly, at least once every year, a budget proposal for the prospective year.[56] The members of the Assembly then examine the proposed budget before they accept it and pass an Appropriation Act.[57] Prior to the legislative elections of November 2019, the ruling party enjoyed a super-majority in the National Assembly, thereby hindering the ability of opposition members to check the spending habits of the government. However, since the latest legislative elections, the South West Africa People's Organisation (SWAPO) has lost its super-majority, and opposition parties can henceforth control the government's fiscal policy more effectively.

The State Finance Act

Like the Constitution, the State Finance Act contains no provision that expressly addresses fiscal prudence. In terms of the Act, the Finance Minister may borrow moneys within and outside Namibia to obtain foreign currency or finance budget deficits.[58] For those purposes, the Minister could enter into agreements with banks and finance institutions, including the central bank and foreign banks, and he could issue treasury bills, public stock, bills of exchange or debentures.[59]

The Act gives the Finance Minister the tools to stop the public debt from spiralling up. Still, these tools are no straightjacket, and they will not preclude unsustainable deficits. In reality, several factors converged and heaped immense pressure on the government and the Finance Minister to drain the purse. The economy has slid into recession since 2016, the Fishrot

54 Constitution of Namibia art 127(1).

55 Constitution of Namibia arts 127(2)-(4).

56 Constitution of Namibia art 126(1).

57 Constitution of Namibia art 126(2).

58 State Finance Act 31 of 1991 secs 29(1)(a)-(b).

59 State Finance Act sec 29(2).

scandal has engulfed the ruling government and the SWAPO party since November 2019, and the COVID-19 pandemic has devastated businesses and families since December of the same year. Thus, the worst economic crisis, the ugliest corruption scandal, and the worst public health disaster all combine to pressure the government into a debt trap.

The central bank law

Unlike the Constitution and the State Finance Act, the new central bank law stands out as that part of the legal system that targets fiscal responsibility closely. The Bank of Namibia Act 1 of 2020 (BON Act) casts Namibia's central bank in fiscal, lending, borrowing and debt-manager roles.

The Act describes the Bank of Namibia (BON) as the fiscal advisor[60] and fiscal agent[61] of the government. In its advisor capacity, BON may 'on its own initiative' share its opinion on the budget.[62] This suggests that BON may advise the Finance Minister on budget policy when, for instance, it considers that Namibia cannot afford more debt or when the debt stock becomes too heavy. However, the Act does not clarify what BON's fiscal agency entails.

The Act allows BON to lend to the government on terms that it negotiates with the Finance Minister.[63] However, the Act forbids BON from lending to the government where the loan exceeds 5 per cent (or, exceptionally, 10 per cent) of the economic aid received by government for the three preceding years.[64] (This economic aid includes loans and grants received by the government.)[65] If lending to the government nears that ceiling, the Act obliges BON to report that fact to the Finance Minister and advise him on how to avoid breaking that ceiling.[66]

Interestingly, the Act imposes a duty on the government, its institutions and statutory bodies to consult BON before borrowing from any source outside the country.[67] BON will then advise them on the terms and financial expediency of the intended borrowing.[68] If BON determines

60 Bank of Namibia Act 1 of 2020 sec 46(1) (BON Act).

61 BON Act sec 48(a).

62 BON Act sec 46(3).

63 BON Act sec 49.

64 BON Act secs 50(3)-(4).

65 BON Act sec 50(1).

66 BON Act sec 46(1).

67 BON Act sec 51(1).

68 BON Act sec 51(1)(a).

that such borrowing is 'financially or economically inappropriate', it must report the matter to the Finance Minister and recommend to him measures that BON deems necessary to remedy the situation.[69]

Last, but not least, the central bank may manage public debt. If the Finance Minister authorises it, BON acts for the government and pays government debt, interest, and any debt-related expenses.[70] If authorised, BON can also issue public debt securities locally or internationally on behalf of the Namibian government.[71]

12.5 Fitting Namibia with a fiscal responsibility law

As just explained, the budgeting process in Parliament and the Finance Minister's borrowing powers may serve to keep finances from veering off rails. Nonetheless, these provisions lack one crucial thing: holism. This means that the presence of these provisions in the legal system will not keep the country from falling into a bottomless debt trap. Hence the necessity of a complete legal framework for fiscal responsibility.

In addition to the elements of FRLs discussed later in this chapter, other provisions of budget system laws may qualify as best practices. These include fiscal space and insurance. Many of the standards or norms deemed best practices boil down to creating fiscal space while grappling with the severe crises. 'Fiscal space' denotes the room in a government's budget that allows the government to spend for a desired purpose without sacrificing the sustainability of its finances or the stability of the economy.[72]

Budget insurance

To drastically improve debt sustainability in the disaster-prone areas of the world, Borensztein et al recommend that governments take out

69 BON Act sec 51(2).

70 BON Act sec 53(1)(a).

71 BON Act sec 53(1)(b).

72 P Heller 'Understanding fiscal space' (2005) International Monetary Fund Policy Discussion Paper PDP/05/4 3. Heller first introduced the term 'fiscal space'. For a different definition, see I Ortiz et al *Fiscal space for social protection: A handbook for assessing financing options* (2019) 9 (defining 'fiscal space' as 'the resources available as a result of the active exploration and utilisation of all possible revenue sources by a government'). After offering their own rendering of the term 'fiscal space', Ortiz et al (10) noted that Heller's definition has ignited controversy. See also AR Ghosh et al 'Fiscal fatigue, fiscal space and debt sustainability in advanced economies' (2013) 123 *Economic Journal* F4. Nonetheless, Heller's understanding of the term suits the purposes of this chapter perfectly.

'catastrophic risk insurance'.[73] While they focused on Belize as a case study of budget insurance in the Caribbean region, one of the world's more disaster-prone areas, nothing bars governments from considering such insurance in other regions. The fact that the Caribbean must weather more disasters than others does not obviate the necessity of insurance for other countries. It only means that countries in other regions will pay lower premia than Caribbean nations. Furthermore, if predictions that other pandemics will hit the globe in the future prove true, then these other regions, including Africa, may wish to reconsider their notion of disaster-prone geography and arrange their finances as though they belonged to disaster-prone areas.

Borensztein et al believe that international organisations have an important part to play in government budget insurance. They claim that they can assist countries when insurance markets are distorted and in easing internal resistance to the purchase of insurance policies. The World Bank and other international institutions have already sponsored the development of insurance and reinsurance markets for national disasters.[74]

I think that the IMF could assume the role of facilitator in insuring government budgets. Actually, in return for its member states agreeing to pay premia, the IMF could serve as the insurer of government budgets. Governments could pass on risks of pandemics, national or global, to an international insurer and mandate that insurer to finance budget deficits when the governments contract huge debts to deal with those pandemics. For want of space, I cannot lay out the nuts and bolts of this insurance scheme in this chapter, but I believe that the idea deserves attention.

If nations in SADC and Africa do not deem it wise to entrust the IMF with such a responsibility, they could launch the African Monetary Fund (AMF)[75] and appoint it to perform the roles of facilitator and insurer.

However, as Borensztein et al note, developing countries do not have affordable insurance options.[76] All the same, this dearth of real alternatives

73 Borensztein et al (n 6).

74 Borensztein et al (n 6) 4.

75 The African Monetary Fund (AMF) has not yet started operating because, though ratified by the requisite number of states, the instruments that established it – the Protocol on the Establishment of the African Monetary Fund and the Statute of the African Monetary Fund – have not yet received enough ratifications to activate the AMF.

76 Borensztein et al (n 6) 5.

should not prevent developing country governments from spending responsibly and devising a framework to guide their expenditures.

12.5.1 Fiscal responsibility

Perhaps the best of the best practices entails establishing a framework for assuring responsibility in fiscal matters. The 2007-2009 financial crisis has prompted scholars to examine more closely fiscal stimuli, government deficits and debt. Apart from concerns about increasing government debt, they started to worry about the sustainability of government debt.[77] Against this backdrop, Kregel advocated a 'responsible' fiscal policy.[78]

For their part, Posner & Blöndal recommended that nations couple actions to jump-start economies with fiscal consolidation.[79] Those that delay fiscal consolidation will pay a steep price economically and politically.[80]

12.5.2 The legal framework for fiscal responsibility

After the 2007-2009 financial tsunami hit the globe, many countries enacted FRLs. In so doing, they aimed to promote fiscal discipline credibly, predictably and transparently.[81]

However, middle-income countries far outnumber advanced countries in adopting FRLs.[82] For example, Brazil and Paraguay enacted a FRL in 2000 and in 2013, respectively. Nonetheless, despite its middle-income

77 See eg JL Palmer & RG Penner 'The hard road to fiscal responsibility' (2012) 32 *Public Budgeting and Finance* 4 (describing fiscal problems in the US indicating that, without major changes in its revenue and spending policies, the country would suffer a sovereign debt crisis like countries did in Southern Europe); P Posner & J Blöndal 'Democracies and deficits: Prospects for fiscal responsibility in democratic nations' (2011) 25 *Governance* 11.

78 J Kregel 'Fiscal responsibility: What exactly does it mean?' (2010) Levy Economics Institute of Bard College Working Paper 206. With respect to sustainable public debt and deficits, Kregel advocates a concept of 'responsible' government policy that conveys the idea that the policies of the government should respond to the needs and wants of citizens by providing not only education and physical security, but economic security as well.

79 Posner & Blöndal (n 77) 11.

80 As above.

81 C Caceres et al 'Structural breaks in fiscal performance: Did fiscal responsibility laws have anything to do with them?' (2010) International Monetary Fund Working Paper WP/10/248.

82 I Lienert 'Should advanced countries adopt a fiscal responsibility law?' (2010) International Monetary Fund Working Paper WP/10/254 4.

status, Namibia is yet to enact its own FRL. Lienert cites a few reasons for the reluctance of advanced countries to embrace FRLs, including the existence of a legal framework that already provides for strong budget systems, supranational rules and political arrangements in countries belonging to the European Union (EU), and botched attempts[83] to insert quantitative fiscal rules in laws.[84]

12.5.3 Main features

FRLs typically feature four key clauses, namely, deficit ceilings, expenditure ceilings, escape clauses and sanctions. Expenditure ceilings can enable governments to cap the wage bill. In Namibia, the IMF and local economists have flagged the wage bill as unsustainable and significantly contributing to deficits and the ballooning debt.

Table 1: Main provisions of fiscal responsibility laws

Types of	**Provisions**
Transparency	The government must present to Parliament the draft annual budget law, a medium-term fiscal plan (covering the next three years), and a debt sustainability analysis. Government agencies must publish reports relating to fiscal policy.
Deficit ceiling	The deficit of the central government must not exceed a certain percentage of GDP.
	Ex-ante medium-term budget plan The average deficit (budgeted) over three consecutive budget periods must not exceed a certain percentage of GDP.
Expenditure ceiling	The rate at which current primary expenditure for the public sector grows must not exceed a certain percentage in real terms.

83 Lienert (n 82) 25-27) explained that quantitative rules in FRL-type legislation failed in advanced countries because quantitative targets, as opposed to qualitative rules, do not allow flexibility for a government to change its medium-term trajectory for fiscal balances and debt.

84 Lienert (n 82) 16-29.

Escape clauses	Parliament can approve a higher deficit (up to a certain ceiling)85 in cases of national emergency; an international crisis affecting the domestic economy; or negative growth.
Debt sustainability	The government must conduct and present a debt sustainability analysis to Parliament.
Sanctions	The FRL deems any deviation from it a dereliction of duty and imposes sanctions on the civil servant(s) responsible for the deviation.

Source: Partly adapted from AC David & N Novta 'A balancing act: Reform options for Paraguay's fiscal responsibility law' (2016) International Monetary Fund Working Paper WP/16/226 4-5

To uphold transparency, the FRL must empower the body or the officer tasked with administering the FRL to publish reports produced by government agencies, with some exceptions carved out in the law.[86]

Debt ceilings

One common strategy for preserving fiscal sustainability consists in adding debt ceilings to fiscal policy. These constraints can also make fiscal policy credible. For the same reason, however, increasing debt ceilings carry costs for the government's reputation.[87]

85 Up to 3% of GDP in Paraguay. See AC David & N Novta 'A balancing act: Reform options for Paraguay's fiscal responsibility law' (2016) International Monetary Fund Working Paper WP/16/226 5.

86 See David & Novta (n 85) 4 (observing that the FRL in Paraguay enshrines greater transparency by mandating open access to reports produced by government agencies, subject to some exceptions); C Pereira 'Brazil's fiscal responsibility law and the quality of audit institutions' (2010), https://www.brookings.edu/wp-content/uploads/2016/06/12_brazil_pereira.pdf (accessed 2 November 2020) (stating that the FRL mandated state audit institutions (*Tribunais de Contas*) to conduct external control of public administration by imposing certain procedural rules, such as rules on reporting transparency); M Melo et al 'Creative accounting and the quality of audit institutions: The Achilles heel of the fiscal responsibility law in Brazil' (2009), http://citeseerx.ist.psu.edu/viewdoc/download?doi=10.1.1.320.6987&rep=rep1&type=pdf (accessed 2 November 2020) (stating a position similar to Pereira's in the publication cited immediately before this one).

87 David & Novta (n 85).

To confront economic downturns, governments must resolve a trade-off between building fiscal credibility and amending the existing fiscal rule to provide themselves with space for counter-cyclical policies.[88]

These practices may involve, for instance, *temporarily lifting debt ceilings*. While African countries, and Namibia in particular, should raise their debt levels, later on they must consider instituting a debt ceiling, which in many cases they have not yet done. In Germany the debt ceiling, the so-called 'debt brake' (*Schuldenbremse*) is found in the Constitution itself.

Escape clauses

Developing nations and members of the SADC may *exempt certain expenditures* from debt ceilings. For instance, governments may decide to exempt public investment expenditures from any debt ceilings. In 2020 Germany invoked an escape clause to suspend its 'debt brake', the debt ceiling engraved in the Constitution, to cushion its economy from the fallout of COVID-19.[89]

Nevertheless, to maintain fiscal credibility and sustainability, governments must accompany this sort of exemption with better public investment management, stronger implementation of FRLs, and stricter adherence to debt ceilings with respect to other expenditures.[90]

To operate the fiscal framework effectively, governments must introduce explicit mechanisms to correct deviations from fiscal rules and to chart the path back to compliance with those rules.[91]

The Auditor-General

In Brazil and Paraguay the FRL conferred on the comptroller general the power to administer how agencies, at different levels of government, apply the FRL. In Brazil, state audit institutions (*Tribunais de Contas*) are ancillary bodies of the legislative branch, although they function like quasi-independent courts.[92] In Namibia, the Constitution establishes

88 David & Novta (n 85) 3.

89 See 'Why German politicians are fighting over the debt brake' The Economist (5 July 2021), https://www.economist.com/the-economist-explains/2021/07/05/why-german-politicians-are-fighting-over-the-debt-brake (accessed 13 July 2021).

90 David & Novta (n 85) 23.

91 David & Novta (n 85) 24.

92 Pereira (n 86) 4.

the Auditor-General.[93] Both the Brazilian audit institutions[94] and the Namibian Auditor-General[95] enjoy a large degree of autonomy.

David & Novta warn against entrusting the Comptroller General (that is, the Auditor-General in Namibia and South Africa) with administering the FRL.[96] Although it works independently from the Finance Ministry, the Comptroller General follows the established practice of generally auditing all government finances, which audit takes place several months after the close of the calendar year.[97] Such lagging audit does not assist the Comptroller General to flag breaches of the FRL early and inform the relevant agencies or officers while they execute the budget so as to help them enforce the law.[98]

Fiscal councils

I propose that governments entrust fiscal councils with the mission to administer the FRL. Experts increasingly view fiscal councils as a way to promote fiscal responsibility because these councils enhance the availability of good information about fiscal policy and provides the right incentives to achieve good outcomes.[99] They independently scrutinise fiscal policies, plans and performance. In particular, these fiscal councils (such as the US Congressional Budget Office and the Swedish Fiscal Policy Council) combat bias towards spending and deficits while improving the quality of fiscal policy debates.[100]

12.5.4 Indebtedness and sustainability

When deciding whether to fix or lift the debt ceiling to cope with the global pandemic, governments will have to ascertain the optimal level of indebtedness. Ascertaining the optimum in this circumstance, like in many others, is no easy task. Moreover, different schools of thought calculate the optimum differently.

93 Constitution of Namibia art 127(1).

94 Pereira (n 86).

95 See Constitution of Namibia arts 127(1), (3)-(4).

96 David & Novta (n 85) 4.

97 As above.

98 As above.

99 R Hemming & P Joyce 'The role of fiscal councils in promoting fiscal responsibility' in M Cangiano, T Curristine & M Lazare (eds) *Public financial management and its emerging architecture* (2013) 205.

100 As above.

Sustainable levels of indebtedness

Today, economists tend to calculate the level of indebtedness in relation to the budget or the gross domestic product (GDP). More often than not, they employ the GDP as a yardstick to determine the sustainability of the debt levels.

In short, economists and policy makers strive to identify the *debt limit.* The debt limit enables policy makers to determine sustainable levels of indebtedness. Specifically, this limit indicates the debt level beyond which a government loses its solvency and dramatically risks defaulting on its growing debt.[101]

Ultimately, debt limits depend on how a government behaves. They evolve with monetary policy (captured by the risk-free interest rate), market reactions and growth prospects.[102] For instance, a debt limit, expressed as a percentage of the budget or the GDP, will increase or decrease depending on whether the government works out an interest rate that matches the probabilities that the economy will expand or contract. Seen from that perspective, debt limits serve less to indicate the time when a government will default and more to signal sustainability given the actual conditions of the economy.[103] This aphorism tells us that, if it borrows beyond its debt limit, the government will not necessarily default on its debt at the precise moment when it exceeds that limit. Rather, the aphorism indicates that, at that moment, the government can no longer guarantee that it will pay back the debt.

Is Namibia's debt sustainable?

Even before the COVID-19 pandemic erupted, the Namibian government lived beyond its means. Indeed, Namibia's public debt increased at an average rate twice higher than the average rate at which its economy grew. The debt that Namibia contracted and the interest that it paid for the debt both increased at an average speed of 26 per cent per year[104] while the nominal GDP only grew at 12 per cent per year.[105] As a consequence,

101 See Ghosh et al (n 72).

102 JM Fournier & F Fall 'Limits to government debt sustainability in OECD countries' (2017) 66 *Economic Modelling* 31, 40.

103 Fournier & Fall (n 102) 31.

104 Mwinga et al (n 20) 22, 25.

105 Mwinga et al (n 20) 25.

capital expenditure as a percentage of GDP growth decreased by 2 per cent.[106]

The ongoing pandemic has darkened Namibia's debt profile. In the fiscal year 2020/2021 it shrunk the economy by 7,9 per cent, 'a historic high' the effects of which cut across all sectors.[107] It reduced government revenue by 4,9 billion N$/Rand and drove up the budget deficit to 10,1 per cent of the GDP, resulting in a public debt standing at 68,8 per cent of GDP.[108]

These numbers mean that, over time, Namibia has been losing its capacity to spend on both essential and social services. In short, these numbers depict a bleak future for Namibia.

