# The Growing Debt Burdens of Global South Countries: Standing in the Way of Climate and Development Goals

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# 1. Executive Summary

Nearly 80 low- and middle-income countries are considered by international institutions as being in or at risk of debt distress. Three-fourths of these countries have also been flagged by environmental experts as particularly vulnerable to the effects of climate change. The combined burden of the climate crisis and increasing debt, perpetuated by an unfair international financial architecture, is a recipe for economic and social devastation: as climate disasters strike, these countries are being forced into choosing between servicing debt and saving lives. This report documents how servicing debt is a direct obstacle to these countries' ability to respond to climate disasters and to finance basic services and long-term development needs. As a result, countries are trapped in a vicious cycle which keeps them indebted, perpetuates vulnerability to the effects of climate change, and prevents progress on the Sustainable Development Goals (SDGs). The response so far from the international financial community has been inadequate to help countries break this vicious cycle. A more ambitious response — combining an updating of debt resolution frameworks, debt relief, more grant-based finance, and a new allocation of Special Drawing Rights (SDRs) — is urgently needed.

- **Doubling debt:** The stock of external public debt in low- and middle-income countries stands at over $3 trillion — a doubling since 2010 — and private creditors hold nearly 60 percent of it. A sustained period of low interest rates in advanced economies in the aftermath of the global financial crisis led to increased capital inflows to developing countries as private investors chased higher returns. However, in recent years there have been economic setbacks to these countries due to the effects of the pandemic, the war in Ukraine, and the rapid rise in interest rates as central banks in advanced economies have pivoted to fighting inflation. As a result, nearly 80 countries are considered by international financial institutions as in or at risk of debt distress. But debt from private creditors comes with high interest rates, short maturities, and is difficult to restructure.
- **Climate costs:** Three-fourths of the countries facing debt difficulties are also designated by environmental experts as highly climate vulnerable. These countries face the least responsibility for the climate crisis but are facing the greatest burdens in terms of the impacts of climate disasters.  The costs of climate disasters can be very high, even for countries

generally considered to be more resilient. For instance, Argentina is projected to lose about 3 percent of its income this year from losses of agricultural exports due to a severe drought. The cumulative loss over the past two decades in a group of climate-vulnerable countries is estimated to have added up to about 20 percent of their annual income.

- **Life and debt:** Interest payments on external public debt have gone up sharply since 2010 in low- and middle-income countries relative to their export revenue. In 2021, interest payments in some climate-vulnerable countries, such as Guinea-Bissau, Lesotho, and Sudan, amounted to between 15 and 25 percent of export revenue. A number of countries in or at risk of debt distress — such as Egypt, El Salvador, The Gambia, Ghana, Kenya, Senegal, and Sri Lanka — paid between 6 and 9 percent of their export revenue in interest payments alone. On average, in 16 low-income countries, interest payments amount to about 4 percent of export revenue and over 10 percent of export revenue if principal repayments are included. This year, total debt service is estimated to exceed non-climate-related SDG investment needs for over 100 countries around the globe. The inability to finance non-climate SDGs has direct human costs and also has an adverse impact on climate resilience, as stronger health, food, and other social systems are needed to withstand the effects of climate disasters. In fossil fuel-dependent economies, higher debt service costs force them to delay the energy transition.
- **Inadequate initiatives:** The international response to the climate crisis and the growing risk of debt crisis has been inadequate. The G20's Common Framework for debt restructuring and relief excludes middle-income countries, has seen poor take-up from eligible countries, and does not cover private and multilateral debt, which comprises 70 percent of the debt stock of eligible countries. The IMF's new climate-focused long-term lending program, the Resilience and Sustainability Trust, is also limited in scope, adds to countries' debt burdens, and potentially imposes harmful austerity measures.
- **What will work:** To keep countries from being forced into austerity, debt resolution frameworks need urgent updating and a venue for rapid and fair debt treatment across all creditor classes. In addition, legislative action can compel private investors to access the same restructuring terms as public sector creditors. Debt relief from all creditors and more grant-based finance from the wealthy countries — which caused the climate crisis in the first place — can provide the funds for climate and development needs in low- and middle-income countries. Most importantly, a new SDR allocation would serve as a quick way to give

climate-vulnerable and debt-constrained countries more fiscal breathing room. The August 2021 SDR allocation was effectively used by developing countries to provide urgent fiscal relief and address other vulnerabilities, and a new allocation — which is being championed by civil society and political actors around the world — would be just as effective.

# 2. Introduction

Developing countries continue to face headwinds impeding economic recovery due to the setbacks triggered by the pandemic, Russia's war in Ukraine, and the rapid rise in interest rates led by the Federal Reserve's 11 interest-rate hikes since March 2022. In the fall of 2022, the UN Conference on Trade and Development (UNCTAD) raised the alarm on a debt crisis in the developing world precipitated by negative spillovers from monetary tightening in advanced economies.[1] Economic activity is expected to remain below pre-pandemic levels in much of the developing world, potentially erasing years of progress made in tackling poverty.[2] These challenges come at a crucial juncture with the world already far behind schedule in the effort to achieve the 2030 Sustainable Development Goals (SDGs) and meet the climate targets set in the Paris Agreement.[3]

The sharp increase in US interest rates over the past 18 months has led to increased financial volatility, exchange rate depreciation, and higher borrowing costs for developing countries.[4] Many low- and middle-income countries hold large amounts of foreign currency-denominated debt, mostly in US dollars, and are being severely impacted by sharp changes in global capital flows — exacerbated by an asymmetric global financial system, which also pressures countries to repay their creditors "when they can least afford it."[5]

A growing number of countries have been identified as in or at risk of debt distress in analyses conducted by the International Monetary Fund (IMF) and United Nations Development Program (UNDP). Out of the 79 countries flagged by these two institutions,[6] 60 have also been

1 UNCTAD (2023a).
2 World Bank (2023).
3 UN (2023).
4 UNCTAD (2023b) and World Bank (2023).
5 UNCTAD (2023b).
6 IMF (2023a) and Jensen (2022). The IMF and UNDP have flagged 62 and 54 countries, respectively, to be at moderate and high risk of debt distress, or in debt distress. We counted a total of 79 countries across both analyses. More information on the institutions' methods can be found in the Appendix.

