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Review Article

Public Debt Composition in SADC: Recent Trends and Puzzles

Richard Makoto*, Takawira Mumvuma, Phineas G. Kadenge

Economics Department, University of Zimbabwe

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***Corresponding author:** Richard Makoto

Abstract

The study analyses the dynamics of public debt composition in SADC. Following years of external debt explosion in the 1980s, countries restructured public debt in the 1990s after adopting the HIPC programme. Using a combination of analytical narratives approach and pattern models, the study found that since the adoption of HIPC in 1996, some SADC countries shifted from external to domestic debt and had relatively low debt ratios as compared to crisis period. However, a puzzle has been observed, even though debt is low; the region has higher debt service under low debt regime as compared to high debt period. Middle income countries are accumulating expensive private debt. Countries that traditionally relied on domestic and private external debt have relatively stable growth rates as compared to those that have shifted from external to domestic debt. The study recommends that countries should ensure a well-diversified debt portfolio composition over time.

Keywords: External debt composition, domestic debt composition, economic growth.

INTRODUCTION

In recent times, the world has witnessed shifts in public debt composition and SADC countries are not an exception. The threat of debt overhang and debt risk profile compelled countries to adopt efficient debt management practices. The choice of debt composition, structure and characteristics, is central in debt management because it has implications on growth as countries will be exposed to risk differently. Some countries are risk-averse while others are risk-takers and these behaviours should be revealed in the choice of debt composition. Most countries with weak government revenues seek debt finance either from domestic or external sources. Traditionally, developing countries were relying on external debt window because of low levels of financial development. Since, government funding needs cannot be satisfied by issuing foreign debt alone, domestic debt has to be issued. These two types of public debt expose the countries to unique risk.

Borrowing from external markets exposes a country to currency mismatch risk but with a benefit of long maturity, while domestic debt subject economies not only to short maturity but high cost on average than external debt. When countries accumulate more domestic debt, the effects could be as detrimental as external debt especially when banking institutions dominate on the holding of government bonds under a condition of low saving rate [1]. Public debt composition and structure depends on government risk preferences. Risk-averse countries opt for domestic debt because it can be easily deflated though at a cost of crowding-out effect. Domestic debt issuance is constrained with the possibility of crowding out the private sector from accessing credit in the money market. This is blamed for low productivity that undermines growth. In countries concerned with the effectiveness of monetary policy, foreign debt will be a second best option because it results in liability dollarisation which renders monetary policy useless. Therefore, regardless of the type of debt, countries should practise efficient debt management.

The literature on issuance of public debt suggests different views on the factors that influence debt choice, structure and composition. The *original sin* literature emphasise the role of country size as the major determinant of public debt currency structure [2, 3]. In this regard, developing countries will be forced to issue domestic currency debt as they are unable to issue foreign debt in their currency. Some suggests that country size, institutional and macroeconomic factors determine the structure of debt issuance [4]. Developing

countries are susceptible to external shocks and natural disasters which have exacerbated the problem of foreign exchange risk [1]. Another strand of literature focused on the cost-risk trade-off as the factors behind public debt composition and structure. The cost of debt varies between domestic and external debt and the later is complicated due to exchange rate risk exposure. In the absence of foreign exchange risk, foreign debt is considered to be less costly due to existence of concessional terms. However, under the external debt window, countries borrow from either official (multilateral and bilateral debt) or private creditors. These debts have unique terms such as debt relief or rescheduling and the cost of default. The proportion of concessional debt depends on World Bank economic classification of whether the country is regarded as low, middle or high income. These statuses vary across time and countries underwent transformation that changed the economic classification. Middle income countries are mostly subjected to high cost debt terms while low income to less expensive debt. A country can borrow high cost debt which it is obliged to repay even when the status changed from middle to low income.

The choice of debt composition must be a strategic choice in order to avoid suboptimum outcomes. Drazen [5] proposed that the key determinant of preference of debt composition is the relative political cost of repudiating foreign compared to domestic debt. The interplay between political forces and economic forces also help to build fiscal theory of debt issuance [6]. A higher level of democracy, leads to a lower level of external indebtness [7, 8]. The composition of the electorate also influences debt composition, bequest-constrained individuals prefer low current taxes and thus high debt [9]; old people prefer external debt to domestic debt than young electorate. Coalition governments are not fiscally responsible and can lead to over accumulation of debt [10, 11]. Election threat can force incumbent governments to strategically accumulate debt biased high cost debt [12, 13, 14]. However, political influences on debt sometimes give precedence to economic conditions [15]. SADC countries went through the process of political and economic transition that affected debt composition. The empirical literature on debt structure and composition is still developing. Most considered either external or domestic debt separately and was aimed at creating data bases of domestic debt [16, 17]. Very few studies analysed the structure and characteristics of debt and to the best of our knowledge studies that critically analysed SADC countries are rare.