12.6 Assessing fiscal responsibility laws

The Namibian government will find it difficult to let the Bank of Namibia act like a fiscal council without, at the same time, subscribing to the neoliberal economics that informs its central bank and its monetary policies. In the same fashion, the government will consider it almost impossible to enact a FRL without furthering efforts to 'commercialise, corporatise and privatise the public sector.'[109] Like mainstream central banking theory and the SADC Model Law that inspired the BON Act,[110] FRLs are neoliberal.

Neoliberalism is a theory of political economy premised on the idea that human welfare flourishes by liberating individual entrepreneurial freedoms and skills within institutions characterised by strong private property rights, free markets and free trade.[111] Neoliberals insist that

106 Mwinga et al (n 20) 26.

107 Ipumbu Shiimi, Minister of Finance 'FY2020/2021 Mid-Year Budget Review and Medium Term Budget Policy Statement', https://mof.gov.na/documents/35641/36583/2020_21+Mid-Year+Budget+Review+and+Medium-Term+Policy+Statement+.pdf/7bade6a3-7108-f792-d0f2-6a534fda937c (accessed 8 March 2021).

108 As above.

109 See S Newberry & J Pallot 'Fiscal (ir)responsibility: Privileging PPPs in New Zealand' (2003) 16 *Accounting, Auditing and Accountability Journal* 467.

110 See eg DP Zongwe 'Three ways to redefine the romance between the central bank and financial markets in South Africa' (2021) 10 *Interdisciplinary Journal of Economics and Business Law* 64, 68-69, 70-71 (explaining that standard theory of central banking and the SADC Central Bank Model Law follows the neoliberal model).

111 D Harvey *A brief history of neoliberalism* (2005) 2.

the state must build and nurture a framework that buttresses those institutions.[112]

Whatever misgivings economists may have about the fiscal BON idea, the BON Act has already refashioned BON into a fiscal council. The question left for debates now concerns the avenues for framing BON within a broader FRL and for infusing BON with features that will make it respond to the needs of citizens, rather than the profit-maximising goals of businesses, more effectively.

12.6.1 Politics, impact and strength of FRL

The neoliberalism behind fiscal responsibility laws

Fiscal responsibility laws drew from New Zealand's Fiscal Responsibility Act of 1994, a legislation that ushered in and entrenched neoliberalism in that country. Kelsey faults the 1994 Act, together with the Reserve Bank Act of 1989, for shifting New Zealand's economy from Keynesian welfarism to neoliberalism.[113] She adds that, unlike other ordinary laws, these two Acts enjoyed 'constitutional' standing.[114]

That FRLs are the offspring of neoliberal thinking poses a major problem because of this paradigm's poor record in the developing countries where the governments imported it. Klein explained how a network of right-wing thinkers take advantage of catastrophes – say a flood or a pandemic – as 'exciting opportunities' for them to launch pro-market neoliberal policies.[115] These policies have further impoverished people in developing countries.[116] If anything, the COVID-19 pandemic may have heralded the demise of the neoliberal state and the ascent of the welfare state.[117]

Unlike FRLs elsewhere, my plea for a FRL in Namibia and for BON to act as fiscal council does not stem from a pro-market agenda. My plea emerges because, over the years, public debt steeply increased in Namibia,

112 As above.

113 J Kelsey '"Regulatory responsibility": Embedded neoliberalism and its contradictions' (2010) 6 *Policy Quarterly* 36.

114 As above.

115 N Klein *The shock doctrine: The rise of disaster capitalism* (2007) 6.

116 Klein (n 115) 171-217, 263-280, 325-340.

117 See K Schwab & T Malleret *COVID-19: The great reset* (2020) 85-89 (observing that, though the neoliberal doctrine had been waning, the COVID-19 pandemic brought the *coup de grace,* making the government important again in tackling systemic problems).

as discussed earlier in this chapter. Unless the government reverses it, this trend will eat away the livelihood of ordinary citizens and mortgage their future. To reduce the risk that the government will unwittingly practise the sort of economics that favours the market at the detriment of low-income households, I recommend below ways in which the proposed fiscal framework can empower the general public and civil society organisations to monitor BON and the nation's purse.

Impact of fiscal responsibility laws

Researchers have only found little, inconclusive empirical evidence that the FRLs have boosted performance (with respect to primary balances, and so forth).[118] Some researchers, however, have maintained that FRLs may have positively impacted other aspects of the problem, such as enhancing transparency, guiding the budget process, improving forecasting, lowering sovereign risk premia, and easing access to government financing.[119]

Other scholars, such as Pereira, appear to have found evidence of certain positive outcomes of FRLs. For Pereira the fiscal situations of Brazil's states have unquestionably picked up considerably since the government passed the FRL in 2000.[120] More importantly, Pereira claims that, following the FRL's enactment, a succession of primary surpluses enabled the government to reduce the GDP/debt ratio.[121] After it peaked at 55 per cent of GDP in 2002, that ratio fell sharply to 36 per cent of GDP in 2008.[122]

The government and audit institutions at national and sub-national levels in Brazil have responded to fiscal constraints by resorting to window dressing and (more) 'creative accounting'.[123] For example, they sometimes delayed unpaid commitments to the next fiscal year, thereby postponing

118 J Thornton 'Do fiscal responsibility laws matter? Evidence from emerging market economies suggest not' (2009) 12 *Journal of Economic Policy Reform* 127 (finding that improved performance in nine emerging market economies resulted from a factor other than FRLs); Caceres et al (n 81) 11 (measuring performance as the level of primary balances and their volatility and finding little empirical evidence linking FRLs to changes in fiscal performance).

119 David & Novta (n 85) 23 (noting that implementing the FRL showed signs of improved budget forecasting, procedures and compliance in Paraguay); Caceres et al (n 81) 11 (stating that adopting the FRL may have positively impacted transparency, the budget process, sovereign debt premia, and access to government financing).

120 Pereira (n 86).

121 As above.

122 As above.

123 Pereira (n 86); Melo et al (n 86).

the effect of those commitments on the primary balance.[124] Although undesirable, these efforts to evade the letter of the FRL through creative accounting reflects the binding nature of the FRL and confirms that civil servants will incur costs for breaching it.[125] Pereira concludes that this response to fiscal constraints undermines the sustainability of fiscal balance.[126]

Attempting to depoliticise fiscal policy

By campaigning for FRLs, I urge governments to depoliticise fiscal policy. I know that this proposition goes against the grain. For instance, some finance experts have pointed out that the way the existing macro-economic orthodoxy pressures governments to depoliticise monetary policy by insulating central banks from politics will not work in the case of fiscal policy. As Hemming and Joyce noted, designing fiscal policy proves more complicated than formulating monetary policy, especially because decisions about tax, expenditure and borrowing have complex and often contentious consequences in terms of distribution.[127] For that reason, they believe that such decisions should only be made by those democratically accountable for their consequences.[128]

In the next parts of this chapter I justify my plea. In essence, I maintain that, of the all the institutions that could assume the mantle of fiscal council in Namibia , the central bank stands out as the one that can advise and restrain the government on fiscal matters most effectively and most independently.

Strengthening the fiscal framework

For David & Novta, whether a FRL works effectively depends, at the end of the day, on measures to strengthen the legal and institutional aspects of the fiscal framework.[129] This generally means that governments must develop systems designed to manage public expenditures so that they can monitor and enforce FRLs adequately.[130] Still, FRLs, however effective in

124 Melo et al (n 86).

125 As above.

126 Pereira (n 86).

127 Hemming & Joyce (n 99) 205-206.

128 As above.

129 David & Novta (n 85) 24.

130 As above.

helping to improve fiscal management, cannot substitute for strong budget frameworks and a commitment to prudent fiscal policy.[131]

12.6.2 Fiscal fatigue

Fournier and Fall calculated a function that gives the value of the debt limit to react to assessments by markets of the probability of a government to default on a public debt.[132] They found that, at high debt levels, the primary balance displays fiscal fatigue.[133] 'Fiscal fatigue' relates to the ability of the primary balance to increase at the same pace as higher interest payments, as debt soars.[134] Fatigue happens when it becomes ever more difficult for a heavily-indebted government to produce sustainable primary balances.

Both fiscal fatigue and markets' assessment of the probability to default on a growing debt – an assessment reflected by interest rate – determine the debt limit beyond which debt cannot roll over. The framework developed by Fournier and Fall illustrates the contingent nature of debt limits and the vulnerability of governments when conditions in the market and the macro-economy change.[135] Their model-based framework calculates the debt limits of advanced economies.

Ghosh et al put forth a framework that employs the notion of fiscal space, which they define as the difference between a country's current debt level and its debt limit.[136] That stochastic model takes into account 'fiscal fatigue' and 'fiscal space'. In other words, fatigue kicks in when, after the debt level rises above a certain threshold, a government abandons efforts to consolidate its finances to repay its debts. This phenomenon implies that governments no longer increase their primary balance to keep their debts from accumulating.[137] Fournier and Fall estimated that, above 170 per cent of GDP, OECD governments exhibited fiscal fatigue.[138] However, at 120 per cent of GDP, governments react strongly to rising debt.[139]

131 As above.

132 Fournier & Fall (n 102) 30.

133 Fournier & Fall (n 102) 32.

134 Ghosh et al (n 72) F5, F6. See also Fournier & Fall (n 102) 30.

135 Fournier & Fall (n 102) 30.

136 Ghosh et al (n 72) F4.

137 Fournier & Fall (n 102) 31.

138 Fournier & Fall (n 102) 32.

139 Fournier & Fall (n 102) 40.

Debt limits vary depending on fiscal fatigue. If fatigue materialises at a lower debt level in the future, debt limits get revised down; if it occurs at a higher debt level, debt limits go up.[140] Using that model, Ghosh et al found in 2013 that debt limits and corresponding fiscal space vary widely across countries, ranging from 150 per cent and 250 per cent of GDP.[141] In addition, a number of countries, such as Greece, Iceland, Italy and Portugal, had little to no fiscal space whereas countries such as Australia and South Korea enjoyed ample space.[142]

However, the debt limits found by scholars[143] such as Ghosh et al will hardly have any relevance for Namibia, SADC countries, or other countries in the developing world because they only applied to 'advanced' economies. Based on the debt limits identified in advanced economies, researchers could maybe hypothesise the debt limit of a given developing country, but the macro-economic conditions that helped to fix the debt limits of developed countries contrast sharply with those obtaining in developing and least-developed countries.

12.6.3 The central bank as fiscal council

As I have explained earlier, the central bank in Namibia acts as a fiscal agent, a fiscal advisor, a lender, a foreign-borrowing expert, and a public-debt manager. I submit that, taken together, *these multiple roles have transformed the central bank into a fiscal council*.

The Bank of Namibia may be better equipped to act as fiscal council than the Auditor-General, the Ministry of Finance, a parliamentary committee such as the Swedish Council, or a specialised agency within the executive branch. Why? Because the BON Act shields the independence of the central bank like no other laws do for any of these other bodies. The BON Act not only safeguards the independence of the central bank,[144] but also penalises any person who interferes with such independence – a criminal offence punished by a fine not exceeding 2 million N$/Rand or

140 Fournier & Fall (n 102) 36.

141 Ghosh et al (n 72) F22.

142 As above.

143 See eg B Fincke & A Greiner 'Debt sustainability in selected Euro area countries: Empirical evidence estimating time-varying parameters' (2011) 15 *Studies in Nonlinear Dynamics and Econometrics* 1 (testing the sustainability of public debt in some countries of the Eurozone, including Portugal, Italy, Ireland, Greece and Spain); B Fincke & A Greiner 'How to assess debt sustainability? Some theory and empirical evidence for selected Euro area countries' (2012) 44 *Applied Economics* 3717.

144 BON Act sec 5.

by a jail term not exceeding 20 years.[145] In so doing, Namibia went much further than what the SADC Central Bank Model Law recommended.[146]

Some scholars have advised against proposals to depoliticise the budget and fiscal policy in the manner that monetary policy is.[147] They reason that fiscal policy has proved more complex and more politicised by nature than monetary policy.[148] They think it naïve to believe that the ruling party would risk becoming unpopular or losing the next elections only in the name of neoliberalism[149] or fiscal prudence. In the process, the BON would likely lose its independence *vis-à-vis* the executive.

However, precisely because electoral cycles will induce the government to spend imprudently, a fiscal council with a legally-enforceable independence can restrain the Finance Minister, thereby functioning like a commitment technology. As Schaumburg and Tambalotti enthused, '[t] hanks to this technology, policymakers can guarantee their own promises' in spite of democratic pressures.[150]

At any rate, the world has entered an age of fiscal prudence after the COVID-19 pandemic has dried state coffers. Even if the drafters of the BON Act never intended to turn it into a fiscal council, they might as well repurpose the central bank now. If Namibian policy makers choose that route, they would still have to embed the BON-fiscal council within a proper fiscal responsibility framework. This FRL would strengthen the fiscal council in its tasks.

Moreover, the BON Act requires the central bank governor to report at least once a year to Parliament about its activities. This requirement ensures that, though operating independently, this central bank would nonetheless account for its actions to the people of Namibia, which aligns with article 95(k) of the Constitution – a provision that presses the government to encourage the masses to influence government policy through debates. The governor could table debt sustainability analysis

145 BON Act sec 5(3).

146 See Southern African Development Community *Explanatory Guide to the SADC Central Bank Model Law* (2011) 53-62.

147 See eg JA Dorn 'Maintaining distance between monetary and fiscal policy' *Cato Institute* (18 November 2020), https://www.cato.org/publications/pandemics-policy/maintaining-distance-between-monetary-fiscal-policy (accessed 1 March 2021).

148 See Hemming & Joyce (n 99) 205-206.

149 Admittedly, New Zealand enacted the first FRL around the time neoliberal policies were on the rise in that country.

150 2005.

in Parliament to facilitate those debates. Although the impact of FRL has remained inconclusive, this reporting requirement, coupled with the strong independence of the BON-fiscal council, should allow the FRL to have the teeth that it needs to succeed. They key here is to have more eyes on the money.

12.7 Conclusion

The COVID-19 pandemic has been a trial of strength for Namibia's fiscus and budget system. The Namibian experience with the COVID-19 is instructive because it gives an idea of how a developing country run by a fairly capable and well-managed government can address the pandemic. As one of Africa's best-governed countries, the Namibian example does not statistically represent governance standards on the continent, but it sets an example that other African countries can aspire to when thinking about what they could realistically and feasibly achieve, if they lift their game, in fighting this pandemic and the next one(s).

At very few points in time in human history have governments met head-on the sort of stark choices that developing nations face now. They either plunge deeper into the debt ditch or watch their economies sink. These brutal realities underscore the quagmire in which the developing country finds itself and test the steel of the country's fiscal architecture.

To enlighten policy makers, fiscal authorities and other stakeholders in contracting more debt more responsibly, this chapter outlined a model fiscal responsibility law, with the central bank as a linchpin. The Bank of Namibia stands in a better position than the Auditor-General, a parliamentary committee or a court, to function like a fiscal council. BON boasts two advantages over these other bodies: First, it enjoys a legally-protected independence, in a country with a sterling reputation for its strict adherence to the law; second, it has greater expertise and more resources in matters pertaining to the macro-economy and system-wide risks.

Critics could counter that, given that fiscal policy can affect the re-election chances of a government, the presence of a fiscal council would impel the government to interfere with the BON's independence or operations. Even if future events vindicated the critics, BON would still be the institution most apt to resist interference from government and other powerful interests.

Hopefully, with the fiscal responsibility framework recommended in this chapter, policy makers will not have to think twice about how to

balance short-term emergency borrowing and long-term development the next time a pandemic comes around.

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13 Resource-backed loans, COVID-19 and the high risk of debt trap: A case study of Zimbabwe

Farai Mutondoro, Anna-Sophie Hobi, Mutuso Dhliwayo and Josephine Chiname

13.1 Introduction

Currently, the COVID-19 pandemic undoubtedly is the greatest threat to human well-being and the global economy. It has deep impacts not only on growth rates and commodity prices but also on countries' sovereign debt. While other indebted countries have received debt relief from the International Monetary Fund (IMF) and the Group of 20 leading economies (G20) resulting in them being able to access new loans to mitigate against the effect of the pandemic to their economies, Zimbabwe has not received much.

Zimbabwe, just as many other resource-rich countries in sub-Saharan Africa, is highly dependent on its mining industry and is in debt distress. The country's debt stock is believed to be around US $17 billion of which a significant portion is being attributed to interest and penalties from failing to pay back the external debt. For every dollar Zimbabwe earns, over 60 cents are from mining sector exports.

A leaked letter by the Minister of Finance to international financial institutions as reported by Africa Confidential reveals that as a result of the COVID-19 pandemic, Zimbabwe's economy could have contracted by between 15 and 20 per cent in 2020.[1] Already before the pandemic, Zimbabwe was struggling to attract foreign investments and loans due to the protracted economic crisis. Standing at the verge of financial collapse and instability, the COVID-19 pandemic is just the latest of Zimbabwe's woes. Chinese banks and international commodity traders are stepping in and filling the gap left by traditional creditors by providing quick and accessible loans using natural resources as collateral. The so-called resource-backed loans (RBLs) are offered to governments or state-owned enterprises and their repayments are either made directly through natural resources, such as minerals or oil (in-kind) or guaranteed by a resource-related income stream.

1 Magaisa (2020) Mthuli Plea, https://bigsr.africa/bsr-mthulis-letter-d1/ (accessed 30 October 2020).

RBLs come at a high price for borrowing countries, often with implications for human rights. The main risks with RBLs lie with the borrower as they become ever more dependent on their extractive sector, the volatile commodity market prices and the foreign lenders. RBLs can contribute to high debt distress which leads to economic crisis. The effects can be devastating. A government may struggle ever more to provide basic services such as health care and education. At the same time, the lenders may benefit from a steady supply of resources, high service fees and rents. Furthermore, RBLs are opaque and lack oversight.

Zimbabwe has been very active in resource mortgaging and six RBLs and resources-for-infrastructure deals estimated to a total amount of US $6,8 billion became known, mostly through the help of investigative journalists and researchers.[2] However, due to the lack of contract transparency in Zimbabwe and the opaque nature of some of these RBLs, the magnitude and extent of RBLs in Zimbabwe is difficult to ascertain. This is despite the fact that the Zimbabwean Constitution and laws demand transparency and accountability. In this chapter we analyse Zimbabwe's natural resource mortgaging through RBLs in the current situation of a global pandemic and a pan-African debt crisis. We include the legal background as well as the social implication of RBLs as Zimbabwe is increasingly using its natural resources as collateral and amending the laws in favour of them. Our main concerns are the negative impacts of RBLs both in terms of the debt burden, corruption risks and human rights. Through a review of secondary data and an interpretive approach, we analyse the RBLs and the human right scenario in Zimbabwe.

