Low-Income Countries Sovereign Debt Challenges

Dalia Hakura
Deputy Division Chief
Strategy, Policy, and Review Department

OCTOBER 29, 2021

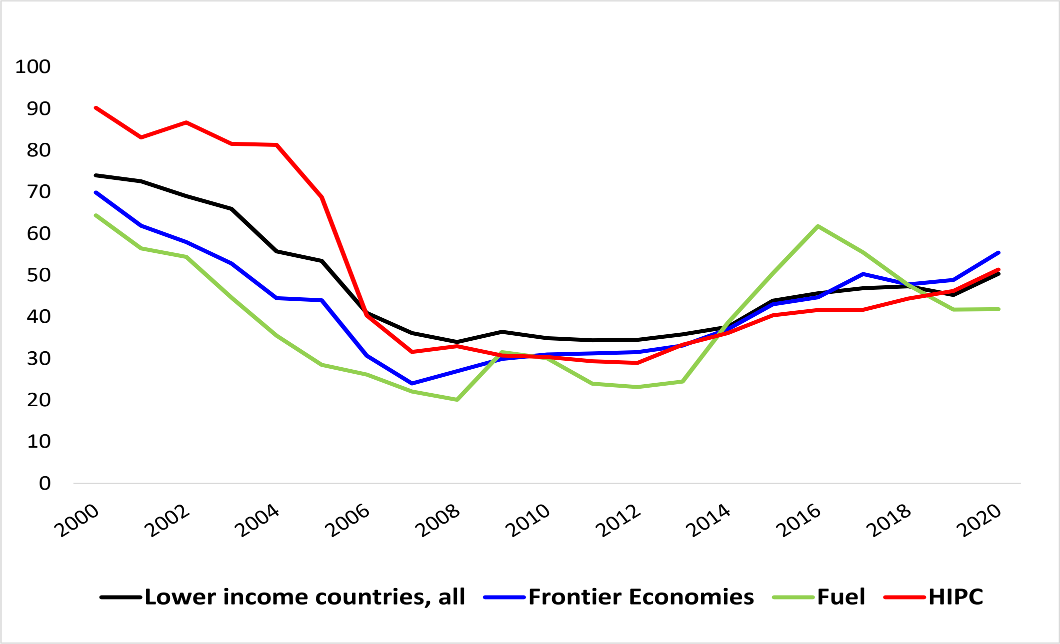
Outline

▪ DSA	Debt Sustainability Analyses
▪ DSSI	Debt Service Suspension Initiative
▪ CF	Common Framework
▪ MPA	Multipronged Approach

COVID-19 exacerbated pre-existing debt challenges

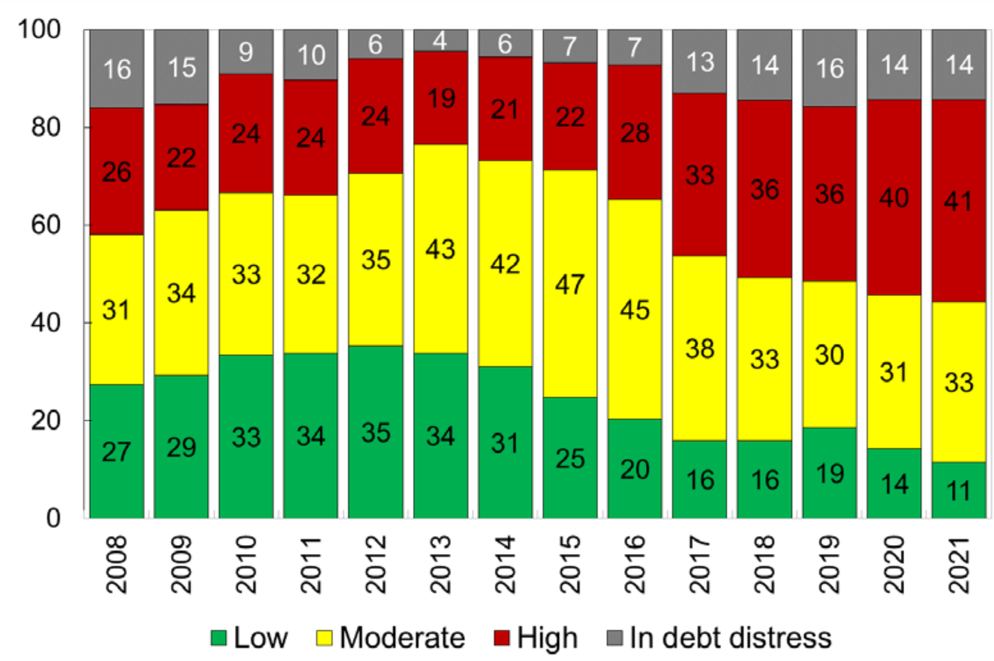
Increase in debt level undoing some of the gains from HIPC

Public Debt Across Low Income Countries
(percent of GDP, median)



