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Sudan's Unsustainable Debt: The Way Out!

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ABSTRACT

The aim of this paper is to identify the main factors behind Sudan's huge external debt, as well as to identify its impact on the country's major economic indicators (especially Foreign Direct Investment (FDI), Per capita income, and poverty). Moreover, the paper will examine the strategies adopted by the government in order to reduce its unsustainable debt including benefiting from the available international initiatives such as Heavily Indebted Poor Countries (HIPCs); besides proposing a way out for the relief of the country unsustainable external debt. The methodology adopted in this paper is descriptive and analytical in nature depending mainly on secondary sources of data. The study indicated that Sudan's debt is unsustainable and the country is highly indebted. Subsequently, statistics by International Monetary Fund (IMF) showed that the present value of Sudan's total external debt, as of December 2012, stood at $ 79 billion, which was equivalent to 150% of GDP, 1,697% of exports and 1,646% of revenues. These ratios are far beyond the threshold of debt sustainability for Less Developing Countries. Although, the country is qualified technically to benefit from the HIPCs initiatives, but the Sudan has been banned from entering into the initiative, partly because the country needs to settle its arrears to the major creditors, i.e., IMF, World Bank (WB), and African Development Bank (AFDB), Paris and Non-Paris Club Creditors, and partly due to political demands imposed by the international community (in general and US in particular) to solve the Darfur problem.

Keywords: Debt indicators, external debt, Sudan, unsustainable debt.
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1.0 INTRODUCTION

Sudan's build-up of external debt can be traced back to the 1970s when the country embarked on large-scale industrialization, financed in part by foreign borrowing on non-concessional terms, and accompanied by government heavy regulation of the economy. This resulted in a rapid build-up of external debt service arrears, which grew from $ 0.2 billion in 1979, to $ 1.3 billion in 1981 and to $ 2.0 billion in 1982. Thus, during the period of 1980-1990 external debt grew considerably from an amount of $ 4.670 billion in 1980 to an amount of $ 15. 303 billion in 1990. The majority of the debt in the 1980s came from official sources, namely multilateral donors including International Monetary Fund (IMF) and World

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Bank (WB); besides bilateral donors (e.g., Paris Club Countries[2]), which amounted to 78.5% of the total debts, whereas the private donors (e.g., private commercial banks) accounted for 21.5% of the total debts (Ahmed, 2008).

The same trend continued during the periods of 1990-1999, 2000-2010; whereas external debt continued to rise from $ 15.834 billion in 1990 to $ 37.5 billion by 2010, of which arrears on debt amounted to $ 21.5 billion (Central Bank of Sudan {CBOS}, 2010; cited by Baba, 2012). By the end of 2013, the country's external debt rose rapidly to a staggering figure of $ 43.8 billion, of which arrears on debt constitutes 86%, including 59% of penalties on delayed payments. Again, bilateral and multilateral debt dominated the portfolio accounting for an average of 69% and 13% respectively (CBOS, 2013).

The aim of this paper is to identify the main factors behind Sudan's huge external debt, as well as to identify its impact on the country's major economic indicators (especially Foreign Direct Investment (FDI), Per capita income, and poverty). Moreover, the paper will examine the strategies adopted by the government in order to benefit from the available international initiatives such as Heavily Indebted Poor Countries (HIPCs); besides proposing a way out for the relief of the country unsustainable external debt. In addition, the paper will explore the Sudan Government attempts regarding negotiating the apportionment of the stock of external debt with the newly independent South Sudan Government. In fact, many Sudanese scholars have addressed the issue of Sudan's external debt problem (Rahman, 1995; Ahmed, 2008; Baba, 2012), but no wider attention has been given to the issue of debt apportionment between the two Sudanese governments, i.e., the Sudan Government and the newly independent South Sudan Government; Perhaps owing to the fact that the secession of Southern Sudan has taken place only four years ago in 2011.

The methodology adopted in this paper is descriptive and analytical in nature depending mainly on secondary sources of data. The paper is organized as follows: the next section explores the origin of the external debt; besides examining its impact on developing countries. Section three reviews causes of Sudan's external debt; while section four examines the strategies adopted by the government in order to utilize debt relief initiatives provided by International Financial Institutions (IFIs). Finally, section five presents the conclusion of the paper and its main findings, as well as the policy implications that related to the main findings.