13.2 COVID-19, debt and the global economy

The COVID-19 pandemic represents a great shock to the global economy. The shock propagated through three key channels, namely, (i) a disruption of global value chains; (ii) restrictions on international mobility, which affected economies and activities differently, depending on their exposure and preparedness; and (iii) a reduction in cross-country remittances. According to the IMF's April 2020 World Economic Outlook, the global economy would experience its 'worst recession since the Great Depression, surpassing that seen during the global financial crisis a decade ago'. Prior to the outbreak, global growth was expected to rise marginally. COVID-19 reduced global economic growth to an annualised rate of -4,5 per cent to -6,0 per cent in 2020, with a partial recovery of 2,5 per cent to 5,2 per

2 http://zimcodd.org/wp-content/uploads/2021/02/The-Bane-of-Resource-Backed-Loans-Implications-for-Debt-Sustainability.pdf (accessed 30 October 2020).

cent projected for 2021.[3] More than 90 per cent of the global economy experienced a contraction in per capita gross domestic product (GDP), the highest share of countries simultaneously contracting since the Great Depression of 1930 to 1932.[4] Goods trade fell rapidly, adding to the economic decline in manufacturing countries.[5] Global trade is estimated to have fallen by 5,3 per cent in 2020.[6] Oil prices lost about 50 per cent of their value, dropping from US $67 below US $30 a barrel in 2020, and metals were projected to decline more than 13 per cent in 2020 while food prices were expected to be broadly stable through 2020.[7] The tumbling of the global economy arising from a plunge in commodity prices and slowdown in economic activity will severely affect the African economy.

In a podcast interview on the impacts of COVID-19 on African economies, Brahima Coulibaly,[8] the director of the African Growth Initiative at the Brookings Institution, stressed that as a result of COVID-19, Africa has a health and an economic crisis with the latter having actually preceded the health crisis because Africa began to feel the effects before it started to register a significant number of cases on the continent. The World Bank's Africa Pulse report of April 2020, entitled 'Assessing the Economic Impact of COVID-19 and Policy Responses in Sub-Saharan Africa' projected that economic growth in sub-Saharan Africa will decline from 2,4 per cent in 2019 to -2,1 to -5,1 per cent in 2020, the first recession in 25 years.[9] Sub-Saharan Africa could face a severe food security crisis, with agricultural production expected to contract between 2,6 and 7 per cent.[10] COVID-19 will further widen fiscal deficits, particularly in commodity-exporting countries and countries dependent on tourism revenues. It is anticipated that remittances that are sources of income for households in

3 Congressional Research Services 'Global Economic Effects of COVID-19' (2021), https://fas.org/sgp/crs/row/R46270.pdf (accessed 30 October 2020).

4 World Bank Global Outlook (2020).

5 The World Bank 'Global economic prospects' (January 2021) Subdued Global Economic Recovery, https://www.worldbank.org/en/publication/global-economic-prospects (accessed 30 October 2020).

6 As above.

7 https://www.cnbc.com/2020/03/08/oil-plummets-30percent-as-opec-deal-failure-sparks-price-war-fears.html (accessed 30 October 2020). Also see World Bank Reports 'Commodity markets outlook: Implications of COVID-19 for commodities' 1 (April 2020) https://openknowledge.worldbank.org/bitstream/handle/10986/33624/CMO-April-2020.pdf (accessed 30 October 2020).

8 Brookings Institute, https://www.brookings.edu/experts/brahima-coulibaly/ (accessed 30 October 2020).

9 AG Zeufack et al 'Africa's Pulse No 21' (April 2020), https://openknowledge.worldbank.org/bitstream/handle/10986/33541/9781464815683.pdf?sequence=18 (accessed 30 October 2020).

10 As above.

Africa and also a source of foreign financing will drop significantly. For Africa, therefore, the COVID-19 pandemic is a double-edged sword: On the one hand it impedes the ability of governments to mobilise revenue and, on the other, it pressurises governments to invest more in public health and welfare mechanisms.

The COVID-19 pandemic pushes governments across the globe into the depth of the debt conundrum, particularly in sub-Saharan Africa, depending on loans from abroad. In late 2020 the IMF writes that '[t]he COVID-19 pandemic has greatly lengthened the list of developing and emerging market economies in debt distress'.[11] While default rates are rising, debt relief and restructuring are urgently needed. According to the African Union (AU), there is a high probability that many countries could face a rise in the stock of external debt and servicing costs due to the increase in fiscal deficits as more emphasis will be placed on to fulfilling social needs, including healthcare systems, socio-economic stimulus to households, small and medium-sized enterprises (SMEs) and businesses.[12]

Already prior to the COVID-19 pandemic, debt in Africa has reached unsustainable levels. Mozambique, for example, had an external debt of US $14 billion. Among others, Mozambique received secret loans of more than US $2 billion for fishing boats using sovereign guarantees, whereby it bypassed Parliament.[13] As in the case of Mozambique, many resource-rich African states are at the brink of extreme debt crises.[14] For sub-Saharan Africa, government debt as a share of GDP has grown from 31,7 per cent between 2010 and 2015 to 50,4 per cent in 2020. Countries such as Cape Verde, Mozambique and Angola record debt levels as high as 118,9 per cent, 106,8 per cent and 90 per cent of their GDP respectively.[15] Since

11 J Bulow et al 'New steps are needed to improve sovereign debt workouts' IMF Fall Issue 2020, https://www.imf.org/external/pubs/ft/fandd/2020/09/debt-pandemic-reinhart-rogoff-bulow-trebesch.htm (accessed 30 October 2020).

12 'Impact of the corona virus on the African economy', https://www.tralac.org/documents/resources/covid-19/3218-impact-of-the-coronavirus-covid-19-on-the-african-economy-african-union-report-april-2020/file.html (accessed 30 October 2020).

13 M Sallen 'External debt complicates Africa's COVID-19 recovery, debt relief needed' (30 July 2020), https://www.un.org/africarenewal/magazine/july-2020/external-debt-complicates-africas-post-covid-19-recovery-mitigating-efforts (accessed 30 October 2020).

14 V Kgomoeswana 'The many resource-rich African countries on the brink of defaulting on their debts is worrisome' *Sunday Independent* (25 October 2020), https://www.iol.co.za/sundayindependent/dispatch/the-many-resource-rich-african-countries-on-the-brink-of-defaulting-on-their-debts-is-worrisome--b3488f7f-9d54-4a7e-9796-b58a12106b14 (accessed 30 October 2020).

15 C Onyekwena & M Amara Ekeruche 'The case for debt relief in Africa amid

2010 the average public debt in sub-Saharan Africa has risen faster than in any other developing region.[16] Sovereign debt and debt to GDP ratio is set to increase as countries invest more in mitigation measures and also seek to stimulate economic productivity. The issue of a COVID-19 debt relief became a topical issue with African thought leaders such as Brahima Coulibaly,[17] Ngozi Okonjo-Iweala,[18] Cristina Duarte,[19] Vera Songwe,[20] Strive Masiyiwa,[21] Donald Kaberuka[22] and Louise Mushikiwabo[23] coming up together in calling for a two-year standstill on all external debt repayments.[24] On 31 March 2020 African ministers of finance had a second online meeting and agreed that for Africa to effectively fight COVID-19, there is an urgent need for debt relief and fiscal stimulus. On 13 April 2020 the IMF suspended debt repayments due to it by the poorest developing economies for the next six months – the programme runs until the end of 2021[25] On 15 April 2020 leaders of the G20 announced the suspension of debt service payments for 73 of the poorest countries from May to the end of 2021.[26] Unfortunately, Zimbabwe was exempted from the list of countries that were offered debt relief. Moreover, debt repayment excludes loans from Chinese and private lenders. Copper-dependent Zambia was the first African country heading towards default on private creditors

COVID-19' (14 April 2020), https://www.africaportal.org/features/case-debt-relief-africa-amid-covid-19/ (accessed 30 October 2020).

16 'Africa's debt crisis hampers its fight against COVID-19' *Economist* (April 2020), https://www.economist.com/middle-east-and-africa/2020/04/11/africas-debt-crisis-hampers-its-fight-against-covid-19 (accessed 30 October 2020).

17 Brahima Coulibaly is the director of the African Growth Initiative at the Brookings Institution.

18 Ngozi Okonjo-Iweala is the former Nigerian Minister of Finance and former managing director with the World Bank.

19 Cristina Duarte is former Finance Minister of Cabo Verde.

20 Vera Songwe is executive secretary of the United Nations Economic Commission for Africa.

21 Strive Masiyiwa is a founder and group executive chairman, Econet Wireless Global.

22 Donald Kaberuka is a former Rwandese Minister of Finance and the 7th president of the African Development Bank Group.

23 Louise Mushikiwabo is secretary-general of the Organization Internationale de la Francophonie and former Minister for Foreign Affairs and Cooperation of Rwanda.

24 O-I Ngozi et al 'Africa needs debt relief to fight COVID-19' (9 April 2020), https://www.brookings.edu/opinions/africa-needs-debt-relief-to-fight-covid-19/ (accessed 30 October 2020).

25 IMF 'IMF executive board approves immediate debt relief for 25 countries' (13 April 2020), https://www.imf.org/en/News/Articles/2020/04/13/pr20151-imf-executive-board-approves-immediate-debt-relief-for-25-countries (accessed 30 October 2020).

26 France 24 'IMF chief asks for continued debt relief as pandemic aid winds down' https://www.france24.com/en/live-news/20211027-imf-chief-asks-for-continued-debt-relief-as-pandemic-aid-winds-down (accessed 16 November 2021). .

during the pandemic. In 2019 it accumulated a debt of US $11,9 billion. After the country sought to delay interest payments for foreign bonds, the private investors were hesitant to cooperate because they suspected the money would be channelled towards the repayment of Chinese loans – Zambia owes a third of its debt to China.[27]

Cash-poor and indebted countries have long struggled to attract foreign investment, to access international capital markets and to receive loans because of the higher financial risks these countries carry. The COVID-19 pandemic exaggerates the need for foreign loans. As one resort, resource-rich countries have in the past 15 to 20 years increasingly been borrowing with their wealth in natural resources serving as collateral – loans that in many oil, gas or mining-based economies have contributed to their current debt distress. Will such loans become more relevant due to COVID-19?

13.3 Resource-backed loans

Institutional donors and private companies are taking advantage of this need and 'help out' by granting resource-backed loans (RBLs) to states and state-owned companies. In return, they receive access to natural resources such as oil, gas and minerals or are repaid through revenues created in the sector. Such deals often come with a high risk and rarely on terms in favour of the borrower. On top of that, resource-backed loans tend to be highly opaque, hard to monitor and prone to corruption. For the often already-indebted and struggling young African nations, resource-backed loans contribute to financial dependencies and debt distress.

We speak of RBLs when referring to loans provided to a government or state-owned company leveraging their natural resource wealth as collateral. The repayment is made either in kind, such as in oil or minerals, from a resource-related revenue generated in the future, or as an asset serving as collateral.[28] RBL is used here as an umbrella term and includes different types of arrangements. Prepayments are generally short-term agreements in which the lender makes up-front payments for the future delivery of natural resources within a few years. These are particularly interesting to trading companies that rely on a consistent supply of commodities.

27 J Cotterill & T Stubbington 'Zambia headed for Africa's first COVID-related debt default' *Financial Times* (22 September 2020), https://www.ft.com/content/0b744d46-46b1-48c3-81cd-be0d78d99262 (accessed 30 October 2020); 'Cash-strapped Zambia takes on China as it seeks debt relief' *TRT World* (13 October 2020), https://www.trtworld.com/magazine/cash-strapped-zambia-takes-on-china-as-it-seeks-debt-relief-40544 (accessed 30 October 2020).

28 D Mihalyi et al 'Resource-backed loans: Pitfalls and potential' (2020) Natural Resource Governance Institute 3.

Other RBLs are long-term and may have a repayment schedule of several decades. If the repayment is done through the income gained from selling natural resources to a third party, terms such as 'pre-financing', 'loans in exchange for resource-receivable' or 'pre-export finance' are used. In these types of loans, the repayment speed is highly depending on commodity prices, especially when the loans are connected to a set quantity or volume of the resource.[29]

Furthermore, RBLs also include collateralised arrangement in which the borrower would use an underground asset such as a part of as mineral reserve or a yet to be developed mine as a collateral. In some cases, a government may grant extraction rights or mineral rights to a lending company, often in return for relevant infrastructure to be built by the company. Arrangements that include the provision of goods, services or infrastructure in exchange for natural resources, natural resource-related repayments or exploration and production concessions and mining rights are also known as '(infrastructure) barter agreements',[30] 'resource-for-infrastructure (R4I) swaps or deals'[31] or as 'resource financed infrastructure'.[32]

13.3.1 RBL borrowers and lenders

Researchers at the Natural Resource Governance Institute (NRGI) analysed 52 resource-backed loans in sub-Saharan Africa and Latin America made between 2004 and 2018.[33] Recipients of RBLs in most cases are state-owned enterprises and national oil companies.

Approximately 53 per cent of the loans to African countries came from Chinese state-owned policy banks such as the China Development Bank (CDB) and Export-Import Bank of China (China Eximbank). CDB granted three loans totalling US $18 billion and China Eximbank 14 loans totalling US $17 billion, among others to Zimbabwe. According to the NRGI, most countries that have borrowed from these two lenders also have Chinese companies active in the resource sector. Moreover, Chinese

29 As above.

30 EITI *Standard (2019)* 'Requirements 4', https://eiti.org/document/eiti-standard-2019#r4 (accessed 30 October 2020).

31 Columbia Centre on Sustainable Investment 'Resource for infrastructure deals', http://ccsi.columbia.edu/work/projects/resource-for-infrastructure-deals/ (accessed 30 October 2020); P Konijn 'Chinese Resources-for-Infrastructure (R4I) swaps: An escape from the resource curse' (2014).

32 H Halland et al 'Resource financed infrastructure. A discussion on a new form of infrastructure financing' (2014) *World Bank Studies* 3.

33 Mihalyi et al (n 28) 3.

loans often come in bundled deals involving infrastructure provisions.[34] Loans tied to infrastructure could be seen as positive exactly because they result in infrastructure being built. Nevertheless, resources-for-infrastructure deals come with high governance risks and can increase a country's sovereign debt.

The Sicomines project in the Democratic Republic of the Congo (DRC) probably is the best-known example of such a mineral barter deal. In 2007 DRC and China signed the Sicomines deal, at the time one of the most significant Chinese investments in Africa. While the DRC was eager to have a number of infrastructure projects financed, the Chinese counterpart gained access to key resources of copper and cobalt. Chinese companies received the mining rights to a mine owned by the Congolese state-owned Gécamines. For the deal, a joint venture named Sicomines was set up. Majority shareholding with 68 per cent was on the Chinese side.[35] In this deal, China Eximbank awarded Sicomines two credit lines, one of US $3 billion for infrastructure and the other of US $3,2 billion for the development of the mine itself. The US $3 billion loan is intended to be paid back through the mine's future profits.[36] Furthermore, the agreement included tax and custom duties exemptions to Sicomines until the US $3 billion infrastructure loan is fully repaid.[37] Over ten years later, researchers conclude that the agreement was less beneficial to the DRC than it was to China: Thanks to the DRC being part of the Extractive Industries Transparency Initiative (EITI), at least some information on the deal was disclosed. Nevertheless, researchers Maiza-Larrarte and Claudio-Quiroga state that the deal was highly opaque in the initial stage and hard to evaluate in financial terms. The DRC loses out on an opportunity because the infrastructure built was of too low-quality a standard, so the natural resources were traded for short-living infrastructure that will not increase economic or social development in the country.[38]

Peter Konijn, from the Erasmus University Rotterdam, suggests that resource-for-infrastructure (R4I) swaps were pioneered by the Chinese state and Chinese companies in their engagement with resource-rich

34 Mihalyi et al (n 28) 11, 15.

35 A Maiza-Larrarte & G Claudio-Quiroga 'The impact of Sicomines on development in the Democratic Republic of Congo' (2019) 95 *International Affairs* 427.

36 Mihalyi et al (n 28) 10.

37 Maiza-Larrarte & Claudio-Quiroga (n 35) 429.

38 S Marysse & S Geenen 'Triangular arm wrestling: Analysis and revision of the Sino-Congolese agreements' in A Ansoms & S Marysse *Natural resources and local livelihoods in the Great Lakes Region of Africa. A political economy perspective* (2011) 237; Maiza-Larrarte & Claudio-Quiroga (n 35) 445.

countries in Africa and they involve the exchange of natural resources for infrastructure.[39] The revenues from the export of natural resources such as oil or copper are used as collateral for a loan to finance infrastructure development. Konijn argues that the first complex R4I swap was initiated in Angola in 2004 when a $2 billion loan from China Eximbank was used to finance the reconstruction of infrastructure damaged during Angola's civil war. The export revenue from 10 000 barrels of oil per day over a period of 17 years would be used to repay the loan. In accordance with the loan agreement, 70 per cent of public tenders for the infrastructure projects related to the R4I swap deal was to be awarded to Chinese construction corporations. At the end of 2011, there were ten major R4I swaps, either concluded or in the process of implementation in eight African countries (Angola, Congo-Brazzaville, DRC, Ethiopia, Gabon, Ghana, Sudan and Zimbabwe) with a total value of approximately $22 billion. The Eximbank provided $38 billion in loans for over 1 000 infrastructure projects in Africa between 2003 and 2011.

Debts accumulated not only through loans from Chinese actors. The Jubilee Debt Campaign states in 2018 that 32 per cent of African government external debt is owed to private lenders.[40] Almost half of the RBLs in sub-Saharan Africa examined by the NRGI come from commodity trading companies such as Trafigura, Glencore and Vitol.[41] Trading companies coordinate the transport of commodities from the mines or oil production sites to the consumers. Trafigura, one of the largest trading companies in the world, describes commodity traders as 'essentially logistics company that use financial markets to fund their operations'.[42] At the interface between physical trade and the financial world, the traders also act as creditors by granting RBLs. In fact, their lending activities are on the rise: Trafigura, for instance, increased it from US $700 million in 2013 to more than US $5 billion in 2019.[43] White writes in the *Financial Times* that '[i]n other words, they engage in shadow banking (non-bank financial activity) – and their role here is growing'.[44]

39 Konijn (n 34 above)

40 Jubilee Debt Campaign 'Africa's growing debt crisis: Who is the debt owed to?' (2018) 1

41 https://www.resourcegovernance.org/sites/default/files/BigSpenders_20141014.pdf (accessed 30 October 2020).

42 Trafigura 'Commodities demystified' (2018) 30.

43 Trafigura 'Prepayments demystified' (2020) 2.

44 N White 'Regulators must now look at commodity trading' *Financial Times* (27 April 2020), https://www.ft.com/content/2f01cf55-d4b7-491e-bda8-5167731 b5ce5 (accessed 30 October 2020).

