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STAFF REPORT FOR 2014 ARTICLE IV CONSULTATION—DEBT SUSTAINABILITY ANALYSIS

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South Sudan is at moderate risk of external debt distress.[1] Based on available data, the external debt stock at present is modest, and the baseline suggests a sustainable debt profile over the next 20 years. The evolution of public debt mirrors that of the public external debt as only a small amount of domestic borrowing is projected. At the same time, the high share of short term debt heightens rollover risks. Alternative scenarios also point to serious vulnerabilities linked to the risk of political and regional instability, protracted governance problems, lack of economic and other critical reforms, and shocks to oil production. If unresolved, these issues could result in rapid debt accumulation and a downgrade of the risk rating. These risks highlight the importance of peace, prudent policies, and a reform program focused on a clean and accountable government.

[1] The risk rating is assessed using Debt Sustainability Framework for Low-Income Countries (LIC DSF). The DSA presented in this document is based on a unified 5 percent discount rate. South Sudan has a "weak" policy performance based on the 2013 CPIA rating (the CPIA score is 2.10). The thresholds, which apply to external public and publicly-guaranteed debt, are: 30 percent for the present value (PV) of external debt-to-GDP ratio, 100 percent for the PV of external debt-to-exports ratio, 200 percent for the PV of external debt-to-revenue ratio, 15 percent for the PV of external debt service-to-exports ratio, and 18 percent for the debt service-to-revenue ratio.

See "Staff Guidance Note on the Application of the Joint Bank-Fund Debt Sustainability Framework for Low-Income Countries"

BACKGROUND

1. **While South Sudan accumulated some debt since 2011, public debt ratios are still at very low levels.** When it emerged as an independent state in July 2011, the Republic of South Sudan had no domestic or foreign debt or arrears. However, a 15-month oil production shutdown between January 2012 and April 2013 and the civil conflict that erupted in December 2013 reduced fiscal revenues and depleted previously accumulated foreign exchange reserves, forcing the authorities to control spending and incur domestic and foreign debt. As a result, by June 2014, the authorities reported that the stock of public debt[2] amounted to about US$953 million or 6.4 percent of GDP; this amount includes short-term domestic debt equivalent to US$407 million (measured at the official exchange rate).[3,4]

2. **Most of the public external debt is of short-term nature and nonconcessional.** In 2012-13, the authorities indicated that they arranged for a US$1 billion short-term oil-guaranteed borrowing facility through the oil companies operating in South Sudan. As of June 2014, the outstanding amount of debt from this facility stood at US$328 million.[5] In addition, a small amount of short-term debt was contracted for purchases of arms (US$59 million in the first half of 2014). Of the remaining external debt, US$158 million was a long-term nonconcessional loan for the construction of the Juba airport.[6]

ASSUMPTIONS

3. **The baseline scenario assumes that the security situation improves gradually over the coming years and that oil production and the economy begin to recover.[7]** Over the medium term, it is assumed that fiscal and monetary policies will be prudent, that the exchange rate is unified at a sustainable level, and that inflation remains at single-digits. At the same time, the government is expected to embark on a well-prioritized reform program, focused on shifting the composition of spending towards social and infrastructure spending, implementing a disarmament, demobilization, and reintegration program, and fostering transparency and accountability in the management of public resources.[8] Public investment is

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[2] Public debt refers to debt of the central government.

[3] In 2012, the authorities sold SSP1 billion of short-term securities to domestic banks and borrowed SSP0.1 billion from another commercial bank. As this debt has been rolled over, the stock as of mid-2014 amounted to SSP1.2 billion.

[4] As a result of the oil shutdown and subsequent fiscal stress, cumulative borrowing from the central bank amounted to SSP4 billion (8.8 percent of GDP). Such borrowing was undertaken on an exceptional basis as it is not permitted under the central bank law. In addition, as the central bank was not adequately capitalized following independence, the government issued bonds to the central bank of which the outstanding amount as of June 30 was SSP2 billion. This debt is not counted as part of the public debt because it consists of intra-public sector obligations.

[5] The authorities plan for additional borrowing of up to US$1 billion in the fiscal year that began in July 2014.

[6] The long-term loan carries an interest rate of 2 percent, has a maturity of 20 years, and a grace period of 5 years.

[7] Estimates and projections for the DSA are based on calendar year calculations. The figures are compatible with the fiscal-year data presented in the staff report on the 2014 Article IV consultation.

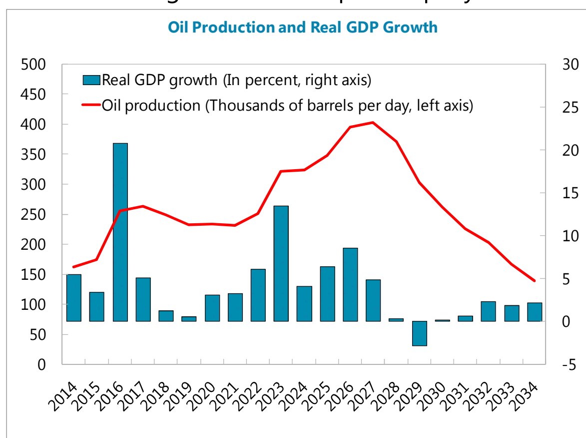
[8] Under the baseline, the authorities are expected to proceed with plans to strengthen public financial management (including oil revenue management), primarily through improving budget execution and preventing domestic arrears,

(continued)

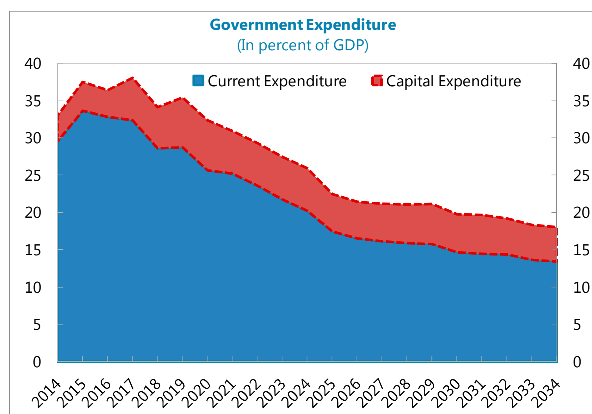
assumed to be moderately scaled up over time, with initial focus on transport and energy infrastructure and the infrastructure damaged by the conflict.[9] This, together with the projected resumption of trade with Sudan and, over time, the expansion of agriculture and mining activities, is expected to support average real GDP growth of about 7 percent per year during the next 10 years (Box 1). The projections of public and publicly guaranteed debt (PPG) are derived from these assumptions.