2.0 LITERATURE REVIEW

The IMF defines the external debt as "the outstanding amount of those actual current, and not contingent, liabilities that require payments of principal and/or interest by the debtor at some points in the future and that are owed to nonresidents by the residents of an economy" (IMF, 1993). Another definition for external debt described it as "all external obligations of maturity of one year or more of outstanding at a particular point in time and are payable in terms of reserves currency or goods and services" (Ahmed, 2008).

Furthermore, the external debt is classified according to donors, whether they are official creditors or private donors; the official creditors could be multilateral such as the IMF or WB, or bilateral (government to government lending). The donors could include private commercial banks and private credit suppliers. Moreover, external debt could also be defined in terms of who shoulders the responsibility of repayment, whether public or private institutions (ibid.).

Another important issue relating to external debt is the concept of "debt overhang", which was defined by Krugman as "a situation where the expected present value of the future country transfer is less than the current face value of its debt". On average, debt overhang occurs when the face value of debt reaches about 55-60% of the GDP or 140% of the exports. In such cases, the initial debt tends to be associated with subsequently low growth (Krugman, 1988; cited by Ahmed, 2008). In addition, Kitabire

[2] Paris Club Creditors contains 16 countries mostly Western besides USA and Japan.

and Kabanda argue that "external debt sustainability is achieved when a country is expected to be able to meet its current and future debt service obligations in full without recourse to debt relief, rescheduling of debt or the accumulation of arrears and without unduly comprising growth" (Kitabire and Kabanda, 2006; cited by Ahmed, 2008).

The origin of the external debt crisis of the Less Developed Countries (LDCs) can be dated back to 1982, when Mexico declared its inability to repay its debt service. Indeed, the international economic environment witnessed major changes in the 70s and early 80s. These changes included the introduction of floating exchange rates to replace the fixed one, which accompanied the 1971 US announcement of the inconvertibility of the dollar into gold (Carvounis, 1984). Additionally, the 1970s witnessed the major petroleum price hikes by OPEC that took place immediately after the 1973 Arab-Israeli War. Moreover, this period was characterized by the deterioration of terms of trade for developing countries, particularly commodity export prices and rising import costs for manufactured goods; this was associated with substantial rises in real interest rates (ibid.).

These changes have had a negative effect on the economies of developing countries, especially the non-oil producing ones. For instance, the oil price hikes added about $16.5 billion to the oil bills of non-oil developing countries (NODCs). Simultaneously, the 'stagflation' and recession that took place in the Western countries due to the rise in energy prices led them to increase the prices of their manufactured imports to developing countries by almost 40%, as well as to reduce their demands for developing countries' exports (ibid.).

Consequently, developing countries' import bills rose drastically while their exports decreased substantially, leading to huge fiscal and trade deficits, as well as a widening gap between saving and investment. Thus, they turned to borrowing on the international markets to cover these gaps. However, their financial crisis became even worse as their debt service grew to unmanageable proportions. For example, Morocco's debt increased by 10% between 1970/1982, while its debt service rose from 11% of goods and services exports in 1970 to 49% in 1982 (Pfeifer, 1999).

When their financial crises became intolerable, the developing countries resorted to seeking the assistance of the World Bank and the IMF. Both the IMF and the World Bank diagnosed the debt problems that were facing developing countries as being related to their balance of payments, as well as to government revenue and expenditure balance (Woodward, 1992). Accordingly, they called for these countries to tighten their monetary and credit policies and to implement structural adjustment programs, which focused mainly on increasing the role of the private sector in the economy while reducing that of the public sector. Furthermore, these programs urged developing countries to move their economies towards free-market conditions, with special emphasis on the adoption of liberalization and privatization policies.

