



An African perspective of fiscal policies and debt management in the wake of the COVID-19 Pandemic

By:

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The COVID-19 pandemic has brought into sharp focus the conversation on money and debt of sovereign economies. Central banks across the board have taken [stringent measures](#) such as emergency rate cuts to keep their economies afloat. Reduced economic activity has however led to the significant reduction in the circulation of money globally. Furthermore, because of the diminishing value of the world's major currencies, especially the US Dollar, many investors are making a run towards safer assets such as gold and precious stones. As a result of the financial crisis generated by the pandemic, African countries face [immense pressure](#) caused by the sudden cessation in foreign direct investment, private capital inflows, and more significant cash outflows.

Evidently, considerable uncertainty prevails with regard to budget forecasts for the 2020 financial year as countries put together emergency fiscal measures and commodity exporters adjust to recent price changes. On average, [projections](#) suggest that for oil-importing countries, fiscal deficits in 2020 could be about 2.5% of the GDP higher than in 2019. The drivers being an increase in expenditure in health spending and discretionary stimulus in some cases. For oil exporters, the deficits could be 3% of the GDP higher as a result of the decline in revenues. The increase in expenditures in oil-exporting countries is expected to be less than for oil-importing countries, given the limited fiscal space and mainly targeted at the health sector.

Indeed, the COVID-19 pandemic is pushing African countries into negative per capita growth. Many African countries have taken a harder hit due to the reduction in oil and commodity prices, weaker currencies and the increase in foreign debt servicing costs. There is a looming [economic recession](#) and experts have forecasted that approximately 20 million jobs could be lost. This has forced governments to make painful [macroeconomic adjustments](#).

Contrary to the reality in African countries, governments and central banks of developed countries around the world have sufficient reserves and proper disaster management fiscal plans since their budgets are largely financed by debt. [According to the IMF](#) the average level of debt in African countries was about 57% of the total GDP in 2019. [Several low-income countries](#) were already at high risk of debts distress, while the rest were running on high debt levels. This is largely due to increased reliance on borrowing from commercial sources, high debt servicing costs, increased exposure to tighter global financial conditions and increased acquisition of debt capital and spending on [infrastructural developments](#).

Consequently, African countries remain unprotected. Although they have the policy space, their capacities to develop and implement proper fiscal management plans and build sufficient reserves are limited. Financial support is crucial to contain the spread of the virus, to protect vulnerable organizations and households, mitigate the overall economic impact and cushion the countries from the economic losses which will still be felt long after COVID-19 has been satisfactorily contained.

Inevitably, the debt levels for African Countries are expected to increase; however, the evolution of the debt levels depend on additional fiscal stimulus, the realization of contingent liabilities, economic growth and currency depreciation which are difficult to predict. To deal with the impact of the COVID-19 pandemic, many African countries have sought additional funding from the International Monetary Fund (IMF), which has proven to be insufficient. Considering Africa's current financing needs, the debt levels will indeed become unsustainable. Hence there is need for transparency and proper debt management policies including debt restructuring and cancellation policies. These policies should be temporary and implemented transparently with the goal being crisis management. All relevant stakeholders should be kept informed and assured that the increase in debt will be properly managed and the funds put to efficient and effective use. Such an approach will ensure the region stays on track to build resilience and restore growth to create employment.

The appropriate policy responses will depend on country-specific circumstances. They can comprise a variety of measures, including exchange rate adjustment, foreign exchange intervention, temporary capital flow management measures, and external financial assistance. In countries with flexible regimes, the exchange rate should be allowed to adjust and act as a cushion for terms of trade shocks. For countries with adequate reserves, foreign exchange interventions can be used to smooth exchange rate volatility to limit financial stress caused by currency mismatches.

Given that countries are facing sudden reversals of external financing, [temporary cash flow management measures](#) could be considered. For instance, lowering of interest rates on borrowing can play an important role in containing the economic situation. Exchange rate flexibility and a drawdown on reserves where applicable should also be considered as part of a wider policy package. Broad-based support from development partners is essential to help the region prepare health systems and raise much-needed financing.

