



Medium-Term Debt Management Strategy



GOVERNMENT OF GRENADA

Medium-Term Debt Management Strategy

2019 - 2021

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2018 Medium-Term Debt Management Strategy (MTDS) 2019-2021

Debt Management Unit

Division of Economic Management and Planning
Ministry of Finance, Planning, Economic and Physical Development
The Carenage
St. George's
Grenada

Tele: (473) 440-2214/ 435-8915

Fax: (473) 440-0775

This document is also available on the website at: <http://www.gov.gd>

**Ministry of Finance, Planning, Economic and Physical Development
GRENADA**

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NOTES

Fiscal Year The Government of Grenada's fiscal year runs from 01 January to 31 December

Local Currency The domestic currency is the Eastern Caribbean Dollar (\$). The EC dollar is pegged to US dollar under the current exchange rate regime (EC\$2.7 = US\$1); a system which has been in place since 1976

Unless otherwise stated all values are in Eastern Caribbean Dollars (\$)

Coverage **The Medium-term Debt Management Strategy includes ONLY Central Government existing debt and projected borrowing. Government guaranteed debt of public entities is not included in the analysis.**

Classification Debt is classified by currency for the purpose of this analysis only

Source The source of all tables and figures is the Ministry of Finance

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ACRONYMS

ATM	Average Time to Maturity
ATR	Average Time to Re-fixing
CARICOM	Caribbean Community
CBI	Citizenship by Investment
CDB	Caribbean Development Bank
CNY	China Yuan Renminbi
CS-DRMS	Commonwealth Secretariat Debt Recording and Management System
DETC	Department of Economic and Technical Cooperation
DMU	Debt Management Unit
ECCB	Eastern Caribbean Central Bank
ECCU	Eastern Caribbean Currency Union
EUR	Euro
FAA	Finance Administration Act
FDI	Foreign Direct Investment
FRL	Fiscal Responsibility Law
FX	Foreign Exchange
GBP	Great Britain Pounds
GDP	Gross Domestic Product
GoG	Government of Grenada
IBRD	International Bank for Reconstruction and Development
IDA	International Development Association
IFAD	International Fund for Agricultural Development
IMF	International Monetary Fund
IRP	Investor Relations Programme
JYP	Japanese Yen
KWD	Kuwaiti Dinars
LIBOR	London Inter-Bank Offer Rate
MoF	Ministry of Finance
MTA	Medium –Term Agenda
MTDS	Medium-Term Debt Management Strategy
MTFF	Medium-Term Fiscal Framework
NIS	National Insurance Scheme
OCR	Ordinary Capital Resources

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OPEC	Organization of Petroleum Exporting Countries
PDM	Public Debt Management Act
PRGF	Poverty Reduction and Growth Facility
PV	Present Value
RGSM	Regional Governments Securities Market
ROC	Republic of China
S1	Strategy 1
S2	Strategy 2
S3	Strategy 3
ST FX	Short -Term Foreign Exchange
T-bills	Treasury Bills
USD	United States Dollar
WB	World Bank
XCD	Eastern Caribbean Dollar
XDR	Special Drawing Rights

DEFINITIONS

Average Time to Maturity (ATM) is a measure which focuses on the timing of repayment. It shows the share of debt falling due within a specific period of time – i.e., shape of the redemption profile.

Average Time to Re-fixing (ATR) is a measure of the weighted average time until all the principal payments in the debt portfolio become subject to a new interest rate.

Bilateral Creditor is a donor government or its agency that provides loans to borrowers in other countries.

Bullet Repayment is the repayment of principal in a single payment at the maturity of the debt

Debt Outstanding is the amount that has been disbursed from a loan but has not yet been repaid or forgiven.

Debt Restructuring is an action officially agreed between creditor and borrower to alter the terms previously established for repayment. In Grenada's context, this has included haircuts/ debt service and debt service reduction exchanges, forgiveness, and refinancing.

Multilateral Creditor is an international institution with governmental membership which conducts all or a significant part of its activities in favour of development and aid recipient countries.

Domestic Debt is the gross outstanding amount, at any given time, of actual liabilities that require payment(s) of interest and/or principal by the debtor at some point(s) and that are denominated in Eastern Caribbean Dollars.

EXECUTIVE SUMMARY

The Public Debt Management (PDM) Act enacted in June 2015 provides the framework for effective debt management, which involves the establishment and execution of a strategy for managing public sector debt. The Medium-Term Debt Management Strategy (MTDS¹) is a plan aimed at achieving a desired debt portfolio consistent with the debt management objectives. It ensures that the Government's funding needs are met with due consideration of its cost and risk objectives. The MTDS, among other considerations, highlights a preferred strategy that can be used over the medium-term (2019-2021).

Grenada's economy expanded by 5.1 percent in 2017. Real growth of 5.2 percent is projected for 2018, an uptick from growth experienced in 2017. Over the medium term (2019-2021) growth is projected to average 4.0 percent driven by construction, education and tourism sectors development. Overall and primary surpluses are forecasted to average 4.3 and 6.3 percent of GDP respectively over 2019-2021. The trade deficit is projected to widen at end 2018 due to higher oil prices and imports related to construction. The economic prospects are positive, but can be affected by a mix of upside and downside risks.

At the end of 2018, **Central Government** debt is estimated to be \$1.97 billion of which external debt amounts to \$1.36 billion and domestic debt \$0.61 billion. Total debt service for the year is estimated to be \$307.7 million or 40.9 per cent of revenue.

With regards to risks in the existing portfolio, the interest rate is subject to moderate risk given the current upward movement of interest rates on the international markets. The Average Time to Re-Fixing (ATR) of the total portfolio is 8.6 years, of which 21.4 per cent is subject to a change in interest rates in one year. The risk resides predominantly in the domestic portfolio given that 31.4 percent of debt is subject to re-fixing in one year, namely treasury bills. Variable rate debt accounts for 6.6 percent of the total portfolio and hence does not pose a significant risk. The refinancing risk profile of the portfolio has an Average Time to Maturity (ATM) of 9.0 years, which exceeds the set target of 8 years and above. The portfolio's exposure to foreign exchange risk is minimal as the majority of foreign currency debt is denominated in USD to which the EC dollar is pegged albeit, with an increasing share of non-USD foreign currency debts, the DMU remains vigilant.