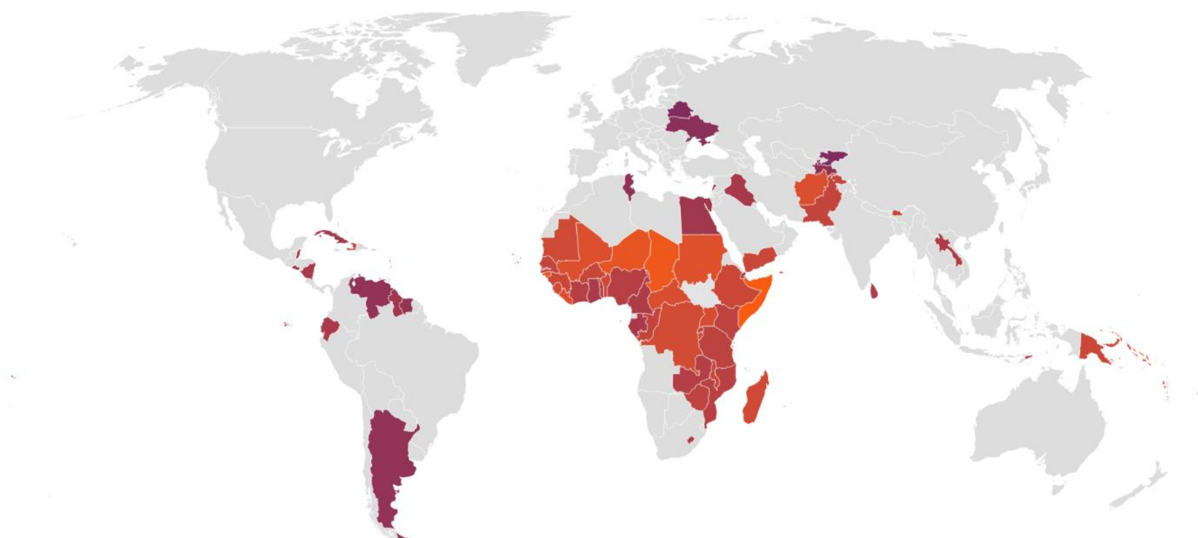
designated by the Notre Dame GAIN Climate Index as highly climate vulnerable.[7] The countries that are both in or at risk of debt distress and particularly vulnerable to climate change can be seen in **Figure 1.**

## Figure 1

## Climate Vulnerability of Low- and Middle-Income Countries Identified as in or at Risk of Debt Distress

ND GAIN Climate Vulnerability Index

more vulnerable -->



Source: IMF (2023a); Jensen (2022); and ND-GAIN (2023).
Note: Out of the 79 low- and middle-income countries in, or at risk of, debt distress, half (39) are in Sub-Saharan Africa, followed by Latin America and the Caribbean (14) and East Asia & the Pacific (11). A total of 61 countries in or at risk of debt distress are highly climate-vulnerable.[8]

More countries are dealing with the physical impacts of climate change and, while low- and middle-income countries generally bear the least responsibility for the climate crisis, they often face the greatest burden in terms of its impacts.[9] The costs of climate disasters can be very high, even for countries generally considered to be more resilient. For example, the drought in Argentina in the spring of 2023 — the country's worst in 60 years — is projected to result in

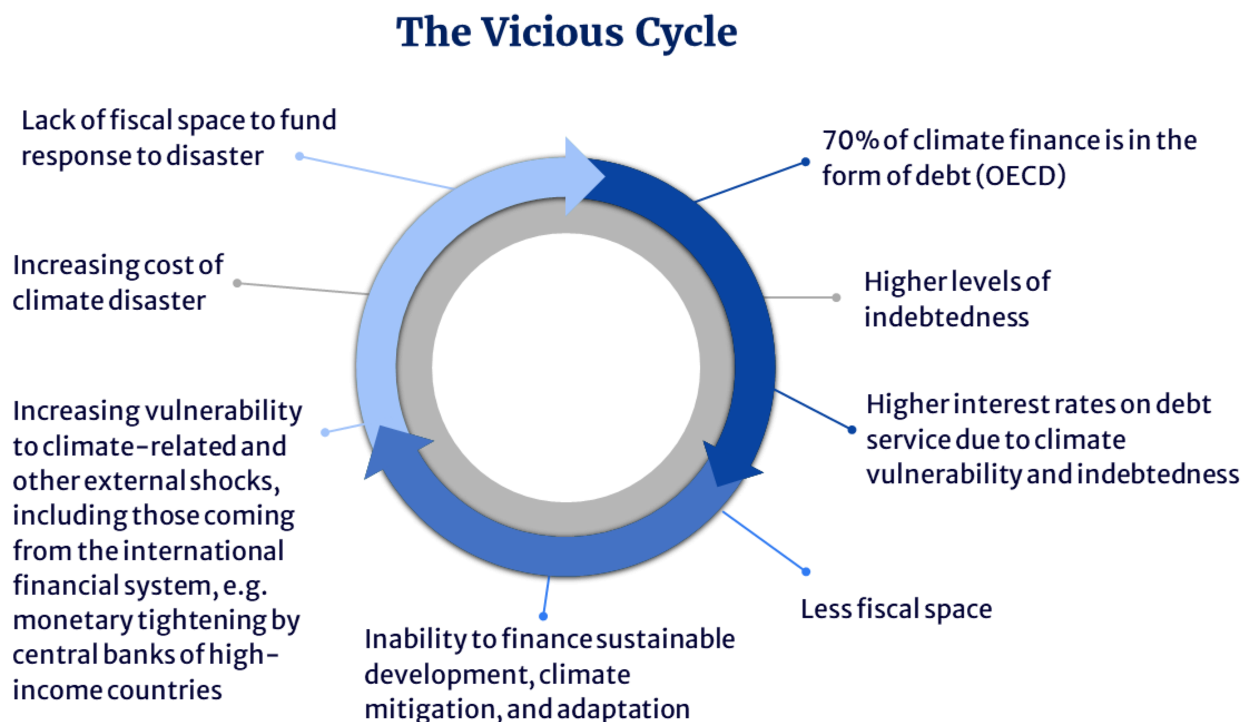
7 ND-GAIN (2023). ND GAIN defines climate vulnerability as the "propensity or predisposition of human societies to be negatively impacted by climate hazards" by assessing "six life-supporting sectors: food, water, health, ecosystem services, human habitat and infrastructure."
8 This does not include South Sudan, St. Vincent and the Grenadines, Kiribati, Marshall Islands, and Tuvalu, for which there is incomplete data in the GAIN Climate Index.
9 Hickel (2020).

about $20 billion in losses to national income, almost three percent of GDP, in 2023 due to a significant decline in exports of grain, soy, and corn.[10]

The SDGs, including climate action, are highly interdependent. Climate change has a direct impact on health, food security, and other basic human needs, while the advancement of social and economic development is key to strengthening resilience against climate shocks and the long-term consequences of climate change.[11] High debt burdens are a direct obstacle to building climate resilience and achieving progress towards the SDGs.