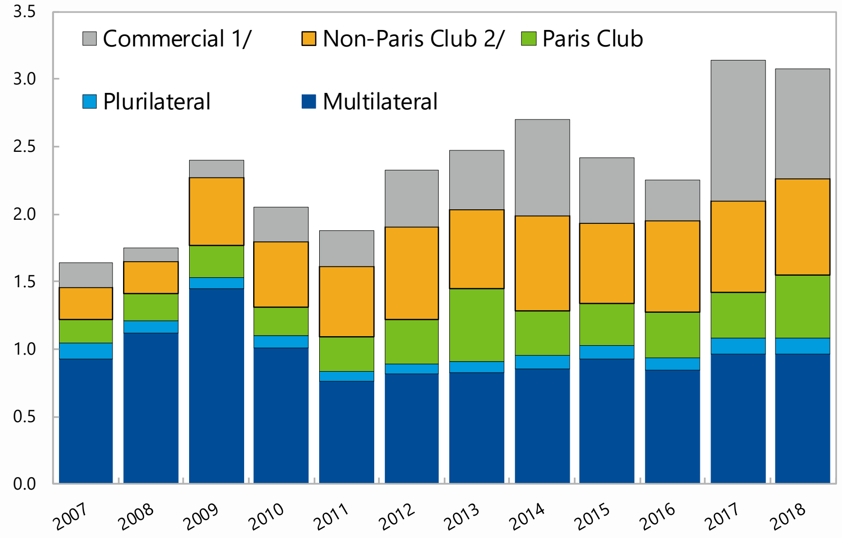
9 downgrades since the onset of the pandemic and 55 percent of LICs at high risk or in debt distress

Evolution of the Risk of Debt Distress
(in percent of LICs with DSAs)



Rising debt levels add to pre-existing challenges

Low Income Economies Disbursed Debt by Creditor Type
(weighted average in percent of GDP)



Source: DRS Database
1/ Includes disbursements from bonds and other instruments
2/ Includes disbursements from China

Pre-existing debt challenges:

- Elevated debt (but not all LICs in the same situation!)
- Lack of transparency and reliability of debt data
- Diverse external creditor base
- Shortcomings in the debt restructuring architecture
- Problems associated with collateralized debt

Additional challenges ahead:

- Elevated financing needs to combat the pandemic and restore convergence path, and meet the SDGs
- Risk of “Great Divergence”, including linked to vaccination

G20 Debt Service Suspension Initiative (DSSI): Liquidity Relief

The DSSI enables eligible countries to defer official debt service to help mitigate the pandemic's impacts.

- First phase: covered May 1 to Dec. 31, 2020; Two extensions: through end 2021

48 DSSI requests (66 percent of eligible countries as of September)

US$10.3 bn debt service deferred from May 2020-June 2021, about half from China

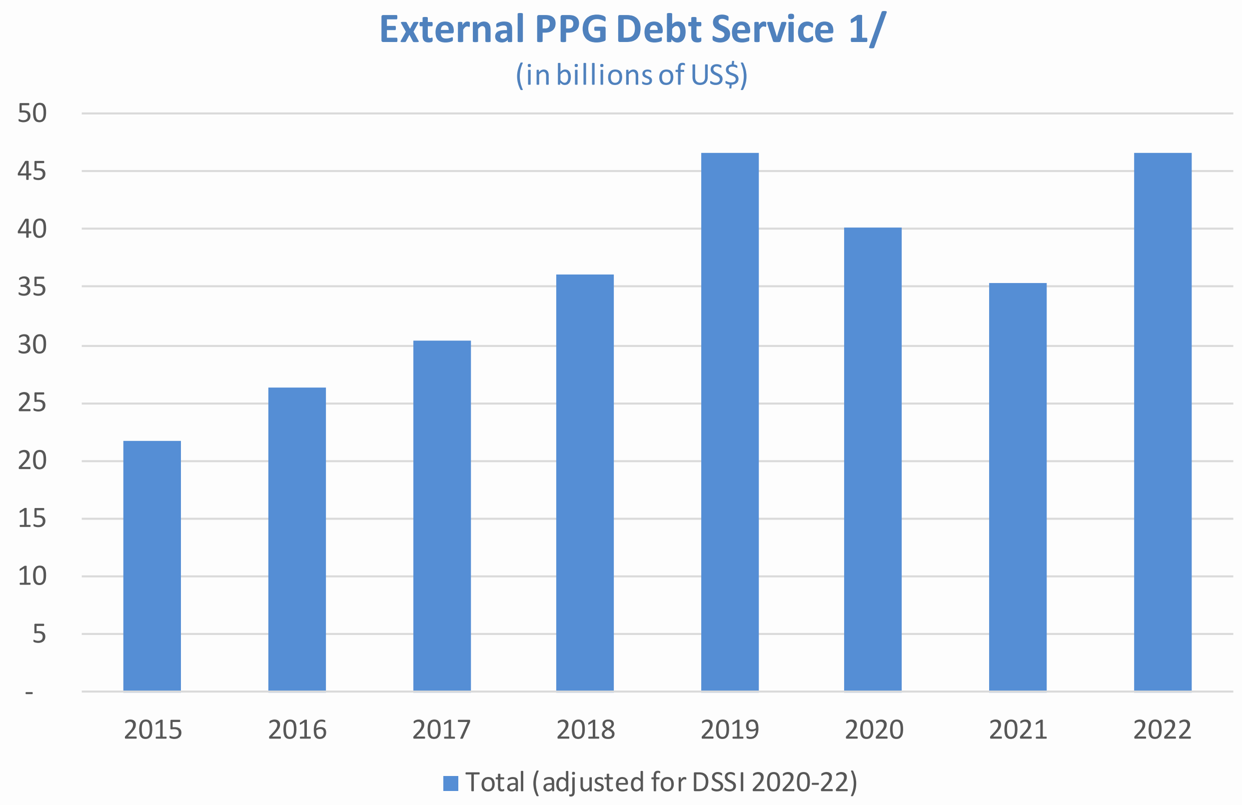
DSSI relief complemented the provision of financial support from the IMF and the WBG

