Sustained Debt Reduction: The Jamaica Exception

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Sharp, sustained reductions in public debt are exceptional, especially recently

- We know this because public-debt-to-GDP ratios have been trending up in advanced countries, emerging markets, and developing countries alike.
- Governments have borrowed in response to financial crises, pandemics, wars and other emergencies, resulting in higher debt ratios.
- But only in rare instances have they succeeded in bringing those higher debt ratios back down once the emergency passed.

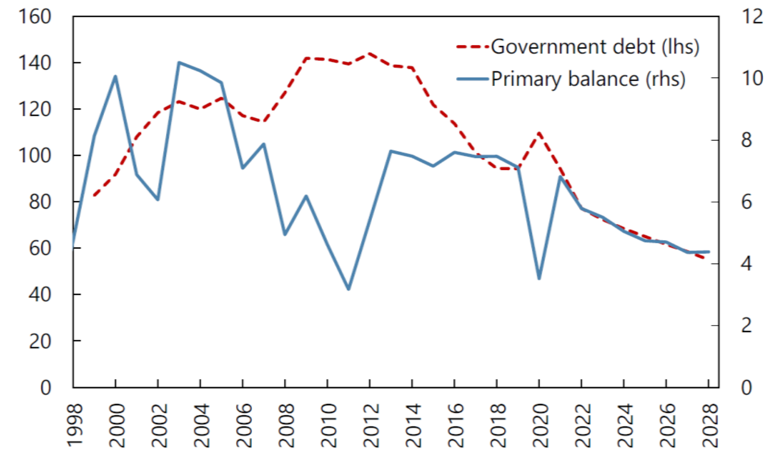
Both economic and political factors underlie this inability to reduce debt ratios

- Slowing GDP growth and rising real interest rates (r-g > 0) make for adverse debt dynamics.
- Ideological polarization and frequent government turnover make it hard to stay the course.
  - Turnover creates an opportunity for a new administration to repudiate the policies of its predecessor, disrupting efforts to sustain substantial primary budget surpluses.
  - Polarization makes it hard to agree on how to share the burden of fiscal adjustment, fraying the coalition favoring debt reduction and causing policies to be reversed.
- These economics and politics leave one pessimistic about the prospects for sustained debt reduction.

Jamaica is an exception

- You can here see what it has done.
    - Since roughly 2013.
- And you can see how it has done it.
    - By running large primary surpluses.

Figure 1. Jamaica: Government Debt and Fiscal Balance, 1998-2028
(Percent of GDP)



Sources: IMF, World Economic Outlook (October 2023).
Note: In fiscal years. Fiscal years run from April 1 to March 31. Figures for 2023-28 are projections.

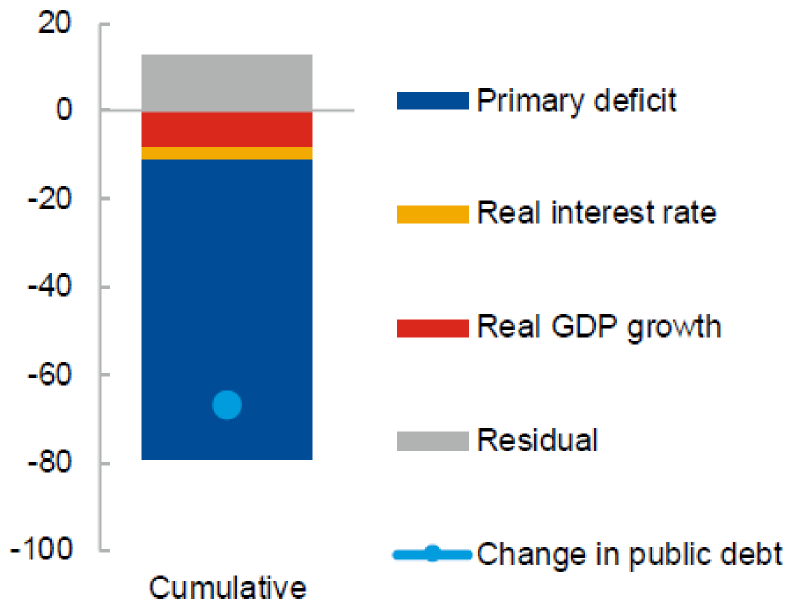
This primary surplus record is exceptional

- At right is the list of all EMDCs that have reduced their debt by 40% of GDP or more over five years (2000-22 inclusive).
- Along with the contribution of the primary surplus in parentheses.
  - Sample excludes advanced countries and major defaults/debt restructurings.