Three strategies were analysed, and all strategies were subject to various stress scenarios including interest and exchange rate shocks of moderate and extreme degrees. The analysis illustrates that Strategy 2 (S2) represents the most feasible option for financing Government's needs in the medium

¹ IMF and World Bank (2009). "Developing a Medium-Term Debt Management Strategy —Guidance Note for Country Authorities" <http://www.imf.org/external/np/pp/eng/2009/030309a.pdf>.

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term and is firmly in line with debt management targets and objectives. It assumes that Government's financing needs will be met by utilizing committed undisbursed debt and re-issuing Government securities on the regional market.

1 OVERVIEW

The debt data utilized for the MTDS encompasses Central Government external and domestic debt. T-Bills are recorded at their discounted value only for the purpose of this Strategy. Government Guaranteed debt, which as at end June 2018 accounted for 3.3 per cent of public debt was not included in the analysis except in cases where these debts have been subsumed by the Government. The MTDS spans a three year horizon (2019-2021) inclusive.

The report is divided in five sections. Following the Overview, section 2 provides a review of the existing debt portfolio with a focus on Central Government. This section includes existing debt stocks and debt service payments, risk analysis, and redemption profile at the end of 2019. Section 3 examines macroeconomic performance, medium term outlook and key risks; section 4 presents alternative strategies to finance the Government's borrowing needs, based on its current economic constraints and the preferred strategy with regard to the cost-risk trade-off. Section 5 proposes the implementation methodology and financing plan for the identified strategy.

1.1 Debt Management Objective

The MTDS sets out the Government of Grenada's (GoG's) objectives and strategy for the management of its domestic and foreign debt for the period 2019- 2021; consistent with the medium-term fiscal framework. The MoF through its DMU, is committed to implementing the debt management objectives as outlined by the Public Debt Management Act, 2015. These objectives are aimed at:

- i. ensuring that the financing needs of the Government are met on a timely basis and that its debt service obligations are met at the lowest cost over the medium-to-long term, in a manner that is consistent with an acceptable and prudent degree of risk;
- ii. providing a framework for the management of public debt in a manner that achieves and maintains sustainable debt; and
- iii. ensuring that public debt management operations support the establishment of a well-developed domestic debt market in the medium-to-long term.

1.2 Implementation of the 2018 Debt Management Strategy

The MTDS implemented for the financial year (FY 2018) emphasized reliance on a mix of domestic borrowing of marketable securities and external concessional borrowing. The target for domestic financing and external financing mix was 65 percent and 35 percent, respectively. The actual position as at end September 2018 shows a financing mix of 64.1 percent and 35.9 percent respectively. In order to reduce the cost of debt and refinancing risk, the FY 2018 MTDS aimed to extend the maturity of domestic short-term over-the-counter debt. Consistent with the strategy, no new financing was raised on the RGSM in 2018, rather, the actual position as at September 2018 indicates a decrease in the

proportion of T-bills by 13.4 percent from 2017 and an increase in the percentage of T- bonds by 100 per cent from 2017.

On external debt, the FY 2018 MTDS envisaged concessional financing primarily from multilaterals with a gradual increase in reliance on bilateral creditors in the outer years. The actual position at the end of September 2018 indicates that 100 percent of external financing was concessional. Disbursements from existing multilateral facilities accounted for 5.5 percent of external financing while the remaining 30.4 percent was received from new concessional loans contracted in 2018. However, as at September 2018 no disbursements from bilateral creditors were received.

The combination of concessional financing and maturity extension resulted in an increase in the ATM of the total portfolio from 8.2 years in 2017 to 9.0 years in 2018 which is in line with the established target of greater than 8 years. Related to the ATM, there was an increase in the ATR of the total portfolio from 7.8 years in 2017 to 8.6 years in 2018. However, the weighted average interest rate of the total portfolio increased to 3.6 percent in 2018 from 3.1 percent in 2017.

2 EXISTING DEBT PORTFOLIO - 2018

This section reviews in detail the composition of **Central Government’s** outstanding debt.

2.1 Composition of Central Government Debt Portfolio

Figure 1: Composition of Central Government Debt

2.1.1 Total Central Government Debt

For the purpose of this analysis debt is classified by currency. External Debt consists of all foreign currency denominated instruments while domestic debt refers to all EC dollar denominated instruments. As at the end of 2018, total Central Government debt is estimated to be \$ 1,965.8 m. This comprises \$1,358.8 m (69.1 per cent) external debt and \$ 607.0 m (30.9 per cent) domestic debt.

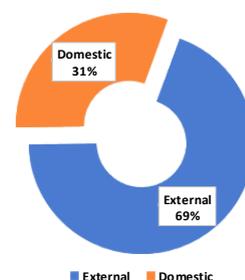


Figure 2: Domestic Debt by Instrument Type

2.1.1.1 Domestic Debt

As at end 2018, domestic debt is estimated to comprise 57.0 per cent bonds, 26.3 per cent Treasury bills, 4.6 per cent Treasury notes, 12.1 per cent loans and other liabilities denominated in XCD.