Within the current international financial architecture, the entrenched process which keeps developing countries indebted, prevents progress on the SDGs, and perpetuates climate precarity, has been referred to as "the vicious cycle."[12] This process is shown in **Figure 2.**

## Figure 2
## The Vicious Cycle




10 Cervantes and Avalos (2023).
11 IPCC (2015).
12 See Crotti and Fresnillo (2021), Debt Justice (2022), ActionAid (2023), and Mejía-Silva (2023).

Low- and middle-income countries lack the resources to cover climate-driven losses and to make necessary investments to build climate resilience. The Climate Vulnerable Forum (CVF), an international association of climate-vulnerable countries, has estimated that 55 of its 59 (now 68) members faced losses of $525 billion, or 22 percent of these countries' total 2019 GDP in current US dollars, due to the effects of climate change between 2000 and 2019.[13] Lacking other sources of finance to cover these losses and damages, low- and middle-income countries often have to borrow in order to respond to increasingly severe disasters like floods, droughts, and tropical storms. In fact, 70 percent of all public climate finance is in the form of loans.[14]

The concomitant increase in debt service payments results in less fiscal space for essential spending on climate adaptation, as well as spending on key public goods, including healthcare, education, and infrastructure.[15] The lack of necessary investment in public institutions further erodes a country's ability to respond to future climate-related disasters, perpetuating the vicious cycle.

These issues are widely acknowledged by multilateral institutions, yet the global financial architecture continues to lack an effective mechanism to address sovereign debt problems.[16] Climate experts continuously warn the public of the dire social, economic, and planetary consequences of delaying climate action, yet thus far international financial institutions have failed to propose any effective plans to break the vicious cycle outlined above and develop sustainable forms of financing for climate and development goals.[17]

# 3. Higher Debt in a Changing Interest Rate Environment

External debt increased sharply for many countries in the decade following the 2009 world recession, which was characterized by low interest rates in advanced economies and loose monetary policy globally.  This section provides an overview of the emerging trends in public sector debt owed to foreign creditors and denominated mostly in US dollars and other foreign

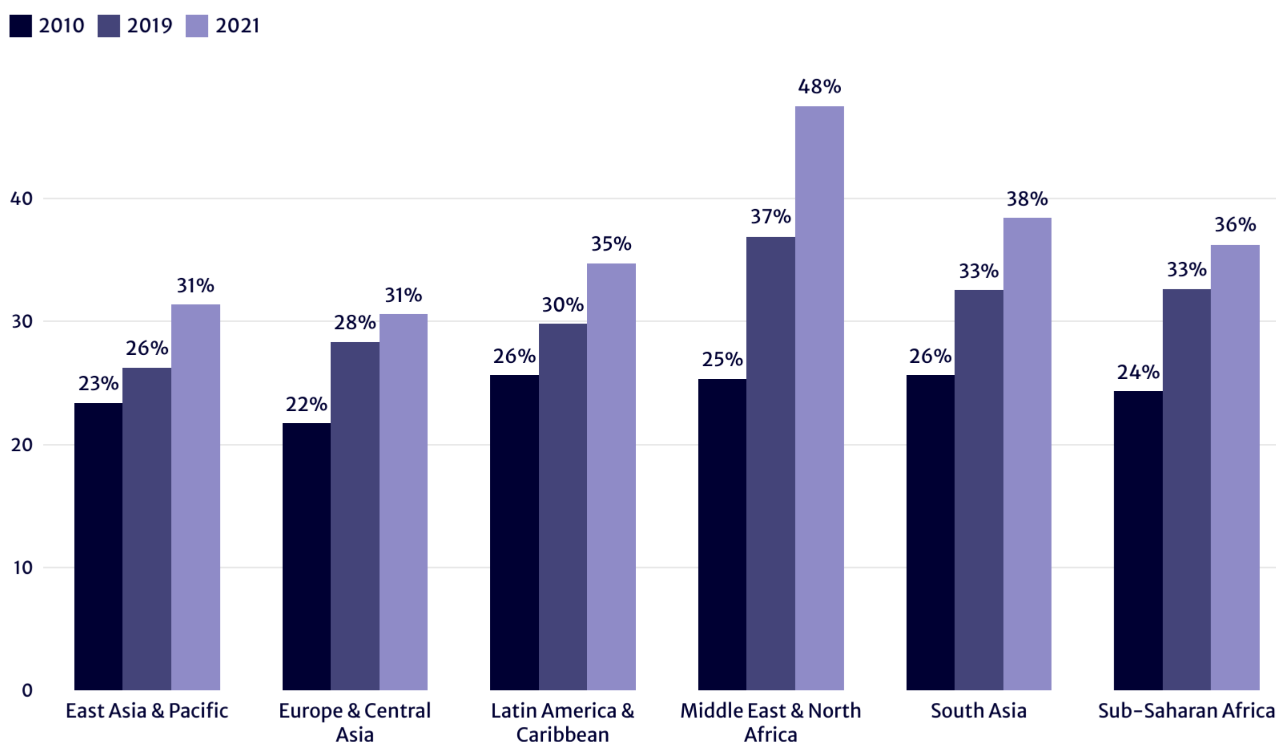
13 V20 (2022).
14 OECD (2022).
15 World Bank (2022a).
16 UN (2021a).
17 Jensen (2022).

currencies, using information made available by the World Bank International Debt Statistics (IDS) database.

The total external public debt stock in low- and middle-income countries doubled from $1.5 trillion to over $3 trillion from 2010–2021. For countries in the Middle East and North Africa (MENA), the average external debt to GDP ratio is 48 percent, and at least 30 percent for countries in all other regions in 2021, as can be seen in **Figure 3**. For countries in MENA, this represents an 88 percent increase since 2010, and an almost 50 percent increase for Sub-Saharan African and South Asian countries relative to GDP. As seen in the figure, the increase in debt precedes the COVID-19 pandemic, which then only further increased the already high level of external borrowing.