40% of GDP or more	
BUL 2000-05	42.5 (12.2)
GEO 2002-07	42.6 (14.9)
JAM 2013-18	**44.4 (37.2)**
IDN 2000-05	44.8 (13.7)
LBN 2006-11	48.9 (12.2)
	44.6 (18.0)
	5

Drivers of Debt-GDP Dynamics, 2013-22

- Using the standard debt decomposition;
- $\Delta b = d + \frac{(r-g)}{1+g} b_{t-1} + sfa$
- One again sees that it's all about the primary surplus.
  - Growth helped a little but was relatively anemic.
  - Negligible contribution of negative real interest rate is a reminder that debt wasn't inflated away.
  - Not restructuring (in this period *sfa* goes in the wrong direction).



So how did Jamaica do it? Our answer comes in two parts

- First, Jamaica adopted fiscal rules that increased fiscal transparency, encouraged formulation of a medium-term plan, and limited fiscal slippage.
- Second, elected officials leveraged Jamaica's hard-won tradition of consensus building – of constructing over the course of 30 years social partnerships aimed at facilitating dialogue, limiting political instability, and reducing political polarization and violence – which fostered *ownership* of the resulting policies.

Fiscal Rules

- Introduced in 2010, the Fiscal Responsibility Framework required the Finance Minister to take measures to reduce, by the end of fiscal year 2016, the fiscal balance to nil, the debt/GDP ratio to 100 percent, and public-sector wages as a share of GDP to 9 percent.
- The framework was strengthened in 2014 to require the minister, by the end of fiscal year 2018, to specify a multi-year fiscal trajectory to bring the debt/GDP ratio down to 60 percent by 2026.
- The FRF included an escape clause to be invoked in the event of large shocks. This prevented the rule from being so rigid, in a volatile macroeconomic environment, as to lack credibility.
- But it included clear criteria and independent oversight to prevent opportunistic use.

But fiscal rules don’t always work (can you say “Europe”?)

- In addition, “democratic corporatism” fostered ownership.
  - Starting in 2013, ongoing discussions within the National Partnership Council, a social dialogue collaboration involving the government, parliamentary opposition, and social partners, culminated in the Partnership for Jamaica Agreement on consensus policies in four areas, first of which was fiscal reform and consolidation.
  - The Partnership for Jamaica Agreement fostered a common belief that the burden of fiscal adjustment would be widely and fairly shared.

EPOC and Polarization

- In addition, the Partnership Agreement…
  - …supported the creation and ensured broad national acceptance of the Economic Programme Oversight Committee (EPOC) to monitor and report on fiscal policies and outcomes, and to provide independent verification that all parties kept to the terms of their agreement.
  - Consensus and less polarization made for policy continuity and continued debt reduction when a different political party took power in 2016. The new government did not reverse the policies of its predecessor.
  - By creating a sense of fair burden sharing, Jamaica’s organized process of consultation thus sustained public support for the operation of the country’s fiscal rules, culminating in March 2023 with the establishment of a permanent, independent Fiscal Commission.

Why did Jamaica follow this distinctive path: Earlier history

- EPOC and the Partnership for Jamaica Agreement that launched and kept Jamaica on the path of debt reduction were products of a distinctive national learning process.
- This began a third of a century earlier with the Electoral Advisory Commission.
- This approach of inclusive consultations, once they proved their efficacy, was transferred to other domains, including the economic, and eventually, the financial and budgetary.
- The decision to start down this road reflected the country's history of race and class division and political violence.
- It was a function as well of leadership: of the conviction of leaders and society, at the end of the 1970s, when the country reached the economic and political brink, that they needed to build inclusive institutions.

Caveat: As always, the full story is more complex

- Debt reduction was facilitated by sound management of the financial system.
- The Jamaican authorities managed the term structure of the debt well.
- They engaged in some clever financial management, notably the Petrocaribe buyback.
- But these two elements – a well-designed fiscal rule, and a partnership agreement creating confidence that the burden of adjustment would be widely and fairly shared – were key.
- Neither element would have worked to achieve sustained debt reduction in the absence of the other. Both were needed in conjunction.

An important question is whether the lessons from Jamaica generalize

- That Jamaica is such an outlier gives reason for doubt. (The list is short.)
- That Jamaica's experience flows from its earlier history (which is not exactly replicable elsewhere) gives further reason for caution.

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An important question is whether the lessons from Jamaica generalize

- At the same time, we can point to other small, open economies (Ireland, Barbados) that applied the same recipe (fiscal rules and "democratic corporatism") and achieved similar results.
  - Albeit in an earlier period, so they are not on this list.
- And Jamaica's own experience suggests that societal divisions are endogenous. They can evolve and be modified over time, not least through the creation and operation of encompassing institutional partnerships.

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