Box 1. Macroeconomic Assumptions: 2014-2034

Real sector: During the next 10 years, annual average real GDP growth is projected to be about 7 percent based on the expected recovery of oil production and non-oil real GDP is assumed to grow at about 5 percent per year. Oil output is projected to increase gradually to about 260 thousand barrels per day by 2017, but decline for 3-5 years after that as production rates fall in aging oil fields. It is also assumed that investment in enhanced oil recovery and new fields after 2020 pushes up production to nearly 400 thousand barrels per day by 2026. Thereafter, oil output is projected to fall to 140 thousand barrels per day by 2034. Real non-oil GDP growth is assumed to recover slowly from its current low base and reach an average of about 7 percent in the 2020s, primarily as a the result of increased activity in agriculture, other mining, and services. Average inflation is projected at about 5 percent during the forecast period, and a gradual real appreciation of the South Sudanese pound is envisaged based on gradual productivity increases and the expansion of the non-oil economy.



Fiscal sector: Driven by the projected path for oil production, total revenue including grants is projected to first rise from 25 percent of GDP to 40 percent of GDP by 2016, then fall between then and 2023, then increase again as oil production picks up, and ultimately converge downwards towards 21 percent of GDP by the 2030s. Non-oil revenues are expected to increase gradually from their current low base of 2 percent of GDP to about 10 percent of GDP by the 2020s and then towards 16.



establishing a single treasury account, reorienting public spending towards development, and implementing the forthcoming Public Procurement Act and the Petroleum Revenue Management Act.

[9] If properly managed, a scaling up of public investment could lead to a meaningful improvement in real incomes in the next two decades. The impact of the scaling up will depend on key structural conditions, such as absorptive capacity, the prudent management of mineral revenue, and the extent of improvements in the business environment. In any case, the process should be timed appropriately and the projects chosen according to their viability and expected return. This, in turn, will require the use of cost-benefit analysis techniques and a well implemented public investment program.

Box 1. Macroeconomic Assumptions: 2014-2034 (concluded)

percent of GPD in the 2030s. About one quarter of oil revenue is expected to be saved for oil stabilization and for future investments, primarily in years in which oil revenues outpace projected spending. Expenditure as a share of GDP is projected to rise somewhat in the medium term and later decline towards 20 percent of GDP in the long run. The profile for expenditure in the next decade mimics a scaling up of public investment that raises the share of public spending to GDP, together with a demobilization and civil service reform program that begins to push the share down by the early 2020s. Capital expenditures are projected to increase from 3 percent of GDP at present to about 7 percent of GDP by 2020 before declining toward 5 percent of GDP in the outer years of the projection period. Based on these trends, the overall fiscal balance (including grants) records a small deficit over the medium term (except in a few years when there is a surplus), before converging to a small surplus by the late 2020s.

External sector: Exports of goods and services as a share of GDP are projected to increase in the medium term, supported by growth in both the oil and the non-oil sectors, and later decline as oil production begins to fade in the late 2020s. The share of imports of goods and services to GDP follows an inverted U-shape profile. It is expected to increase in the medium term because of the scaling up of public (and later private) investment but decrease after the mid-2020s as the non-oil economy develops and import substitution begins to take hold. Grants are projected to remain at around 6 percent of GDP in the next few years and decline towards 3 percent by the end of the forecast period.

4. **Medium to long-term external borrowing assumptions include a mix of concessional and nonconcessional loans.** Given the projected fiscal situation and large infrastructure needs, the authorities are likely to contract some external debt in the medium-term.[10] A large part of this debt will likely be nonconcessional (especially in the next 3 years), although the authorities would like to approach multilateral and bilateral partners for concessional resources at some point. These and the above macroeconomic assumptions are modeled in the baseline, yielding external public sector borrowing requirements of about US$5 billion in the next 10 years. In the long term, higher oil and non-oil revenues are expected to bring external borrowing down to near zero.[11, 12]

[10] The authorities are discussing with China loans for infrastructure projects to be implemented during the next 10 years. An initial framework agreement comprising oil-guaranteed loans of US$1 billion is being finalized; the bulk of this funding will be for a road project. In addition, the authorities, together with the Kenyan authorities, plan to embark on a US$1.3 billion project for a highway between Juba and Eldoret in Kenya, an extension of fiber optics connection to Juba, and trade facilitation. The highway will allow speedier connection between South Sudan and the Mombasa port in Kenya. Of the US$1.3 billion, about US$530 million is estimated to correspond to the portion of the highway that will go through Kenya. The project is expected to be financed by the World Bank, China's EXIM bank, the African Development Bank, and, possibly, other lenders and is expected to extend until 2025. The projected amounts of borrowing for these projects are implicitly embedded within the baseline assumptions of the DSA.