## Figure 3

## Average External Public Debt Stock as a Percent of GDP in Low- and Middle-Income Countries

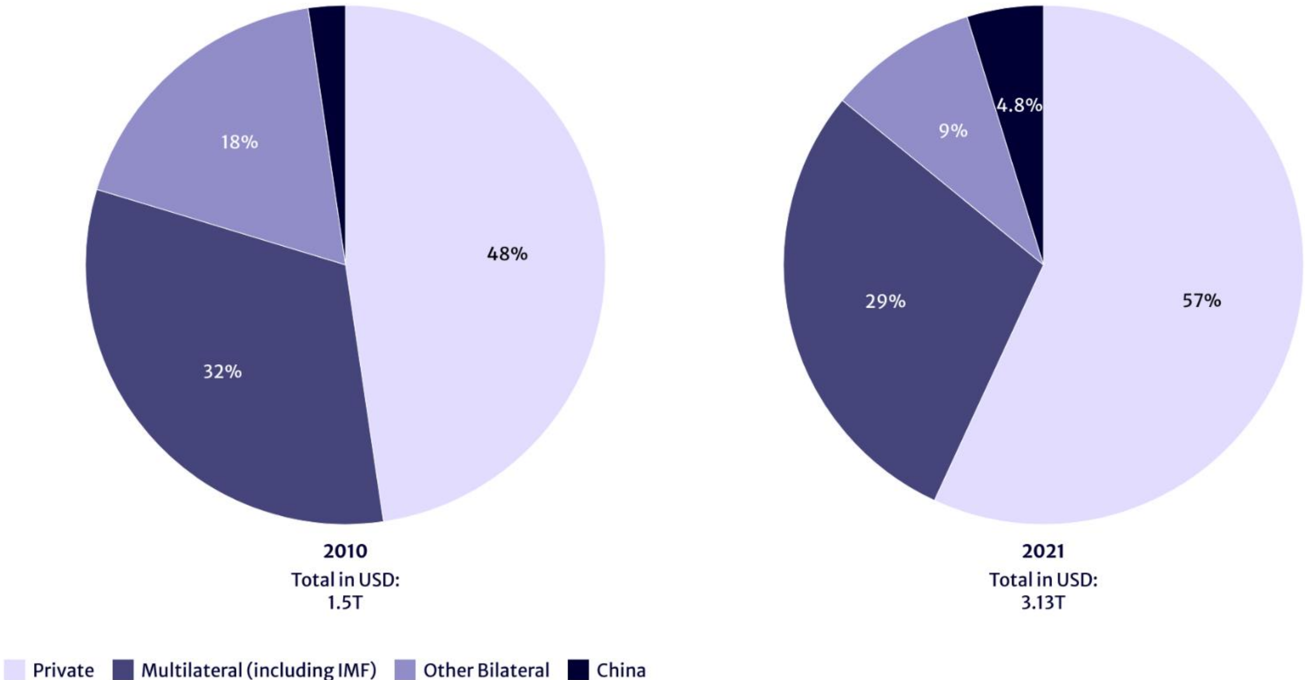



Source: IMF (2023c) and World Bank (2022c): External Public and Publicly Guaranteed Debt Stock, including IMF debt. Authors' calculation.
Note: Calculation includes 113 countries, excluding China.

**Figure 4** illustrates the total external debt stock of low- and middle-income countries, excluding China and disaggregated by creditors. External debt held by private creditors grew the fastest and was estimated at $1.8 trillion in 2021 — more than the total external public debt of low- and middle-income countries in 2010. While the role of China as a creditor has grown significantly in relative terms compared to 2010, overall it holds only 4.8 percent of the total external public debt of low- and middle-income countries as a bilateral lender.

## Figure 4

## Owners of External Public Debt Stock in Low-and Middle-Income Countries



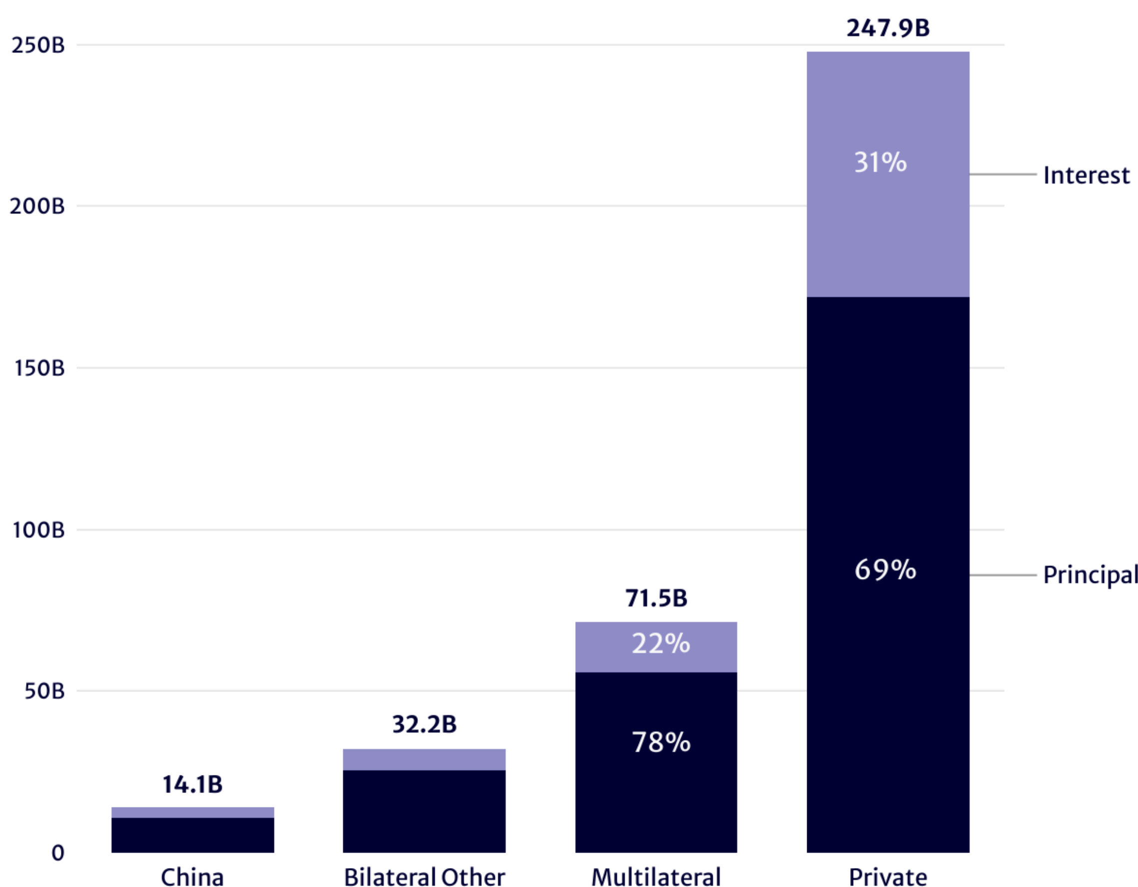

Source: World Bank (2022c): External Public and Publicly Guaranteed Debt Stock, including IMF debt. Authors' calculation.
Note: Calculation includes 118 countries, excluding China.