This study is not going to detail the crowding out effect, but explain the debt composition and structure, explore the risk profile of domestic and foreign debt. The major objective is to explore debt structure and characteristics in post HIPC and domestic debt dependent SADC countries. The growth implication of their risk taking behaviour will also be analysed. In so doing the study will be extending domestic debt literature in both dimensions of characteristics and data base [16, 18]. In the SADC literature, the study will help to characterise the public debt risk taking behaviour of good reforming (domestic debt dependent countries) countries and compare it to usually bad reformers (post HIPC countries) which are usually forced to reform due to external influences. Good reformers traditionally are domestic debt dependent while bad reformers are foreign debt dependent. The study is not focusing on the factors behind the evolution of debt composition, but exploring the revealed borrowing behaviour and carry out a comparative analysis between the identified two groups of countries. A combination of analytical narratives approach and pattern models is used as appropriate methodology. The sample includes a post HIPC country on reforming path (Malawi), crisis country which is weak on reforms (Zimbabwe) and domestic debt dependent countries which are good reformers (South Africa and Mauritius). These 4 countries are used for a detailed comparative analysis. The sample is suitable as it consists of all key attributes of debt crisis, debt relief and good debt management. The analysis is for the period 1980 to 2016, over the period some countries experienced debt crisis and adopted HIPC programme.

The rest of the paper is organised as follows, section 2 discusses the dimensions and characteristics of debt in post HIPC and domestic debt dependent countries, while in section 3 we provide an analysis of recent trends in the composition of public debt and the rise of domestic debt. In section 4, we briefly explain a comparative analysis of growth performance of post HIPC and domestic debt dependent countries. Section 5 concludes and proposes some policy recommendation for the study.

Debt Dimensions and Characteristics in Selected Countries: Pre and Post HIPC Period

SADC nations are amongst the LDCs that took advantage of ease external debt window in the 1980 and borrowed heavily from foreign sources. The composition of public debt in the 1980s was biased towards external debt than domestic debt because of low developed domestic debt markets. SADC region has experienced external debt crisis in 1980s and 2000s due to a combination of exchange rate volatility and natural disasters. Malawi, Tanzania, and Zambia had debt to GDP ratios of above 100% when the crisis emerged between 1982 and 1986. However, Zambia had an extreme debt ratio of over 400% in 1986. In 1995, public debt was unsustainable and stifled growth in these countries. The international community [2] responded to this indebtedness problem through the

[1] For instant, terms of trade due to volatility in commodity prices in the international markets

[2] In particular World Bank and IMF

Highly Indebted Poor Countries (HIPC) debt relief programme in 1996. Malawi, Tanzania, and Zambia were amongst the candidates for the programme which managed to reduce the official debt stocks to sustainable levels.

In the post HIPC, SADC introduced a macroeconomic convergence policy framework with set a target debt ceiling of 60% and deficit target of 5% of GDP. The debt ratio in most HIPC candidates is very low, for instance in 2013, the debt ratio was around 40% which was less than the regional target (60%). However, exceptions are noted; Mauritius and Zimbabwe had debt ratios of nearly 100%. The transitional cost of debt relief contributed to the revision of external debt terms. In the post HIPC period, both official and private creditors reduced the cost and increased the maturity and grace periods. Official creditors offer an average maturity of 20 years with an average cost of 2% per annum. Contrary to this, private creditors offer short to medium term debt (average maturity is less than 10 years) at higher interest rate (average around 5%). The average grace period is 6 and 4 years for official and private creditors respectively. This difference in terms of debt was a cause of concern as puzzling outcomes are notable in most economies. The dimensions and characteristics of public debt have changed. Given these debt terms and charging structure of debt, SADC countries are facing high debt service burden under low-debt regime in the same way as happened in the 1980s high debt regime. Most SADC countries are experiencing official debt burden rather than private debt burden.

Figure 1 and 2 present the volume and cost of debt during the crisis period (1980-1990) and post HIPC (2011-2014).