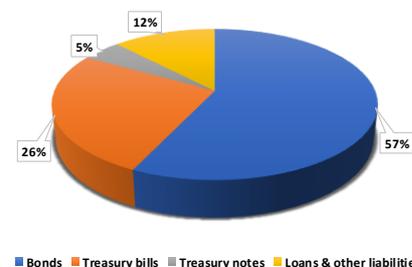


Figure 3: External Debt by Creditor Category

2.1.1.2 External Debt

The composition of external debt as at end 2018 is estimated to be as follows: multilaterals 61.9 per cent, bilateral creditors 12.9 per cent, international bondholders 21.4 per cent, export credit 3.7 per cent and finally commercial loans 0.1 per cent. Multilaterals include IDA, which is estimated to disburse the most in 2018, followed by CDB, IMF, OPEC, IBRD and IFAD. Bilaterals include Kuwait, Trinidad, EXIM Bank of China and Bank of Alba.

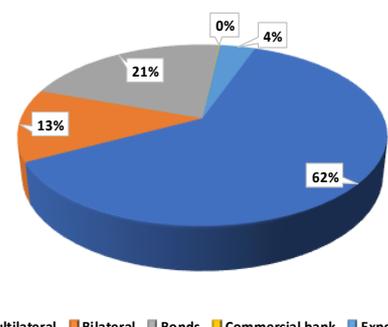
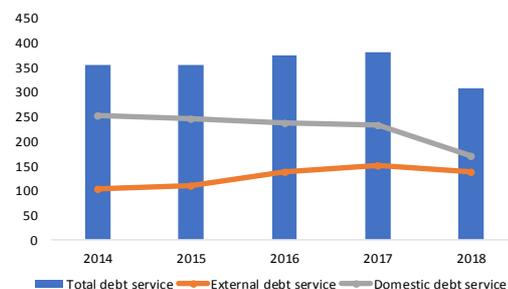


Figure 4 : Debt service payments 2014-2018

2.1.2 Debt Service Payments

Total debt service payments increased over the period 2014 to 2017. However, debt service payments at end 2018 are estimated to decrease by 19.0 per cent when compared to 2017 in part due to principal reductions received from second phase of haircut on the 2030 sovereign bonds. Additionally, there was a 5 percent reduction in the stock of domestic debt in 2018.



2.2 Risk Analysis of the Debt Portfolio

The debt portfolio has inherent risks related to market conditions; basic cost and risk indicators were calculated and analysed. The main portfolio risks are covered in this section.

2.2.1 Interest Rate Risk

The Average Time to Re-fixing (ATR) is a measure of the weighted average time until all the principal payments in the debt portfolio is subjected to a new interest rate. Grenada's debt portfolio has an ATR of 8.6 years of which 21.4 per cent of total debt is subject to a change in interest rate in one year (Table 1). Interest rate risk is mainly inherent in the domestic debt portfolio with a relatively short ATR of 7.1 years. As reflected, 31.4 per cent of its debt is subject to re-fixing in one year due to the relatively short maturity profile of domestic instruments (less than one year). In contrast, the ATR for the external debt is 9.2 years with 17.0 per cent of this debt re-fixing in one year. In addition, a relatively large proportion 90.4 of external debt is contracted on fixed rate terms. The remaining 9.6 per cent reflects variable rate debt owed to multilateral and bilateral creditors.

2.2.2 Refinancing /Rollover Risk

Rollover/refinancing risk shows the vulnerability of the portfolio to higher costs for refinancing maturing debt obligations within a period or in extreme cases if the debt cannot be rolled over at all. With an overall operational target of greater than 8 years, the Average Time to Maturity (ATM) of Grenada's debt portfolio is 9 years which surpasses its target. This is mainly skewed towards the external debt portfolio which has an ATM of 9.8 years of which 8.3 percent matures in one year. In contrast, domestic debt is mainly exposed to refinancing risk due to its relatively short maturity profile. The ATM of domestic debt is 7.1 years of which 31.4 per cent will mature in one year and is subjected to refinancing/rollover risks since a significant portion of short-term debts are rolled over.

2.2.3 Foreign Exchange Risk

Foreign exchange risk measures the exposure of the portfolio to changes in the exchange rate. Grenada's debt portfolio is minimally exposed to foreign exchange risk. Debt contracted in foreign currency accounts for 69.1 per cent of the total debt portfolio. This is in line with the target of less than or equal to 75 percent set for foreign exchange debt. Debt contracted in USD (73.0 per cent) has the largest share of the total foreign debt. Non-USD denominated debt comprises of debt in XDR (23.6 per cent), Kuwait (2.8 per cent), GBP (0.3 per cent) and EUR (0.2 per cent).

Table 1: Cost and Risk Indicators for the Existing Debt Portfolio as at year end 2018

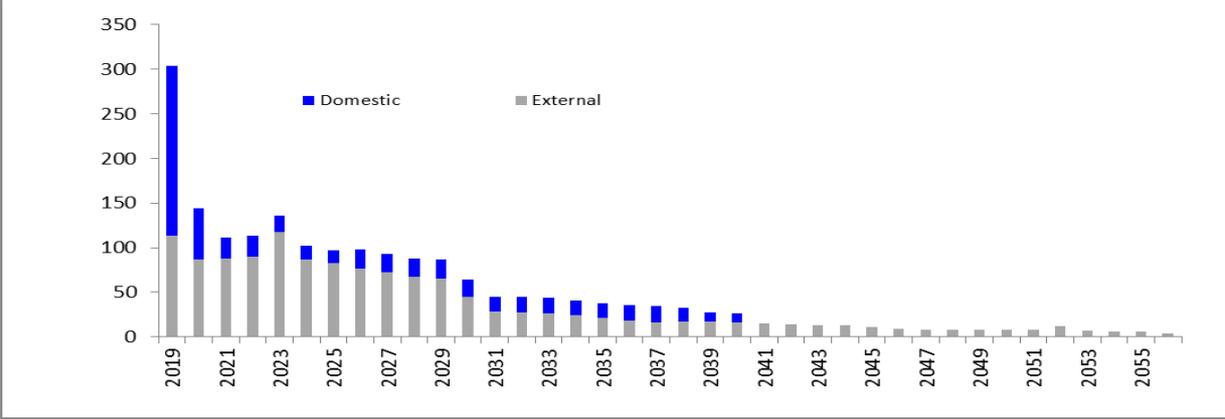
Risk Indicators		Foreign Currency Debt	Domestic Currency Debt	Total Debt
Amount (in millions of XCD)		1,358.8	607.0	1,965.8
Amount (in millions of USD)		503.3	224.8	728.1
² Central Government Debt as % GDP		42.2	18.8	60.9
PV as % of GDP		34.5	18.8	53.1
Cost of debt	Interest payment as % GDP	1.4	0.8	2.2
	Weighted Av. IR (%)	3.2	4.3	3.6
Refinancing risk	ATM (years)	9.8	7.1	9.0
	Debt maturing in 1yr (% of total)	8.3	31.4	15.4
	Debt maturing in 1yr (% of GDP)	3.5	5.9	9.4
Interest rate risk	ATR (years)	9.2	7.1	8.6
	Debt re-fixing in 1yr (% of total)	17.0	31.4	21.4
	Fixed rate debt (% of total)	90.4	100.0	93.4
FX risk	FX debt (% of total debt)			69.1
	ST FX debt (% of reserves)			21.2