Prominent borrowers of traders are Chad and Congo-Brazzaville. In 2014 Chad's state oil company agreed to supply crude cargos in return for a US $1,45 billion loan from Swiss commodity and mining giant Glencore. Two years later the Glencore debt alone accounted for 98 per cent of Chad's external debt. Most of the country's oil production went into the repayment leaving little left for other services and expenses. Oil is Chad's primary source of revenue and it struggled immensely to pay off the debt, despite it having been restructured.[45] With the oil price tumbling in early 2020 and the pandemic hitting already-indebted countries hard, Chad asked Glencore to suspend the payments which would be oil shipments of US $115 million for the year.[46]

The oil-producing Republic of the Congo (Congo-Brazzaville) finds itself in a similarly severe debt crisis. The country has both borrowed from China Eximbank as well as from commodity trading companies. The country received cash-for-oil loans from Switzerland-based traders Trafigura (US $1 billion); Glencore (US $850 million); and Gunvor (US $625 million).[47] The Congo is highly indebted – its external debt was peaking in 2017 at 117 per cent of the GDP. According to the IMF, Congo still owed US $966 million to Glencore and US $268 million to Trafigura in September 2019.[48] The government has taken these RBLs without public consultation and tenders and, therefore, was highly criticised by civil society. Moreover, an investigation by the Swiss non-governmental organisation (NGO) Public Eye revealed that Gunvor not only benefited from inflated lending rates and additional charges, but also obtained its contracts after its employees had offered secret payments to government officials.[49] A Swiss court held Gunvor criminally liable. One of its employees was sentenced to 18 months' imprisonment for bribery.[50] Generally, the size, terms and timeframe of an RBL can enormously affect countries such as the DRC, Chad and Congo-Brazzaville. Moreover,

45 N White 'Oil-hungry Western companies are contributing to huge debt problems in Africa – G20 leaders need to fix this' *The Independent* (30 November 2018), https://www.independent.co.uk/voices/africa-oil-companies-g20-summit-fix-glencore-debt-chad-a8660606.html (accessed 30 October 2020).

46 A Soto & K Hoje 'Chad asks to suspend payments on Glencore oil-backed loan' *Bloomberg* (20 September 2020), https://www.bloomberg.com/news/articles/2020-09-20/chad-asks-to-suspend-payments-on-glencore-oil-backed-loan (accessed 30 October 2020).

47 Mihalyi et al (n 28) 10.

48 IMF 'Republic of Congo. Staff Report for the 2019 Article IV Consultation. 34' (2020).

49 Public Eye 'Wie gemschmiert: Ölhändler Gunvor im Kongo', https://www.publiceye.ch/de/themen/rohstoffhandel/gunvor-kongo (accessed 30 October 2020).

50 D Sheppard & N Hume 'Gunvor faces scrutiny of historical dealings in West Africa' *Financial Times* (28 August 2018), https://www.ft.com/content/762b453e-aad7-11e8-94bd-cba20d67390c (accessed 30 October 2020).

when coupled with lacking public oversight, they create spaces for corrupt practices. In economically weak or indebted countries, RBLs contribute to high debt distress often leading to an economic crisis. Transparency and sustainability are the key challenges of resource-based borrowing.

13.3.2 Challenges with RBLs

The NRGI points out a number of advantages attached to RBLs: RBLs might be positive in the light of infrastructure development and may offer cheaper and faster loans to governments.[51] The African experiences, however, have shown the massive challenges and risks of RBLs. RBLs are hard to monitor, complex and often with several actors involved. They are, moreover, often off-budget and not subject to budgetary safeguards, parliamentary scrutiny, public tenders and government oversight because the borrower is seldom the government directly but a state-owned entity.[52]

Opacity

There is an increased governance risk attributed to state-owned companies with many not publishing financial reports. According to a report by the IMF, 62 per cent of national oil companies reviewed in the study were ‘weak’, ‘poor’ or ‘failing’ in regard to public transparency.[53] The terms and conditions of RBLs are rarely available in the public domain and obtaining reliable information is extremely difficult. This might not come as a surprise considering that the involved parties have little interest in transparency when trading off their national resources for fast money – often at the expense of the population and the generations to come. This lack of transparency resulted in an immense risk of corruption, as the Gunvor case in Congo-Brazzaville showed.

The EITI is pushing for the disclosure of RBLs and has included related requirement in their 2019 Standard. It requires implementing countries to disclose barter arrangements (for instance, resources-for-infrastructure deal) as well as any sales of the state’s share of production or other revenues collected in kind.[54]

51 https://resourcegovernance.org/sites/default/files/documents/resource-backed-loans-pitfalls-and-potential.pdf (accessed 30 October 2020).

52 N White ‘Commodity traders: Lenders of last resort for Africa’s oil-producers’ *Global Witness* (3 July 2019), https://www.globalwitness.org/en/blog/commodity-traders-lenders-of-last-resort/ (accessed 30 October 2020); Mihalyi et al (n 28) 8.

53 D Manley, D Mihalyi & PRP Heller ‘Hidden giants. It’s time for more transparency in the management and governance of national oil companies’ IMF 57.

54 EITI *Standard (2019)* ‘Requirements 4.2 and 4.3’, https://eiti.org/document/eiti-standard-2019#r4-2 (accessed 30 October 2020).

Unsustainability and the debt problem

The fundamental problem with RBLs is that a high risk lies with the borrower: A country becomes ever more reliant on its extractive sector and may be stuck and forced into oil or mineral production for decades. Moreover, the borrower is exposed to the volatile market prices. If prices for the commodity fall or the agreed-upon volume cannot be produced within the often very short timeframe given, the borrower has to deal with the consequences. In the case of a country heading towards insolvency, the possibility of a rescheduling the repayment to achieve a sustainable debt situation is not necessarily available from lenders of RBLs.[55] This concerns both RBLs granted by commodity traders and Chinese policy banks. At the same time, the lenders may benefit from a steady supply of resources and revenue from the high service fees and rents. Due to the little public information available on RBLs, it is difficult to estimate the prices of especially long-term resources-for-infrastructure-deals and evaluate the overall fairness of it.[56] No doubt that fast-growing debt is a recipe for disaster; its effects can be devastating. A government may no longer be able to provide basic public services to the population such as education and health care. While the G-20 agreed to suspend debt repayment for the poorest countries due to the current pandemic, this does not automatically include private sector lenders. At the same time the growing instability exaggerated by the COVID-19 pandemic and the high demand in minerals make RBLs increasingly important, especially for mining-dominated nations such as Zimbabwe.

13.4 COVID-19 and the Zimbabwean economy

A report by Africa Confidential exposes a letter by the Zimbabwean Minister of Finance, Mthuli Ncube, to David Malpass, president of the World Bank, Kristalina Georgieva, managing director of the IMF, and Akinwumi Adesina, president of the African Development Bank, asking them for support with the rescheduling or cancellation of all Zimbabwe's foreign bilateral debt arrears and help in clearing all its multilateral arrears.[57] It is reported that the letter indicated that the Zimbabwean economy contracted sharply in 2019 and that the economy could further

55 N White 'Hey, big lenders' *Global Witness* (30 November 2018), https://www.globalwitness.org/en/blog/hey-big-lenders/ (accessed 30 October 2020); Mihalyi et al (n 28) 33.

56 Maiza-Larrarte & Claudio-Quiroga (n 35) 424.

57 Africa Confidential 'Zimbabwe government close to collapse as Ncube sends plea for cash' (30 April 2020), https://www.africa-confidential.com/article/id/12945/Zimbabwe_government_close_to_collapse_as_Ncube_sends_plea_for_cash (accessed 30 October 2020).

contract by 15 to 20 per cent due to the COVID-19 pandemic. Moreover, the Minister indicated that the government needs $200 million for unexpected spending to fight the pandemic and referred to World Bank estimates that the country's financing gap is nudging $1 billion for health, education, food security and social protection. As noted above, on 13 April 2020 the IMF cancelled debt repayments due to it by the poorest developing economies for the next six months.[58] Zimbabwe was exempted from the list of countries that were offered debt relief. Africa Confidential reports that 'senior finance officials in Washington say that grand corruption and state violence have to go before they resume economic cooperation with Harare'.[59] Thus, the Zimbabwean government is in a dire financial position and cannot unlock financial streams from traditional lending institutions. The key question is how Zimbabwe will finance its way out of the COVID-19 impact. Zimbabwe's economy is underpinned on mining and the huge reliance on mining explains why the Zimbabwean government of entreated the mining sector for relief on 19 April 2020 and allowed the mining sector to resume full operations.

A paper by the Zimbabwe Environmental Law Association (ZELA) and the Centre for Natural Resource Governance (CNRG) partly attributes the government's decision to fully re-open the mining sector on government's inability to access COVID-19 external financing.[60] The paper makes it clear that due to the centrality of mining to the economy, mining operations, in particular coal mining, continued even during the 21-day lockdown. Mining, therefore, underpins Zimbabwe's hope for economic recovery. Prior to the COVID-19 pandemic, the government of Zimbabwe had formulated an economic recovery plan that is hinged on mining. The government's vision to transform the country into an upper middle-income economy by 2030 is based on mining. Through this strategy, mining projects should unlock US $12 billion in revenues by 2023: Gold is expected to contribute US $4 billion, platinum US $3 billion, chrome, iron, steel, diamonds and coal will contribute US $1 billion, with lithium being expected to bring in US $500 million while other minerals will fetch US $1,5 billion. The huge reliance on mining is likely to push the Zimbabwean government further in using minerals resource and other natural resource as security to access foreign financing. Already prior to

58 IMF (n 25).

59 Africa Confidential (n 57).

60 Zimbabwe Environmentral Law Association 'COVID-19: Mining Sector and Communities Situational Report' (2020), http://www.zela.org/covid-19-mining-sector-and-communities-situational-report/ (accessed 30 October 2020).

the outbreak of COVID-19, Zimbabwe was mortgaging their resources to access foreign financing.[61]

13.5 Mining in the Zimbabwean economy

Zimbabwe's mining sector has grown in importance over the past few decades. The decreasing viability of the agricultural and industrial sectors, coupled with the vast mineral resource, has played a role in heightening the importance of the sector. Presently, there are more than 40 different minerals in Zimbabwe, including diamonds, platinum, gold, nickel, copper, iron ore, zinc, chromium ores, asbestos, vanadium, lithium, tin and coal.[62] In 2018, gold, platinum group minerals (PGM), diamonds, nickel, chrome and coal dominated the sector and accounted for 95 per cent of the value of minerals generated in Zimbabwe.[63]

By the year 2019 mining contributed about 16 per cent to the country's GDP, more than 60 per cent of exports and accounted for a significant share of foreign direct investment (FDI).[64] Due to its intense labour requirements, the sector has created formal employment for over 45 000 people.[65] Mining has also been a source of livelihood for millions across the country who engage in artisanal and small-scale (ASM) mining. It is estimated that ASM, especially of gold, directly provides a livelihood for more than one million people.[66] In 2018 ASM contributed 65,5 per cent of gold deliveries to Fidelity Printers and Refineries. Gold deliveries from

61 Global Witness 'A crude awakening: The role of the oil and banking industries in Angola's civil war and the plunder of state assets', https://cdn.globalwitness.org/archive/files/pdfs/a per cent20crude per cent20awakening.pdf (accessed 15 September 2020).

62 Mining Weekly 'Myriad of opportunities in Zim's mining sector' (8 September 2017), https://m.miningweekly.com/article/myriad-of-opportunities-in-zimbabwes-mining-sector-2017-09-08 (accessed 15 September 2020).

63 'State of the mining industry 2018 Report: Prospects for 2019' (November 2018), https://www.icaz.org.zw/imisDocs/State%20of%20the%20mining%20industry%202018%20report%20prospects%20for%202018.pdf (accessed 8 September 2020).

64 G Chigumira et al 'Enhancing natural resources management in Zimbabwe: Case studies of mineral exploitation, forestry management, wildlife management and solar exploitation' (2019), http://www.zeparu.co.zw/sites/default/files/2019-05/ENHANCING%20NATURAL%20RESOURCE%20MANAGEMENT%20IN%20ZIMBABWE%20for%20web.pdf (accessed 30 July 2020).

65 Government of Zimbabwe (2016) P Jourdan et al 'Mining sector policy study' Zimbabwe Economic Policy Analysis and Research Unit (2012), http://www.zeparu.co.zw/sites/default/files/2018-03/Mining%20Sector%20Policy%20Study%20pdf.pdf (accessed 12 November 2020).

66 PACT 'A gold opportunity, scoping study of artisanal and small-scale gold mining in Zimbabwe' (2015), https://www.pactworld.org/a%20golden%20opportunity (accessed 25 August 2020).

small-scale producers increased from 13,2 tonnes in 2017 to 21,7 tonnes in 2018.[67]

13.6 Economic contraction and the RBL route for Zimbabwe

Despite these seemingly and expected positive attributes of the mining sector, mining in Zimbabwe has been associated with worrisome ills, such as corruption throughout the commodity value chain, illicit financial flows, revenue leakages, violence among artisanal miners and the signing of opaque mining agreements under the 'mega deals' policy narrative of the previous government and the 'open for business' mantra during the current government regime. The opacity associated in Zimbabwe's mineral sector is evident in the granting of licences, the negotiation of contracts, production data, the collection, allocation expenditure and accounting of mineral revenue,[68] also affecting agreements covering RBLs in Zimbabwe.

As shown by Table 1 below, RBLs have a long history in Zimbabwe dating back to 2004 when a case gained media attention in Zimbabwe which involved Chinese corporations, namely, China North Industries Corporation (NORINCO) and Anhui Foreign Economic Construction Company (AFECC). Since the 2000s Zimbabwe was alienated from the international community, and at the same time China was seeking direct access to natural resources.[69] One of the first RBLs to be reported in Zimbabwe was with NORINCO, active in both the defence industry and in providing engineering contracting. In 2006 NORINCO was said to have supplied mining equipment to Hwange Colliery Company (in which the government of Zimbabwe is the majority shareholder) worth US $6,2 million in exchange for coal and coke to NORINCO's smelters in the Democratic Republic of the Congo.[70] Additionally, NORINCO was reported to have supplied arms to the government of Zimbabwe in exchange for mining concessions and mineral exports to China.[71]

67 https://www.zimbabwesituation.com/news/artisanal-mining-can-boost-economy/

68 M Dhliwayo & M Sibanda 'From Zimbabwe mining revenue transparency initiative to the extractive industries transparency initiative' (2019) *Zimbabwe Environmental Law Association*, http://www.zela.org/from-zimbabwe-mining-revenue-transparency-initiative-to-the-extractive-industries-transparency-initiative/ (accessed 25 November 2020).

69 A Karkkainen 'Does China have a geo-economic strategy towards Zimbabwe? The case of the Zimbabwean natural resource sector' (2015) 14 *Asia Europe Journal* 185.

70 'Hwange in barter deal with Chinese Ndamu Sandu' *Zimbabwe Independent* (12 May 2006), https://www.theindependent.co.zw/2006/05/12/hwange-in-barter-deal-with-chinese/ (accessed 26 October 2020).

71 Karkkainen (n 69) 12.

AFECC, a large construction China state-owned enterprise, entered Zimbabwe's diamond mining sector in 2009 through a joint venture (Anjin Investments) with the Zimbabwe defence forces. According to Karkkainen, the mineral revenue from Anjin Investments was used to finance the National Defence College.[72] The RBL was structured in such a manner that China Eximbank advanced a loan of US $98 million to the government of Zimbabwe through the Ministry of Finance and this was to be repaid using the latter's share of profits from Anjin Investments.[73] Gross human rights violations have resulted in this engagement: In the diamond field of Marange, Anjin Investments has been accused of polluting the Save Odzi Rivers jeopardising the right to a healthy environment and water of Marange and surrounding communities. In a blatant disregard of the Zimbabwean environmental laws and policies, Anjin Investments, assisted by state security, detained environmental management agency officers for trying to carry out their mandate to inspect and monitor water pollution.[74] The environmental management agency officers were detained by mine management and the military for trying to inspect and monitor water pollution.[75] Further, the use of excessive force by the state security and private security at Anjin Investment mining claim as well as unfair labour practices have also raised concerns over the operations of the Chinese mining company.[76]

China is not the only country with which Zimbabwe has been associated with respect to RBLs in Zimbabwe. Reports connect Belarus, India and Russia with RBLs in Zimbabwe. For instance, in 2015 the Belarus Digest reported that Zimbabwe and Belarus had entered into an agreement which allowed Zimbabwe to access capital equipment and technical know-how regarding the mining of rivers.[77] This agreement was entered into despite the fact that Belarus had no proven record of

72 S Nyaira 'Diamond-financed Defence College deal exposes Zimbabwe's China ties' *VOA News* (2011), http://archive.kubatana.net/html/archive/econ/110616voa.asp?sector=ECON (accessed 21 October 2020).

73 Karkkainen (n 69).

74 S Mtisi 'Diamond mining and human rights in Marange: Examination of state and non-state actors' duties and liability for human rights violations' unpublished LLM dissertation, Midlands State University, 2015 60.

75 Informal discussions with Environmental Management Officers in Mutare (16 April 2016).

76 'Outrage over brutal Chinese labour practices'. https://www.theindependent.co.zw/2012/04/12/outrage-over-brutal-chinese-labour-practices/ (accessed 27 October 2020).

77 I Gubarevich 'Belarus Digest Belarus and Zimbabwe aim at 'mega deals' (8 December 2015), https://belarusdigest.com/story/belarus-and-zimbabwe-aim-at-mega-deals/ (accessed 26 October 2020).

expertise in river bed mining.[78] This may make one believe that these deals are entered into for political expedience and not necessarily for economic viability and without the interests of the ordinary Zimbabwean at heart. With regard to Russia, on 10 January 2020 the *Standard*, one of Zimbabwe's daily newspapers, reported that the government of Zimbabwe was contemplating an agreement with Russia involving the replacement of the former's military helicopters with payments based on the exchange of minerals. Further, it was reported that the government, faced with fuel shortages, was also negotiating a deal with Russia wherein it is provided with oil in exchange for diamonds.[79]

In 2019, Bloomberg writes that Zimbabwe secured a US $500 million loan from Afreximbank in order to stabilise its currency. In return, the government offered platinum production as collateral.[80] Shortly afterwards the newspaper writes that 'the main collateral for African Export-Import Bank's US $500 million loan to Zimbabwe is a mine that hasn't been dug yet'.[81] The loan should be paid back within four years through revenues of a mine. The mine is held by Great Dyke Investments, a venture between Russian investors and the Zimbabwean military's Zimbabwe Defence Industries Ltd. Yet, the mine is not developed and struggles to attract further investors. Platinum could come from other sources, including large-scale platinum mines in Zimbabwe. In autumn 2020 Bloomberg journalist Marawanyika revisited Grand Dyke Investments, which lies 65 kilometres outside of Harare, only to learn that significant amounts of funding still are needed to transform the exploration site into a platinum-producing mine.[82]

The common trend among the reported RBLs entered Zimbabwe is the involvement of the military and the opaqueness of the agreements. Information regarding the RBLs is mainly based on rumours in the media and media statements and reports. The governments of Zimbabwe, China, Belarus or Russia do not seem to want to be transparent on the terms of

78 O Manayiti 'Belarus gold mining deal questioned' (4 November 2018), https://www.thestandard.co.zw/2018/11/04/belarus-gold-mining-deal-questioned/ (accessed 21 October 2020).