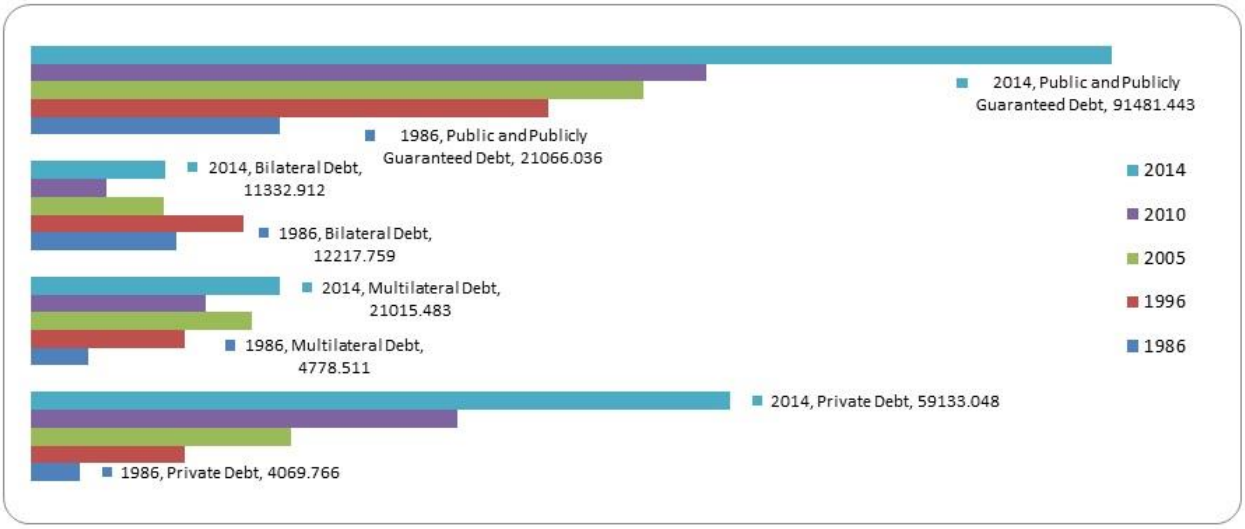

Fig-1: Composition of External Debt stock

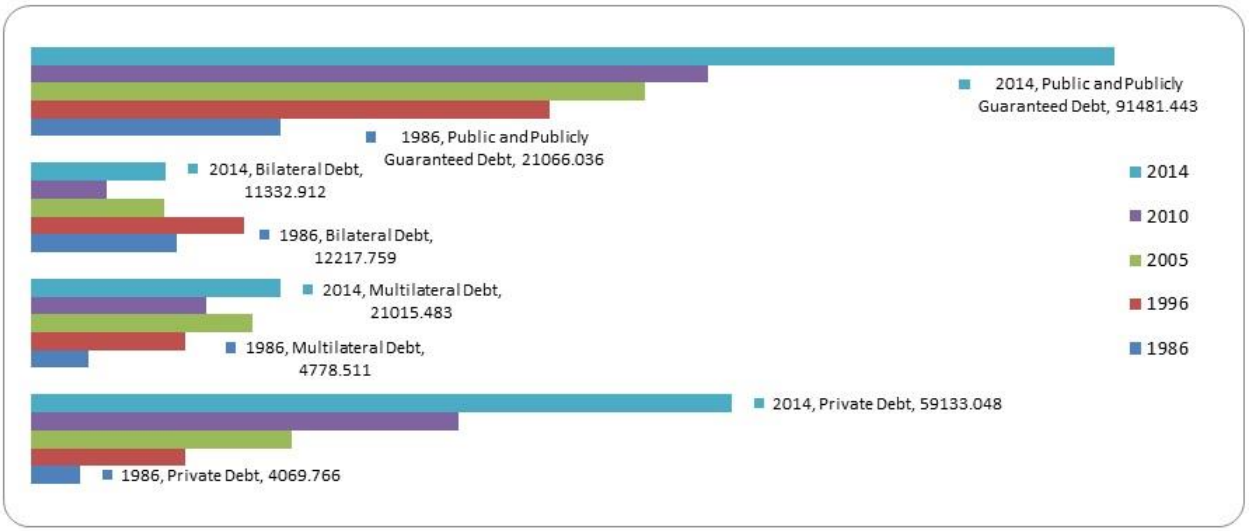

Fig-2: Composition of External Debt service

Source: Author's compilation using data from World Bank Economic Indicator (2014). All values are in millions US$. Countries include Malawi, Tanzania, Zambia, Zimbabwe, DRC, South Africa, Lesotho, Swaziland, Mauritius, and Mozambique.

The stock of external debt in these selected SADC countries increased from US$21.066 billion in 1986 to US$91.481 billion by 2014 *(figure 1)*, whilst total external debt service increased from US$1133.779 million to US$4920.654 million respectively. During the first crisis period of 1986, bilateral debt constituted the largest portion of US$12.22 billion as compared to US$4.78 billion and US$4.07 billion amounts of multilateral debt and private debt respectively. In the post HIPC period, in particular 2014, private debt was US$59.133 billion of the US$91.48 total external debt which implied 64.6% exposure to private debt. Policymakers and academics rarely talk of the consequences of private debt. This hidden debt and the shifts in creditor composition can bring new dimensions in the debt growth literature. In 1986 the composition of debt service was US$325.4 million, US$299.9 million and US$508.43 million for bilateral, multilateral and private debt respectively. In 2014, private debt service was US$3.7 billion, multilateral debt service US$719.6 million whilst bilateral was US$462.4 million from debt stocks of US$59.13 billion, US$21.02 billion and US$11.3 billion respectively. Private debt remained a threat and the debt obligations in post HIPC are much higher as compared to the crisis period of 1986 and early 2000s.

The dimensions of debt radically changed since the 1986 debt crisis. The growth implications of these changes varied from country to country. A graphical approach was used to explore the debt-growth relationship for selected countries.

Malawi: Debt Growth Dynamics

Historically, the country has experienced fiscal imbalances with an external financing requirement of nearly 50% in some years. The fiscal disequilibria and low saving rates, forced the country to adopt a debt policy biased towards external finance. The country is among the first crop of SSA countries that borrowed heavily in the 1980s. Figure 3 presents the historical debt-growth dynamics. The debt ratio further rose to an all-time high of 175% in 1995. This high level was unsustainable resulting in the country qualifying for the HIPC programme in 1996. The country reached completion point in 2005, since then, the debt ratio was on downward trend and in recent times, it is below 40%.