3.0 CAUSES OF SUDAN'S EXTERNAL DEBT

Sudan's external debt crisis, like many such crises in developing countries, was partly due to external factors as outlined by the previous section. However, several Sudanese scholars argue that domestic factors were also responsible for the country's external debt crisis. They mainly refer to the neglect of Sudan's principal export crop (cotton); the absence of an external debt mechanism in the country (the external debt unit at CBOS was established in 2000); and economic corruption (Rahman, 1995). Other factors include reliance on foreign aid and finance, and the use of such finances in low-yielding projects; mismanagement of debt and lack of coordination between institutions dealing with external debt; adoption of overvalued exchange rate, which led to distorted factor and commodity prices, discouraged exports and led to import reliance; inadequate capacity to negotiate with donors has reduced its economic gains, and deprived it of soft borrowings and resulted in enlargement of indebtedness. Furthermore, reliance on heavy taxation of exported sectors and productive sectors has discouraged productiveness and increased cost of production; the war in Blue Nile, South Kordofan, and Darfur area continues to hamper development efforts; besides the negative impact of the droughts and desertification waves on people and livestock (Ahmed, 2008).

Sudan like many LDCs have been overburdened by formidable debt and its debt seems to be unsustainable; whereas its external debt amount to $ 42 billion in 2012 and its external debt indicators persist at very high level as shown by the following table.

Table 1: Debt sustainability analysis for Sudan

Year	Indicative Threshold	2012
PV of debt to GDP	30	170
PV of debt to exports	100	1567
PV of debt to revenue	200	1468
Debt Service to exports	15	37
Debt service to revenues	18	35

Source: IMF (2012).

Regarding the impact of external debt crisis on certain economic indicators (specifically FDI, Per capita income, and poverty), one should note that external debt has affected negatively the amount of FDI; whereas FDI was zero during the period 1990-1995, and amount to only $ 0.7 million in 1996 before rising sharply to $ 101.2 million in 1997 due to some good GDP growth rates; as well as successful efforts undertaken by the government to improve its economic relationship with some Arab and Asian countries. The country also witnesses a remarkable increase in the magnitude of FDI during the period 1998-2006 due to the exploration and production of oil reaching a record high of $ 3.5 billion in 2006, which made Sudan Africa third largest recipient for FDI (ibid.).

On the other hand, external debt has had a negative impact on per capita income, a study conducted by (Ahmed, 2008) indicates the negative relationship between the growth of per capita income in real terms and the stock of external debt in the Sudan during the period of 1980-2006; whereas the negative coefficient of external debt ranges from -0.20 to -0.89.

Regarding external debt impact on poverty (with 46.5% of the population under the poverty line) one should note that debt service repayments drain sizable resources. This hinders Sudan ability to attract FDI and concessional financial resources. Also, lack of access to concessional financing has important negative implications on the economy and the country efforts to reduce poverty, finance infrastructure and social programs, and on programs designed to bring about innovation and job creation, which are all critical for revitalizing the economy (Sudan Debt Relief and Arrears Clearance Strategy "SEDRACS", 2013).

4.0 STRATEGIES ADOPTED BY THE GOVERNMENT TO UTILIZE DEBT RELIEF INITIATIVES

The Sudan government has made an exerted effort regarding rescheduling of its external debt since 1980s. Thus, signed four bilateral debt rescheduling agreements with its Paris Club Creditors during the period of 1981-1984. In addition, the government called for the cancellation of its bilateral external debts in 1987 including government loans and commercial guaranteed (Ahmed, 2008). However, Sudan was not able to meet all conditions set in the various agreements including those with non-Paris Club Creditors[3].

The period of 1990-2000 witnesses a shaky relationship with IFIs especially the IMF, with Sudan outstanding external debt amounting to $ 20 billion, without any genuine policy adopted by the government to tackle this debt. Consequently, the Fund started to take action against Sudan, which ended in September 1990 by declaring the country as non-cooperative state. The Fund even went a step further by suspending the country's voting rights in August 1993. Moreover, in April 1994 the executive Council of the IMF submitted a draft proposal calling for the compulsory withdrawal of Sudan from the

[3] Non-Paris Club Creditors include some Arab and Asian Countries such as Saudi Arabia, China, and India.

Fund. But two years later in 1996 the Fund decided to suspend efforts to force Sudan to withdraw its membership (Strategic Institute, 1998).

Although, in August 1999 the IMF Executive Board lifted its declaration of non-cooperation regarding Sudan; and the country regained its full membership in the Fund, and its complete voting rights. Nevertheless, the Fund assistance to the country was limited to technical aid only.

