Addressing Debt Vulnerabilities

by

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Public debt increased already significantly before the onset of the COVID-19 pandemic, which then further worsened debt dynamics.
Real GDP growth slowed in low- and middle-income countries over the past decade, worsening automatic debt dynamics…

…In addition, most countries recorded persistent primary deficits over the past decade.
AS A RESULT, THE RISK OF DEBT DISTRESS INCREASED...

The risk of external debt distress worsened in countries covered by the LIC DSF in line with rising debt levels. Currently, more than half of LIC DSF countries are at high risk of external debt distress or in distress.

13 countries saw their risk of external debt distress rating deteriorate since the onset of the COVID-19 crisis in March 2020.

Source: LIC DSF Database as of October 2022.
Government debt in default in lower-middle income countries increased from US$ 36 billion in 2015 to US$ 168 billion in 2021. Defaults in low-income countries reached US$ 82 billion in 2021, higher than in high-income countries...

...However, the wave of defaults has not materialized yet, as debt in default is concentrated in few countries still.
Emerging market & developing countries face significant debt service payments.

DSSI-Eligible LICs and MICs – US$ 200 bn.
Investment Grade Non-DSSI MICs – US$ 432 bn.
Non-Investment Grade Non-DSSI MICs – US$ 517 bn.

Some 120 low- and middle-income countries face more than US$ 1.1 trillion in debt service payments on public and publicly guaranteed external debt between 2023 – 2025.

REFINANCING RISKS HAVE INCREASED

Widening spreads increase the borrowing costs of many low- and middle-income countries, increasing refinancing risks. Some have effectively lost access to markets.
Endorsed by the G20 and the Paris Club to facilitate timely and orderly debt treatment for DSSI-eligible countries

Need for debt treatment and required restructuring envelope based on an IMF-WBG Debt Sustainability Analysis (DSA)
Consistent with the parameters of an “upper credit tranche” (UCT) IMF-supported program (>100% of quota per year or cumulative >300% of quota)

To qualify for a CF debt treatment, countries must either have
Unsustainable debt, which limits access to official or private financing, or large external financing needs, in excess of financing from the IMF, World Bank, and other sources

The CF mandates that the debtor seek comparable treatment by other official bilateral and private sector creditors
BUT THE COMMON FRAMEWORK HAS NOT FULLY DELIVERED YET

- Slow progress with the current CF countries
- Coordination issues among creditors
- Unwillingness to request an IMF UCT program with associated conditionality (e.g., owing to political cycle)
- Access to alternative sources of financing / draw down existing buffers
- Choose to accumulate arrears and engage in bilateral discussions on a debt treatment
- Feel uncertain about whether the CF will work for them
- Fear of loss of international market access or significant increase in borrowing cost and risk
- Some may benefit from the recent rise in oil prices and some commodity prices which can provide relief to the fiscal and external accounts
OPTIONS FOR THE WAY FORWARD

• **Greater clarity needed on the steps and timeline of debt treatment**
  Timely formation of the CC and provision of financing assurances, guidelines for the work of the CC, clear steps in the CF process, guidelines to address the lack of debt transparency, and early engagement of official creditors with the debtor and with private creditors, more effective participation by private sector creditors and creditor of large bilateral debt.

• **Introduction of a debt service suspension for the duration of the negotiation** G20 commitment to a debt service standstill on official obligations for countries requesting a CF debt treatment.

• **Transparent assessment of the CoT.** Official bilateral creditors should provide more clarity on how CoT will be effectively enforced, beyond the parameters already included in the CF. Clear rules for the enforcing comparability of treatment to facilitate agreements between debtors and creditors.

• **Expanding the eligibility for CF treatment beyond the DSSI eligible**
  Small islands and other vulnerable systemic middle-income countries.
THANK YOU