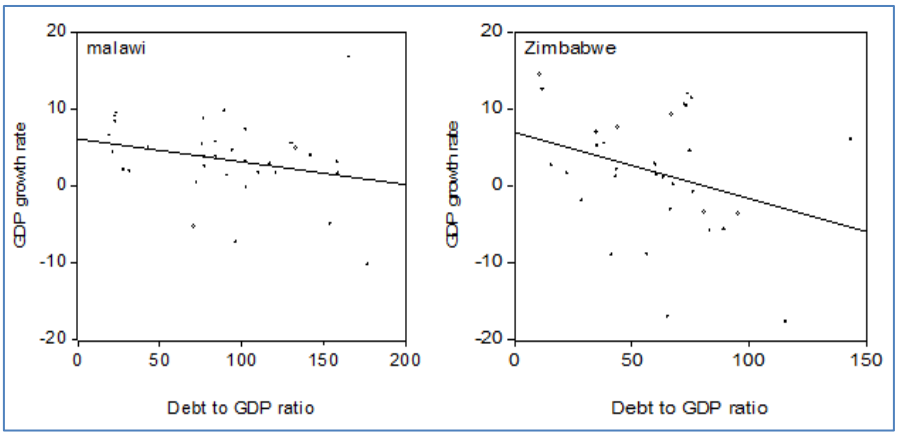

Fig-3: Debt –growth and Debt structure for Malawi and Zimbabwe
Source: Author's compilation using data from World Bank Development Indicator database 2015

Low growth has been recorded during the debt crisis period (1982-2004) and moderate growth after the debt crisis and successful implementation of the HIPC programme. The scatter diagram deduces a negative relationship between growth and debt ratio. Low debt levels are associated with high growth whilst high debt levels with low growth rates. During the crisis period (1982-2004), most preference was placed on multilateral debt and least on private debt. In the post HIPC period, the country experienced moderate growth as compared to low growth of the crisis period and data from World Bank [16] indicators revealed that proportion of concessional loans averaged 100% and 98% of total bilateral and multilateral debt respectively. The average maturity decreased from 42.6 years (HIPC) to 34 years (post HIPC), the cost decreased from 3% to 1% for official debt and from 10% to 0% for private debt. Debt restructuring and improved reputation with creditors explains the external debt favourable terms.

Zimbabwe: Debt Growth Dynamics

According to World Bank, Zimbabwe is classified as a fragile state as political uncertainty and low economic freedom are hampering economic recovery efforts. In the 1990s the country accelerated external borrowing as a result of droughts, currency devaluation, BOP and fiscal imbalance. The country incurred this debt under unfavourable debt terms as it was classified as a middle income country. The debt has a short grace period of less than 2 years and short maturity with a minimum of 6 years and maximum of 17years compared to Malawi. Data from World Bank [14] indicators showed that, the average cost of debt over 1980-86 was 5.4% and 11% for official and private

debt respectively and 3.4% and 6.9% over 1996-2005 respectively. In 1999, the country defaulted on external debt and was subsequently slapped with stiff sanctions from international financial institutions due to arrears accumulation.

Since then, the debt ratio has been increasing not because of new debt issuances, but interest compounding as a result of arrears accumulation and was exacerbated by falling GDP. The cost was relatively high compared to other SADC countries. The country is currently in debt distress and did not qualify for debt relief under HIPC. The growth implications of this debt are illustrated in figure 3 where a negative relationship between debt and growth is observed. Low debt levels of less than 50% are associated with positive growth while debt levels of more than 50% are accompanied by negative growth. In the 1980s, private debt was higher than official debt and the debt switch of the 1990s saw an increase of official creditors. Official creditors have strict measures of punishing defaulting countries. The cost of repudiation of official debt are high as they include austerity measures. Since 1999 Zimbabwe had recorded economic recession.

A comparative analysis in domestic debt dependent countries reveal a different situation.

Mauritius: Debt Growth Dynamics

The country has a well-diversified economy and a track record of good governance and institutional arrangements. Public debt has always been minimal and sustainable following perennial budget surpluses and prudent external debt policies. The debt mix reveal that whenever private debt is high for a certain period, official debt is low in that period; and if official debt is high, private debt will be low. The country prefers short term and relatively high cost debt compared to low income countries. Figure 4 shows no apparent relationship between debt and growth. This debt policy and debt profile is accompanied by moderate growth during the period. There is relatively stable positive growth of around 5% under low debt ratio of below 20% and high debt ratio of more than 80% (figure 4).

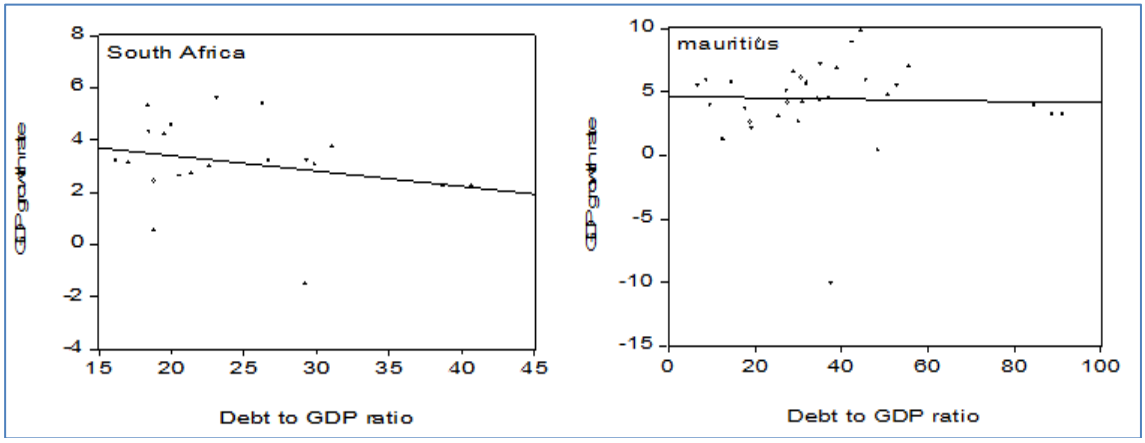

Fig-4: Debt –growth and Debt structure for Mauritius and South Africa

Source: Author's compilation using data from World Bank development indicator database 2015