2.2.4 Redemption Profile

The redemption profile depicts the amortization of outstanding debt and it reflects the risks inherent in the structure of the existing debt portfolio (Figure 5). A high portion of domestic debt is due within one year for redemption. This is affected by short term debt maturing within one year. In addition, Government has signalled its intention to pre-pay a portion of outstanding claims in 2019. External debt has a relatively smooth redemption profile and a longer maturity period. It is characterised by concessional loans from multilateral and bilateral creditors. Debt service is delayed until 2023 with selected creditors to conclude negotiations on outstanding liabilities, hence the spike in the debt amortization in that year.

² The scope of debt utilized for the MTDS analysis represents Central Government debt. Government Guaranteed debt of public entities was not used in this analysis.

Figure 5 Redemption profile as at end 2018 (XCD Million)



3 MACROECONOMIC PERFORMANCE, MEDIUM -TERM OUTLOOK AND KEY RISKS

3.1 Public Finance

Grenada's fiscal accounts continue to improve, achieving a primary balance after grants of \$ 146.3m or 4.5 percent of GDP for the first nine months of 2018, 24.2 per cent above the amount in the same period of 2017. A primary balance after grants of \$199.6m or 6.2 percent of GDP is estimated at the end of 2018, 35 percent higher than the budgeted amount. Based on the projected outturns for revenue and expenditure, Government's overall surplus and primary surplus are forecasted to average 4.3 and 6.3 per cent of GDP respectively in 2019-2021. This can result in downward pressure on future borrowing volumes. It is anticipated that public debt will be reduced to its FRL's target of 55.0 per cent of GDP in 2020 based on in house debt sustainability analysis conducted.

The GoG has been establishing a prudent liquidity position, with the accumulation of deposits in the National Transformation Fund (NTF) and a Sinking Fund. This provides a level of financial protection to cover possible future losses or even for treasury operations.

The Government's Medium-term Fiscal Framework (MTFF) 2019-2021 has been prepared to ensure compliance with the Fiscal Responsibility Law (FRL) No. 29/2015 (as amended in 2017). It is also framed to support the Government's Medium-term Agenda (MTA), which is being developed with support from the World Bank. The objective of the MTA is to anchor medium-term development planning and strategic interventions to accelerate inclusive, job-rich growth, as well as poverty reduction. In relation to fiscal policy, the primary objective for the medium-term is debt reduction. Accordingly, the Government will continue to deploy revenue and expenditure strategies such that primary surpluses exceeding the FRL's fiscal rules are generated to keep public debt on a firm downward trajectory in the MTFF period.

Table 2: Fiscal Projections for 2019-2021 (MTFF)

Grenada Fiscal Projections						
<i>In millions of Eastern Caribbean Dollars</i>						
	2019		2020		2021	
	Projected	as a % of GDP	Projected	as a % of GDP	Projected	as a % of GDP
TOTAL REVENUE AND GRANTS	964.2	28.5	932.2	26.2	949.0	25.7
CURRENT REVENUE	780.4	23.1	821.5	23.1	853.8	23.1
Tax revenue	726.5	21.5	764.7	21.5	794.8	21.5
Taxes on Income	157.4	4.7	165.7	4.7	172.2	4.7
Taxes on Property	28.0	0.8	29.5	0.8	30.5	0.8
Taxes on Domestic Goods & Consumption	156.8	4.6	165.1	4.6	171.6	4.6
Taxes on International Trade & Transacti	384.3	11.4	404.5	11.4	420.4	11.4
Non - Tax Revenue	53.9	1.6	56.8	1.6	59.0	1.6
Grants	183.7	5.4	110.7	3.1	95.2	2.6
TOTAL EXPENDITURE & NET LENDING	834.2	24.7	780.9	21.9	766.0	20.7
CURRENT EXPENDITURE	637.8	18.9	637.7	17.9	636.8	17.2
Personal Emoluments,Wages, Allowances & social contributions	275.4	8.1	272.2	7.6	272.5	7.4
Goods and Services	124.8	3.7	126.1	3.5	125.1	3.4
Interest Payments	72.0	2.1	67.7	1.9	64.9	1.8
Transfers	165.6	4.9	171.7	4.8	174.3	4.7
Net Lending	0.0	0.0	0.0	0.0	0.0	-
Capital Expenditure	196.4	5.8	143.2	4.0	129.2	3.5
Current Balance (before Grants)	142.7	4.2	183.8	5.2	217.0	5.9
Overall Balance (after Grants)	129.9	3.8	151.3	4.3	183.0	4.9
Primary Balance (before Grants)	18.2	0.5	108.3	3.0	152.6	4.1
Primary Balance (after Grants)	201.9	6.0	219.0	6.2	247.9	6.7
Memo item						
GDP (Nominal market prices)		3,381.5		3,559.4		3,699.2
Real GDP growth (%)		4.2		3.9		3.9

Source: MOF

3.2 Monetary Sector

The fixed exchange rate regime under the Eastern Caribbean Currency Union (ECCU) has been pegged to the USD for over 40 years³. The currency peg reduces margin to manoeuvre monetary policy within the ECCU, but it also provides stability for the portfolio because foreign currency debt is dominated by the US dollar so there is minimal exchange rate risk on Government's debt portfolio.