The Sudan Government continued its effort in solving or reducing its huge external debt by establishing an external debt unit at the Central Bank of Sudan in 2000. The unit designated as the sole institution to be dealt with Sudan's external debt, its magnitude, the burden indicators, debt sustainability, documentation of various debt owners, contractual agreements, principal of the debts, and interests (Nagem Eldin, 2006; cited by Ahmed, 2008)[4].

In spite of the signing of the Comprehensive Peace Agreement (CPA) with the South in 2005, but the IMF policy towards Sudan remains the same during the period 2001-2014. Although the international community and IFIs promised to contribute in solving Sudan's external debt problem if the two parties reach to an agreement on disputed issues. As a result of this agreement the South was able to declare its independent from the North in 2011. The immediate impact of the secession is reflected into serious threat to economic stability and economic growth, which in turn compromise the government ability to reduce poverty. Indeed, the secession of Southern Sudan resulted in the country losing three quarters of its oil production; half of its fiscal revenue; two third of its international payment capacity[5]. Consequently, the budget and balance of payment deficits have escalated and this was reflected in the high inflation rates that escalated to 40% and the devaluation of the Sudanese Pound by almost 66%.

Given the economic situation of Sudan, the ability of the country to find a sustainable solution to the problem without access to debt relief is impossible. In addition, the capacities of the government to service its debt would be at the expense of providing basic service to the needy population. For this reason, the Government has felt the need to introduce its External Debt Relief and Arrears Clearance Strategy (SEDRACS) in October 2013, as a basis for seeking assistance from the international community.

The SEDRACS comprised two categories: immediate to short term strategy, and medium to long term measures. The immediate to short term strategy focuses on implementation of sound macro-economic policies including reforms in budget, tax administration, and debt management. Also, implementation of arrears clearance plan especially with the country's major donors (IMF, WB, Paris and Non-Paris Club Creditors); as well as subsequent normalization of relationship with these institutions and countries. Alternatively, medium to long term strategy involves addressing the debt issue in a more comprehensive and integrated manner, since immediate and short term strategies show that the country would not be able to attain debt sustainability up to 2032. Therefore, Sudan appeals for a special fast track debt relief (SEDRACS, 2013).

Regarding the government effort to benefit from HIPCs initiative, we realize that the country meets both of its criteria. Hence, according to the IMF staff report on Debt Sustainability Analysis (2012), the present value of Sudan's total external debt, as of December 2012, stood at $ 79 billion, which was equivalent to 1,697% of exports and 1,646% of revenues. These ratios are far beyond the threshold of debt sustainability for Less Income Countries[6].

The progress made by the government toward finalizing the technical work required to advance towards the decision point of the HIPCs initiative was even praised by the IMF in its 2012 report, advocating that:

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[4] In the last three decades the Sudan Government did not have one single unit or department empowered with all aspects of the external debts (Ahmed, 2008).

[5] During the period 2000-2010 oil contributed with 11% of GDP; 40% of domestic revenue; 90% of export earnings; and 15% of industrial value added (SEDRACS, 2013).

[6] The HIPCs has a range of criteria for evaluating debt sustainability; which was defined by where debt to exports of goods and services is equal or more than 150%, and where debt divided by government revenue is equal to or more of than 250%.

> "The Sudan government has taken three important steps: it has reconciled over 90% of the end-2010 external debt in collaboration with creditors; Parliament has approved an ambitious interim-PRSP in June 2012; and Sudan has implemented 13 Staff-Monitored Programs (SMPs) with the Fund since 1997, establishing a sound track record of cooperation on economic policies and payments. Furthermore, Sudan has indicated its desire to continue demonstrating a strong commitment to cooperation with the Fund on policies and the payment of arrears" (IMF, 2012).

However, it seems that political factors rather than economic ones banned the country benefiting from the HIPCs initiative.

One should also mention that the estimates by the Sudan Technical Working Group (TWG[7]) showed that granting Sudan debt relief under HIPCs initiative would reduce Sudan's external debt to 150% of estimated exports. This is based on the assumption that Sudan would reach the HIPCs Initiative's Decision Point by the end of 2013 and the Completion Point by the second half of 2015. Based on the above assumptions, the estimated HIPCs debt relief would range between US$ 10.3 billion to US$ 11.1 billion in PV terms (SEDRACS, 2013).