[11] Similar to recent borrowing for infrastructure, we assume that the bulk of the borrowing for building the basic infrastructure between 2015 and 2022 would be at a 4.5 percent interest rate, 15 year maturity, and 5 year grace period, implying that the grant element could fall substantially in the medium term (Figure 1). As oil production increases over time and the fiscal position improves, borrowing requirements, especially at nonconcessional rates is

(continued)

5. While the baseline scenario is plausible, recent instability and the risks ahead could lead to worse outcomes. These risks involve lack of political inclusiveness, failure to embark on economic reforms, unresolved territorial issues with Sudan and the expiration of the oil sharing agreement in 2016, and protracted rent seeking behavior and corruption (see alternative scenarios below for a simulation of some extreme risks). These risks, which would prolong fragility, underscore the importance of a commitment to internal peace, economic reforms, good relations with Sudan, and close cooperation with the international community.[13]

EXTERNAL DEBT SUSTAINABILITY ANALYSIS

6. Under the baseline, external debt dynamics appear to be favorable given the country's abundant oil and mining resources. All baseline debt indicators are below their threshold values. Debt ratios change only slightly over the medium term reflecting the repayment of short term loans and some borrowing projected for infrastructure projects. The debt-to-GDP ratio is projected to peak at around 20 percent in 2021 and decline thereafter. The present value (PV) of external debt-to-exports is projected to reach about 50 percent by 2022 and then decline to about 7 percent. Lastly, the PV of the debt-to-revenue ratio is also manageable and expected to fall below 4 percent by 2034.[14]

7. However, a disruption to oil production and/or severe political instability, insecurity, and insufficient reforms, could quickly destabilize debt ratios. The DSA simulates two alternative customized scenarios to illustrate these risks. The scenarios are extreme in that their likelihood is rather lower than other, more moderate scenarios of recurrent political turmoil and mild reforms or a short interruption of oil production; thus the simulations are intended to just illustrate some extreme, yet still possible risks. They also highlight the need to prevent conflict and foster political inclusion and equitable development.

8. The first scenario illustrates the effects of a shock to oil production similar to the shutdown experienced in 2012. The simulation shows that, under this scenario, the PV of debt-to-GDP ratio would exceed the 30 percent threshold for a few years (see Figure 1) before returning to normal later in the decade, while other debt ratios will also breach their respective thresholds.[15]

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assumed to fall to negligible levels from 2023 (to about US$30 million a year). The lower nonconcessional borrowing needs raises the average grant element for new borrowing in the long run.

[12] This DSA excludes remittances given their insignificance in the country's economy (net remittances were 1 percent of GDP in 2011).

[13] See "Republic of South Sudan: Staff Report for 2014 Article IV Consultations".

[14] The path of external debt residuals follows that of the non-interest current account balance and net FDI inflows which in turn are driven mostly by oil projections. Because oil exports and FDI flows in the DSA template do not reflect net debt creating flows in the BOP, the external debt residuals are higher than normal in the medium to long-term.

[15] Both scenarios assume that the authorities are able to borrow to cover their fiscal and balance of payments gaps. We assume that the additional borrowing under the alternative scenarios is at 4.5 percent interest, 15 years maturity with grace period of 5 years. However, it must be noted that heightened levels of country risk may lead to a situation whereby most sources of financing may become unavailable. Such an extreme scenario would lead to much more severe economic disruptions.

9. **Another extreme scenario in which political instability and insecurity continues unabated for several years combined with sluggish reforms could lead to a progressive decline in real GDP per capita and destabilize debt ratios.** Under such scenario, the investments needed to prevent a decline in oil production (and to start production in new fields) are assumed to be postponed until the late 2020s.[16] The results are summarized in Figure 1, which shows that all the debt ratios (PV of debt-to-GDP, PV debt-to-exports, PV debt-to-revenue, debt service-to-exports and debt service-to-revenue) breach their respective thresholds within a few years. Even as the situation is assumed to improve gradually by the early 2020s, debt ratios remain elevated through the end of the projection period because of pressing fiscal and infrastructure needs.

10. **Lack of resolution in Sudan's debt could potentially lead to discussions with Sudan on the allocation of its foreign debt.** Under a cooperation agreement signed with Sudan in September 2012, Sudan committed to assume all external debt of former Sudan subject to securing a "firm commitment" of international creditors for debt relief (i.e. Sudan's reaching the HIPC decision point) no later than two years from the date of agreement (this was termed the "zero option"). Absent such commitment, the agreement states that the two countries may discuss how to apportion the debt. Upon expiration of the two-year window, the two countries agreed in November 2014 to interpret the zero option in a "flexible" manner and extended the timing for debt relief until October 2016. In the meantime, the authorities indicated that South Sudan remains committed to support Sudan's efforts to obtain debt relief. Even if discussions were to be held in the future on how to apportion Sudan's debt, it is not possible to speculate at this point on what the allocation could be. Given the above, this risk has not been quantified in the DSA.

PUBLIC SECTOR DEBT SUSTAINABILITY ANALYSIS

The evolution of public debt indicators mirrors that of the external debt. The DSA assumes that a small portion of domestic public debt is generated in the long run as the result of the development of a domestic treasury bill market, leading to a stock of public debt that is marginally larger than that of external debt. In the medium-term, the increase in debt ratios in the DSA reflects the projected amount of borrowing that will be needed to gradually scale up public investment and the asymmetry between such profile and that of oil receipts which in turn leads to a moderate amount of external borrowing in the baseline (Table 3 and Figure 2). As a result, under the baseline, the PV of public debt remains below the 30 percent benchmark implying that the public sector debt would also be sustainable.

CONCLUSION

11. **While the baseline scenario points to a sustainable path for South Sudan's debt, uncertainties about the path of oil revenue and the country's fragility put the country at a moderate risk of debt distress.** Under the baseline scenario, debt trajectories are below their respective thresholds, as

[16] The projection implies that oil production could fall from the current level of 160 thousand barrels per day to about 100 thousand barrels per day by the mid-2020s. In this situation, public debt rises to about US$6.3 billion by 2018 (all debt thresholds are breached) and climbs further to US$14.6 billion by end-2024.

prudent policies and the implementation of key economic reforms would support a moderate amount of external borrowing to fund investment projects. However, risks abound, and alternative scenarios with protracted instability and/or disruptions in oil production can significantly increase the risk of debt distress. Other dimensions of the country's fragility include weak governance and institutions, which also elevate risks to debt sustainability.

12. The analysis highlights the preconditions for stability and debt sustainability in South Sudan. These are political inclusion and peace, good relations with Sudan, prudent economic policies, fiscal reforms, and a transparent and efficient management of public resources (especially oil and mining).