³ The peg maintains a rate of 2.7 XCD per USD.

The monetary council of the ECCB reduced the minimum savings rate in 2015 from 3.0 per cent to 2.0 per cent and this translated to lower interest rates. The pass through of decreased spreads / interest rates should result in savers seeking to increase their rates of return and to expand their investment portfolio thereby improving competition on the market.

3.3 Real Sector

Preliminary estimates based on data for the first nine months of 2018 indicate that the economy will continue along a positive trajectory in 2018 with projected growth of approximately 5.2 percent. The medium-term economic prospects are positive. Real GDP growth (at market prices) is projected to average 4.0% over the period 2019-2021. Growth will be carried by public infrastructure development, as well as the expected continuation of the relatively strong performances in the construction, education and tourism sectors. Meanwhile, inflation is estimated to edge up in the short term on account of rising international oil prices, as well as possible increases in the prices of imported products should international trade wars escalate. Over the medium term however, inflation is expected to moderate with expansions in global oil production and the anticipated easing in trade tensions. High sustained economic growth over the medium term will contribute to debt reduction. Conversely, lower than expected growth will adversely affect tax revenues, which may increase social spending ultimately leading to increased borrowing needs by Government.

3.4 External Sector

The merchandise trade balance continued to deteriorate at the end of the first half of 2018. A trade deficit of \$591.1m was estimated for the end of June 2018 above the deficit of \$481.0m recorded during the same period of 2017. This deterioration was driven by a 22.2 percent increase in the value of imports to \$626.2m. The value of exports is estimated to have increased by 11.2 percent to \$35.1m buoyed by growth in re-exports and domestic exports of 42.1 percent or \$3.3m and 8.7 percent or \$31.8m respectively. Re-exports expanded primarily due to machinery and transport equipment that were repatriated and to a lesser extent by miscellaneous manufactured articles. Domestic exports' expansion was driven mainly by higher earnings from agricultural exports of nutmegs with a 34.3 percent rise to \$5.8m. Despite these increase, the external trade deficit is projected to widen on account of higher levels of import of construction material, general increase in economic activity and rising oil prices internationally. Any increases in commodity prices can be inflationary that may effectively increase the nominal debt stock and the cost of debt service of non-US foreign currency denominated debt. Low foreign currency earnings as a result of depressed exports and increased imports can adversely affect the country's ability to meet external debt service payments.

3.5 Outlook for Debt Management

The development of a well-functioning Regional Government Securities Market (RGSM) provides an avenue through which the GoG can raise debt financing efficiently to meet the Government’s needs. Albeit over-the-counter transactions also have its place in the borrowing programme. Recognising the need to build its investor relationships, in 2018, the GoG with the support of the IMF and ECCB did preliminary work to develop an Investor Relations Programme (IRP). Going forward, the IRP will be executed by front office of the Debt Unit and will include: regular interactions with its investors, increased utilisation of the RGSM as a platform for auctions, greater co-ordination with the ECCB and regional governments and getting more in touch with the issues affecting efficiency.

3.6 Risk Sources and Potential Impact Factors

The table below details sources of potential risk on the existing debt portfolio and the related impact on debt management.

Table 3: Risk Sources and Potential Impact

RISK SOURCE	IMPACT ON	DEBT-RELATED RISK
GDP decline	Taxes and revenues	Weak debt repayment capacity
Deterioration in fiscal position	Primary balance	High financing needs
Current Account Deficit & FDI reduction	Balance of Payments	Need for external financing (private / public)
Currency depreciation	Debt Portfolio	High FX debt service
Terms of Trade	Commodities prices Exchange rate	High FX debt service
Low appetite for long-dated securities	ATM	Roll-over risk
Reducing stock of concessional external debt	Interest Rates and maturity	Potential drain on reserves/ pressure on the balance of payments

4. MEDIUM-TERM DEBT MANAGEMENT STRATEGY

4.1 Targets and Ranges for Key Risk Indicators

The existing cost and risk structure, while moving in the right direction, is not yet satisfactory and, for that reason, the interim targets have been revised relative to the last Strategy. The strategic benchmarks established in the adopted strategies over the last three (3) years to finance the Budget have resulted in the structure of Central Government debt evolving favourably from 2015 to 2018.

Table 4: Risk Targets and Ranges

Risk Indicators	2018	2021
	Current	Target Range
*Central Government Debt as % of GDP	60.9	<=55%
Interest payment as % of GDP	2.2	<=2.5%
Debt maturing in 1yr (% of total)	15.4	<=20%
Debt maturing in 1yr (% of GDP)	9.4	<=10%
ATM Total Portfolio (years)	9.0	>=8 years
ATR (years)	8.6	>=10 years
FX debt as % of total	69.1	<=75%

**Central Government debt only*

One of the debt management objectives is to achieve and maintain sustainable debt. This target is guided by the FRL (2015) which states that the Public Debt⁴-to-GDP ratio must not exceed 55 per cent. The target for 2021, is for Central Government debt-to-GDP to be less than or equal to 55.0 per cent. This risk indicator has been declining from 84.7 per cent (2015), to 65.8 per cent (2017) and is currently estimated to be 60.9 per cent (end 2018). This rapid decline was supported by the debt restructuring activities that have now ended, as well as fiscal improvement. The interim target for 2021 is to be equal to or below 55.0 per cent. Meeting this target will require reducing the stock of debt and/or increasing economic growth.