- From April 2020 through June 2021, disbursements from the WB (IBRD, IDA, and RETF) amounted to US$31.1bn, of which US$8.8bn on grant terms (US$28bn in net transfers).
- From April 2020 through June 2021, the IMF disbursed US$23bn (US$19.6bn in net transfers) through its various facilities, including CCRT

G20 Debt Service Suspension Initiative (DSSI): Liquidity Relief

- **Fiscal monitoring** supported by the IMF and the World Bank suggests that COVID-related spending (1.6 percent of GDP) far exceeded the liquidity support from the DSSI in 2020 (US$5.7 billion, about 0.5 percent of GDP)
  - DSSI participants' fiscal efforts to address challenges from the pandemic are expected to broadly continue in 2021
- **Private sector participation encouraged on a voluntary basis:**
  - IIF released the terms of reference to facilitate voluntary private sector involvement;
  - Nonetheless, very few countries elected to make DSSI requests to private creditors;
  - No private creditors participated on a voluntary basis

Liquidity pressures rise in 2022 as DSSI expires and bond maturities push debt service up to pre-pandemic levels



Source: WB DRS.
1/ Debt service for 2020 to 2022 is based on debt contracted through end-2019.

- DSSI helped push down debt service payments to US$35bn in 2021, compared to US$47bn in the last year before the pandemic
- Debt service payments could rise by US$11bn back to US$47bn in 2022
- A further debt service increase in 2023 on DSSI repayments and maturing Eurobonds, could be negative for market access in some cases

G20 Common Framework (CF)

Key Features

- Aims to coordinate Paris Club and Non-Paris Club official bilateral creditors to achieve timely and orderly sovereign debt restructurings for DSSI-eligible countries
- Can help both countries facing unsustainable debt situations and countries where a reprofiling can smooth temporary high financing needs
- Debtor must seek an IMF UCT-quality program and comparable treatment from other (official and private) creditors

Important milestones

- 3 countries have requested a CF so far (Chad, Ethiopia, Zambia)
- CCs have been formed for two cases, and official financing assurances provided for one case

CF: Implementation Issues and Next Steps

Implementation Issues

- First cases have experienced delays in the formation of the creditor committee and in obtaining official financing assurances. First cases are still ongoing.
- Need to generate more demand, incl. by building confidence among debtors in the CF
- Perimeter limited so far to the 73 countries that were eligible to the DSSI

Latest G20 commitment

- "Timely, orderly and coordinated efforts to provide more certainty to debtor countries and facilitate IMF and MDBs provision of financial support"
- "Early engagement of borrower countries and private creditors in the CF process"
- "Creditor Committees may discuss and find appropriate solutions on a case-by-case basis for countries that have requested the CF"
- Encouraged progress on the first cases: Chad, Zambia, and Ethiopia

Actions Beyond the DSSI and CF

- **Further strengthening of private sector participation in debt restructuring**
  - Use of Collective Action Clauses (CACs) in bonds has helped in past 10-years, but there remains room for improvements
    - Sub-sovereign bonds and non-bonded debt (e.g., syndicated loans) often lack majority restructuring provisions
    - The use of collateral and collateral-like instruments has increased, which has the potential to complicate sovereign debt restructurings
    - More widespread use of state-contingent clauses could be encouraged

IMF-WB Multipronged Approach (MPA) and COVID-19

- **The MPA is joint IMF-WB work with countries to address debt vulnerabilities by:**
  - supporting public debt transparency,
  - strengthening capacity to manage debt, and
  - applying accurate debt analysis tools and well-designed IFI policies
- **COVID-19 raises the urgency of implementing the MPA, and requires adjustments:**
  - Scaling up and recalibrating capacity development toward areas critical to reduce debt vulnerabilities (e.g., debt recording and reporting, managing near-term refinancing risks)
  - Adapting mission modalities across debt, cash, and fiscal management CD to a virtual format where possible and introducing on-demand and just-in-time online training.
  - Increased creditor outreach: IMF/WB collaboration to support countries' implementation of the G20 DSSI and Common Framework.
  - Ongoing rollout of recently approved IMF Debt Limits Policy and of the Debt Sustainability Analysis for Market Access Countries (MAC DSA).

Thank you