Table 1. Republic of South Sudan: External Debt Sustainability Framework, Baseline Scenario, 2011-2034 1/

(In percent of GDP, unless otherwise indicated)

	Actual			Historical 6/ Average	Standard 6/ Deviation	Projections									
	2011	2012	2013			2014	2015	2016	2017	2018	2019	2014-2019 Average	2024	2034	2020-2034 Average
External debt (nominal) 1/	**...**	**1.4**	**4.8**			**5.6**	**12.4**	**11.6**	**14.1**	**16.9**	**18.8**		**12.9**	**1.2**	
of which: public and publicly guaranteed (PPG)	...	1.4	4.8			5.6	12.4	11.6	14.1	16.9	18.8		12.9	1.2	
Change in external debt	...	...	3.4			0.7	6.9	-0.8	2.5	2.7	1.9		-2.9	-0.4	
Identified net debt-creating flows	...	...	5.3			1.8	7.7	-3.8	-2.1	-5.5	-3.3		-2.1	-0.3	
Non-interest current account deficit	**-17.8**	**26.4**	**0.6**	**-0.4**	**16.5**	**-0.4**	**4.9**	**-2.9**	**-0.7**	**-3.7**	**0.0**		**-1.4**	**0.5**	0.1
Deficit in balance of goods and services	-40.8	31.9	-3.4			-6.8	-1.6	-13.3	-10.0	-5.6	-1.3		-5.6	-0.5	
Exports	70.2	9.9	35.5			42.1	35.0	52.0	47.8	42.8	39.0		31.5	10.3	
Imports	29.4	41.8	32.1			35.4	33.4	38.7	37.7	37.2	37.8		26.0	9.8	
Net current transfers (negative = inflow)	-4.4	-9.5	-7.0	-7.6	2.0	-4.1	-2.5	-1.2	2.2	-5.5	-5.5		-2.3	-0.6	-1.9
of which: official	-2.5	-2.7	-4.6			-4.0	-3.9	-3.8	-3.3	-2.9	-3.0		-1.2	-0.3	
Other current account flows (negative = net inflow)	27.4	3.9	11.0			10.4	8.9	11.6	7.2	7.4	6.8		6.5	1.6	
Net FDI (negative = inflow)	**0.3**	**0.5**	**4.9**	**0.8**	**2.4**	**2.0**	**2.5**	**1.3**	**-1.3**	**-2.2**	**-3.8**		**-0.4**	**-0.9**	-1.2
Endogenous debt dynamics 2/	**...**	**...**	**-0.1**			**0.2**	**0.3**	**-2.2**	**-0.1**	**0.4**	**0.5**		**-0.3**	**0.0**	
Contribution from nominal interest rate	...	...	0.0			0.4	0.5	0.4	0.4	0.5	0.6		0.5	0.0	
Contribution from real GDP growth	0.0	...	-0.3			-0.2	-0.2	-2.5	-0.5	-0.2	-0.1		-0.8	0.0	
Contribution from price and exchange rate changes	0.0	...	0.2			...	...	...	...	...	...		...	...	
Residual (3-4) 3/	**...**	**...**	**-1.9**			**-1.1**	**-0.8**	**3.0**	**4.6**	**8.3**	**5.2**		**-0.8**	**-0.1**	
of which: exceptional financing	...	...	-0.2			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
PV of external debt 4/	...	...	2.2			5.2	11.0	9.6	11.7	14.1	16.0		11.4	0.7	
In percent of exports	...	...	6.3			12.3	31.3	18.5	24.6	33.0	40.9		36.0	6.7	
PV of PPG external debt	**...**	**...**	**2.2**			**5.2**	**11.0**	**9.6**	**11.7**	**14.1**	**16.0**		**11.4**	**0.7**	
In percent of exports	**...**	**...**	**6.3**			**12.3**	**31.3**	**18.5**	**24.6**	**33.0**	**40.9**		**36.0**	**6.7**	
In percent of government revenues	**...**	**...**	**12.4**			**20.8**	**39.2**	**27.4**	**35.1**	**46.7**	**59.6**		**42.3**	**3.4**	
Debt service-to-exports ratio (in percent)	**0.0**	**0.0**	**0.0**			**3.8**	**12.6**	**8.5**	**0.9**	**1.2**	**1.7**		**3.7**	**3.5**	
PPG debt service-to-exports ratio (in percent)	**0.0**	**0.0**	**0.0**			**3.8**	**12.6**	**8.5**	**0.9**	**1.2**	**1.7**		**3.7**	**3.5**	
PPG debt service-to-revenue ratio (in percent)	**0.0**	**0.0**	**0.0**			**6.4**	**15.8**	**12.6**	**1.2**	**1.7**	**2.5**		**4.4**	**1.8**	
Total gross financing need (Billions of U.S. dollars)	-3.1	2.9	0.6			0.6	2.2	1.0	-0.3	-0.9	-0.6		-0.2	0.0	
Non-interest current account deficit that stabilizes debt ratio	...	...	-2.8			-1.2	-2.0	-2.1	-3.2	-6.5	-1.9		1.5	0.9	
Key macroeconomic assumptions															
Real GDP growth (in percent)	-8.9	-46.8	24.2	-4.9	31.1	5.5	3.4	20.7	5.1	1.3	0.6	6.1	5.9	2.2	3.6
GDP deflator in US dollar terms (change in percent)	20.7	12.6	-10.5	9.6	13.8	5.0	5.6	-16.1	8.3	5.3	5.1	2.2	10.8	5.7	7.3
Effective interest rate (percent) 5/	...	...	0.0	0.0	...	10.3	10.2	2.9	4.1	3.9	3.8	5.9	3.7	2.6	3.5
Growth of exports of G&S (US dollar terms, in percent)	29.0	-91.6	299.3	67.0	165.2	31.4	-9.2	50.5	4.5	-4.4	-3.7	11.5	3.3	0.4	2.1
Growth of imports of G&S (US dollar terms, in percent)	23.5	-14.9	-14.7	0.2	18.6	21.9	3.3	17.2	11.1	5.1	7.4	11.0	0.1	0.0	1.6
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	52.9	17.0	13.1	16.7	15.7	8.0	20.6	29.6	29.6	25.2
Government revenues (excluding grants, in percent of GDP)	22.0	11.4	18.0			25.0	27.9	35.1	33.5	30.2	26.8		26.8	20.0	24.2
Aid flows (in Billions of US dollars) 7/	0.5	0.7	0.7			0.3	0.7	0.8	0.9	0.8	0.9		0.7	0.5	
of which: Grants	0.5	0.7	0.7			0.3	0.7	0.7	0.8	0.8	0.9		0.7	0.5	
of which: Concessional loans	0.0	0.0	0.0			0.0	0.0	0.1	0.1	0.1	0.0		0.0	0.0	
Grant-equivalent financing (in percent of GDP) 8/	...	...	...			2.2	5.6	5.9	5.5	4.9	4.9		2.0	0.6	1.7
Grant-equivalent financing (in percent of external financing) 8/	...	...	...			98.0	60.0	52.9	62.6	61.8	65.0		97.1	96.0	90.0
Memorandum items:															
Nominal GDP (Billions of US dollars)	17.7	10.6	11.8			13.1	14.3	14.5	16.5	17.6	18.5		35.0	89.2	
Nominal dollar GDP growth	9.9	-40.1	11.1			10.7	9.2	1.3	13.8	6.6	5.6	7.9	17.3	8.0	11.2
PV of PPG external debt (in Billions of US dollars)			0.3			0.7	1.2	1.4	1.9	2.5	3.0		4.0	0.6	
(PVt-PVt-1)/GDPt-1 (in percent)						3.5	4.3	1.0	3.8	3.3	2.8	3.1	-0.6	-0.3	0.0
Gross workers' remittances (Billions of US dollars)	0.4	0.4	0.3			0.3	0.3	0.3	0.3	0.3	0.3		0.3	0.2	
PV of PPG external debt (in percent of GDP + remittances)	...	...	2.2			5.1	10.7	9.4	11.5	13.9	15.7		11.3	0.7	
PV of PPG external debt (in percent of exports + remittances)	...	...	5.8			11.6	29.4	17.7	23.6	31.6	39.2		35.1	6.5	
Debt service of PPG external debt (in percent of exports + remittanc	...	...	0.0			3.6	11.8	8.2	0.8	1.2	1.6		3.6	3.4	