Interest payments as a percent of GDP, shows declines from 3.6 per cent (2015) to 2.2 per cent (2018) which has been driven by both lower interest rates achieved through highly concessional loans and a reducing stock of debt. The GoG has also benefitted from declining yields on the RGSM. Consistent

⁴ Public Debt according to the FRL includes:

- the total stock of public sector debt from domestic or external sources for any purpose including the total sum of debt guaranteed by the government including contingent liabilities assumed by the government, but excluding contingent arising from, as a result of, or in connection with public-private partnership;
- the debt and contingent liabilities of statutory bodies and state owned enterprises; and
- such sums as may be necessary to defray expenses in connection with such liabilities.

with the GoG's debt management objective to have a low cost of debt, the target is to maintain the current cost of debt below 2.5 per cent.

Debt maturing in 1 year as a share of total Central Government debt is set to be less than or equal to 20.0 per cent of the total debt. While this may appear as a high concentration of repayments in the short-term, it reflects the importance of Treasury-bills in the development of the domestic market and also meeting statutory requirements for the financial sector. This indicator has declined from 17.8 per cent (2015) to 15.4 per cent (2018), reflective of the conversion of Treasury-bills to Treasury notes in 2018. As a share of GDP, the target is to keep the risk below 10.0 per cent.

Extending the ATM and ATR of the total portfolio to 8 years or more and 10 years or more respectively reduces the refinancing risk and avoids pressures on the GoG to securing new sources of finance. Also, in the short to medium term, the GoG will be running budget surpluses which covers a sizeable portion of the gross financing needs. Existing debt is primarily from concessional sources and development partners with long maturities. It is anticipated that lengthening the maturity is feasible. The policy of the Government, as is reflected in this MTDS, emphasizes implementation of existing Public Sector Investment Projects (PSIP) and draw down on committed undisbursed balances from external creditors on concessional terms.

While the targeted ratio of 75.0 per cent of the Central Government debt portfolio being denominated in foreign currencies suggests a high exposure to foreign currency risk, this is manageable as there is a large share of foreign currency debt denominated in USD. There is little volatility in the USD/XCD rate due to the peg. Risks of valuation changes due to exchange rate movements and market expectations suggest that the XCD will depreciate against the XDR. Non-USD foreign currency debt has been increasing as a share of external debt in the portfolio; and will be monitored closely in the implementation of the strategy.

4.2 Assumptions and Potential Financing Sources

The MTDS (FY2019 -2021) embodies the Government's key strategic debt management objectives and as such, preparation of the Strategy is based on the following assumptions:

- Utilization of a portion of the primary surplus to repay debt and;
- Utilization of committed undisbursed balances

Over the medium term (2019 – 2021), the existing official creditors including multilateral and bilateral creditors will continue to support Grenada's development programmes. Generally, external financing will be denominated mainly in USD and XDR, at fixed interest rates, although a portion of multilateral credit is contracted at variable rate (Table 5).

Table 5: Proposed Terms of Financial Instruments

Creditor/Instruments	Maturity (Years)	Grace (Years)	Interest Type	Currency
Multilateral	20 – 25	10	Fixed	USD
Multilateral	13 – 20	6 – 7	Variable	USD
Multilateral	36	10	Fixed	XDR
Bilateral_NPC⁵	18-20	5	Fixed	USD
2yr Note (Bullet)	2	1	Fixed	XCD
5yr Bond (Bullet)	5	4	Fixed	XCD

4.3 Alternative Strategies

Three (3) alternative debt management strategies were considered. They vary by the mix of borrowing between domestic and external sources, fixed and variable interest rates, and maturity and grace periods.

Strategy 1 (S1): This strategy represents the status quo and reflects the current practice of re-issuing domestic debt (T-bills). Under this Strategy, there is no new borrowing, rather multilateral and bilateral (non-Paris Club) creditors are considered to provide project financing based on committed and undisbursed debt, as well as assumed improvements in implementation capacity and project readiness. This assumption is maintained throughout the medium term, albeit, at an overall reduced amount. However, there will be a consistent level of project financing from the multilaterals. Residual financing needs are met primarily by T-bill issuance.

Strategy 2 (S2): This strategy considers the extension of the maturity of the domestic portfolio by gradually introducing longer-dated securities. Consistent with this Strategy, the intent is to convert short-term securities into two-year and five-year bonds in 2019 and 2020 respectively. Further, a portion of short-term debt is also assumed to be repaid over a three-year period from surpluses. Similar to S1, there is no new borrowing on the external side, rather external financing is met from committed undisbursed debt.

Strategy 3 (S3): This Strategy increases external financing relative to domestic financing, while maintaining the extension of the Treasury-bill maturities and repayment of short-term debt. On the external side, this strategy replaces some of the traditional multilateral creditors with semi-concessional bilateral funding.

⁵ NPC – Non Paris Club Bilateral Creditor

Table 6: Strategy Considerations

⁶ Strategy	Average Financing Mix (%) (Ext: Dom ⁷)	Objective
S1	54:46	Status quo- reflects a combination of the current borrowing practices and committed financing
S2	52:48	Domestic Market Development- use of longer-term domestic instruments to fill funding gap while extending maturing of existing T bills.
S3	67:33	Utilize more multilateral and bilateral funding to fill funding gap

The robustness of the alternative debt management strategies are assessed under three stress scenarios for interest and exchange rates with differing impacts; moderate and extreme. The shocks help to identify the vulnerabilities of the strategies to external shocks. The magnitude of the shocks was determined by the historical experiences of the interest rates in external markets and Grenada. Possible macroeconomic risks facing Grenada's economy are also considered. For the shocks, it is assumed that the market variables (interest rates and exchange rates) will increase over the medium-term. Also, the model assumes consistent growth in nominal GDP for the respective years in the period under consideration.

Baseline Scenario: In the baseline scenario the reference rates for 3-month re-fixed instruments are forecasted to increase marginally over the period 2019-2021. In addition, there are no expected exchange rate changes in the major foreign borrowing currencies that is, the USD and XDR. However, the CNY is expected to depreciate marginally over the projection horizon.