As can be seen in Figure 4, private creditors are now the largest holders of external public debt in low- and middle-income countries, with 57 percent of the total stock. Debt from private creditors comes with higher interest rates, shorter maturities, and is difficult to restructure, putting extra pressure on developing countries in times of crisis.[18] This is especially true for middle-income countries, which have almost no access to concessional finance and in which the

18 Albinet and Kessler (2022).

majority of the world's poor lives.[19] Payments to private creditors make up two-thirds of the total debt service for low- and middle-income countries, as shown in **Figure 5.**

## Figure 5
## External Public Debt Service, Interest and Principal by Creditor Type, in Low and Middle-Income Countries (2021)




Source: World Bank (2022c): External Public and Publicly Guaranteed Debt Service, including IMF debt. Authors' calculation.
Note: Calculation includes 120 countries, excluding China.

A sustained period of low interest rates in advanced economies in the aftermath of the global financial crisis led to increased capital inflows into developing countries, as investors sought higher returns.[20] However, the aggressive tightening pursued by the US Federal Reserve in the

19 Crotti and Fresnillo (2021); World Bank (2022d).
20 UNCTAD (2023a).

past 18 months has resulted in a reversal of capital flows, increased volatility, currency depreciation, and widening bond yield spreads.[21]

Countries that are identified as climate vulnerable face even worse borrowing terms than others. In a study of CVF member countries, Buhr and Volz found that the average cost of debt in a sample of developing countries was higher by 117 basis points due to their climate vulnerability, meaning that they paid $40 billion in additional interest on government debt from 2008–2018.[22] This includes $62 billion in higher interest payments in both the public and private sectors. They estimated that interest payments would increase by up to $168 billion between 2018–2028.[23]

The growing risk of a global debt crisis is to a large extent driven by rising interest rates around the world, led by the US Federal Reserve, as well as other advanced economies increasing interest rates in response to domestic inflation concerns.[24] Resulting capital flight from low and middle-income countries, and thus declining foreign reserves, have also increased external borrowing costs. In 2022, low- and middle-income countries experienced net outflows of $94 billion, mostly from bond funds.[25] By the end of 2021, approximately 30 percent of low- and middle-income countries had no access to credit markets, up from 10 percent in 2019.[26]

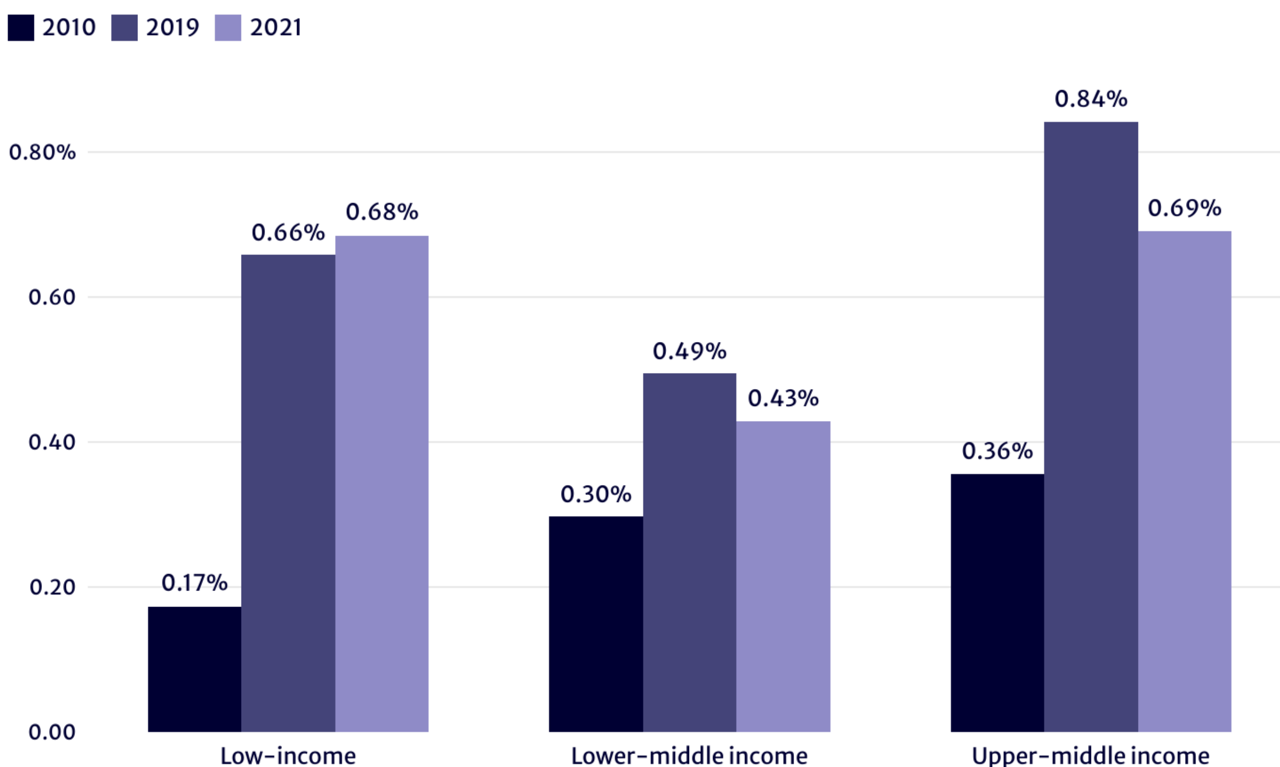
# 4. The Trade-off Between Debt, Development, and Climate Resilience

The rise in external borrowing means that the resources spent servicing foreign debt have also gone up across the developing world. As shown in **Figure 6**, since 2010, interest payments have quadrupled for low-income countries relative to GDP. They have also increased by 44 percent and 94 percent in lower-middle-income and upper-middle-income countries, respectively.

21 UNCTAD (2023a).
22 Buhr and Volz (2018).
23 Buhr and Volz (2018).
24 UNDESA (2023) and AfD (2022).
25 UNCTAD (2023b).
26 Bolton et al. (2022).

## Figure 6

## Average Interest Payments on External Public Debt as a Percent of GDP in Low- and Middle-Income Countries




Source: IMF (2023c) and World Bank (2022c): External Public and Publicly Guaranteed Debt Service, including IMF debt. Authors' calculation.
Note: Calculation includes 114 countries (22 low-income, 50 lower-middle-income, and 42 upper-middle-income, excluding China).

Given global economic conditions and rising interest rates, debt servicing costs have increased substantially since 2021, and will likely remain elevated to dangerous levels for many countries beyond 2024.[27] During good economic times, countries are able to roll over principal payments with ease. However, in the current context of increased risk and distress, access to international markets is increasingly limited, meaning that some countries make principal payments as well. Further, the cost of borrowing is higher for those with access, increasing the resources spent on servicing debt. Total debt service, including both interest and principal payments, reached 2 percent of GDP on average for low-income countries in 2021.