On the other hand, both Sudan and Southern Sudan Governments have agreed on a Zero Option[8] to resolve the external debt issue in which Sudan will retain all external debt liabilities and all external assets of the Republic of Sudan. The signed cooperation agreement related to the Zero option stipulated that the two countries will work together i.e. undertakes a "Joint Approach", to the international partners to assist Sudan in addressing its external debt problem including direct debt relief from creditors under HIPCs; as well as to provide assistance in lifting all economic sanctions imposed on Sudan (CBOS, 2015).

Based on the Zero Option and upon the initiative of the African Union (AU), a tripartite committee was formed, composed of representatives from the African Union High Implementation Panel (AUHIP), the two governments of Sudan and South Sudan. The committee was tasked to follow up and resolve the debt issues. Accordingly, the AUHIP has approached several creditors to assist the two parties in dealing with the debt problem. Initially, the AUHIP creditor outreach started to bear some fruits as some creditors (i.e. UK and USA) made provisional allocation in their respective budgets for treatment of Sudan's debt (SEDRACS, 2013). One should note that the failure to resolve Sudan's debt based on the principle of the Zero Option, will consequently lead to debt apportionment for both external assets and liabilities as a fall back option[9].

5.0 CONCLUSION

It is clear from our previous analysis of Sudan's external debt magnitude, debt burden indicators and debt sustainability analysis, Sudan's debt is unsustainable and the country is highly indebted. Subsequently, statistics by IMF indicated that the present value of Sudan's total external debt, as of December 2012, stood at $ 79 billion, which was equivalent to 150% of GDP, 1,697% of exports and 1,646% of revenues. These ratios are far beyond the threshold of debt sustainability for Less Developing Countries. Moreover, Sudan case gives further proof to the debt overhang hypothesis introduced by Krugman, since these ratios exceed the ones determined by the hypothesis, i.e., 55-60% of the GDP or 140% of the export.

Although, the country is qualified technically to benefit from the HIPCs initiatives, but the Sudan has been banned from entering into the initiative, partly because the country needs to settle its arrears to the

[7] The objective of TWG is to inform creditors on progress made in implementation of CPA, especially on technical debt issue. It includes members from IMF, WB, ADB, Paris and Non Paris Club Creditors.

[8] The Zero Option had been used before in the case of Former Soviet Union, as well as the case of Pakistan and Bangladesh (Baba, 2012).

[9] At first the zero option indicated that the decision point of HIPCs can be reached by October 2014, now extended to October 2016.

major creditors, i.e., IMF, WB, and AFDB, Paris and Non-Paris Club Creditors, and partly due to political demands imposed by the international community (in general and US in particular) to solve the Darfur problem. In fact, the US economic sanctions and political pressure implemented against Sudan since 1993, when the country was added to the list of states sponsoring terrorism, has a negative effect on the normalization of relationship with both IFIs and Western Countries.

Therefore, the Dialogue with the US and other Western Countries needs to be invigorated and consolidated by genuine government effort in the political arena, whereas efforts should be made to move away from this vicious circle of continuing crisis of political legitimacy. Accordingly, the government should engage in a wider political debate with the opposition political parties, civil society leaders, and other social forces in order to ensure an inclusive peace process and reconciliation for the Darfur region in particular and for the whole country in general. We should also mention that the pace and success of the dialogue with creditors will greatly depend on the willingness and flexibility of all creditors especially the US, because without the debt relief and sanctions lifting Sudan cannot access the official development assistance and important technology markets.

Moreover, Sudan's debt strategy should continue to focus on avoiding reliance on non-concessional borrowing securing external support on highly concessional terms, and increasing the grant element of external borrowing received to finance necessary development and infrastructure expenditures. Consequently, priority in investment should be given to infrastructural activities (such as roads, electricity, water and sanitation) and productive sectors mainly the agricultural sector, which still hold the future potential in terms of natural resources, employment, income and opportunity for growth in the future. This should be strengthening by providing more stable political and business environment; besides adopting prudent public debt and macro policies.

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