Scenario 1: Exchange Rate Shock

- a) Moderate: A 15 percent depreciation of the domestic currency against the XDR and CNY in 2019, which is sustained thereafter.
- b) Extreme: A 30 percent depreciation of the domestic currency against the XDR and CNY in 2019, which is sustained thereafter.

Scenario 2: Interest Rate Shock

⁶ The Government of Grenada contracted debt denominated in Chinese Yuan from one of its strategic bilateral partners. The proceeds of this loan will be used to on-lend to a local SOE.

⁷ Ext:Dom – Foreign Currency (external) Debt Sources : Domestic Currency Debt Sources

- a) Moderate: A 100 basis points rise in the domestic T-bill cap rate, and 200 basis points rise in 3 month reference interest rate and any other floating rate instruments. The shock was applied to the projected baseline interest rate for each year of the Strategy period.
- b) Extreme: A 200 basis points rise in the domestic T-bill cap rate, and 400 basis points rise in the 3-month reference interest rate and any other floating rate instruments. The shock was applied to the projected baseline interest rate for each year of the Strategy period.

Scenario 3: Combination Shock- is the moderate interest rate scenario (200 basis points on floating rate debt) combined with a moderate exchange rate scenario (15 percent depreciation on the XDR and CNY) in 2019 and sustained thereafter.

4.3.1 Cost Risk Analysis under Different Strategies

Table 7 illustrates the cost and risk indicators under each of the strategies. The robustness of the strategies is assessed by comparing the outcomes under the baseline and the shock scenarios discussed above. The debt-to-GDP ratio declines across each of the strategies compared to the current period end 2018. Present value of the debt in each of the strategies was significantly reduced relative to the current period. Moreover, the interest payment as a percent of GDP was also lowered across all the strategies, likewise the implied interest rate decreased across all strategies relative to the current period.

The associated risks with each of the strategy were assessed based on established targets outlined in Table 7. As it relates to refinancing risk, the results indicated significant improvements across all three strategies relative to the current period. Specifically, the percentage of debt maturing in one year fell significantly across all three strategies, which contributed to an increase in the ATM beyond the established target of at least eight years.

With respect to the interest rate risk, the alternative strategies resulted in a lengthening of the average time in which the interest rate of the portfolio will be subject to change- ATR- (years).

The foreign debt as a percentage of total debt ratio declined marginally when Strategies 1 and 2 are considered while the ratio increases significantly in Strategy 3 relative to the current period (2018). These results are expected given the varying financing combinations considered under the various strategies over the period (2019 - 2021) and the bias towards external financing in Strategies 3. A high level of foreign debt in the portfolio reflects heightened risk as the share of debt denominated in foreign currency (non-USD) is subject to exchange rate risk.

Table 7: Cost Risk Indicators of Alternative Strategies

Risk Indicators		2018	As at end 2021			Target
		Current	S1	S2	S3	
Nominal debt as % of GDP		60.9	55.76	55.77	55.66	Max 55%
Present value debt as % of GDP		53.1	48.42	48.40	47.53	
Interest payment as % of GDP		2.2	1.96	1.97	1.91	2.5%
Implied interest rate (%)		3.6	3.54	3.54	3.44	
Refinancing risk	Debt maturing in 1yr (% of total)	15.4	5.48	5.48	5.49	max 20 %
	Debt maturing in 1yr (% of GDP)	9.4	3.06	3.06	3.06	Max 10 %
	ATM External Portfolio (years)	9.8	9.99	10.01	10.48	
	ATM Domestic Portfolio (years)	7.1	9.19	8.74	9.19	
	ATM Total Portfolio (years)	9.0	9.84	9.75	10.25	min. 8 yrs
Interest rate risk	ATR (years)	8.6	9.34	9.36	9.70	10 yrs
	Debt refixing in 1yr (% of total)	21.4	11.50	10.69	12.18	
	Fixed rate debt (% of total)	93.4	93.36	94.17	92.69	
FX risk	FX debt as % of total	69.1	68.96	68.32	73.39	max 75%
	ST FX debt as % of reserves	21.2	16.89	16.89	16.89	

4.4 Selected Strategy

Strategy 2 which emphasizes utilization of committed undisbursed balances and domestic market development outperformed the alternative strategies with respect to the risk indicators and represents the best alternative to capture Government’s preferences in terms of cost and risk.

Relative to the current period, S2 recorded an increase in the ATM by 0.75 years and an increase in the ATR by 0.76 years over the medium run. The share of fixed rate debt is highest in S2 while the share of non-USD debt in the portfolio is projected to be lowest at 68.3 in S2 by 2021. With respect to the cost and risk trade-off, although S2 is slightly more expensive relative to S3 lower refinancing, interest rate and foreign currency risk highlights the cost and risk trade-off.

Market Risks – Exchange Rate

In the chosen Strategy (S2) identified financing is restricted to securities denominated in domestic currency and drawdown of committed undisbursed funds from multilateral organizations that are denominated in USD.

The ECCB, which is the monetary authority, maintains sufficient foreign exchange reserves to support the EC dollar that is pegged to the USD. The backing ratio’s (i.e. foreign assets to demand liabilities) statutory limit is 60.0 per cent and the Bank’s minimum operational backing ratio is currently 80.0 per cent. However, the ECCB has been able to maintain operational limits well above 90.0 per cent over the last eight years.

Non-USD debt currently represents approximately 17.0 per cent of the foreign currency debt portfolio. Under S2, the planned financing option includes XDR disbursements from IDA equivalent to \$ 5.0 million and from Kuwait Fund for Arab Economic Development equivalent to \$17.8 million over the medium term, while projected XDR principal repayments are equivalent to \$ 32.0 million. Loans

denominated in GBP and EUR represent less than 1.0 per cent of the portfolio; despite the volatility of these two currencies, the impact on the portfolio and debt servicing is considered negligible. External Debt Service to International Reserves fluctuated by a maximum of 0.9 per cent after the application of 15.0 per cent depreciation (moderate) and 30.0 per cent depreciation (extreme) shock scenarios to the baseline; resulting in a ratio of 26.0 per cent as at the end of 2021 (Figure 6).

