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Financing for Development

First session of the Preparatory Committee for the fourth International Conference on Financing for Development

Multi-Stakeholder Round Table Discussion on "Debt and debt sustainability"

Wednesday, 24 July 2024, 15:00 – 16:30

Concept Note and guiding questions

Borrowing is critical for financing investments in sustainable development. Sovereign debt enables countries to invest in health, education, and other critical areas. Financing for productive investments can improve debt sustainability in the medium term: a growing economy helps to raise domestic tax and other revenue. However, unsustainable debt levels can constrain policy space, hinder investment on the Sustainable Development Goals (SDGs), and lead to fiscal crises. High sovereign debt burdens also raise the cost of borrowing for private companies, impacting domestic business activity and growth. Countries encumbered by severe debt challenges thus lack the capacity to grow out of a debt crisis.

Since 2015, debt levels in developing countries have risen sharply, exacerbated by the COVID-19 pandemic and global financial conditions. Despite significant efforts to strengthen debt crisis prevention and resolution since 2015 – including the Debt Service Suspension Initiative (DSSI), The G20 Common Framework, and the Global Sovereign Debt Roundtable (GSDR), and increasing use of innovative debt instruments – improvements have not been sufficient to counteract growing debt challenges. **Many developing countries continue to experience a sustainable development crisis due to debt service burdens crowding out needed SDG investments and high risk of debt distress.**

Half of least developed countries (LDCs) remain at high risk of or in debt distress. The median debt service LDCs reached 12% of government revenue in 2023, the highest level since 2000. Debt service burdens now consume over a fifth of tax revenue in 25 developing countries, with 45, including 29 LDCs and other LICs, spending more on debt servicing than on health; 19, including 8 LDCs and other LICs, spending more on debt service than on education; and in 21, including 4 LDCs and other LICs, spending more debt service than public investment.

The international community thus faces **three related challenges: i) supporting heavily indebted countries to be able to finance investments in the SDGs and climate action; ii) strengthening debt crisis prevention, and iii) resolving debt crises more effectively when they do occur**.

Innovative debt instruments can help countries enhance fiscal space, support investments in SDGs and climate action, and provide breathing space to countries facing exogenous shocks. There has been increased interest in instruments which allow countries to redirect debt service payments toward investments, such as debt-for-climate and debt-for-SDG swaps. These are useful for countries that have limited fiscal space for SDG investments, though they are not a means to restore debt sustainability in countries with solvency challenges. Other mechanisms, such as debt

buy-backs, sweeteners, and guarantees can also being considered as appropriate. But to date, there is no institutional home or structure mandated (or dedicated) to support countries in these efforts. Several official creditors have also recently committed to adopting Climate-resilient debt clauses (CRDC) in their lending, which can enhance resilience of borrowers and thus contribute to debt crisis prevention.

Effective debt management is also critical for preventing debt crises. With capacity support from international organizations, many countries have improved debt recording, monitoring, and reporting systems. But more work is needed to enhance debt management capacity, and debt transparency. Enhanced transparency, which the Addis Agenda has called for, requires additional efforts by both debtors and creditors.

Since 2015, the international debt architecture has seen important reforms of debt restructuring mechanisms, particularly since the outbreak of COVID-19. The G20 Debt Service Suspension Initiative (DSSI) provided cash-flow relief to eligible countries; the G20 Common Framework aims to provide deeper relief for qualifying countries on a case-by-case basis; the Global Sovereign Debt Roundtable (GSDR), established in 2023, promotes dialogue on processes and practices.

Yet, the current resolution framework remains characterized by delays and inefficiencies. Private creditor participation in debt restructurings remains challenging, leading to inequitable burden-sharing. Implementation of the G20 Common Framework has been slow. At the same time, several jurisdictions have advanced efforts to resolve debt crises through domestic legislation by protecting developing countries from aggressive creditor actions and facilitating smoother debt restructuring processes. In light of the changes in the global debt landscape since 2015 and the commitments of the Addis Agenda that remain unfulfilled across, it will be critical to develop new solutions.

Questions for Discussion

1. Financing investments in sustainable development

- How can the international community better help countries with high debt burdens create space for investment in the SDGs, productivity and future growth? What tools or mechanisms are available or could be developed to lower the cost of borrowing and address high debt service burdens that crowd out SDG investments?
- What would the appropriate institutional structures be to support these efforts? Can existing institutions be utilized or are new institutions needed?

2. Strengthening debt crisis prevention

- What are the most critical policy efforts needed to prevent debt crises?
- How can the use of contingent debt features be made more systematic?
- How can legal frameworks and institutional capacity in creditor and debtor countries be further strengthened to support public debt transparency?

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3. Debt restructuring

- What new technical support and advisory services are needed to help debtor countries navigate negotiations in a complex creditor landscape?
- How can existing debt restructuring frameworks and policies be strengthened to incentivize faster debt restructuring, and how can remaining gaps in the architecture be closed? How can the international community address the creditor coordination challenge and the power imbalances between debtor countries and creditors?
- How can debt sustainability assessment frameworks be improved?