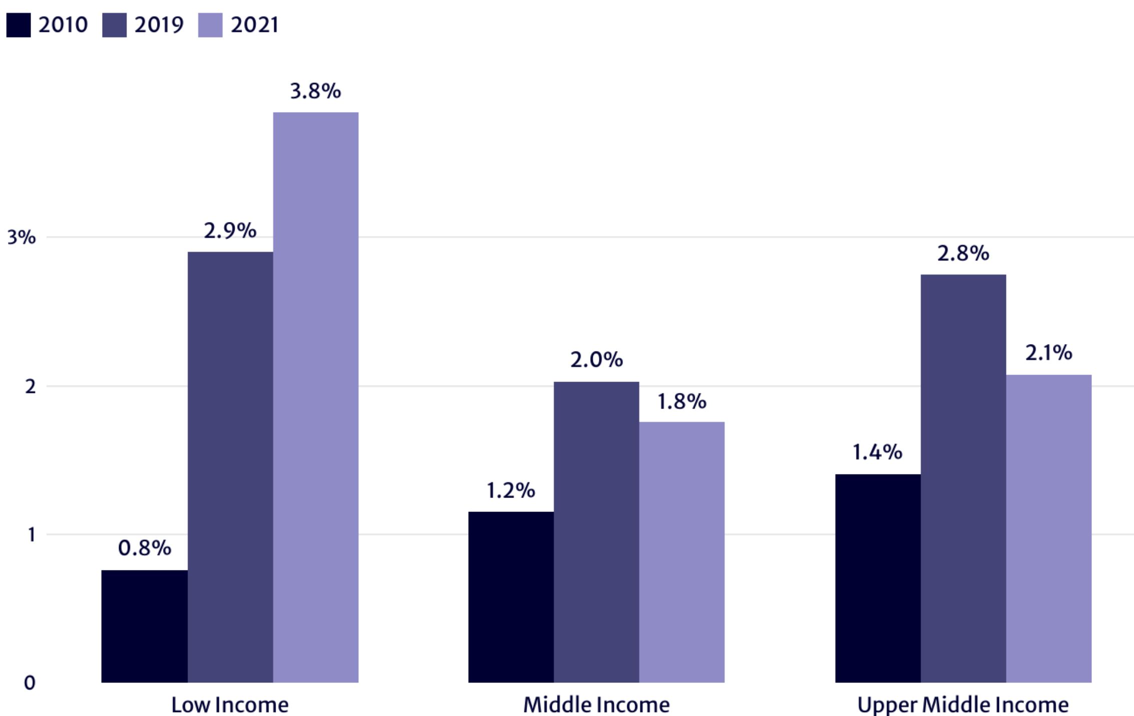
27 Albinet and Kessler (2022).

Interest payments have also increased significantly relative to export revenue, one of the main sources of foreign currency reserves in low- and middle-income countries. This erosion of foreign reserves by high debt payments can threaten a country's balance of payments stability, as well as reduce its ability to cover the cost of necessary imports and maintain financial stability.

As can be seen in **Figure 7**, interest payments on external public debt have quintupled relative to export revenue in low-income countries since 2010. They have increased by about 50 percent in the lower-middle income and upper-middle income categories. Low-income countries, on average, paid close to 4 percent of export revenue in interest payments alone in 2021. Including principal repayments, total debt service cost over 11 percent of export revenue on average in low-income countries. **Figure 8** shows that climate-vulnerable countries like Sudan, Guinea-Bissau, and Lesotho paid 25.5 percent, 16.4 percent, and 16 percent of their export revenue on interest payments in 2021, respectively.

## Figure 7

## Average Interest Payments on External Public Debt as a Percent of Export Revenue in Low- and Middle-Income Countries




Source: World Bank (2022c): External Public and Publicly Guaranteed Debt Service, including IMF debt. Authors' calculation.
Note: Calculation includes 105 countries (16 low-income, 49 lower-middle-income and 40 upper-middle-income, excluding China).

**Figure 8**

**Low- and Middle-Income Countries in or at Risk of Debt Distress by Interest Payments on External Public Debt to Export Revenue Ratio (2021)**

| Country | IMF Risk (2023) | UNDP Risk (2022) | Interest/Exports (2021) |
|---|---|---|---|
| Sudan | In debt distress | N/A | 25.5% |
| Guinea-Bissau | High | High risk of distress | 16.4% |
| Lesotho | Moderate | N/A | 16.0% |
| Sri Lanka | N/A | 1.3 | 8.9% |
| Ghana | In debt distress | 4 | 8.2% |
| El Salvador | N/A | 3.3 | 8.1% |
| Kenya | High | 7.3 | 7.7% |
| Gambia, The | High | High risk of distress | 7.4% |
| Egypt, Arab Rep. | N/A | 7.3 | 6.8% |
| Senegal | Moderate | N/A | 6.2% |

Source: IMF (2023a); Jensen (2022); and World Bank (2022c): External Public and Publicly Guaranteed Debt Service, including IMF debt. Authors' calculation.

# 5. External Public Debt Service Compared to SDG Investment Needs

Using estimates for SDG investment needs and contrasting them with external public debt service reveals that total debt service will exceed non-climate-related SDG investment needs for 102 countries in 2023.[28] More than half of these countries (57) are in or at risk of debt distress. Interest payments alone will exceed investment needs in seven countries, as shown in **Figure 9.**

28 Authors' calculation according to data reproduced from Ramos et al. (2023), and World Bank (2022b).

## Figure 9

## Number of Countries in which External Public Debt Service Exceeds Climate and other SDG Investment Needs (2023 Estimate)

| Category | Interest Only | Total Debt Service |
|---|---|---|
| Climate investment needs | 2 | 39 |
| SDG investment needs (except climate) | 7 | 102 |

Source: Authors' calculation according to World Bank (2022c), and Ramos et al. (2023).
Note: Estimates of investment needs are based on aggregates scaled to GDP.

Moreover, in the last decade, external debt service has consistently increased compared to spending on education and health in low- and middle-income countries, according to UNCTAD.[29] The inability to finance non-climate SDGs impacts climate resilience, as stronger health, food, and other social systems are better able to withstand shocks from climate disaster.

Not only do high external debt service payments crowd out necessary social investment, but they also have a direct impact on a country's ability to invest in climate needs. In 2023, external public debt service is projected to exceed climate investment needs in 39 low- and middle-income countries, as shown in Figure 9.[30] Most of these countries (32) are in or at risk of debt distress.