Sources: South Sudanese authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.

2/ Derived as [r - g - ρ(1+g)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

4/ Assumes that PV of private sector debt is equivalent to its face value.

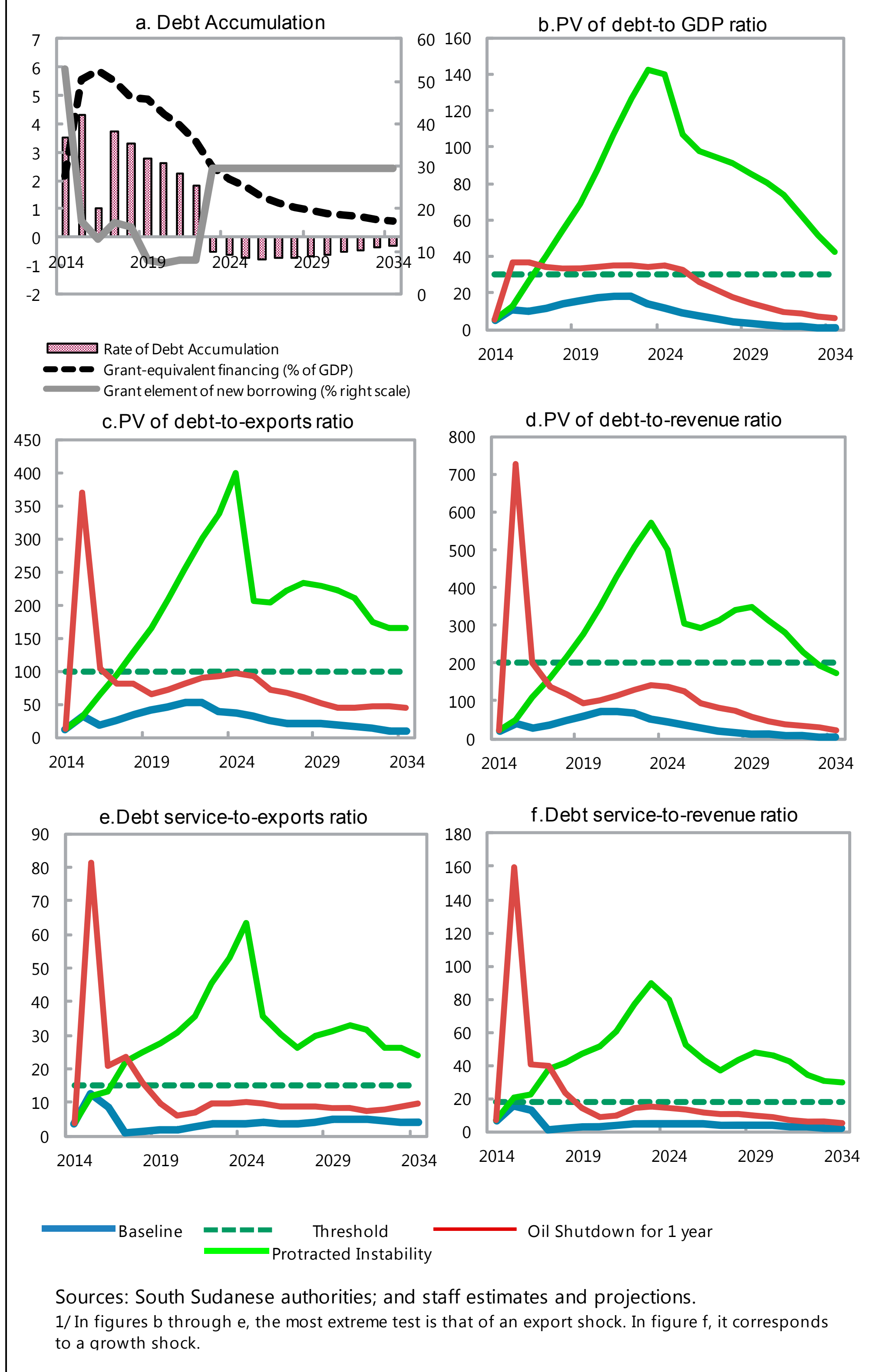
5/ Current-year interest payments divided by previous period debt stock.