79 https://allafrica.com/stories/202001310661.html

80 G Marawanyika (2019), https://www.bloomberg.com/news/articles/2019-05-20/zimbabwe-got-loan-from-afreximbank-using-platinum-as-collateral (accessed 21 October 2020).

81 R Ndlovu & L Prinsloo (2019), https://www.bloomberg.com/news/articles/2019-05-22/zimbabwe-secures-500-million-backed-by-an-unmined-metal-deposit (accessed 10 January 2021).

82 G Marawanyika (2020), https://www.bloombergquint.com/business/russian-plan-to-dig-biggest-zimbabwe-platinum-mine-clears-hurdle (accessed 10 January 2021).

the agreements, which in turn impedes citizen accountability and scrutiny. Mortgaging natural resources is a clear sign of a lack of creditworthiness and a struggle to attract banks as lenders. Minerals become Zimbabwe's last resort.

Given the increasing need to finance the economic recovery of a country negatively impacted by the COVID-19 pandemic and its limited access to finance, Zimbabwe still has to engage international commercial entities, RBLs may seem attractive to the government going forward. It is worth noting that other than mortgaging its resource for loans, Zimbabwe has also been swapping some of its resource rights in return for infrastructure development in what is known as resource-for-infrastructure (R4I) swaps (see Table 2). The NRGI data set shows that between 2004 and 2016 Zimbabwe contracted RBLs that constitute 2 per cent of the GDP.

Table 1: Data on some of the RBLs in Zimbabwe

Agreement years	Loan Value ($)	Borrower entity	Lending country	Lender entity	Associated Project
2004	110	ZESA- Rural Electrification Agency	China	CATIC	Purchase of rural electrification agency equipment
2006	200	Government	China	Eximbank	Purchase of agricultural equipment
2011	98	Government	China	Eximbank	Construction of the National Defence College

(Source: Data Extacted from the Resource Backed Loans : Pitfalls and Potential. A report by the NRGI)

Table 2: Data on R4I swaps in Zimbabwe

Year	Project Description	Loans	Terms			Conditions (resource used	Additional agreements to secure the loan
			Interest	Grace	Period in years, per cent in years		
2007	Construction of three thermal plants and chrome mine	$1.3 billion	A memorandum of understanding was signed to finance three power plants with chrome export revenues. Reports issued in 2010 indicate that the agreement had not materialised				
2009	Development of platinum mine	$ 5 billion	A memorandum of understanding was signed to 50 per cent equity in a $40 billion platinum concession for a $5 billion concession credit line. In 2011 a credit line limited to $3 billion was still under discussion				
2011	Construction of the National Defence College	$98 million	2 per cent	7	20	Diamonds from Marange	If there is any change of laws for government policies in Zimbabwe making it difficult for either party to perform its obligation, China could declare all the sum payable immediately

Source: (Konijn 2014, Chinese Resources- For Infrastructure (R41) Swaps: An Escape from the Resource Curse)

13.7 RBLs and Zimbabwean laws

Even though Zimbabwean laws do not specifically mention RBLs, some legal provisions regarding public finance management, especially on debt and borrowing, are worth noting. To begin with, the Constitution of Zimbabwe has a comprehensive chapter on public finance management (chapter 17) with section 298 clearly setting out the principles that should guide public finance management in Zimbabwe. In terms of section 298(1)(a) of the Constitution, one of the key aspects of public financial management is that there must be transparency and accountability in financial matters. Transparency is defined as 'increased flow of timely and reliable economic, social and political information, which is accessible to all relevant stakeholders'.[83] Accountability can be either vertical in that it is demanded from below by citizens, or horizontal in that institution of the state check abuses by other public agencies and branches of government and impose a requirement to report sideways.[84] With RBLs, the Zimbabwean government seems to be ignoring this critical provision. Information regarding the extent of the loan, repayment terms and period and the quantity and value of the minerals exchanged for the loans is hard to obtain. This makes it difficult for citizens to participate and hold the government to account where RBLs are concerned. Section 298(1)(f) goes even further to mention that public borrowing and all transactions involving the national debt must be carried out transparently and in the best interests of Zimbabwe. Considering the RBLs discussed earlier, one would wonder whether they are in the best interests of Zimbabwe or are only saddling present and future generations with debt and mortgaging the future of Zimbabwe. In a country where the public health system was failing and the education system deteriorating around the time when RBLs with AFECC were entered into, it cannot be said that these loans were contracted in the best interests of the country.

Closely related to transparency is the right of citizens to access information held by the government and public entities to enforce a right or for public interest and accountability. Without credible and timely information on RBLs, citizens and other government agencies cannot hold the responsible ministries to account as expected in terms of section 298(1) of the Constitution of Zimbabwe. In support of the correlation

83 T Vishwanath & D Kaufmann ' Towards transparency in finance and governance' (2003) *SSRN Electronic Journal* 10.2139/ssrn.258978 (accessed 26 October 2020).

84 A Schedler 'Conceptualizing Accountability' in L Diamond, MF Plattner & A Schedner (eds) *The self-restraining state: Power and accountability in new democracies* (1999).

between access to information and accountability, the High Court of Zimbabwe in *Hitschmann v City of Mutare* observed:

> There is no doubt access to information held by public institutions more so for purposes of ensuring that they complied with the law in carrying out their obligations ensures accountability by these public bodies. If the courts fail to give effect to these constitutional provisions that promotes transparency and accountability by public bodies, then the ability of citizens to hold public actors to account will be violated.

Dealing with similar provisions of access to information in the South African Constitution, the Constitutional Court in *Brűmmer v Minister for Social Development and Others* held:[85]

> The importance of this right … in a country which is founded on values of accountability, responsiveness and openness, cannot be gainsaid. To give effect to these founding values, the public must have access to information held by the State. Indeed, one of the basic values and principles governing public administration is transparency. And the Constitution demands that transparency 'must be fostered by providing the public with timely, accessible and accurate information.

The manner in which RBLs are contracted in Zimbabwe does not seem to respect the principles of public finance management set out in the Constitution. For instance, the RBL involving AFECC, China Eximbank, Anjin and the construction of the National Defence College was only made available to Parliament for approval within 24 hours before the date of debate, which many legislators viewed as not sufficient time to read and meaningfully debate the agreement.[86] While the debate in Parliament allowed for some of the terms of the agreement to become public, such as the 2 per cent per annum interest to the loan, seven-year grace period within which only interest will be paid, repayment in bi-annual instalments for 13 years and the preferential treatment of Chinese goods, technologies and services during the construction of the National Defence College, this disclosure does not meet the requirements of prompt and timely disclosure as the public was aware of the provisions only after the agreement had been signed by the executive and approved by Parliament.[87] While this RBL was contracted before the promulgation of the current Constitution, the government has not changed the manner in which it conducts itself

85 2009 (6) SA 323 (CC) para 62.

86 http://archive.kubatana.net/html/archive/legisl/110606veritas.asp?sector-legisl (accessed 26 October 2020); House of Assembly Hansard Zimbabwe (31 May 2011).

87 World Bank (n 5) 1.

with regard to RBLs, as the alleged agreements involving Belarus and Russia indicate.

In addition to citizens' accountability, Parliament also has a role to play in oversight where RBLs are concerned. The Constitution of Zimbabwe empowers Parliament to play a vital oversight role on loan agreements and public debt, and this includes RBLs. For instance, section 300 gives Parliament the power to enact a law that sets limits on the borrowing by the government, the public debt and debts whose repayments are guaranteed by the government of Zimbabwe. The section went on further to provide in terms of subsection (4)(b) that the minister has an obligation to report twice annually to Parliament on the performance of loans raised by the state, and loans guaranteed by the state. In keeping with section 300, the Public Debt Management Act (chapter 22:21) was promulgated into law in 2015.

While the Public Debt Management Act has provisions compelling the government of Zimbabwe to obtain parliamentary approval of borrowing in excess of limits set by law (70 per cent of the national GDP) which may apply to RBLs, the setup of the Parliament proves to be a limitation to the effectiveness of these provisions. The Zimbabwean Parliament tends to be dominated by one party which also constitutes the government and, given that the Parliament operates through a whipping system, the independence and watchdog role of Parliament is adversely impacted.[88] Another constitutional provision of importance in the RBL discourse is section 327 of the Constitution of Zimbabwe. Section 327(3) provides:

> An agreement which is not an international treaty but which (a) has been concluded or executed by the President or under the President's authority with one or more foreign organisations or entities, and (b) imposes fiscal obligations on Zimbabwe, does not bind Zimbabwe until it has been approved by Parliament.

This provision is encompassing and covers RBLs. In a functioning democracy, this provision provides an opportunity to ensure that RBLs or any other agreements entered into by the government are in the national and public interest. Parliamentary oversight is an important tool.[89] The

88 P Mushoriwa 'Improving the investment climate – Suggestions on legal aspects of public debt management', http://www.mushoriwapasi.co.zw/2020/04/13/improving-the-investment-climate-suggestions-on-legal-aspects-of-public-debt-management/ (accessed 21 October 2020).

89 S Mtisi & M Matsvaire 'Secretive constitutional amendment mischief: Implications of Constitutional Amendment Bill No 2 on Transparency and Accountability in Zimbabwe's Mining Sector', http://www.zela.org/secretive-constitutional-

import and nature of parliamentary oversight on RBLs and mining contracts in general in Zimbabwe is further at risk as the government is proposing an amendment to section 327 through clause 23 of the Constitutional Amendment Bill. The amendment seeks to remove the requirement of parliamentary approval on agreements signed between the government and international entities. The proposed amendment and the failure of the government to enact a law to provide for the negotiation and performance of mineral concessions and other rights is an indication of the unwillingness of the government of Zimbabwe to promote transparency and accountability in the mining sector.

13.8 Conclusion

This chapter has shown that as a result of economic contraction which started way back in 2000, Zimbabwe engaged in the process of mortgaging its resources in return for loans. The mortgaging of resources through RBLs is likely to continue in the future as the Zimbabwean economy has taken a hit from the COVID-19 pandemic. Comparing RBLs across the African continent, the Zimbabwean examples are in line with challenges these loans have caused. An assessment of the Zimbabwean RBLs that have been known to be signed so far reveals that RBLs have been opaque and involved little or no citizen participation, lack parliamentary oversight and some have resulted in gross human rights violations, such as the conduct of Anjin Investments in the diamond field of Marange. Governmental regulation regarding RBLs is increasing instead of restricting and reducing their risks. There is a need, therefore, for several policy responses to this challenge. In terms of Domestic Resource Mobilisation (DRM), Zimbabwe needs to consider financing its own development not through loans but through innovative ways that include improving the tax regime to allow more investors, curtailing corruption to avoid leakages in the mining sector as well as promoting value addition on raw materials. In the short run, there is a need for a policy and law to guide the contraction of loans through the mortgaging of resources, and Parliament needs to be involved in that process. That law and policy should spell out a threshold of what is permissible in terms of resource mortgaging. Parliament's involvement in this process is under threat from the proposed constitutional amendment 23 which seeks to remove Parliament from reviewing performance contracts in Zimbabwe. It becomes critical for civil society in Zimbabwe to lobby and advocate parliamentary oversight over all mining contracts. Parliament also needs capacitation so that they have an informed view

amendment-mischief-implications-of-constitutional-amendment-bill-no-2-on-transparency-and-accountability-in-zimbabwes-mining-sector/ (accessed 26 October 2020).

when they review contracts and licences. Transparency will be key in any RBL to come, both in the contraction of new loans and the monitoring and progress of debt servicing.

On the other hand, there is also a need for the international community to demand the same amount of transparency, room for rescheduling and restructuring, obligations for responsible resource-based lending and borrowing and financial oversight as there is for traditional loans. RBLs have so far received little attention. Responsibility lies not only nationally but also globally. The future generation's resources should not be sold out for today's short-lived greed.

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14 Towards utilisation of domestic resources in settling Zimbabwe's sovereign debt

Jimcall Pfumorodze

14.1 Introduction

Currently, there are discussions involving Zimbabwe and international financial institutions and countries to which it owes money. The profile of these creditors include the World Bank, the African Development Bank (AfDB), Paris Club creditors and other creditors. These ongoing discussions are part of efforts to have the over US $8 billion external debt restructured.[1] Zimbabwe has submitted several proposals for a debt-restructuring process to those institutions and countries to which it owes money. Zimbabwe's external debt stand at around US $8,2 billion, of which US $6,34 billion is accumulated arrears. Multilateral institutions are owed US $2,65 billion, of which 90 per cent are arrears. To the World Bank Group, the arrears are US$1.33 billion, for African Development Bank US$689 million while arrears to the European Investment Bank are US$ 329 million and US$ 28 million are for other multilateral creditors. Bilateral external debt is estimated to be US$5.56 billion, of which arrears constitute 71 per cent of the bilateral debt. Of this amount, US $3,63 billion is for Paris Club creditors while the remaining US $1,63 billion is for non-Paris Club creditors.[2] These external arrears prevent the country from accessing fresh financing from global financial institutions and traditional bilateral and commercial creditors. Zimbabwe is one of the highly-indebted countries in the world but was not considered in the Highly Indebted Poor Countries (HIPC) Initiative and the Multilateral Debt Relief Initiative (MDRI) as it did not meet the criteria.[3] The situation is exacerbated by the COVID-19 pandemic and its economic impacts, which needs urgent attention in terms of preventative measures as well as for the vaccination programme.

1 Zimbabwe, The National Budget Statement, presented to the Parliament of Zimbabwe on 26 November 2020, by Prof Mthuli Ncube, Minister of Finance and Economic Development, Harare.

2 As above. See also https://www.afdb.org/en/countries/southern-africa/zimbabwe/zimbabwe-economic-outlook (accessed 1 January 2021).

3 See International Monetary Fund Heavily Indebted Poor Countries (HIPC) Initiative and Multilateral Debt Relief Initiative (MDRI) Statistical Update, December 2014 7.

The concept of sovereign debt management and restructuring is broad.[4] In the case of Zimbabwe, it encompasses the repayment of the principal amount and interest thereon, and also

> negotiations and application of new loan agreements with private banks and international financial institutions (IFIs); establishment of a new structured framework for re-engaging with the international community – so as to normalise relations and seek removal of economic and political sanctions; utilisation of donor grants, special drawing rights (SDRs) and new loans; introduction of new debt instruments; and debt restructuring.[5]

This chapter focuses on public external debt. This refers to loans and borrowings that are made by creditors located outside the country's borders in foreign currency with a view to supplementing domestic financial resources.[6] It also includes government guaranteed loans that are taken by parastatals, private entities such as banks or even individuals. Thus, public and publicly-guaranteed external debt (PPGED) refers to both debts to foreign creditors taken by the government itself and those the government has guaranteed.

This chapter, therefore, seeks to evaluate the Zimbabwean strategies with which Zimbabwe has come up in its sovereign debt restructuring. It will start by giving a brief background on how Zimbabwe has managed its sovereign debt. This is followed by a discussion on sovereign debt management strategy and plans that were implemented in Zimbabwe between 2010 and 2020 and an examination of the current challenges. It will analyse a set of proposals that have been suggested to date and test their suitability as responses to the current debt crises in the light of the challenges posed by the COVID-19 pandemic.

14.2 Background to and context of the Zimbabwe's public debt

Sovereign debt has a long history in Zimbabwe.[7] The debt history of Zimbabwe cannot be fully appreciated outside the political context. For

4 US Das, MG Papaioannou & C Trebesch 'Sovereign debt restructurings 1950-2010: Literature survey, Data, Stylised Facts, IMF Working Paper 2012 7.

5 T Saungweme & NM Odhiambo 'A critical review of the dynamics of government debt servicing in Zimbabwe' (2018) Studia Universitatis 'Vasile Goldis' Arad Economics Series Vol 28 Issue 3/2018 ISSN: 1584-2339; (online) ISSN: 2285-3065.

6 C Mbawu & P Nkala 'A critical review of the implementation challenges of the Zimbabwe Accelerated Arrears Clearance Debt and Development Strategy (ZAADDS)' (2018) 9 *Journal of Economics and Sustainable Development* 13.

7 N Mupunga & P le Roux 'Analysing the theoretical and empirical foundations of

this reason, the history has been divided into four phases, which will be discussed in detail in the following paragraphs.

The first phase was from independence to 2008, where there was accumulation of debts and a reluctance to repay under the ZANU PF government. At independence in 1980 Zimbabwe inherited US $700 million from the Rhodesian government of Ian Smith.[8] The Rhodesian government was using the money to buy weapons in the 1970s to use in the war against the people of Zimbabwe who wanted independence. Such purchase of arms by the Rhodesian government was against United Nations (UN) sanctions. The Zimbabwean government was under international pressure to take on the debt, which pressure was accompanied by promises of donor funding for reconstruction and development by Western countries that promised over US $2 billion for this purpose.

It may be argued that the debt inherited by Zimbabwe from the Rhodesian government was an odious debt.[9] The concept of odious debts usually is invoked where there is a change in political regime. The new regime would seek to avoid, in whole or in part, some debts that were incurred by its predecessor, on the grounds that they were used in a way that was harmful and not beneficial to the interests of the people of the country. Thus, this becomes both a moral and legal justification for not honouring the debt. The concept has been raised in the concept of state succession where the original debtor has ceased to exist. Arguably, it can apply even where there is a change of government.

However, the doctrine is difficult to successfully argue in practice. One of the challenges is that the creditor should have knowledge of the odiousness of the debt. It is difficult to prove the subjective knowledge of the creditor. Furthermore, a country would not wish to raise the doctrine of odious debts as it may affect the creditworthiness of the regime. Creditors may be hesitant to lend to the regime in the future.[10]

public debt dynamics in Zimbabwe' (2014) *Economic Research Southern Africa* (ERSA) 1; MA Matandare & J Titi J 'Public debt and economic growth nexus in Zimbabwe' (2018) 9 *Journal of Economics and Sustainable Development* 84; Saungweme & Odhiambo (n 5) 20.

8 African Forum and Network on Debt and Development (AFRODAD) 'The impact of indebtedness on human rights in Zimbabwe' (2019) *Africa Portal* 11.

9 KS Openshaw & CR Terry 'Zimbabwe's odious inheritance: Debt and unequal land distribution' (2014) *JSDLP-RDPDD* 42.

10 R Howse 'The concept of odious debt in public international law' Discussion Paper 185, July 2007, UNCTAD, United Nations, UNCTAD/OSG/DP/2007/4.