African countries, through the African Union, can take advantage of the continental monetary system to mitigate the effects of the financial strains. An immediate response would be to create a policy emulating the Special Drawing

Rights of the IMF, allowing countries to obtain funding from the AU without the typical eligibility requirements. Initiatives such as the [US African Growth and Opportunity Act \(AGOA\)](#) should be open to all African countries without political conditionalities. These measures will not only alleviate the burden for African Countries but also pave the way for them to establish fiscal policies that mitigate the impact of the pandemic and the looming economic recession.

Further, to bridge financing gaps caused by large external shocks, countries should proactively seek external funding. In this regard, mobilizing concessional funding is essential to ensure that necessary fiscal steps can be taken, especially for countries in debt- distress that have no access to market financing. This will require coordinated support from IFIs and the G-20 and other development partners.

At the international level, there is a need for a sovereign debt restructuring policy providing austerity measures to ensure debt repayment as well as a fair, rules-based distribution of losses should a country become insolvent. The policy should also re-examine the forms of financing extended to countries during this and future pandemics to ensure that the financial assistance does not increase their debt burden. In addition, the conditions attached to the assistance should not undermine investment in public health systems to deal with the pandemics and the resultant economic downfalls. With the support of the World Bank and IMF, countries should also push for a [moratorium](#) on bilateral debt for the duration of this crisis.

When undertaking discretionary financial support, African countries should focus on fiscal programs targeting the most affected sectors and households to alleviate liquidity constraints. They should also ensure transparency and accountability in managing the spending necessary to manage the impact of COVID-19. As [reported by the ILO](#), more than half of the population in African countries are employed in the informal sector; this may present some difficulty in the implementation of the programs.

African Governments, therefore, must take unique approaches to the implementation of fiscal policies in this regard. The following are some of the options available:

1. Tax relief. Temporary tax relief may be considered, including reducing rates on turnover and income taxes, extending tax deadlines, expediting value-added tax returns and tax exemptions of health, and other essential products. This approach has been adopted by the Kenyan Government, where the President, Hon. Uhuru Kenyatta issued a [directive for a tax relief](#) to be implemented through the [Tax Amendments Act, 2020](#) is passed into law. The Tax amendments include 100% income tax relief for low-income earners, reduction of corporate tax from 30% to 25% and reduction of value-added tax from 16% to 14% amid the COVID-19 pandemic.
2. Public support. This could take the form of government guarantees and subsidized loans, particularly for [hard-hit sectors](#), such as tourism which is a big income earner for Sub Saharan countries. However, sector-specific support should be based on merit and done transparently to ensure good governance. For instance, [Ghana](#) has put in place a six- month moratorium on principal payments for entities in the airline and hospitality industries which have been particularly affected by the crisis.

Countries could also prioritize scaling up and facilitating [access to existing social programs](#), possibly through broader targeting. Cash transfers through mobile money can also be considered to reach people at scale, particularly people in the in marginalized communities, provided that recipients can be identified based on readily available socioeconomic information.

Once, the health crisis subsides, the fiscal policies should be adjusted to reduce debt vulnerabilities. The objective of long-term financial stability, sustainability, and the availability of adequate financing and efficiency in domestic resource mobilization should guide the pace and extent of adjustment. Countries should also focus on efficiency gains in current spending. Encouraging production to will be a key factor to minimize the effects of the pandemic on economic growth. Such an approach would help to ease the burden of the temporary negative effect on economic activity, without compromising financial sustainability. It would also help to contain the effects of potential volatility in the international debt market.

In conclusion, African countries are very diverse in terms of their current debt situation, debt management practices and government securities markets. [Debt management](#) is, therefore, a vital component of the appropriate fiscal

policy for the management of the negative impact of COVID-19 on the economy of African countries. However, debt management alone cannot solve structural problems and macroeconomic imbalances. Rather, a holistic approach including an appropriate debt level, debt restructuring, and maintenance of healthy domestic and continental forex markets can contribute to preventing sovereign insolvency despite the negative effects of this pandemic to African countries.

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