South Africa: Debt Growth Dynamics

The country is classified as an emerging economy and considered as a good economic reformer in the SADC region. In comparison to regional economies, the country has a well-developed financial system and advanced industrial base. The Ministry of Finance [12] reported that more than 80% of total debt was domestic debt. The country external debt preferences are skewed to private debt (90% of external debt) which is a high cost debt that require macroeconomic discipline. However, the debt has long maturity and grace period of 10.8 and 9.4 years respectively [16]. Public debt has always been minimal and sustainable following good fiscal practices and good debt management policies. The debt ratio is around 40%, and is lower than the SADC target ratio of 60%, it is observed that low debt ratios between 15-25% is associated with moderate growth of around 4%, while high debt ratio (greater than 35%) are associated with low growth (see figure 4). The scatter diagram depicts a negative relationship between debt and growth a phenomenon usually observed in low income countries.

Recent Trends: Changing Composition and the Rise of Domestic Debt

In the post HIPC period, there was a remarkable shift in debt composition towards domestic debt after a decade of external debt crisis. New dimension and characteristics have emerged as countries developed domestic debt markets and created debt management offices. However, these domestic debt markets are relatively unsophisticated [3] as the norm in other SSA. Traditionally, middle-income countries relied on domestic debt markets than international capital markets. Amongst them are South

[3] *see* Christensen, (2004); for detailed analysis of debt markets in SSA.

Africa and Mauritius, Zimbabwe had resorted to domestic debt after the 1999 debt default. Several non-traditional domestic debt dependent countries are resorting to domestic debt in the post-HIPC period. These include Zambia, Malawi and Tanzania and responded to the economic crisis through a series of economic and institutional reforms.

New Dimensions and Characteristics of Domestic Debt

The analysis of domestic debt reveals interesting structures in terms of maturity, instrument traded, investor base, and costs. Most of the domestic debt is issued through marketable instruments in the form of treasury bills and bonds. The degree of mix depends on the level of financial development. Countries are issuing both medium and long term bonds with maturity ranging from 2 to 15 years. However, these differ from country to country and comparable between good and bad reformers. The major challenge of debt issuance is low secondary market activities and the thin investor base. The characteristics of selected individual countries from good and bad reformers are explored. Good reformers have very deep financial markets (M2/GDP ratio) while bad reformers have fair to shallow financial markets.

The region has struggled to diversify the investor base due to relatively low secondary market activity with the exception of domestic debt dependent countries (SA, Mauritius). In most countries, the investor base is thin with central bank and monetary institutions dominating while non-bank players do not exist in some markets. The structure of domestic debt is shown on figure 5.

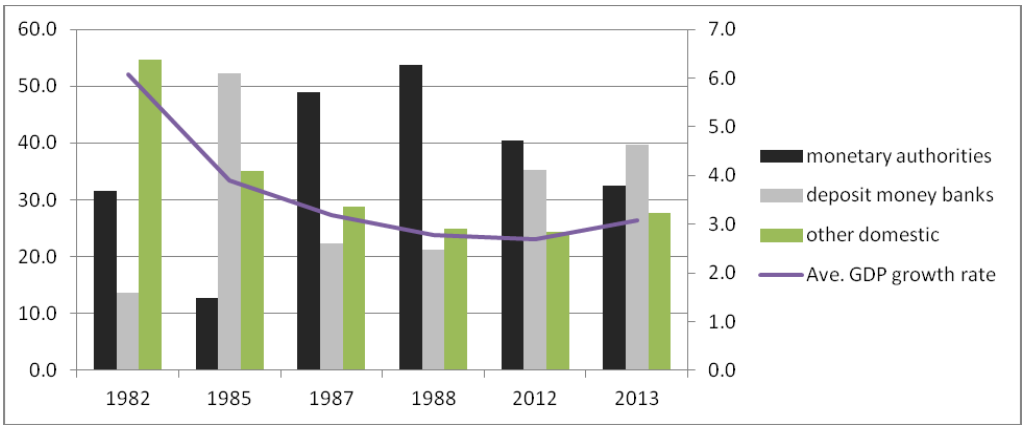

Fig-5: Holder composition of domestic debt and growth in selected SADC countries

Source: Author's compilation using data from annual reports from Central Banks. The sample included South Africa, Malawi, Zambia, Tanzania, Zimbabwe, Mauritius, Seychelles.

From figure 5, on average monetary authorities (Central Bank) are the major holder of domestic debt alongside the banking institutions (deposit money banks mostly commercial banks). The public is a relative small component of domestic debt holder. This structure clearly reveals that the investor base is thin in SADC which can be taken as an indicator of less developed domestic debt markets. Governments may be hold hostage by a small group of investors. The growth implication of this structure is captured by the average GDP growth rate which shows a decline from 6% in 1982 to around 3% in 2012. In the early 1980s, the investor base was biased towards the public holders while in the late 1980s it shifted to central bank holders and commercial banks. This is the period when SADC countries experienced official debt burden and crisis. Given the poor state of domestic debt markets, the Central Bank was the major financier through money creation. In recent times, the structure of debt composition has not changed as it is still biased towards banking institutions.