The 1980s were characterised by borrowing by the Zimbabwean government. Although Zimbabwe was promised developmental aid by Western countries, such aid did not materialise. Instead, Zimbabwe had to borrow to pay the Rhodesian loan as well as for the reconstruction after the destruction by the war. Furthermore, Zimbabwe also borrowed funds for drought relief. Some bilateral loans were tied to purchasing goods from the lending countries. For instance, the United Kingdom (UK) was tied to buying products from British companies such as General Electric. In addition, there were UK-backed loans that were given to Zimbabwe for the purchase of British-made Hawk aircraft. By the end of the 1980s Zimbabwe was spending a quarter of government revenue on debt repayment.

By 1990 Zimbabwe had to take financing loans from the International Monetary Fund (IMF) and the World Bank, in order to keep repaying the debt.[11] However, the IMF and World Bank pressured the government to liberalise its economy and to cut down on public spending. As a result, the 1990s were characterised by cutting down on public expenditure, trade liberalisation, deregulation of financial markets and prices and the relaxation of labour laws. These suggested economic policy reforms were expected to yield higher economic growth, bigger trade surpluses and increase the employment rate in the country. However, in practice the opposite results were achieved. Between 1990 and 1997 the economic growth retarded. Furthermore, the rate of unemployment almost doubled and there was a huge trade deficit. As a result, Zimbabwe started to default on its debt in 2000.[12]

Between 2000 and 2010 Zimbabwe was in default and did not even bother to make any payment plans. Prior to 2010 there was no comprehensive debt resolution strategy. As a result, arrears on external debt payments continued to accumulate. This has affected Zimbabwe's creditworthiness, especially with respect to multilateral financial institutions such as the IMF and the World Bank. These debts and arrears are blocking further access to multilateral financial institutions and are hampering the attraction of foreign direct investment. This in turn makes it difficult to revive and resuscitate the economy.

Thus, the first phase was characterised by the taking of new loans to repay other loans. It seems as if that was the debt strategy that backfired as the government started to default on the payment of the debts and accumulated many arrears and was left with a debt overhang. This

11 Mbawu & Nkala (n 6) 10.

12 Mupunga & Le Roux (n 7) 1; Mbawu & Nkala (n 6) 10.

development is consistent with the debt overhang theory, which states that where a government has defaulted and has a large debt obligation, it has no incentive to repay, especially when it has been in power for a long time.[13]

The second phase is from 2008 to 2013. The year 2008 witnessed a Global Political Agreement which saw the formation of the Government of National Unity (GNU) which was made by the then three main political parties, namely, the Zimbabwe African National Union Patriotic Front (ZANU PF); the Movement for Democratic Change (MDC); and the Movement for Democratic Change N (MDC-N). Mr Tendai Biti was appointed Minister of Finance and Economic Development and he spearheaded efforts to re-engage the creditors and discuss strategies for arrears and debt clearance. In terms of strategies and plans, the Zimbabwean cabinet approved the Zimbabwe Accelerated Arrears, Debt and Development Strategy (ZAADDS) in 2010.[14] This was the road map for the clearance of arrears and payment of debt. It was under the ZAADDS where a Debt Arrears Clearance Committee was formed, and in 2015 the Committee came up with the payment plan that was known as the Lima Plan, 2015-2018. The ZAADDS and subsequent plans are discussed in detail later in this chapter.

During the GNU, there was a new Constitution that also dealt with issues of public debt management. In 2010 the government established the Debt Management Office as a department in the Ministry of Finance. In 2015 this office was established on a statutory basis in terms of the Public Debt Management Act.

Overall, the second phase during the GNU was characterised by a drive to repay the external debts as evidence by several reforms that were made, including the debt strategies, the debt office as well as constitutional reforms concerning sovereign debts. This can be explained in light of the debt overhang theory, which states that where there is a change in government, the new government would want to clear the old debts, since it needs new financing and has little incentive to postpone payments on the old debt.

The third phase started at the end of the GNU. The tenure of the GNU ended in 2013 and the ZANU PF government was back in power. The momentum in coming up with strategies for debt repayment continued

13 K Keboyashi 'A theory of public debt overhang' (2013), https://ideas.repec.org/p/hit/cisdps/589.html (accessed 15 January 2021).

14 www.zeparu.co.zw

as witnessed by the passing of the Public Debt Management Act in 2015. Furthermore, the Debt Arrears Clearance Committee, which was formed in 2015, came up with the payment plan which was known as the Lima Plan, 2015-2018.[15] However, there was no proper implementation of the plan, as will be discussed later in this paper. As a result, the Lima Plan was not successful.

The final phase started in November 2017 and continues to the present. November 2017 witnessed the removal from power of Zimbabwe's President Robert Mugabe who had been in power for 37 years. He resigned amid protests by the people and a pending impeachment effort in Parliament. His resignation divided opinion as some were of the view that it constituted a *coup d'état*. However, that discussion is beyond the scope of this chapter. What is worth noting is that the post-Mugabe period, which saw the appointment of a new President, Emmerson Dambudzo Mnangagwa, is known as the Second Republic. As the new government, it is making concerted efforts to re-engage with the international community and implement the repayment plan.

However, the Second Republic has not had a smooth ride due to the outbreak of natural disasters and the COVID-19 pandemic. In 2019 and 2020 the Zimbabwean economy sustained a recession wherein it was estimated that that the gross domestic product (GDP) contracted by -6 per cent and -4.1 per cent respectively.[16] This is mainly due to the contraction in many sectors of the economy, including agriculture, mining, manufacturing, tourism and electricity generation.

14.3 Importance of sovereign debt management in Zimbabwe

Literature suggests that there is a relationship between government debt servicing and economic growth.[17] High debt-servicing costs create economic and financial uncertainties and discourage foreign investment.[18]

15 www.rbz.co.bw

16 Republic of Zimbabwe, National Development Strategy 1, January 2021 to December 2025, 16 November 2020, Harare, 5.

17 J Roos *Why not default? The political economy of sovereign debt* (2019); Saungweme & Odhiambo (n 5); A Carlos, P Braga & GA Vincelette *Sovereign debt and the financial crisis: Will this time be different?* (2011); L Rieffel *Restructuring sovereign debt: The case for ad hoc machinery* (2003); M Megliani *Sovereign debt: Genesis-restructuring-litigation* (2015); Das et al (n 4); DS Kamlani 'The four faces of power in sovereign debt restructuring: Explaining bargaining outcomes between debtor states and private creditors since 1870' PhD thesis, London School of Economics and Political Science, 2008.

18 B Clements, R Bhattacharya & T Nguyen 'Can debt relief boost growth in poor

Currently, Zimbabwe is in debt arrears. The Zimbabwean debt status has been dubbed as a development issue without the 'resolution [of which] there shall be no access to development resources from the international financial institutions'.[19] The arrears status with multilateral creditors has rendered the country ineligible to access funding from these institutions, as well as most other sources of finance. Clearing the external debt would unlock fresh capital injections 'which would accelerate inclusive and sustained economic growth and poverty reduction[20] and would normalise relations with creditors'. Therefore, the need to clear arrears is critical.

Zimbabwe's debt burden has affected the country's credit rating. Zimbabwe has lost out on several funding opportunities from international creditors. This has led to the suspension and or cancellation of a number of projects.[21] The projects that stalled include the US $400 million package from China for the expansion of the Kariba South power station;[22] the US $15 billion per year World Bank's Infrastructure Recovery Asset Platform; the US $ 500 million Rapid Social Response Programme; and the US $10 billion Infrastructure Crisis Facility.[23] Thus, the resolution to the burden 'will unlock fresh financing for critical infrastructure reconstruction projects and economic recovery programme that will significantly improve the quality of life of the ordinary Zimbabwean'.[24]

countries?' (2005) International Monetary Fund Economic Issues 34; J Baneth 'Some determinants of debt service sustainability in low-income aid dependent countries' (2003) 1; P Krugman 'Financing vs forgiving a debt overhang' (1988) 29 *Journal of Development Economics* 407; TJ Moss & HS Chiang 'The other costs of high debt in poor countries: Growth, policy dynamics, and institutions' Issue paper on debt sustainability 3, Centre for Global Development (2003) 1.

19 A Bvumbe cited 'On addressing Zimbabwe's huge debt burden', Brown Bag Dialogue Series, UNDP.

20 Zimbabwe Strategies for Clearing External Debt Arrears and the Supportive Economic Reform Agenda (2015) 2.

21 United Nations Development Programme 'Why a debt overhang is not good for the economy' Brown Bag Dialogue Issues 3.

22 As above.

23 As above..

24 Tendai Biti (former Minister of Finance) Foreword to the Zimbabwe's Accelerated Arrears, Debt and Development Strategy (ZAADDS).

14.4 A decade of debt management in Zimbabwe: An assessment of Zimbabwe's sStrategy 2010-2020

14.4.1 The Zimbabwe Accelerated Arrears, Debt and Development Strategy, 2010

This is the debt resolution strategy that was initiated in 2010 during the inclusive government. It was aimed at resolving Zimbabwe's debt problem. This strategy was motivated by the need to deal with Zimbabwe's unsustainable debt overhang and the country's lack of capacity to address the debt burden and attract new financing. This was during the GNU when there were serious attempts at dealing with the country's debt crisis. During this period there were several debt serving challenges that were faced by Zimbabwe.[25] These included 'liquidity constraints due to poor economic performance; lack of proper public sector financial management principles; improper composition and structure of the public debt; low investor confidence; low industrial and export competitiveness; and poor economic relations with the international donor community'.[26] The main features of the strategy were the following:

- the establishment and operationalisation of the Debt Management Office;
- reconciliation and validation of external debt;
- negotiating with creditors for arrears clearance, debt relief and new financing;
- re-engagement with international community on the removal of sanctions; and
- leveraging resources for debt clearance.

There are legal instruments that work hand in glove to operationalise this strategy.[27] The main instrument is the Public Debt Management Act 4 of 2015, which provides for the management of public debt in Zimbabwe; the establishment of the Public Debt Management Office on a statutory basis and provision for its functions and administration; provisions for the raising, administration and repayment of loans by the state and for the giving of guarantees in respect of certain loans; among other things. Other legislation includes the Constitution of Zimbabwe, the

25 D Danha et al 'Zimbabwe Equity Strategy 2015: At cross roads' (2015) Harare: IH Securities; International Monetary Fund (2016b); Zimbabwe 2016 Article IV Consultation: Staff Report; Press Release; and Statement by the Executive Director for Zimbabwe. Washington DC: International Monetary Fund.

26 Saungweme & Odhiambo (n 5).

27 As above.

Reserve Bank of Zimbabwe Act (chapter 22:15), the International Bank Loans Assumptions Act (chapter 22:08) and the Former Administration (Liabilities) Act (chapter 22:06). The main features of the ZAADDS are discussed below.

The establishment and operationalisation of the Debt Management Office

This office was established and became operational in 2010. In 2010 it was established merely as a department in the Ministry of Finance and Economic Development. In 2015 the Public Debt Management Act was passed which provided a statutory basis for the Debt Management Office. This Act also stipulates the functions and administration of the Debt Management Office. It also provides for the raising, administration and repayment of loans by the state and for giving guarantees in respect of certain loans. The functions of the Debt Management Office are provided for in section 5 of the Act. The Public Debt Management Office advises the Minister of Finance and Economic Development with respect to borrowings, negotiates with creditors on government borrowing and guaranteed loans, prepares and publishes annual borrowing plans as well as a medium-term debt management strategy. It also compiles and reports on all public debt arrears.

The ZAADDS encountered several implementation challenges and was subjected to much criticism. The Debt Management Office has been accused of lacking autonomy, resources as well as capacity.[28] Negotiations with creditors for arrears clearance, debt relief and new financing have not been successful. Zimbabwe is in a weak position in these negotiations and there is a lack of trust and confidence by creditors.[29] In addition, creditors have been accused of double standards when dealing with Zimbabwe. Furthermore, the operation of the principle of comparable treatment of creditors affects efforts at creditor negotiating. The attempt to leverage resources for debt clearance has been unsuccessful due to the fragile economic situation, disagreements on the valuations of resources as well as government's inconsistencies on natural resources policies.[30]

Reconciliation and validation of the external debt

The exercise to verify the actual amounts the government owes began in 2011. This audit is also a way of mitigating against fiscal indiscipline. The

28 Mbawu & Nkala (n 6) 20.

29 Mbawu & Nkala (n 6) 22.

30 C Mbaiwa Zimbabwe Coalition on Debt and Development, Sustainable and Inclusive management Framework for Zimbabwe (SIDMaF) (2019) 23, ZIMCODD: Harare.

main criticism of this exercise is that it lacks transparency. The information on reconciled and validated debt statistics is not publicly availed and even when done, it would be late.

Negotiation with creditors

In terms of the ZAADDS, the government would negotiate with creditors for arrears clearance, debt relief and new financing. In pursuit of this strategy, the government successfully engaged with the IMF to undertake a staff-monitored programme, which was successfully completed in 2015. The programme focused on key reforms showing that the country has the capacity to undertake the reforms required for funds-supported programmes. This was a pre-condition for negotiating arrears clearance and debt relief. Furthermore, in 2015 the government constituted a Debt Arrears Clearance Committee (DACC). The mandate of this Committee was to develop strategies to resolve the country's debt burden mainly with respect to international financial institutions. The Committee came up with the Lima Plan which was presented at the sidelines of the IMF/ World Bank annual meeting in Peru that was held from 8 to 12 October 2015. The plan was accepted by the creditors, namely, the African Development Bank, the Work Bank and the IMF. The details of the Lima Plan are discussed in the following part.

14.4.2 The Lima Plan, 2015

The Lima Plan (2015-2018) was the debt and arrears clearance plan that Zimbabwe negotiated with its international creditors. It involved the following:

- the use of domestic resources; it already transferred part of its special drawing rights (SDR) holdings kept by the IMF to clear the US $107,9 million debt in arrears;
- the use of a bridging loan, where African Export-Import Bank (Afrexim Bank) was to pay the AfDB loan; and
- the use of medium to long-term loan facility to pay other creditors, including the World Bank.

In accordance with the above plan, Zimbabwe managed to clear its US $107,9 million arrears with IMF in 2016. However, it is still in the process of settling a debt of about US $2,2 billion to other international financial institutions, including the World Bank and the AfDB.[31] The

31 M Mutize 'Zimbabwe wants to raise money through a sovereign bond: Why is this ill-advised' *The Conversation* (5 August 2020).

Lima Agreement expired in November 2018.[32] The Lima Plan was not implemented effectively due to non-conclusive negotiations on settling outstanding arrears. The international creditors wanted the implementation of some economic reforms that include enhancing investor confidence, the transformation of state-owned enterprises, the ease of doing business and fiscal consolidation. Zimbabwe did not undertake these reforms to the satisfaction of the international creditors, so the anticipated financial support did not materialise.[33]

14.4.3 The Transitional Stabilisation Programme 2018 to 2020

The Transitional Stabilisation Programme (TSP) is one of the main economic plans laid down in Zimbabwe's Second Republic in order to resuscitate the economy. It was spearheaded under the new Finance Minister, Professor Mthuli Ncube. Among other things, the TSP sought to integrate Zimbabwe into global financial markets.[34] This includes re-engaging cooperating partners over resolving Zimbabwe's external payment arrears. It also involves putting in place a comprehensive and coherent macro-economic policy framework, underpinned by a strong programme of fiscal adjustment and structural reforms.

At the time when the TSP was formulated, Zimbabwe's foreign debt amounted to about US $5,6 billion which consisted of the following:

- multilateral creditors, US $2,2 billion;
- the Paris Club, an informal group of creditor nations, US $2,7 billion;
- non-Paris Club creditors, US $700 million.

The TSP emphasised that in terms of sequencing, Zimbabwe needs to first and simultaneously clear its arrears to the AfDB, the World Bank and the European Investment Bank. This would be done as part of efforts to unlock external new financing required by the productive sectors.

32 B Mpofu 'Why Lima plan stalled' *The Independent* (15 September 2017).

33 Zimbabwe Coalition on Debt and Development, Statement on Arrears Clearance Strategy, 2015; T Biti 'Putting lipstick on a crocodile: Zimbabwe's sinister reengagement agenda' (16 April 2016), www.facebook.com (accessed 10 November 2020); PA Chinamasa *Zimbabwe: Strategies for clearing external debt arrears and the supportive economic reform agenda* (September 2015).

34 Zimbabwe 'Transitional Stabilisation Programme Reforms Agenda October 2018-December 2020: Towards a prosperous and empowered upper middle-income society by 2030' (5 October 2018); Harare; Labour and Economic Development Research Institute (Zimbabwe), Review of the Transitional Stabilisation Programme (TSP) (August 2020); L Chitongo, P Chikunya & T Marango 'Do economic blueprints work? Evaluating the prospects and challenges of Zimbabwe's transitional stabilisation programme' (2020) 9 *African Journal of Governance and Development*7.

14.5 Zimbabwe sovereign debt and COVID-19

The ZAADDS and the subsequent strategy were created without taking into account the COVID-19 pandemic, as by then it was not foreseeable. By early 2020, when the COVID-19 pandemic started to hit Zimbabwe, the country was already under a huge a heavy debt burden, and liable to pay debt arrears. The economy already was not performing well and the health delivery system was near collapse, punctuated by health personnel, including doctors and nurses, that were striking.

Faced with this challenge, the Zimbabwean government attempted to open negotiations and seek negotiations with its international creditors. On 2 April 2020 the Minister of Finance and Economic Development, Professor Mthuli Ncube, wrote a letter addressed to the heads of the IMF, the World Bank, the European Investment Bank, the AfDB and the Paris Club of Creditors.[35] The essence of the letter was to reschedule the payment of arrears and to allow Zimbabwe to access fresh finance in order to mitigate the effects of COVID-19.

The letter did not receive a favourable response. The Paris Club responded to this letter of assistance in the negative.[36] It gave the conditions that must first be met for Zimbabwe to normalise its relations with the international community. First, Zimbabwe had to implement substantive and sustainable political and economic reforms, in particular regarding respect for human rights, especially freedom of assembly and expression. Second, Zimbabwe should implement a staff-monitored programme by the IMF as an important first step of engagement. Third, Zimbabwe should clear World Bank and AfDB debt of over US $2 million.

This brings into question the relationship between sovereign debt and human rights. In 2012 the United Nations Commission on Human Rights came up with Guiding Principles on Foreign Debt and Human Rights.[37] These guidelines are meant to be followed by states and private, public, national and international financial institutions in the management of sovereign debt. These principles include the following:

- ensuring the primacy of human rights;
- equality and non-discrimination;

35 Reuters Staff 'Implement substantive reforms, Paris Club creditors tell Zimbabwe' *Reuters* (8 July 2020).

36 As above.

37 https://www.undocs.org/A/HRC/20/23 (accessed 20 January 2021).

- the progressive realisation of human rights;
- the state must ensure that the minimum core human rights obligations arising from debt repayment obligations are met;
- the obligation to avoid retrogressive measures on human rights obligations arising from debt repayment obligations or commitments;
- creditors and debtors share the responsibility of preventing and resolving unsustainable debt situations; and
- transparency, participation and accountability in debt contraction and management by the states.