In this calculation, climate investment represents adaptation and resilience needs, as well as the energy transition away from fossil fuels.[31] Regarding adaptation in particular, Bolton et al. report that costs exceed fiscal space in 22 out of 29 low-income countries that have published estimates.[32]

High levels of debt servicing also push fossil fuel-dependent economies to delay any possible energy transition.[33] Financing external debt requires the accumulation of foreign exchange reserves, which for many countries is obtained predominantly through the export of fossil fuels and other extractive industries, forcing countries to rely on these sectors. Indeed, ten percent of

29 UNCTAD (2023b).
30 Authors' calculation according to data reproduced from Ramos et al. (2023), and World Bank (2022b).
31 Ramos et al. (2023).
32 Bolton et al. (2022).
33 Mejía-Silva (2023).

countries in or at risk of debt distress are fossil fuel-dependent economies which would require significant investment for a just and sustainable transition.[34]

# 6. Not Meeting the Moment

As has been shown, given the exceedingly burdensome debt situation in low- and middle-income countries, many are unable to finance climate adaptation or energy transition needs without perpetuating the vicious cycle. Recognizing the need for climate finance, the G20 countries in 2010 pledged to mobilize $100 billion per year by 2020 through the United Nations Framework Convention on Climate Change (UNFCCC). However, only $83.3 billion— less than one year's pledge — had been allocated in 2020, mostly in the form of loans.[35]

The true cost to the developing world is much higher, with adaptation costs in low- and middle-income countries alone reaching upwards of $340 billion per year by 2030.[36] Currently, only about $29 billion in funding is provided each year by wealthier countries.[37] The United Nations Environmental Programme (UNEP) estimates that the adaptation financing gap in developing countries is up to 10 times higher than international adaptation financial flows and will likely increase.[38]

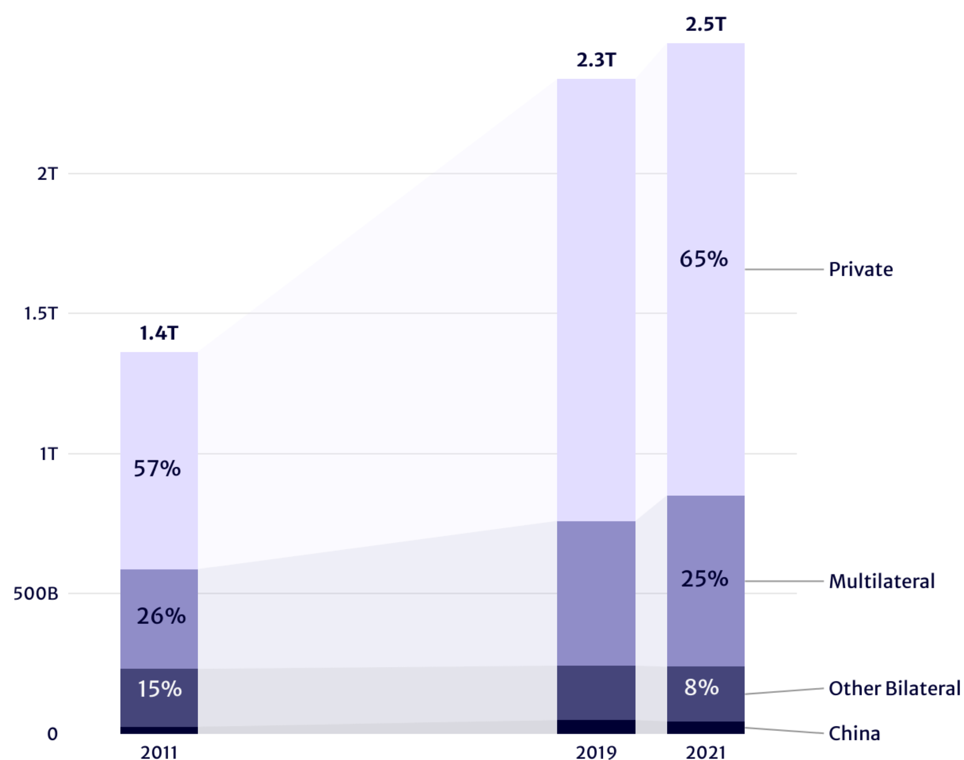
Against this backdrop, the institutional and global response to the challenges faced by developing countries to the intersecting climate crisis and coming debt crisis has been insufficient relative to their scope and existential consequences. Recent multilateral initiatives have done little to provide meaningful relief, and in some cases, have perpetuated indebtedness, keeping countries trapped in the same vicious cycle.

In 2020, the G20 launched the Debt Service Suspension Initiative (DSSI) which offered a limited number of low-income countries the option to suspend payments on bilateral debt at the height of the pandemic. DSSI was followed by the Common Framework (CF) which proposed a venue for countries to seek restructuring and relief post-DSSI.[39] The program, however, does not cover debt from private and multilateral creditors, which comprises the majority of low- and middle-income countries' external debt stock — approximately 70 percent in 2021 for those that are eligible, as shown in **Figure 11**.

34 Coffin, Dalman, and Grant (2021); IMF (2023a) and Jensen (2022); and authors' analysis.
35 OECD (2022).
36 UNEP (2022).
37 UNEP (2022).
38 UNEP (2022).
39 G20 Italy (n.d.).

## Figure 10

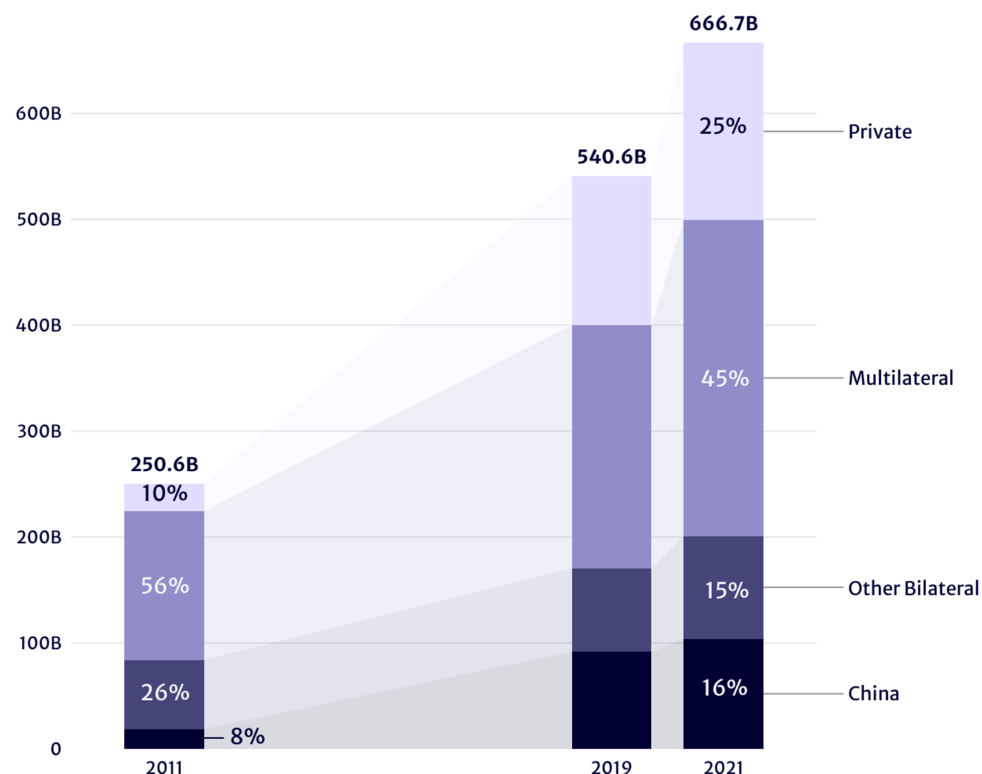
## The Composition of External Public Debt Stock of DSSI-CF Ineligible LICs and MICs (excluding China) (2011-2021)




