Tomorrow's Affairs
Analysis of today
Assessment of tomorrow

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Rich countries would reap benefits if they helped poorer countries face debt crisis

The worst debt crisis in history currently confronting developing countries was never likely to be solved by the G20 finance meetings taking place this week in Rio de Janeiro, with the world dominated by geopolitical divisions.

But the Latin American debt crisis of 1982 and the debt crisis of the 1990s will pale in comparison with the current one unless there is urgent progress, says a report by the campaign group Debt Relief International.

More than 100 countries are having to make savage cuts to spending on health, education and climate mitigation, with debt servicing absorbing 8.4% of GDP in 144 developing countries, says the report.

However, a "reverse blood transfusion" using readily available measures would allow poor nations to quickly reduce their debt burden, says the UN Trade and Development Agency (UNCTAD).

Such action requires political will on the part of richer countries. But rising nationalism and isolationism have already dented multilateral co-operation in recent years.

Cheaper loans made possible by wealthier countries would not only improve the lives of the most impoverished people but contributed to global stability, an avowed aim of Western politicians.

The markets are not in distress, people are

UNCTAD, a UN agency working to improve trade for developing countries, has outlined several measures that could be rapidly put in place.

Indebted nations could be exempted from surcharges paid to the IMF to quickly free up $2 billion. Another tool is a provision by the World Bank and other lenders of guarantees to lower interest rate premiums paid by developing countries. They could also benefit from the automatic suspension of interest payments when hit by natural disasters.

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"What we need to be aware is that the markets are not in distress, people are," Rebeca Grynspan, former vice-president of Costa Rica and now head of UNCTAD, told AFP. "We are in a debt crisis."

Several factors lie behind the current situation, including shocks such as the COVID-19 pandemic, Russia's invasion of Ukraine, and rises in interest rates around the world but notably US benchmark rates starting in March 2022.
According to the World Bank, the world's 75 poorest countries will have to spend more than $185 billion or 7.5% of their combined GDP to service their debts, a quadrupling over the last decade.

The challenges in low-income countries

During the pandemic, international institutions took some steps towards reform that would allow cheaper financing for poorer countries, notes Mark Suzman, CEO of the Bill & Melinda Gates Foundation, in a recent Foreign Affairs article.

In 2020, the G20 launched the Common Framework, an initiative intended to help creditors collaborate on debt restructuring for borrowing countries. In 2021, the IMF unlocked the equivalent of around $650 billion in special drawing rights, a reserve asset that countries can exchange for currency when needed.

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But only four countries, Chad Ethiopia, Ghana and Zambia, have applied for debt treatment under the G20 framework. Under the IMF's move, most of the assets it disbursed went to countries that do not need it, such as the US and Japan, because of the IMF's shareholding structure, says Suzman.

"The challenges in low-income countries are, by and large, the result not of indiscriminate borrowing but of climate change-induced shocks, a pandemic, and far-off wars," Suzman wrote."The leaders of developing countries are not looking for free money, and they recognise that debt financing is not a one-way street."

How to reduce mass migration?

The strategic imperative for wealthier countries to reduce poorer countries' burden of loan servicing was also stressed by the Carnegie Endowment for International Peace.

Higher incomes in poorer countries would increase demand for imports from richer countries while reducing demand for aid to the mutual benefit of both. It could even help to reduce mass migration, a key demand of many nationalist politicians, such as Donald Trump.

IMF data show that among the countries with conflict and climate risks and significant debt burdens are Afghanistan, Chad and □aiti, from which many people want to flee.

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If Western countries made reforms, such as amending finance laws, reallocating IMF special drawing rights, or buying out Chinese debt held by developing countries, national security and climate risks would be eased.

"Intuitively, it is easy to view debt forgiveness or restructuring as being harmful to creditor countries, since it requires a reduction in the value of assets on creditor balance sheets," said Carnegie.

"However, the 'loss' to the creditor needs to be kept in perspective because in the absence of debt relief, there is no probable scenario in which the debt-distressed country would be able to repay the full liability."

To help sharpen minds at G20, the UN Development Programme noted that it is all too "easy to be persuaded the world is only going downhill" so it summarised in its Signals Spotlight 2024 report some ideas for tackling development and other global challenges.

These include growing recognition that there are alternatives to current economic models that include climate considerations, such as circular or regenerative economies, the potential of AI to narrow development gaps in, for example, agriculture and healthcare, and young people's engagement in democracy in channels other than the ballot box including social media.

"Although only 17% of the UN Sustainable Development Goals are on track to be achieved by 2030, Signals Spotlight proposes that human ingenuity gives grounds for continued optimism," UNDP said.

But for any of these ideas to gain traction, they have to become part of the discourse in the rich world to win support among electorates grappling with their own relative economic insecurity.