Country Analysis

The analysis involves a brief review of country domestic debt policy and market. This would be followed by trend analysis on debt switching and the composition of domestic debt. Two graphs will aid the analyses that are domestic- external debt composition and domestic debt composition and growth.

Post HIPC countries*: *A Comparative Analysis

Countries that adopted the HIPC programme reformed and changed their debt choice. The nature and characteristic of debt profile is explained below. Heterogeneity exists among the post HIPC member countries as explained in the following section.

Malawi

Debt composition profile is presented in Figure 6.

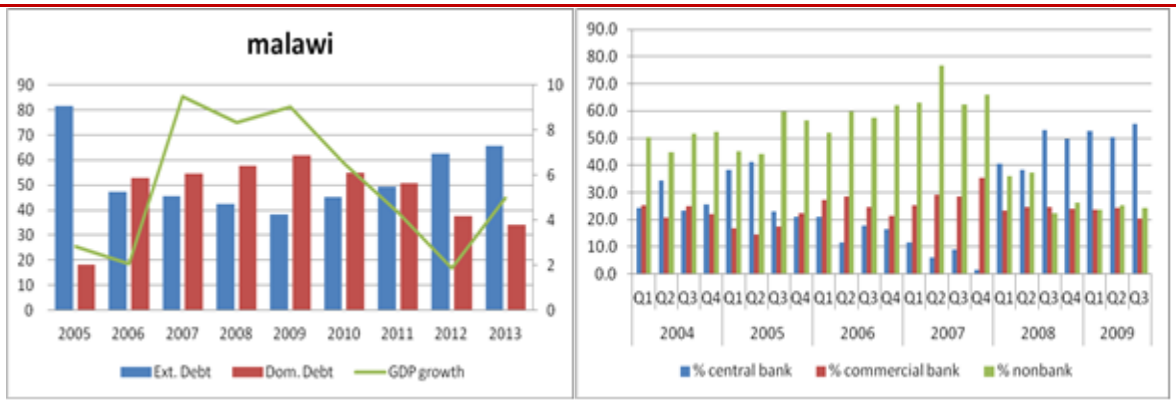

Fig-6: Dimensions and Characteristics of Debt Composition in Malawi
Source: Author's compilation using data from Central Bank of Malawi annual reports (2010, 2012, 2014, 2016)

In post HIPC period, Malawi was aggressive in retiring external debt and accelarated the use of domestic debt from 18.3% of total debt in 2005 to 52.7% in 2006 before reaching an all time high level of 61.7% in 2009. During this period, the country recorded high growth rates ranging 6-9%. However since 2010, there was a reversal as the country started to accummulate more external debt than domestic debt and de-accelaration of economic growth was experienced. Domestic debt holder composition is biased towards non-bank holders followed by commercial banks. However in recent times, the Central Bank is the major holder of domestic debt. putting the country at risk of deficit monetisation.

Tanzania

The country did not follow an aggressive approach in retiring external debt. Figure 7 summarises the debt profile.

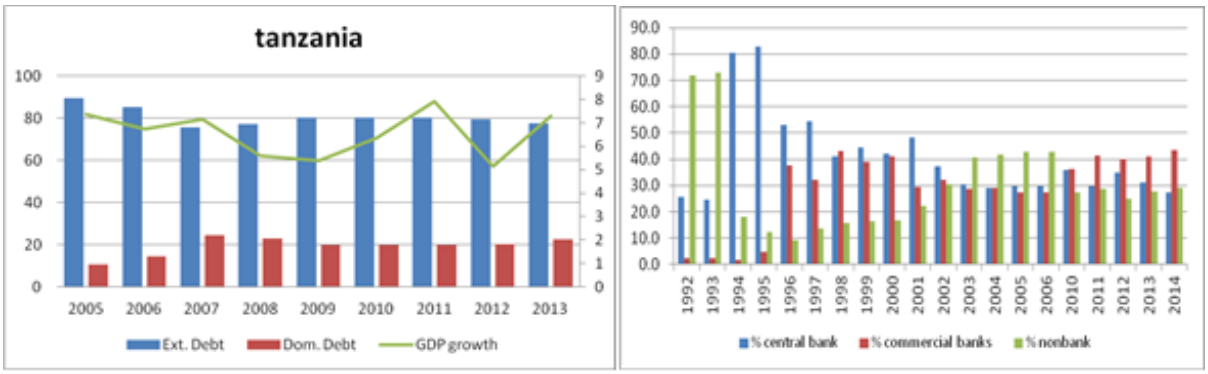

Fig-7: Dimensions and Characteristics of Debt Composition in Tanzania
Source: Author's compilation using data from Bank of Tanzania annual reports (2010, 2012, 2014, and 2016)

Tanzania, took a gradual approach in switching from external to domestic debt, in 2005, domestic debt consitute 10.5% of total debt which slightly increased to 14.6% in 2006. Since 2007 the proportion of domestic debt is oscillating around 20% of total debt. With this composition, the country experienced positive growth which oscillated around 5-8%. Analysis of domestic debt holder composition reveals that in the early 1990s, the non-bank holder was the main creditor followed by the Central Bank. However, this characteristic changed in the late 1990s where banking institutions (Central Bank and commercial banks) emerged as the main creditors. However in recent times, a new dimension emerged there is a rise in the non bank creditors although commercial banks are the main creditors. The Central Bank holding of domestic debt is decreasing which is a rational behaviour though commercial bank dominance may indicate the prevelance of the crowding out effect.