6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

7/ Defined as grants, concessional loans, and debt relief.

8/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

Figure 1. Republic of South Sudan: Indicators of Public and Publicly Guaranteed External Debt under Alternatives Scenarios, 2014-2034 1/



Sources: South Sudanese authorities; and staff estimates and projections.
1/ In figures b through e, the most extreme test is that of an export shock. In figure f, it corresponds to a growth shock.

Table 2. Republic of South Sudan: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2014-2034

(In percent)

								Projections									
	2014	2015	2016	2017	2018	2019	**2024**	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034
PV of debt-to GDP ratio																	
Baseline	5	11	10	12	14	16	**11**	9	7	6	4	3	3	2	2	1	1
A1. Alternative Scenario: Protracted Instability	5	13	27	40	54	69	**139**	106	98	94	91	85	80	74	62	52	42
A2. Alternate Scenario: 1 Year Oil Shutdown	5	37	36	34	33	33	**35**	33	26	21	18	14	12	10	8	7	6
A3. New Public Borrowing on Less Favorable Terms[1]	5	10	12	14	18	20	**15**	13	10	8	7	6	5	4	4	3	3
PV of debt-to-exports ratio																	
Baseline	12	31	18	25	33	41	**36**	31	25	21	20	20	18	15	13	9	9
A1. Alternative Scenario: Protracted Instability	12	30	64	95	128	164	**398**	205	204	221	232	228	222	211	174	164	164
A2. Alternate Scenario: 1 Year Oil Shutdown	12	370	102	82	81	64	**96**	93	72	68	60	50	44	43	47	47	45
A3. New Public Borrowing on Less Favorable Terms[1]	12	27	22	30	41	51	**48**	42	35	32	31	34	34	34	34	31	30
PV of debt-to-revenue ratio																	
Baseline	21	39	27	35	47	60	**42**	38	29	22	17	14	12	9	7	5	5
A1. Alternative Scenario: Protracted Instability	21	51	108	161	215	277	**499**	303	291	312	338	348	312	281	227	193	172
A2. Alternate Scenario: 1 Year Oil Shutdown	21	728	202	138	119	94	**135**	124	94	80	74	59	45	38	34	31	22
A3. New Public Borrowing on Less Favorable Terms[1]	21	34	33	43	58	74	**56**	51	42	32	27	24	23	21	19	17	15
Debt service-to-exports ratio																	
Baseline	4	13	9	1	1	2	**4**	4	4	4	4	5	5	5	5	4	4
A1. Alternative Scenario: Protracted Instability	4	12	13	22	25	28	**63**	35	30	26	30	31	33	32	26	26	24
A2. Alternate Scenario: 1 Year Oil Shutdown	4	81	21	23	16	9	**10**	10	9	9	9	8	8	7	8	9	10
A3. New Public Borrowing on Less Favorable Terms[1]	4	13	8	1	2	2	**5**	5	5	5	5	6	7	7	8	6	6
Debt service-to-revenue ratio																	
Baseline	6	16	13	1	2	2	**4**	5	4	4	4	3	3	3	3	2	2
A1. Alternative Scenario: Protracted Instability	6	20	22	38	42	47	**79**	53	43	37	44	48	46	42	34	31	29
A2. Alternate Scenario: 1 Year Oil Shutdown	6	160	41	40	23	14	**14**	13	11	11	11	10	8	7	6	6	5
A3. New Public Borrowing on Less Favorable Terms[1]	6	16	13	2	2	3	**6**	7	6	5	5	4	5	4	4	3	3
Memorandum item:																	
Grant element assumed on residual financing (i.e., financing required above baseline)	5	5	5	5	5	5	**5**	5	5	5	5	5	5	5	5	5	5

Sources: South Sudanese authorities; and staff estimates and projections.

1/ Assumes that the interest rate on new borrowing between 2014-2034 is 2 percentage points higher than the baseline while he grace and maturity are the same as baseline.

Figure 2. Republic of South Sudan: Indicators of Public Debt Under Alternative Scenarios, 2014-2034 1/

Sources: South Sudanese authorities; and staff estimates and projections.
1/ Revenues are defined inclusive of grants.

Table 3. Republic of South Sudan: Public Sector Debt Sustainability Framework, Baseline Scenario, 2011-2034
(In percent of GDP, unless otherwise indicated)