Although these are only guidelines, they make a strong case for human rights considerations, which are very relevant in this time of COVID-19. Although these are not binding on the parties, it would have been better if the international creditors and Zimbabwe had attempted to find a common ground for renegotiation and relief for Zimbabwe during the COVID-19 pandemic. This would be in line with the UN Guiding Principles on Foreign Debt and Human Rights summarised above.

14.6 Options for Zimbabwe's sovereign debt restructuring

Zimbabwe is a complex issue. The debt burden is unbearable, given that 90 per cent of the total debt is made up of arrears and penalties continue to accrue unabated. The economy is at its worst and this is exacerbated by the COVID-19 pandemic and natural disasters such as floods and droughts. On a positive note, the government of the Second Republic is determined to re-engage with the international community as well as external creditors. Thus, this presents an opportunity for the country to be re-integrated into the international economy. However, there are complications that need to be overcome if Zimbabwe is to get out of this maze. This calls for the cooperation of both Zimbabwe and its various creditors.

It is undeniable that the first step that needs to be undertaken by Zimbabwe is to re-engage with creditors. Zimbabwe should develop its plans to be used as the basis for renegotiation with its creditors. Due to the divergence of creditors, there may not be a one-size-fits-all plan, hence the need for specific plans depending on the type of creditor and the governing legal framework. For instance, one plan can address international financial institutions, the other one for Paris Club creditors and another for non-Paris Club creditors. The issue of re-engagement is supported by the IMF in its Zimbabwe Debt Sustainability Analysis, where it recommended that Zimbabwe needs to reach 'an agreement with creditors on a comprehensive treatment of Zimbabwe's external debt and

arrears'.[38] In the view of the IMF, the re-engagement with the international community would also help to restore debt sustainability.

There are options available to Zimbabwe to secure debt relief and restructuring. Professor Mthuli Ncube, who currently is Zimbabwe's Minister of Finance and Economic Development, has discussed some of the available options.[39] First, Zimbabwe can request to be considered for the HIPC Initiative.[40] However, this is not an easy option as the IMF and World Bank would need to re-open the HIPC eligibility requirements and determine whether Zimbabwe meets the criteria. One of the requirements is that Zimbabwe needs to demonstrate that it has performed well under the economic adjustment programmes of the World Bank and the IMF. Currently, Zimbabwe is on an IMF staff-monitored programme.

The second option presented by Professor Ncube is that the international community can create a *sui generis* debt relief approach for Zimbabwe.[41] The third is an *ad hoc* debt restructuring under the auspices of the Paris Club.[42] Given the complexities of Zimbabwe's crisis, it is suggested that a *sui generis* approach would be the most suitable as it takes into account Zimbabwe's peculiar situation. For example, Zimbabwe is not part of the Debt Service Suspension Initiative (DSSI) as it is in arrears to the International Development Association (IDA), causing it to be ineligible.[43] Since Zimbabwe is not part of the DSSI, it has to plead its case individually with the creditors for debt relief.

The question then would be, what should be the *sui generis* approach that should be followed by Zimbabwe?

First, Zimbabwe needs to clear its debts to the international financial institutions such as the World Bank and the AfDB, who are all preferred creditors.[44] It is only then that it can seek debt treatment by the Paris Club.

38 IMF Zimbawe Staff Report for the Article IV Consultations-Debt Sustainability Analysis (12 February 2020) 1.

39 M Ncube 'Zimbabwe's options for sovereign debt relief' *Daily Maverick* (3 September 2018).

40 As above.

41 As above.

42 As above.

43 See C Humphrey & S Mustapha 'Lend or suspend? Maximising the impact of multilateral bank financing in the COVID-19 crisis' Working paper 585 (July 2020), www.odi.org (accessed 13 January 2021).

44 G Chigumira, N Mupunga & E Chipumho 'An assessment of arrears clearance and sustainable debt options for Zimbabwe' Zimbabwe Economic Policy Analysis and Research Unit (ZEPARU) (November 2018).

Paris Club creditors 'provides debt treatments to debt countries in the form of rescheduling, which is debt relief by postponement or, in the case of concessional rescheduling, reduction in debt service obligations during a defined period or as of set date'. In the case of Zimbabwe, it will need to negotiate for a suspension of payment and a moratorium on interests for at least two years so that Zimbabwe has the space to deal with the challenges posed by the COVID-19 pandemic.

With respect to the payment plan to the international financial institutions, it is suggested that the Zimbabwe plan should have the following key elements in mind:

- the suspension of payment obligation for at least two years (as discussed above);
- the use of a bridging loan, from African Export-Import Bank (Afrexim Bank) and/or other source;
- the issuance of a long-term sovereign bond;
- the use of domestic resources to repay the bridging loan and other debts.

These elements, besides the payment suspension, are assessed in the following paragraphs.

14.6.1 Use of a bridging loan

A bridging loan is crucial for the success of the plan. A bridge loan is an interim financing facility for a government, business or individual that helps it until the next stage of financing is reached.[45] It generally is used to pay back an existing loan, as well as other capitalisation needs. Due to a lack of goodwill, it is very difficult for Zimbabwe to obtain a bridging loan or grants. The major criticism is that this borrowing to repay strategy results in the perpetuation of indebtedness.[46] During the Lima Plan in 2015 Zimbabwe sought to get a bridging loan from the Afrexim Bank and the negotiations were unsuccessful. However, there now is a change in the political leadership and the new leadership is keen to engage with creditors. Thus, the government can re-engage the Afrexim Bank. In October 2020 it was reported that Zimbabwe intends to borrow US $1,9 billion from G7 countries in order to repay its debts.[47] Thus, Zimbabwe can approach multiple sources for a bridging loan. However, once the bridging loan has been secured, there remains a need to re-pay that loan and other creditors.

45 Mbawu & Nkala (n 6) 10.

46 Carlos et al (n 17); Megliani (n 17); Das et al (n 4).

47 'Zimbabwe to borrow 1,9 billion USD from G7 countries to repay its debt' (15 October 2020), www.news.cn (accessed 3 February 2021).

It is recommended that such payments should be done using long-term sovereign bonds and domestic resources if Zimbabwe is to escape a debt trap. The main issue is to avoid taking other loans to pay the loan again.

14.6.2 Long-term sovereign bond

A long-term sovereign bond may be defined as 'a process where the government sells bonds to investors on either domestic or international financial markets to raise funds'.[48] It has been argued that a long-term sovereign bond is not the correct way to go in Zimbabwe at the moment.[49] This is because the economic and political conditions in Zimbabwe would make the pursuit of this a futile exercise because the poor performance of the economy.[50] Mutize highlighted the fact that these fundamentals relate to internal political and economic fundamentals. He highlighted some factors that are worthy of consideration.[51] First, Zimbabwe does not have a sovereign credit rating from international credit rating agencies. The rating plays an important part as a key input in determining yield and coupon payment on a bond. Although countries without sovereign credit ratings have sold bonds, this has been done at high rates. Second, there is currency instability caused by the introduction of a currency and subsequent loss of value. Third, the weak currency taints the attractiveness of the bond that is issued since it increases the risk of default and debt sustainability, particularly if repayments are to be made in hard currency. Fourth, the goodwill of the government has been eroded due to the economic crisis in the country coupled by a bad reputation on defaulting payments to international financial institutions. Fifth, the government has been hostile to the private sector. For instance, on 29 June 2020 the government ordered the closure of the stock exchange, accusing it of fuelling currency devaluation. The stock exchange was later re-opened. Thus, Zimbabwe should first demonstrate a political will to restore business confidence if it is to successfully issue a long-term sovereign bond.

14.6.3 Use of domestic resources

Mineral resources

One of the suggestions that have been touted is mortgaging revenues from mineral resources, which entails linking revenues from minerals to future

48 Mutize (n 31).

49 As above.

50 As above.

51 As above.

debt service payment.[52] Zimbabwe has a vast store of mineral resources which, if properly managed, can be used to repay the country's debts. At one point, the then President of Zimbabwe, Robert Mugabe, mentioned that Zimbabwe has lost around US $15 billion due to mismanagement.[53] At the moment, royalties from the proceeds of mineral resources to the government are not significant. A full discussion on this aspect has a whole chapter dedicated to it in the book.

Sale of municipal land around the biggest cities and sale of agricultural farms across the country

It has been mooted that Zimbabwe can sell municipal land around its cities in order to raise money for servicing the debts. While there is a demand for land in big cities, the cost of servicing the land may be high to the extent that there may be a small margin between the cost of servicing the land and the selling price. Furthermore, due to the bad performance of the economy, the buying power of most people has been eroded, with the result that there will be a low demand for such land sales. In addition, mortgage loans are not viable in the current economic situation of high inflation.

Alternatively, Zimbabwe can sell commercial farms for agricultural purposes. At its independence, Zimbabwe was known as the bread basket of Africa.[54] This was mainly because of viable land titling, especially freehold, which was for all commercial farms. Because the commercial farms were freehold land, they could be used as commercial security against loans that were meant for agricultural activities. This was one of the factors that supported productivity in the commercial farms. All this changed with the advent of the land reform programme from the late 1990s which saw most of the commercial farms being nationalised by the government.[55] One of the consequences of this nationalisation is a lack of productivity on the farms.[56] The land reform programme was

52 S Nkhata 'Leveraging on debt sustainability for sustainable development' Brown Bag UNDP.

53 See Staff Reporter 'Mugabe's missing $15 billion saga intensifies' (7 December 2017), https://www.iol.co.za/business-report/mugabes-missing-15-billion-saga-intensifies-12283828 (accessed 10 January 2021).

54 See http://www.fao.org/3/i6022e/i6022e.pdf (accessed 10 January 2021).

55 RG Muchetu 'Agricultural land-delivery systems in Zimbabwe: A review of four decades of Sam Moyo's work on agricultural land markets and their constraints' (2018) 57 *African Study Monographs.*

56 M Mutema 'Land rights and their impacts on agricultural efficiency, investments and land markets in Zimbabwe' (2003) *International Food and Agribusiness Management Review* 50.

characterised by chaos and farm invasion to the extent that the court ruled that there was no 'programme' at all.[57] The invaders had no title to the land and also did not have sufficient resources to continue with productivity. The government allocated some of the nationalised land to 'new farmers' who also had no title to the land except offer letters. As a result, the land could not be used as collateral in accessing loans from the banks. With these farmers having no resources, and unable to borrow, there is less productivity on the farms, which contributed to bad economic performances. Zimbabwe is now importing grains and meat.

To solve the issue of chaotic land reform, Zimbabwe has come up with a Land Commission that is tasked with the administration of agricultural land,[58] including the development of 99-year lease agreements with respect to agricultural land. For it to be effective, such a lease agreement should be bankable so that it can act as collateral. So far such a bankable instrument has not been developed and there are ongoing consultations with stakeholders. This can possibly be a viable option if such sale or lease is accompanied by a secure land tenure system. If properly administered, a substantial amount may be raised using this method. In addition, this will also promote agricultural production which can stimulate economic growth,[59] more than the sale of residential land.

14.7 Conclusion and recommendations

Zimbabwe is in debt crisis. Zimbabwe still faces the following major economic challenges: high government debt; low industrial and export competitiveness; a narrow revenue base; and subdued investor confidence. Zimbabwe has engaged in numerous debt-servicing reforms and policies, which included the re-engagement process with the creditor community, new public debt-servicing methods, such as the usage of special drawing rights in the payment of the IMF loan in 2016, and the contraction of new loans to pay off debt arrears, the use of domestic resources and efforts to campaign for the removal of sanctions.

In the context of the COVID-19 pandemic and human rights, it is recommended that international creditors should reconsider their stance and attempt to find a common ground for renegotiation and relief for Zimbabwe in this time of the COVID-19 pandemic. This would assist

57 *Commercial Farmers Union v Minister of Lands & Others* 2000 ZLR 469 (S).

58 Land Commission Act (ch 20:29).

59 S Moyo & W Chambati *Land and agrarian reform in Zimbabwe: Beyond white-settler capitalism* (2013).

Zimbabwe to have more resources towards the management, control and mitigation of the effects of the pandemic. This would be in line with the UN Guiding Principles on Foreign Debt and Human Rights. Zimbabwe needs the renegotiation of the payment plan and to commit to that payment plan. The government should implement the economic reforms previously agreed with multilateral lenders. These include the reduction of the government's double-digit fiscal deficit and adopting reforms to allow market forces to drive the functioning of foreign exchange and other financial markets. There is a need for a credible reform programme to stabilise and strengthen the economy.

Undoubtedly, there is a need for a bridging loan or facility to clear all the arrears. The downside of this method has been noted, but it is a necessary step in resolving the Zimbabwean debt conundrum. However, the clearance of such loan should be by the use of domestic resources. The most preferred way is through the sale of agricultural commercial farms, which have a ripple effect of stimulating economic recovery and growth.

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15 Building back better post-COVID 19: Lessons learnt and the future of sovereign debt management and restructuring in SADC

Daniel D Bradlow and Magalie L Masamba

15.1 Introduction

African countries need foreign exchange to fund their development. They obtain these funds through export earnings, through foreign investments or through borrowing. Given the exchange rate risk associated with these debts, African governments always face a challenge in managing their external debts so that they do not pose a serious risk to their development strategies. Despite their best efforts, there is always the possibility – and at times the reality – that their debt management strategies will be undermined by issues outside their control such as changes in commodity prices, changes in key country interest rates, exchange rates, public health crises, and geopolitical developments. As a result of these changes, African countries can lose access to affordable external financing or can become unable to meet their debt obligations in a timely manner. African countries have also been forced into a debt crisis by their institutional and policy shortcomings, including ineffective or opaque debt management operations, and flawed macro-economic policies.

Regardless of their cause, these crises, in turn, can adversely affect the ability of the debtor states to formulate and implement effective policies, to finance education, health and social welfare, to promote job creation and to address developmental problems such as a lack of infrastructure and corruption. The need to meet their debt obligations can also force countries to favour those activities that generate foreign exchange in the short term regardless of their longer term impacts on the environment and local communities, especially vulnerable population groups such as women, children and the elderly.

History, therefore, teaches us that the management of Africa's sovereign debt is not only a financial matter. It also has important macro-economic, political, social and environmental ramifications. The salience of these inter-connected issues has been intensified by the COVID-19 pandemic and the increased demands it has placed on government finances and their responsibility to tackle the challenges of poverty and inequality. This suggests that there is a need for both academics and policy makers to pay careful attention to Africa's external debt and to explore the possibility for

more creative and effective approaches to the management of this debt. While there is a need to explore this issue at a continental level, it is also important to explore the sovereign debt issue at regional and national levels. This book has adopted the latter approach and has concentrated on the Southern African Development Community (SADC) region. In doing so, it brought together 18 contributing authors with different areas of expertise and different perspectives on the SADC region's debt situation. In an effort to chart a way forward for the region, the contributing authors addressed the following four themes:

- the impact of structural changes in the global economy on the SADC debt landscape;
- the challenges of sovereign debt management and restructuring in the SADC region;
- the implications of the lack of transparency on the accumulation and use of sovereign debt;
- options for incorporating human rights and social considerations into sovereign debt renegotiations and restructuring.

The book takes two approaches in developing these themes. First, some chapters provide a general overview of Africa's debt landscape, with a particular reference to the situation in the SADC region by presenting recent data, trends and dynamics. Most of the authors of these chapters also explore the role that the international financial institutions, particularly the International Monetary Fund (IMF), play in the region. Some of these authors further explore the link between debt and other areas such as international trade and human rights and the legal issues arising from these linkages. Second, the book contains six case studies that discuss how specific SADC member states have addressed particular aspects of these four themes.

This final chapter seeks to draw lessons from these two sets of chapters regarding the four themes in the book. Its goal is to provide the basis for developing a new and more sustainable and resilient approach to sovereign debt in Africa, in general, and the SADC, in particular. The chapter has two goals. The first goal is to provide an overview of the lessons that can be drawn from their research. The second objective is to draw some policy-relevant conclusions about the debt situation in the SADC region and to offer some suggestions for future research on the topic.

15.2 COVID-19 and sovereign debt in SADC: What have we learnt so far?

Not surprisingly, the COVID-19 pandemic has adversely affected the public finances, including the external debt situation, of all African countries. However, the impact has not been uniform, in part because some countries entered the pandemic in better economic shape than others, and in part because of the specific structural features of each state's political economy. The result is that the economies of some countries have been more severely affected by the pandemic than others.

In this regard, the SADC region is not unusual. There is substantial variation in the social and economic situations of the 16 member states. In his chapter Kessler provides a detailed overview of the debt landscape of the SADC countries, assessing both their pre-pandemic situations and the economic shock that the COVID-19 pandemic gave to their economies and their policy responses to the pandemic. He demonstrates that there was considerable variation in their situations. He notes that some countries entered the crisis vulnerable to debt distress (Angola and Zambia) having experienced deterioration in their debt sustainability profiles and downgrades in their credit ratings. Other countries entered the crisis with more sustainable debt profiles and so were better able to manage their debts during the crisis (Comoros, Democratic Republic of the Congo (DRC), Lesotho, Madagascar and Tanzania). Nevertheless, he notes that all the SADC states now face challenges in accessing new external finance.[1]

Herman supports this observation. In his chapter he details the 'inescapable surge in foreign borrowing' among developing countries that followed the advent of the pandemic.[2] Herman's assessment draws three main lessons from the experience of poorer countries, including those in Africa, in general, and SADC, in particular, during crises such as the COVID-19 pandemic. First, these countries are likely to resort to borrowing in order to meet their society's various health, social and economic needs. The alternative is for them to fall short on meeting these needs. Second, many of these countries, because of the relatively high level of their pre-pandemic debt burdens, will require external support. Although grants are the preferred form for this assistance, these countries are likely to have to resort to a mix of grants and loans. Third, these

1 See M Kessler ch 3 'Debt service suspension in Southern African Development Community countries'.

2 B Herman ch 2 'International assistance in catastrophes need not bankrupt countries'.

countries have a need for 'escape clauses'. This means that, in order to avoid being overwhelmed by their debt obligations, they will need their creditors to provide some debt relief during the crisis. This does not free the debtor countries from the need to make good use of all their available sources of finance, including the limited relief that is available through initiatives such as the Debt Service Suspension Initiative (DSSI).[3]

The role of the IMF in this regard merits specific attention. As Edwards discusses in his chapter, historically its importance arises from both the financial support it offers to its member states and the policy advice it provides during its regular surveillance of the economies of its member states. The latter form of support, the author notes, needs to be critically evaluated because the 'influence of the IMF over states and over markets is increasingly being challenged'. Edwards argues that IMF surveillance should be more transparent and he calls for the IMF's policy advice during surveillance to become less opaque and more directly responsive to and useful in the actual situation in each state.[4] This conclusion also helps underscore the importance of transparency in government policy making and implementation in general, including in the sovereign borrowing process. This conclusion also points to the importance of ensuring that all the stakeholders in particular governmental actions, including sovereign borrowing and debt management, have access to all the relevant information.

