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Debt levels to remain high in next five years amid widening fiscal gaps, lawmakers informed

ISLAMABAD: At a time when the debt levels are unsustainable and alarmingly high, the government on Friday revealed that it will borrow additional funds in the next five years owing to greater need for bridging the fiscal deficit and keeping it within the projected target.

Debt Office of Finance Division Director General Abdul Rehman Warraich shared these details after parliament asked the government to explain its five-year debt management plan, projected strategic targets of debt maturity and diversification.

Rehman informed the NA's Standing Committee on Finance, led by Asad Umar, that the government would borrow almost $22bn from external sources by end June 2020, which will increase total external public debt to around $98bn.

The government has projected to payback almost $8bn by June 2020. The DG also explained that medium-term debt strategy (MTDS) is focusing on projection, which the government believes that it can be achieved over the next five years.

The standing committee's members expressed their apprehensions with regard to the measures adopted in this regard.

Briefing the committee, the DG said that based on these flows; it was not possible for the government to meet all the strategic targets over the next five years owing to the fact that debt levels are very high. "But, we will make significant progress to our strategic targets," he added.

The Finance Division has made long- and medium-term projections for both domestic and external debt.

At the end of last fiscal year, domestic debt was 66pc of the total public debt while external debt was 34pc. The government has projected that, in the long run, the ratio of domestic debt will be raised to 70pc while that of external debt to be lowered to 30pc.

Govt aims to shift towards Shariah-compliant, bilateral borrowings

However, the DG said these targets might be unachievable due to rising financing needs. This ratio, he said, is going to be worse over the next five years. The external debt is going to be 41pc by the end of FY24 and domestic debt to be 59pc, he added. The change in these ratios depends on the economy's performance.

External debt

At the end of FY19, the multilateral/bilateral debt ratio was 73pc of the total external debt, while debt raised through Euro/Sukuk bonds issued in international capital market, constitutes 9pc and commercial bank loans make up for the remaining 18pc.

The DG claimed that the government would be able to significantly lower commercial borrowing and increase the debt raised through Eurobond/Sukuk from current 9pc to 14pc share in the total external debt in the next five years. The government wants presence in the international capital market in order to ensure transparency.

The long-term targets, projected for external debt, are very ambitious and government projects to lower share of commercial banks to 12pc from current 18pc in total external debt. “The government doesn’t want to borrow from the international commercial banks”, he said while adding that the strategic target in this regard is 5pc in the long run.

He said the government’s strategy is to increase the level of borrowing from multilateral/bilateral sources, which is concessional in nature, and raise its ratio to 80pc in the long term. However, in the next five years, the government will only be able to reduce the share to 73pc from the existing 74pc.

Domestic debt

The DG said that, now, the domestic debt is a big challenge for the government. He said that by the end of last fiscal year, domestic debt has a short period of maturity, which has compelled the government to blow out in market and refinance a huge amount of domestic debt.

He claimed that the maturity profile of domestic debt improved owing to the fact that almost all the government borrowing from the central bank was converted into long-term debt with maturity period between 1-10 years. The government, he said has also committed to stop borrowing additional funds from the central bank.

Because of re-profiling, the DG said the maturity ladder of domestic debt has improved.

It is clear from the data that at the end of the FY19, the short-term debt ratio stood at 27pc of the total domestic debt with a maturity period of less than a year.

The government projects that this will be lowered further to 20pc over the next five years. The long-term projection is 15pc for short-term debt in overall total domestic debt.

The medium-term debt ratio – with maturity period of 1-5 years -- stood at 30pc in FY19, and is projected to remain at the same level over the next five years. The ratio of debt, with maturity period of more than five years, will be increase to 50pc by FY24 from 44pc in FY19.

“We think that over the next five years, we may not be able to achieve our strategic targets due to constraints. We can only bring down short-term debt to 20pc while the long-term debt will be improved to 55pc of the domestic debt”, he said.

At the end of FY19, fixed rate debt stood at 45pc of the total domestic debt while floating rate debt stood at 55pc. “We would like to see the drastic change in these proportions. We have targeted that the fixed rate debt should be increased to 70pc while reducing the floating rate debt to 30pc in the long term. We will enhance fixed rate debt to 53pc while reducing the floating rate debt to 47pc in the next five years”, the DG explained.

He said that increasing the proportion of Sharia-compliant debt instruments is the priority of the government.

At the moment, 99pc debt is raised though conventional instruments while only 1pc is from Shariah instruments. There is plenty of liquidity available with Shariah-compliant institutions, he added.

Over the five years, “we can see to increase the proportion of Shariah-complaint debt to 10pc from 1pc.

“As a percentage of total public debt, the domestic debt is at 66pc -- almost two-thirds while one-third or 34pc is external debt.

“We believe in the long run, the external debt should not be more than 30pc because it creates exchange rate exposure and repayment burden for the government”, he said.

The DG said that he did not see any major chances for the government achieving these targets.