	Actual			Average 5/	Standard Deviation 5/	Estimate	Projections								
	2011	2012	2013			2014	2015	2016	2017	2018	2019	2014-19 Average	2024	2034	2020-34 Average
Public sector debt 1/	0.0	4.9	8.1			8.7	14.5	11.6	14.1	16.9	19.2		13.5	1.4	
of which: foreign-currency denominated	0.0	1.4	4.8			5.6	12.4	11.6	14.1	16.9	18.8		12.9	1.2	
Change in public sector debt	0.0	4.9	3.2			0.6	5.9	-2.9	2.5	2.7	2.3		-3.0	-0.4	
Identified debt-creating flows	...	...	...			5.1	4.7	-6.9	0.2	-2.1	1.2		-2.4	-5.6	
Primary deficit	-4.5	15.7	6.7	2.2	9.2	5.5	4.3	-4.0	1.1	-1.8	1.4	1.1	-0.5	-5.5	-1.8
Revenue and grants	25.0	17.8	24.4			27.1	32.7	40.2	38.3	34.6	31.5		28.8	20.6	
of which: grants	2.9	6.4	6.3			2.1	4.8	5.1	4.9	4.4	4.6		2.0	0.6	
Primary (noninterest) expenditure	20.5	33.5	31.0			32.6	37.0	36.1	39.5	32.8	32.9		28.3	15.1	
Automatic debt dynamics	...	...	...			-0.3	0.5	-2.8	-1.0	-0.4	-0.3		-1.9	-0.1	
Contribution from interest rate/growth differential	...	...	...			-0.2	-0.7	-2.5	-0.3	0.1	0.2		-0.7	0.0	
of which: contribution from average real interest rate	...	...	...			0.2	-0.5	0.0	0.2	0.2	0.3		0.2	0.0	
of which: contribution from real GDP growth	0.0	0.0	-0.9			-0.4	-0.3	-2.5	-0.6	-0.2	-0.1		-0.9	0.0	
Contribution from real exchange rate depreciation	...	...	...			-0.2	1.2	-0.4	-0.7	-0.4	-0.5		...	...	
Other identified debt-creating flows	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	...	...	...			-4.6	1.1	4.0	2.4	4.9	1.2		-0.6	5.1	
Other Sustainability Indicators															
PV of public sector debt	...	...	5.5			8.3	13.1	9.6	11.7	14.1	16.4		11.9	0.9	
of which: foreign-currency denominated	...	...	2.2			5.2	11.0	9.6	11.7	14.1	16.0		11.4	0.7	
of which: external	...	...	2.2			5.2	11.0	9.6	11.7	14.1	16.0		11.4	0.7	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 2/	-4.5	...	6.7			11.2	14.7	6.2	1.6	-1.3	2.1		0.7	-5.1	
PV of public sector debt-to-revenue and grants ratio (in percent)	...	...	22.6			30.7	39.9	24.0	30.6	40.8	52.2		41.4	4.4	
PV of public sector debt-to-revenue ratio (in percent)	...	...	30.6			33.2	46.8	27.4	35.1	46.7	61.2		44.5	4.6	
of which: external 3/	...	...	12.4			20.8	39.2	27.4	35.1	46.7	59.6		42.3	3.4	
Debt service-to-revenue and grants ratio (in percent) 4/	0.0	0.0	0.0			5.9	13.5	11.0	1.1	1.5	2.1		4.1	1.7	
Debt service-to-revenue ratio (in percent) 4/	0.0	0.0	0.0			6.4	15.8	12.6	1.2	1.7	2.5		4.4	1.8	
Primary deficit that stabilizes the debt-to-GDP ratio	-4.5	10.8	3.5			4.9	-1.6	-1.1	-1.4	-4.5	-0.9		2.5	-5.0	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	-8.9	-46.8	24.2	-4.9	31.1	5.5	3.4	20.7	5.1	1.3	0.6	6.1	5.9	2.2	3.6
Average nominal interest rate on forex debt (in percent)	...	...	...	...	...	10.3	10.2	2.9	4.1	3.9	3.8	5.9	3.7	2.6	3.5
Average real interest rate on domestic debt (in percent)	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Real exchange rate depreciation (in percent, + indicates depreciation)	-22.9	-7.9	13.4	-5.0	15.0	-3.2	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	57.3	10.5	-10.5	18.1	28.4	5.0	42.4	5.6	8.3	5.3	5.1	11.9	10.8	5.7	7.3
Growth of real primary spending (deflated by GDP deflator, in percent)	0.4	-12.9	15.0	0.7	11.4	10.6	17.4	17.9	14.8	-15.8	0.8	7.6	0.1	-19.3	-1.4
Grant element of new external borrowing (in percent)	...	...	...	...	...	52.9	17.0	13.1	16.7	15.7	8.0	20.6	29.6	29.6	...

Sources: South Sudanese authorities; and staff estimates and projections.
1/ Refers to general government gross debt
2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.
3/ Revenues excluding grants.
4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.
5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 4. Republic of South Sudan: Sensitivity Analysis for Key Indicators of Public Debt 2014-2034

		Projections						
	2014	2015	2016	2017	2018	2019	2024	2034
PV of Debt-to-GDP Ratio								
Baseline	8	13	10	12	14	16	12	1
A1. Alternative Scenario: Protracted Instability	8	16	30	44	58	73	144	43
A2. Alternate Scenario: 1 Year Oil Shutdown	8	42	41	38	35	34	35	6
PV of Debt-to-Revenue Ratio 1/								
Baseline	31	40	24	31	41	52	41	4
A1. Alternative Scenario: Protracted Instability	31	54	101	147	196	247	481	173
A2. Alternate Scenario: 1 Year Oil Shutdown	31	425	175	128	108	86	126	24
Debt Service-to-Revenue Ratio 1/								
Baseline	6	13	11	1	1	2	4	2
A1. Alternative Scenario: Protracted Instability	6	28	30	44	49	53	89	28
A2. Alternate Scenario: 1 Year Oil Shutdown	6	135	50	46	31	17	13	5

Sources: South Sudanese authorities; and staff estimates and projections.

1/ Revenues are defined inclusive of grants.

Statement by the IMF Staff Representative on the Republic of South Sudan
December 15, 2014

This statement contains information that has become available since the staff report was circulated to the Executive Board. This information does not alter the thrust of the staff appraisal.

1. **Foreign exchange reserves remain critically low and the exchange rate in the parallel market has depreciated further.** At end-November 2014, the net foreign assets of the central bank amounted to US$340 million (less than 3-weeks of imports), compared to US$379 million at end-September. Reflecting the difficult macroeconomic situation, the exchange rate in the parallel market also depreciated, from SSP 5.3 per U.S. dollar in October to SSP 5.8 per U.S. dollar at end-November.

2. **Financing the fiscal deficit remains challenging in light of the ongoing conflict and low oil prices.** While production remains subdued, staff estimates that if the most recent oil prices persist for the remainder of the fiscal year, the average price for South Sudanese oil could be about 5 U.S. dollars lower compared to the baseline in the staff report, leading to a further worsening of the fiscal balance equivalent to 1.6 percentage points of GDP (US$235 million).