Similar transparency and access to information issues arise from the chapter by Gallagher and Wang.[5] They maintain that the current approach to debt sustainability, with its focus on specific debt ratios, is inadequate. Instead, they argue for a balance sheet approach that focuses on the assets and liabilities of the sovereign debtor rather than on debt ratios. Based on this alternative approach, these authors propose some policy options for dealing with the SADC region's current debt woes. First, they call for the IMF to issue more special drawing rights (SDRs) and to arrange for a favourable allocation or reallocation for use by African countries. Second, they suggest that the IMF increase the size and speed of disbursement of its emergency liquidity facilities. Third, they propose that creditors adopt a balance sheet approach in assessing the possibility of refinancing the debts of countries facing debt repayment difficulties. Fourth, they focus on the specific issue of China's role as a creditor in Africa and propose that it adopt tailored and innovative approaches in restructuring its credits.

3 Kessler (n 1).

4 M Edwards ch 4 'The IMF and debt surveillance in SADC countries'.

5 K Gallagher & Y Wang ch 5 'Sovereign debt via the lens of asset management: Implications for SADC countries'.

Finally, they advocate the use of debt for nature swaps in dealing with particular debt crises.

The second part of the book is a series of six case studies. These case studies analyse how Mozambique, Namibia, South Africa, Zambia and Zimbabwe have addressed specific aspects of the complex questions relating to debt management that were raised in the first group of chapters. In each of the case studies the author, after presenting the case study, offers some recommendations on how to adopt a more creative approach to the issues raised in the case study. For example, in the Zambian case study N'gambi advocates the use of the Basic Principles on Sovereign Debt Restructuring Processes of the United Nations (UN) (sovereignty, good faith, transparency, impartiality, equitable treatment, sovereign immunity, legitimacy, sustainability and majority restructuring) to guide the country's restructuring.[6] To N'gambi, this would make the process more inclusive and would facilitate a debt restructuring process that offers Zambia a better chance of designing and implementing a sustainable and inclusive post-debt crisis development strategy.

A recurring theme in these case studies is the importance of transparency in debt management and restructuring. The Zambian case study highlights the challenge created by the lack of transparency of Chinese loans to Zambian entities. The author notes that the opaqueness of Chinese loans means that most stakeholders cannot learn enough about these loans to be able to adequately assess their impact on the country's debt sustainability. This risks undermining their confidence in the government's approach to its debt problems and their willingness to support its associated policy initiatives. The lack of transparency also constrains the willingness of other creditors to give Zambia any debt relief because they cannot be sure that the net effect of their actions will not simply be to free up funds to service Chinese debts.

Mozambique is another country that dramatically highlights the importance of transparency. In his chapter Koen discusses the litigation that has arisen from the revelations in 2016 that Mozambique had borrowed approximately US $2 billion without informing Mozambique's Parliament or recording the debts in the government public accounts.[7] The crisis that the revelation of these debts caused for the country is a compelling demonstration of the severity of the risks of opaqueness in

6 SP Ng'ambi ch 11 'Sovereign debt: A case study of Zambia'.

7 L Koen ch 10 'The renegotiation of sovereign debt tainted by corruption: Mozambique's 'secret' debt in perspective'.

debt transactions. In this sense, it underscores the relevance of the Institute for International Finance's Principles for Debt Transparency (2019).[8]

Another important demonstration of this point is the chapter by Mutondoro, Hobi, Dhliwayo and Chiname in which they discuss the challenge of resource-backed loans in Zimbabwe. This form of borrowing has been substantially used by Zimbabwe to help fill the country's financing gap.[9] In their chapter the authors have highlighted the risks – high borrowing costs, lack of transparency in the debt terms, and potential negative human rights implications – associated with this form of borrowing. While their chapter makes a compelling case for treating such loans with caution, they do not discuss how the country should address the debt crisis caused in part by these loans. This issue is taken up by Pfumorodze. He uses his contribution to this book to assess the various options for dealing with Zimbabwe's debt and for proposing some possible new approaches, such as the use of municipal debt to repay Zimbabwe's debt.[10] It is clear from his chapter that the key missing ingredient in dealing with Zimbabwe's multilateral and bilateral debt is political will.

Another theme that emerges from the case studies is the importance of coherent financial regulation. The chapters by Aren, looking at debt management in South Africa, and by Zongwe, discussing the role of the central bank in regard to public finance in Namibia, both serve to underscore this observation. Aren in her chapter shows that the lack of adequate laws and regulations dealing with debt management can facilitate corruption and enable illicit financial flows from SADC countries. She also makes a number of policy recommendations to help South Africa deal with these challenges. First she proposes that the country increases government spending to address key social and economic needs and that it avoids adopting austerity measures during the current economic difficulties. Second, she calls for the country, if necessary, to promote a multilateral approach to renegotiating its debts, including with its private creditors. This is a version of the Common Framework for Debt Treatments beyond the DSSI (Common Framework) but for middle-income countries.[11] Third, she advocates increased resource mobilisation,

8 Institute of International Finance 'Principles for debt transparency' (10 June 2019), https://www.iif.com/Publications/ID/3387/Voluntary-Principles-For-Debt-Transparency (accessed 21 April 2021).

9 F Mutondoro, A Hobi, M Dhliwayo & J Chiname ch 13 'Resource-backed loans, COVID-19 and the high risk of debt trap: A case study of Zimbabwe'.

10 J Pfumorodze ch 14 'Towards utilisation of domestic resources in settling Zimbabwe's sovereign debt'.

11 In November 2020 the G20 approved the Common Framework which aims at restructuring sovereign debts of least-developed countries. In the words of the G20,

including a proposal for what she describes as a 'minute taxing of domestic and cross-border digital transactions'.

In his chapter Zongwe argues that central banks should play a more important role in managing the public finances of developing countries. However, he cautions that they can only do so if their efforts are guided by effective laws and regulations. He proposes that Namibia should adopt a fiscal responsibility framework and makes some recommendations for the content of the framework. He further suggests that this framework could serve as a model for other countries in the region.

Another concern addressed by the contributors to this book is the shortcomings in the debt renegotiation process. Three authors in this publication explore the restructuring options available to the SADC member states and how far they deal with deeper structural issues such as human rights and development. In his contribution Jackson explores the link between sovereign debt and bilateral investment agreements and the potential challenges that the bilateral investment treaties (BITs) could create for sovereign debtors in difficulty. These challenges can arise if sovereign debt agreements fall within the definition of 'investments' contained in these agreements. He notes that the SADC model investment law adopts a relatively narrow definition of investment that excludes sovereign debt. In addition, by not including a most favoured nation clause in the model law, SADC has sought to protect its member states from the risk that BITs can be used to bring cases against sovereign debtors in difficulty.[12] This is an important protection for the SADC countries, particularly given the absence of an overarching legal mechanism for sovereign debt restructuring. He encourages the countries in the region to make use of the SADC model BIT should they decide to draft and enter into any more BITs. Nevertheless, some sovereign debtors are exposed to potential litigation under their current BIT. The size of this risk is unclear and it remains to be seen whether these countries will become defendants in debt-related BIT arbitration.

'[t]he Common Framework brings together G20 and Paris Club creditors to coordinate and cooperate on debt treatments, on a case-by-case basis, initiated at the request for a debt treatment by an eligible debtor country', with Chad being the first country to make use of the mechanism. See G20 'G20 Common Framework for debt burden relief dialogues for Low-Income Countries' (8 April 2021), https://www.g20.org/g20-common-framework-for-debt-burden-relief-dialogues-for-low-income-countries.html (accessed 21 April 2021).

12 R Jackson ch 6 'Sovereign debts under bilateral investment treaties: Does the SADC Model BIT navigate the controversy?'

Muriungi in his contribution also focuses on the implications of the lack of a sovereign debt-restructuring mechanism. He notes that this situation should push countries to pay more attention to the terms of the contracts for any debt transactions into which they may enter. In this regard, he offers an overview and assessment of how debtors, *ex ante*, can use these contracts to strengthen their position in case of a crisis. He also suggests that they do have some options for mitigating their situation *ex post*.[13] His discussion highlights that, in the absence of a formal overarching sovereign debt-restructuring mechanism, sovereign debtors are forced to deal with their creditors on an *ad hoc* basis. This means that when countries find themselves burdened by unsustainable debt or are in default, there are not many options beyond the painful one of having to renegotiate with each of their various categories of creditors.

Masamba also highlights some of the problems that arise because of the lack of a global rule of law for debt restructuring. The author argues that the difficulties of present-day debt restructuring transcend the procedural concerns. She argues that the aspect that has been less discussed relates to fairness, or the lack thereof. In particular, she notes that this gap in the international legal order impedes the capacity for debtor states to link their need to restructure their sovereign debts to their obligations to respect, protect and fulfil the human rights of their citizens.[14] Consequently, to her, an ideal approach to restructuring necessitates addressing the multifaceted complexities in a holistic manner – by considering and then tackling both the substantive and procedural concerns.

These three chapters highlight the problems that arise from the lack of an overarching sovereign debt legal framework. Not only does this adversely affect the range of issues that can be easily addressed in these renegotiations, but it also exacerbates the power imbalance between the sovereign debtor and its creditors. It does this both by, in effect, excluding certain topics such as human rights from the scope of the negotiations and by requiring the debtor to deal with each category of its creditors separately. While the international community has made various efforts to develop generally-accepted norms and principles on debt restructuring, these have not yet gained sufficient acceptance to provide the basis for fair, equitable and effective debt renegotiations. Thus, there still is a need for a new set of norms and standards and a holistic framework that incorporates human rights and environmental and social considerations as well as

13 M Muriungi ch 7 'Managing and restructuring sovereign debt in the SADC region in the context of the COVID-19 pandemic'.

14 M Masamba ch 8 'Sovereign debt restructuring and human rights in SADC: Is there a false binary between the two fields in legal discourse?'

economic and financial ones. The precise design of this framework and how it should be implemented are still topics that remain open to debate by scholars and policy makers. The lack of such norms and standards and of such a framework both increases the demands on the resources of the debtor and weakens its bargaining power relative to its various creditors.

15.3 Mapping a way forward for Africa and SADC

The publication of this book was aimed at stimulating debate and research on how to more effectively deal with the issue of sovereign debt in the SADC region. It was also intended to produce some policy-relevant recommendations for the region. In so doing, the editors and contributors sought to look beyond the COVID-19 pandemic and to focus more closely on the broader structural weaknesses in the international debt management landscape. This has been motivated by the fact that the debt woes of the continent, and the SADC, not only predate the pandemic, but that they are also being exacerbated by the deeper structural weaknesses and vulnerabilities being exposed by the pandemic. In other words, the pandemic is merely another factor contributing to the difficult debt situation of some of the SADC states rather than the sole cause of the country's debt crisis.

A close review of the lessons that have been drawn from the contributions to this book indicates that there are a number of recommendations that policy makers should consider as they determine how to address the SADC debt situation in the coming years. These recommendations are the following:

(a) **Debt transparency: The countries in the region should adopt comprehensive debt data disclosure requirements and state borrowing procedures that are transparent, participatory and that facilitate holding the relevant decision makers accountable.** Debt transparency is the cornerstone of reform of debt management. There are numerous aspects of debt transparency but a key requirement is the transparency of the sovereign's financial transactions. This includes the contractual terms and arrangements for enhancing the security of the loan, for example, in the case of resource-backed loans. This requires developing national debt disclosure initiatives as part of fiscal management. The multilaterals already have some transparency initiatives. For example, the World Bank has a Debt Reporting Heat Map for International Development Association countries.[15] Nevertheless, strengthening public

15 World Bank 'Debt transparency: Debt reporting heat map' (10 May 2021), https://www.worldbank.org/en/topic/debt/brief/debt-transparency-report (accessed 19

debt transparency should still be at the core of the transformation of the borrowing, spending and restructuring approaches in SADC.

Transparency on its own will not ensure responsible borrowing. Other requirements include participation, as appropriate by all stakeholders and accountability. Thus, there is a need for the debt management frameworks of countries to provide avenues for participation, as appropriate, by all stakeholders in the borrowing process and a mechanism through which these stakeholders can hold the sovereign accountable for the outcomes of its debt-management practices. While this does not mean that all decisions concerning the accumulation, spending and restructuring of debt require holding public forums, it does mean that there is a need for policy makers to be well aware of the concerns of those affected by their debt-related decisions. Notably, countries should not only share data and debt-related information with multilateral institutions, but within national frameworks, platforms should be developed to make publicly available, with appropriate safeguards, data, including contracts and any other relevant information on the financial transactions of the sovereign. Further actual engagement is necessary, for instance, with the full variety of civil society organisations.

(b) **Good governance: Strengthening national debt management policies to deal with issues of governance.** Beyond the issue of debt transparency, the issue of debt management more broadly is critical. Sovereign debt management is an aspect of general governance of the states. Consequently, the states' debt management practices should conform to all the principles of good governance. In this context, the key principles are transparency, participation, accountability, reasoned decision making and effective institutional arrangements.

(c) **Legal predictability: strengthening contractual provisions in debt contracts.** It is important to recognise that debt by its very nature is a contractual relationship. Consequently, it is important for both the debtor and its creditors that their contractual arrangements are as comprehensive as possible. This means that their contracts should fairly allocate risks between the parties according to who is better able and more willing to accept the risks and should provide the parties with clear answers to as many of the issues that could arise between them as possible. This will always be the case, but it is particularly important as long as there is no international framework for debt restructuring. Consequently, SADC policy makers need to provide guidance to their debt managers on what terms and conditions they can accept in their contractual negotiations. In this regard, they should consider drafting model contracts and promoting training of their debt negotiators on the technicalities of debt negotiations. African countries should be innovative, but they do not

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need to reinvent the wheel. Lessons can be drawn from experiences of other sovereign and, where appropriate, corporate borrowers with debt contracts and from the various model contractual clauses developed by industry associations.[16] This means that the countries in the region should keep abreast of developments in financial contracts, including recent innovations in contract drafting and the problems arising from particular clauses.[17]

(d) Comparability of treatment: ensuring that where needed, restructuring of sovereign debts is conducted with all the creditors participating on comparable terms. It is in the interest of SADC debtors to ensure that they can offer and can show that they have offered all their creditors comparable treatment. The benefit of being able to demonstrate to all their creditors that they are not asking more from them then they are asking from other creditors should enhance the creditor's confidence in the debtor and the realism of their demands. It should also give them comfort that any relief they provide will benefit the debtor and not other creditors. This in turn should facilitate the debtor's efforts to reach agreement with all its creditors.

(e) Developing a holistic approach: Re-imagining the future of debt management and restructuring holistically in terms of both the process and substantive considerations.

There are diverse stakeholders in the sovereign debt restructuring process – the citizens of the debtor states, multilateral creditors such as the World Bank and IMF, international organisations such as the UN, institutional arrangements such as the Paris Club, bilateral creditors, and private creditors such as bondholders, institutional investors of various sorts and commercial banks. The sovereign debtor must seek to effectively engage with each of these actors. This suggests that there could be a need to develop a uniform and comprehensive mechanism for restructuring all these different classes of debt and for dealing with cross-cutting issues,

16 In 2014 the International Capital Markets Association developed a model collective action clause and model *pari passu* clause. See IMCA Group 'Standard collective action and *pari passu* clauses for the terms and conditions of sovereign notes', https://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/Primary-Markets/primary-market-topics/collective-action-clauses/21 (accessed 19 April 2021).

17 Among the most popular of these innovations is the strategic incorporation of contractual clauses, eg collective action clauses (CACs). CACs are contractual clauses that provide that changes to critical terms of the contracts be made by a predetermined supermajority of bondholders. However, the use of aggregated CACs in debt contracts is only one of these innovations. For a discussion on CACs, see F Weinschelbaum & J Wynne 'Renegotiation, collective action clauses and sovereign debt markets' (2005) 67 *Journal of International Economics* 47. Also see SJ Choi & G Gulati 'Innovation in boilerplate contracts: An empirical examination of sovereign bonds' (2004) 53 *Emory Law Journal* 929.

such as human rights, and the environmental and social concerns of the citizens of the debtor countries.

It is indisputable that sovereign debt is not only a financial issue. It has implications for the social, political, economic, cultural and environmental situation in the debtor country. It also has implications for the ability of the debtor state to meet its international legal obligations to protect, respect and promote the human rights obligations of its citizens.18 Increasingly it is also being recognised that the way in which both the official and private creditors treat their sovereign debtors has implications for their own compliance with their international responsibilities and/or obligations. For example, the bilateral official creditors are bound by the international legal commitments of their sovereign. These commitments may include human rights and environmental treaty obligations. Similarly, the private creditors could have responsibilities to their stakeholders, which include the citizens of the debtor state under the treaty obligations of their home states, their own policies and the applicable international norms and standards, some of which some will have incorporated into their own policies.[19]

15.4 Conclusion

As indicated, the purpose of this book was to stimulate a policy-relevant debate about the management of sovereign debt in the SADC region. The arguments and ideas in it both raise questions regarding the issue of sovereign debt in the SADC, in particular, and Africa, more broadly. The authors also propose possible approaches that could improve the management of this debt. However, the subject is too complex to be addressed comprehensively within the confines of one book. Consequently, the editors of the book caution that the book should be seen as a starting point for a more rigorous discussion of the topic rather than as defining the

18 The human rights obligations of states are enshrined in various international and regional human rights instruments. The duty to 'respect', the duty to 'protect' and the duty to 'fulfil' is most relevant in the context of economic, social and cultural rights. The United Nations Declaration for Human Rights (1948) recognises an individual's right to social security (art 22); a right to an adequate standard of living which includes access to essential social services including medical care, health and clothing (art 25); and the right to education (art 26). The International Covenant on Economic, Social and Cultural Rights is fully dedicated to economic, social and cultural rights which include, but are not limited to, the rights to social security and social protection in arts 9 and 10 respectively; an adequate standard of living and to food in art 11; health in art 12 and the right to education in art 13. Similar rights are also enshrined in regional instruments, in the African context, the African Charter on Human and Peoples' Rights (1981). Of relevance as well are civil and political rights as contained in the International Covenant on Civil and Political Rights and other regional instruments.

19 Many financial institutions have acknowledged the relevance of international human rights and environmental norms and standards to their work.

outcomes of such a discussion. There are too many issues that it has not addressed for this to be the case. For example, it has not delved into such issues as sovereign debt and green growth and climate change, the debt implications of public-private partnerships, and the general implications of the state's contingent liabilities. In addition, given the nature of debt in the SADC region, the book has neither fully addressed the complex challenge of the treatment of privately-held sovereign debt, nor does it provide an in-depth comparison of the management of the debt owed to Paris Club and non-Paris Club lenders. These are all topics that merit further research, assessment and debate. We hope that other researchers and people interested in this topic will build on our effort and address these topics, particularly as it applies to specific regions in Africa.

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