Domestic Debt Dependent Countries: A Comparative Analysis

The implications of the composition and market structure of domestic debt on risk and costs need an evaluation. The countries are issuing both fixed rate and variable interest rate debt. Given the illiquid nature of most markets, interest rates risks is high. In good reforming countries, the use of variable interest rate is on the rise compared to bad reformers or forced reformers. Maturity structure of debt may provide a guide on risk as short and medium term instruments may expose a country to refinancing risk. The literature uses indicators such as average maturity, short term debt (1 year). Cost indicators like weighted average interest rate (WAIR) and simple average are used.

Mauritius Domestic Debt Dimensions and Characteristics

This is a middle income country with high degree of financial sophistication compared to other SADC countries (M2/GDP approx. 80%). It has a relatively well developed domestic debt market. Figure 8 summarises the debt profile.

Fig-8: Debt Composition in Mauritius

Source: Author's compilation using data from Central Bank of Mauritius annual reports (2010, 2012, 2014, 2016)

From fig. 8, unlike post HIPC countries, Mauritius possesses a unique debt structure. The country uses more of domestic than external debt owing to its highly diversified domestic debt markets. There is a high proportion of long (above 50%) and medium (about 35%) term debt. This shows that the country is not exposed to refinancing risk implying less risk because of long maturity. However, there is high costs of domestic debt.

South Africa: Domestic Debt Dimensions and Characteristics

The country has a well-developed financial system that matches Mauritius. Figure 9 summarises the debt profile.

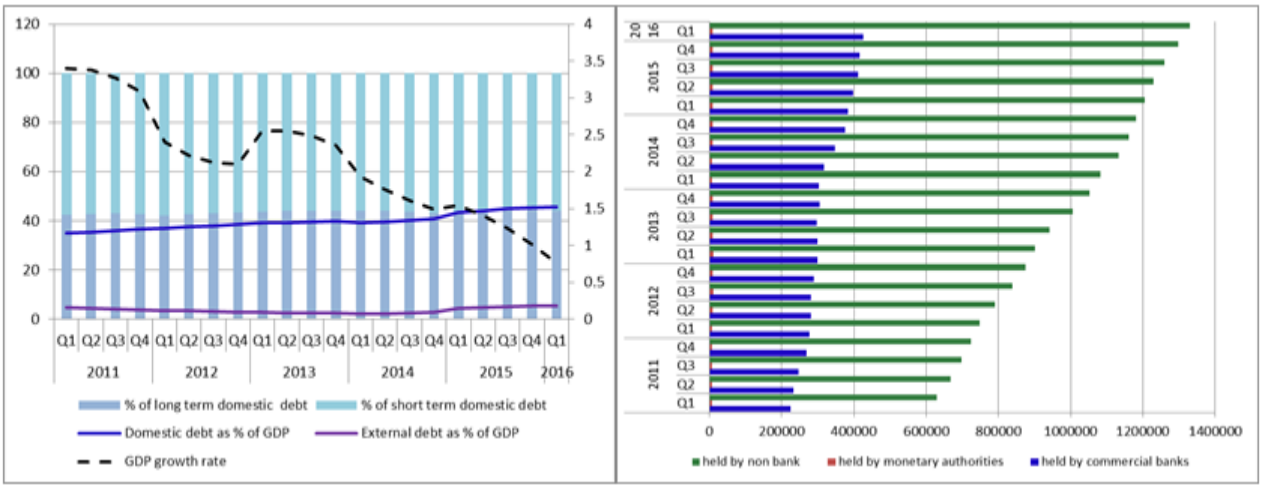

Fig-9: Debt Composition in South Africa

Source: Author's compilation using data from South African Reserve Bank online data base (2014) and National Treasury Budget Review (2017)

Traditionally the country depends on domestic debt (above 80% of total debt) as is the case with Mauritius (see fig.8). However, the country has an exactly opposite behaviour to Mauritius. It has a high proportion of short term debt (above 50%). This shows that the country is exposed to refinancing risk. Most of the debt is issued to non-bank a holder which is contrary to post HIPC countries that rely on banking institutions as major holders.

Growth Implications: A Comparative Analysis of Performance Differential- Post HIPC vs. Domestic Debt Dependent Countries

The region has experienced oscillations of positive and negative GDP growth rates. Growth in middle-income countries is averaging in the range 4-5% while low-income countries are recording high growth rates above 7%. The leading low-income countries in growth are Mozambique and Tanzania. Growth in fragile states is very slow because recovery is underway. Between 2000 and 2005, the average growth

rate was 1.3% in fragile states, 9.3% in oil exporting countries, 5.4% in low-income and 4% in middle-income. However for the period 2006-08, there was remarkable increase in growth in all groups with the highest being 17.9% in oil exporting country, 6.9% in low-income countries against a regional target growth rate of 7% per annum. The region recorded an average real GDP growth of 4.7% for 2000 – 2005 and 6.5% for 2006-2008. However, in recent years the region has recorded variations in growth rates across nations. In 2009 the growth rate was 3% which increased to 5.9% in 2010. The debt-growth nexus can be revealed by figure 10 which summarises the real GDP growth for HIPC that are changing debt composition and domestic debt dependent (middle income) countries.