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December, 17, 2014

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2014 Article IV Consultation with South Sudan

On December, 15, 2014, the Executive Board of the International Monetary Fund concluded the Article IV consultation[1] with South Sudan.

South Sudan is a fragile state with acute challenges. Since it became an independent state in 2011, institution building and development have been hindered by volatile relations with Sudan, a 15-month shutdown of oil production, and more recently, a civil conflict. Although rich in natural resources, the economy is centered on oil production and subsistence agriculture, with almost all consumer goods being imported.

Economic performance has been mixed in recent years. Real Gross Domestic Product (GDP) growth has displayed high volatility, the result of changes in oil and agricultural production. Inflation rose in an initial period of economic instability in 2011-12 but was contained in 2013-14 thanks to fiscal and monetary restraint and lower food prices. However, serious challenges remain, including distortions in the foreign exchange market and in budget execution, lower international oil prices, and subdued oil production. As a result, financing the budget for 2014/15 is challenging and will likely require policy decisions given the otherwise potentially adverse impact on economic stability and inflation.

The medium-term outlook could be promising, but there are serious risks. Assuming peace, regional cooperation, and economic reforms, oil production could increase in coming years and the potential for other mining and non-oil activities (especially agriculture and forestry) could be unlocked, leading to strong GDP growth and allowing for investments in social sectors and the public infrastructure. However, there are several risks on the horizon, including unresolved political and security issues, continued governance problems, and insufficient progress on critical economic reforms.

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

Executive Board Assessment[2]

Executive Directors agreed with the thrust of the staff appraisal. In welcoming the completion of the first Article IV consultation with South Sudan, Directors noted that the country faces formidable near-term challenges from the ongoing civil war, volatile relations with Sudan, large swings in oil production and prices, and weak institutions and governance. Against this background, Directors underscored the urgent need for measures to address fiscal imbalances, including exchange rate unification, and stressed the importance of peace and political inclusion to set the basis for growth and development.

Directors agreed that reduced oil revenues and lack of room for public expenditure cuts call for policy actions on a variety of fronts to close the financing gap in the fiscal accounts and restore macroeconomic stability. They supported the authorities' intentions to mobilize non-oil revenue, and emphasized the importance of improving expenditure management and preventing domestic arrears, primarily through the enforcement of monthly budget allocations, a strict control of extra-budgetary expenditures, and steps to set up a single treasury account. Directors cautioned against increased central-bank financing of the fiscal deficit, which would fuel inflation and further weaken the local currency.

Directors underscored the need to unify the exchange rate and adopt a market-based system for allocating foreign exchange. Exchange rate unification would significantly reduce the fiscal imbalance, remove incentives for corruption, and improve price signals to favor private investment and non-oil economic activities. An adjustment in the exchange rate peg to a realistic level would also help stem foreign reserve losses. Directors urged the authorities to remove the multiple currency practices and exchange restrictions as soon as possible.

Directors stressed the urgency of improving transparency and accountability in the management of mineral resources, government expenditures, and central bank operations. They encouraged the authorities to enact the Petroleum Revenue Management Act, and called for the implementation of recommendations from the 2012 audit of the central bank and the wide dissemination of oil, fiscal, and financial data.

Directors emphasized that strong and concerted policy efforts will be needed over the medium term to foster economic development and build institutions. Priorities include restoring depleted reserve buffers, reorienting public spending toward social sectors and infrastructure, implementing public financial management legislation, and addressing the legacy of war. These tasks will require strong leadership and cooperation from the international community, including continued technical assistance.

[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

Republic of South Sudan: Selected Economic Indicators[1]

Population (millions; 2012/13):	10.6	Per capita GDP (US$) (2012/13):	1116
IMF Quota (current; millions SDR; % total):	123; 0.05%	Literacy rate (%) (2009):	27
Main exports:	Oil	Poverty rate (%) (2009):	51
Key export markets:	China, Malaysia, Japan	Paved road density:	0.02km/100km^2

	2011/12 Act.	2012/13 Act.	2013/14 Prel.	2014/15 Proj.
Output and Prices				
Real GDP growth (%)	-25.1	-26.7	30.7	-7.5
Oil production (millions of barrels per year)	70.5	18.3	66.2	58.5
Inflation, average (%)	59.2	22.7	-5.6	11.2
South Sudan's oil price (US dollars per barrel)	96.4	97.6	97.8	81.7
Central government finances				
Revenue and grants (% GDP)	27.7	11.6	25.9	28.6
Of which: grants (% of GDP)	3.6	7.1	2.2	4.8
Of which: oil revenues (% of GDP)	23.0	1.7	21.6	20.0
Expenditure (% GDP)	27.9	26.4	28.9	35.4
Current	22.7	22.5	24.9	32.3
Of which: Payments to Sudan (% of GDP)		0.0	5.9	6.0
Capital	5.3	3.8	3.9	3.0
Fiscal balance (% GDP)2	-0.2	-14.9	-3.0	-6.7
Public debt (% GDP)	0.0	9.5	6.4	10.3
Money and Credit				
Broad money (% change)	…	-15.3	20.0	21.1
Reserve money (% change)	…	-36.1	37.0	21.4
Credit to private sector (% change)	…	84.5	7.2	24.2
Balance of payments				
Current account (% GDP)	9.5	-18.0	7.7	-4.9
Net foreign assets of the central bank (in months of imports, end of period)	4.8	0.9	0.5	0.5
External debt (% GDP)	…	6.4	3.6	9.0
Exchange rate				
Official rate (SSP per dollar; period average)	3.0	3.0	3.0	…
Parallel market rate (SSP per dollar; period average)	4.0	4.4	4.3	…

Source: South Sudanese authorities; and IMF staff estimates and projections.
[1] The data corresponds to fiscal year (July to June).
[2] Includes statistical discrepancy and payment of domestic arrears.