



# WHAT NEXT?

## Implications of a Government of Ghana Sovereign Debt Restructuring

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# INTRODUCTION



1

Hints of the Government of Ghana's consideration of restructuring its sovereign debt in the wake of negotiations with the IMF regarding the sustainability of the country's debts has made rounds.

2

There is likelihood of restructuring local debt compared to external debt which is in line with the expectations of market watchers.

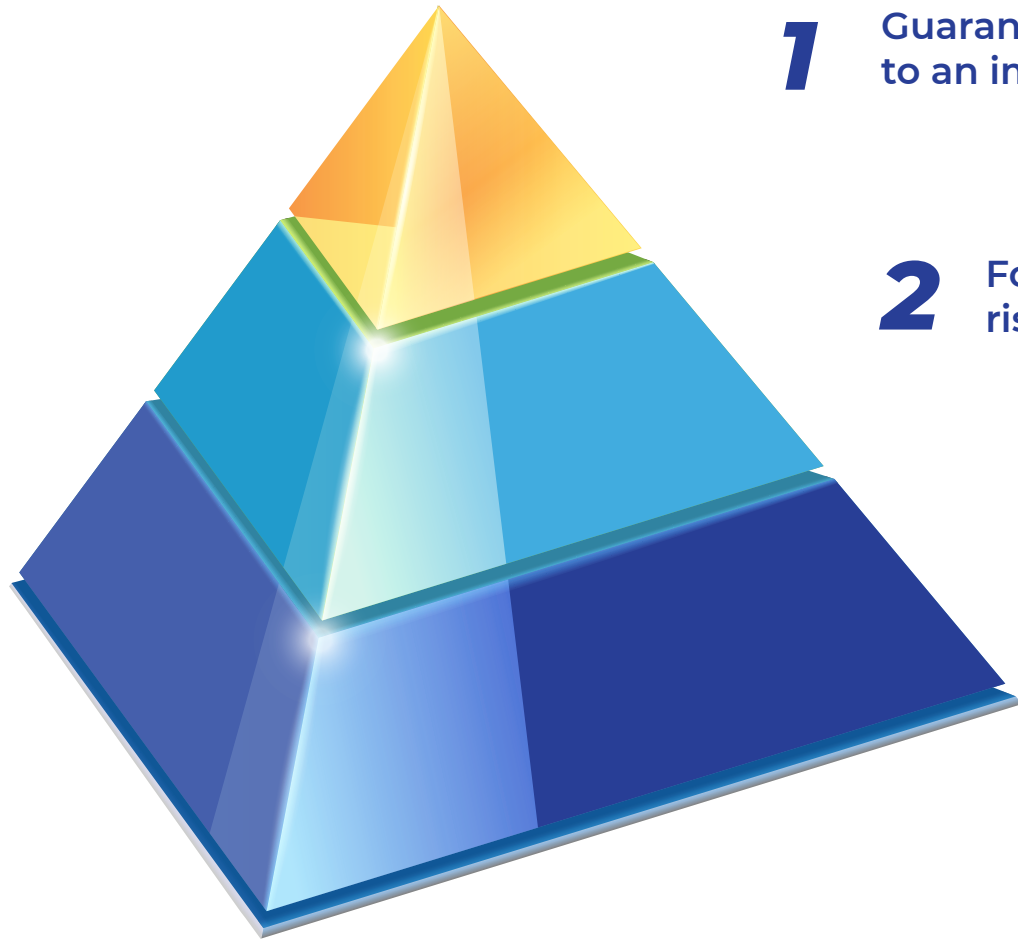
3

In the ranking of debts, external debts have a higher seniority compared to local currency debts. This consideration is due to the dire consequences of defaulting on external debt, the length of time for its restructuring and the involvement of different creditors with different aims.

4

Defaulting external debt may lead to pitching the sovereign against very powerful investors and being drawn into long legal tussles.

# DEBT SENIORITY



- 1** Guarantees to *“Too Big to Fail”* entities which is analogous to an implicit put option
- 2** Foreign currency debt which is conceptually analogous to risk-free debt minus an implicit put option
- 3** Base currency money and local currency debt which are conceptually analogous to ‘equity’ and can consequently be valued as a ‘call’ option.

*Too Big to Fail Entities are financial institutions whose collapse can lead to the collapse of the financial system because of their size and connections with other institutions*

Source: Gray and Malone, 2008

# BALANCE SHEETS OF ECONOMIC AGENTS

## Assets

## Liabilities + Equities

### 1 Government Sector Balance

Foreign currency reserves	Guarantees to <i>"Too Big to Fail"</i> entities
Net fiscal assets	Base currency money and domestic currency debt (call option on public sector assets).
	Foreign currency debt (Risk-free debt less a put option)

### 2 Household Sector Balance Sheet

Present value of Household Income	Loans to Financial Institutions
Treasury Securities	Other Debt
Mutual Funds	Household equity
Real Estate	

# BALANCE SHEETS OF ECONOMIC AGENTS

## Assets

## Liabilities + Equities

### 3 Financial Sector Balance Sheet

Securities including Treasury Securities	Deposits and other debt (risk-free debt minus an implicit put option)
Loans	Equity (implicit call option on the assets of the financial sector)
Government financial guarantee (analogous to a put option)	

### 4 Corporate Sector Balance Sheet

Corporate Assets	Loans to Financial Institutions
	Other Debt
	Equity (implicit call option on the assets of the corporate sector)

# COSTS AND BENEFITS OF RESTRUCTURING TO GOVERNMENT

## Costs

Dented credit and default risk free status of government

Payment of higher risk premiums after gaining access to the international markets

Limited investment options for individuals and institutions

Threat to current and future pensions



## Benefits

Reduction in the country's debt levels

Increase in sovereign debt sustainability



# OUR EXPECTATIONS



## OUR RECOMMENDATIONS *(in order of preference)*

01

Extend maturities of debt holdings

02

Reduce interest rates on debt holdings

03

Haircut on principal values



# CONCLUSION

1

In pursuing a debt restructuring agenda it is important for government to indicate the various restructuring scenarios to allow for a better understanding by market participants

2

Stress testing on the proposed debt restructuring and its impact on the financial sector and economy for clarity

3

Clearly defined mitigating factors on any negative outturn and remedial actions such as regulatory measures, recapitalisation plans, liquidity support and setting a financial sector stability fund

4

A well executed debt sustainability plan must be properly designed for economic stability. This is to ensure its future sustenance.

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