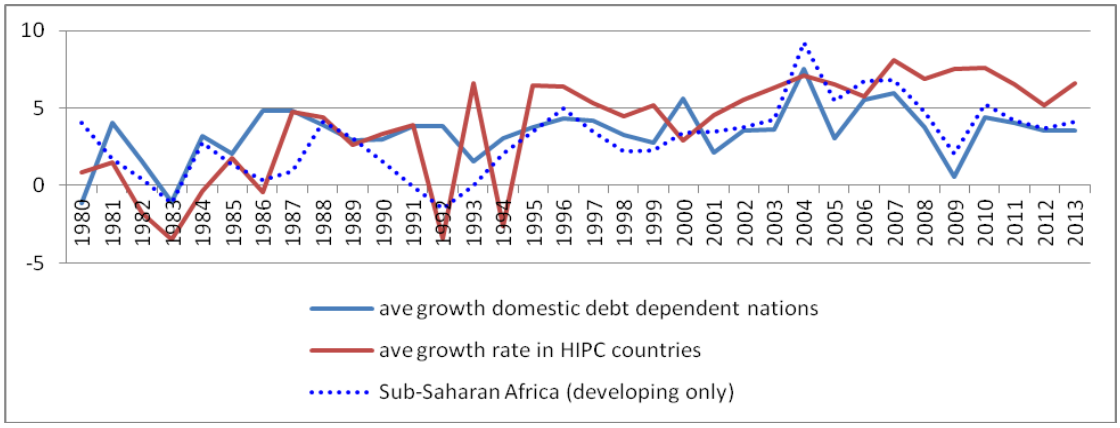

Fig-10: Economic growth in post HIPC and Domestic Debt Dependent Countries in SADC
Source: Author's compilation using data from World Bank Economic Indicator (2014)

From fig.10, the average growth rate was below 5% and most years over the period 1980 -2016, for both post HIPC and domestic debt dependent middle income countries between 1980 and 2016.

Debt crisis and HIPC period (1980-2000)

HIPC has experienced negative growth rate in 2 cycles: 1981 until 1984 and 1992 -1994. These periods have been accompanied by an increase in external debt burden in most HIPC-to-be countries. On the contrary, domestic debt dependent countries experienced higher growth during this period when economic recession was being experienced in external debt crisis countries (later candidates for HIPC). Generally these countries have good economic policy reforms in contrast to HIPC which were largely bad or forced reformers. Since 1996, the year when HIPC was adopted, there was a shift in economic performance between the two groups. High economic growth rate was observed in HIPC compared to middle income (domestic debt dependent). Positive growth rate, although low, were recorded in HIPC from 1997 up to 2000 and later increased to around 5% in 2001. During this period, external debt was declining as countries were nearing completion points. The low growth rate in HIPC during the debt crisis and HIPC implementation periods could be attributed to debt overhang effects and austerity induced transitional costs respectively.

Post HIPC period (2005-2016)

In the post HIPC period, countries were substituting more domestic debt for external debt and were forced to reform. In recent times, HIPC countries are achieving about 5% growth rate while domestic debt dependent middle income is less than 5%. The combination of debt relief, economic policy reforms and the use of domestic debt help propel economic growth. Moreover, it is common practice that decades of economic decline are accompanied by high growth as the countries recover. However, since 2010, both groups of countries are experiencing subdued economic performance following the global economic slowdown. The negative growth rate is more pronounced in domestic debt dependent countries than post HIPC. This could be explained by differences in global economic integration. Even though the growth rate is positive, it is still below the region's annual GDP growth target of 7%.

CONCLUSIONS AND POLICY RECOMMENDATIONS

The study investigated debt composition in selected SADC countries using a comparative analysis between post HIPC and domestic debt dependent countries. An analysis of the trends revealed puzzling debt composition outcomes. Generally the countries have relatively low debt ratios which are below regional debt ceiling of 60% except for one country in debt distress. The debt ratio is averaging 40% in both domestic debt dependent countries and post HIPC. In Malawi and Zimbabwe low debt levels of less than 40% were associated with high growth of approximately 5%, whilst high debt levels of more than 50% were accompanied by low growth. The negative correlation was observed in South Africa whilst for Mauritius no correlation between debt and growth even up to debt levels as high as 100%. During debt crisis, Malawi had huge external debt stock and after HIPC programme switched to domestic debt through aggressive retirement of external debt, and the major creditors were Central Bank and non-bank holders.

For domestic debt dependent countries, heterogeneity was observed in terms of risk profile. South Africa preferred short term domestic debt and private external debt with non-bank holders being the major holder of domestic debt. In contrast Mauritius preferred long term domestic debt and official creditors (multilateral and bilateral external debt). Post HIPC was recording higher growth rates than domestic debt dependent countries. The study recommend that countries should promote a well-diversified investor base for domestic debt such as limiting the Central Bank's role in the holding of domestic debt and promoting the participation of non-bank holders. Private debt should be kept minimal to avoid high debt service costs.

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