Foreign debt as a percentage of total debt over the medium term is estimated to reduce slightly to 68.3 per cent from the current proportion of 69.1 per cent, well within the established maximum limit of 75.0 per cent. The chosen strategy thus continues to mitigate against the debt portfolio's exposure to foreign currency risk in the medium term.

Market Risks – Interest Rate

Variable rate debt as a percentage of the total Central Government debt portfolio is projected to decline to 5.8 per cent as at end 2021. The interest payments-to-GDP ratio is projected to fluctuate from the baseline by 0.1 per cent under a moderate shock (2 per cent) scenario and 0.3 per cent under extreme shock (4 per cent) scenario. As at end 2021, under adverse interest rate movements the ratio of interest payments to GDP would reflect a maximum of 2.2 per cent (Figure 7). Exposure to interest rate risk is hence marginal under S2.

Refinancing Risk

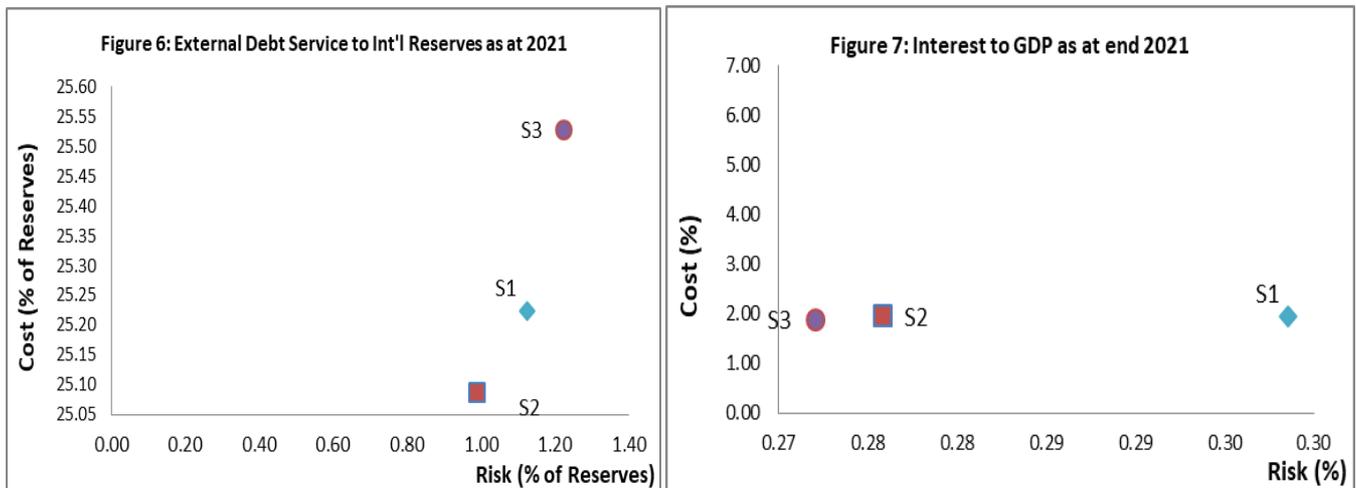
S2 facilitates an extended ATM for the total portfolio, although marginal, while the ATM for the domestic debt portfolio is improved by over a year. Debt maturing in one year as a percentage of total debt and debt maturing in one year as a percentage of GDP would improve significantly by end of year 2021, 5.5 per cent and 3.1 per cent respectively. This is consistent with the goal of retiring a portion of short-term securities and introducing longer-term securities into the portfolio.

Notwithstanding the extension in the ATM and the reduction in the ratio of debt maturing in one year as a percentage of GDP or total debt, the redemption profile is reflecting a spike in 2019. This is indicative of the high level of short-term securities in the portfolio and accelerated payment of portion of outstanding domestic debt. This implies exposure to refinancing risk. The Strategy however, mitigates this risk by retiring higher priced over-the-counter treasury bills on a phased basis. This will take effect over the years 2020 and 2021.

Development of the Domestic Market

Strategy 2 aims to support the development of the domestic capital market. Some of the measures that will be undertaken include further development of the IRP initiated in July 2018. This will provide a framework towards the plan identified that includes retiring over-the-counter instruments and encouraging these investors to participate in the auctions of GoG's securities on the RGSM. The introduction of a 5-year or 7-year bond on the RGSM in the amount of XCD 20.0 million in the year

2020 and the re-issuance of the currently outstanding 2-year note are further measures aimed at utilizing the domestic capital market.



5 BORROWING PLAN

The Annual Borrowing Plan (ABP) is developed based on the GoG financing requirement for the fiscal year. The ABP details the projected funding sources to cover financing after revenues and expenditure have been considered. The Government’s financing requirement is projected at \$ 337.1 million or 10 percent of GDP in 2019.

Table 8 illustrates the borrowing plan for the year 2019. The expected sources of funding include local currency issuances, projected at \$ 173.5 million or 51.5 percent of total financing. This is consistent with the implementation of Government’s strategy objective to foster development of the domestic securities market.

The funding from external sources is projected to be \$163.6 million or 48.5 percent of financing requirements and will include multilateral and bilateral loans in the form of budget support and on-going support for PSIP.

Table 8: Annual Borrowing Plan 2019

	Budget Amt. EC\$
External Funding	163.6
Multilateral	91.9
Bilateral	71.7
Domestic Funding	173.5
<i>Treasury Bills</i>	

GOVERNMENT OF GRENADA

RGSM	100.0
Non-RGSM	43.5
<i>Bonds</i>	
RGSM	26.0
Non-RGSM	4.0
TOTAL	337.1