Source: World Bank (2022c): External Public and Publicly Guaranteed Debt Stock, including IMF debt. Authors' calculation.
Note: Calculation includes 51 countries, excluding China.

## Figure 11

## The Composition of External Public Debt Stock by Creditor Type for DSSI-CF Eligible Countries (2011-2021)




Source: World Bank (2022c): External Public and Publicly Guaranteed Debt Stock, including IMF debt. Authors' calculation.
Note: There are 73 DSSI-CF eligible countries. This figure includes 67 for which data is available.

Only four countries have signed up to the Common Framework: Ethiopia, Chad, Ghana, and Zambia, and the ensuing process has been slow to deliver any results. Further, middle-income countries, represented in **Figure 10**, are ineligible for the CF and concessional financing more generally, despite having significant climate and development needs.

Other programs and recent concessional instruments, with the exception of the August 2021 allocation of Special Drawing Rights (SDRs), have similarly failed to mitigate the crisis. The Catastrophic Containment Trust (CCRT), launched in 2015, provides countries with temporary relief from their repayments to the IMF after a disaster, but its capacity is insufficient compared to the scope of climate-related catastrophes in low- and middle-income countries. Concessional and long-term lending instruments like the IMF's Resilience and Sustainability Trust (RST) and Poverty Reduction and Growth Trust (PRGT) are also limited in scope, add to countries' debt burdens, and potentially come with harmful conditionality, such as austerity measures.[40] The August 2021 allocation of $650 billion in SDRs, on the other hand, provided significantly more support to developing countries during the pandemic without creating more debt, despite their somewhat uneven distribution, which allocated a large part to advanced economies, as can be seen in **Figure 12**.

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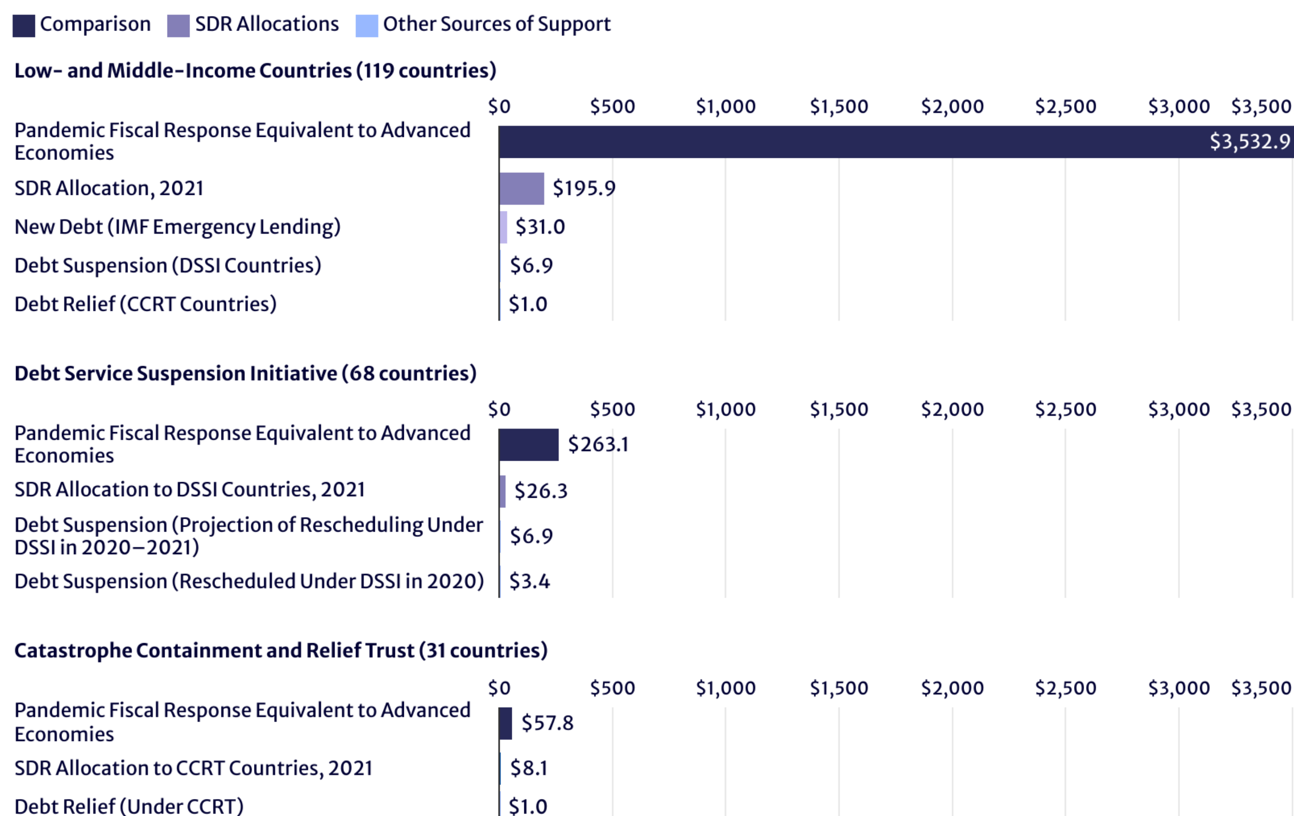
40 Vasic-Lalovic (2022).

## Figure 12

# SDR Allocation in 2021, and Other Sources of Support, by Country Groupings (USD Billions)




Source: Reproduced from Cashman, Arauz, and Merling (2022).

Higher income countries can rely on measures such as currency swaps to access liquidity during a crisis like the COVID-19 pandemic, enabling a comprehensive fiscal response, as shown in Figure 12. On the other hand, many lower- and middle-income countries continue to have little option other than seeking IMF loans.[41] Beyond a few emergency loans limited in size and scope, IMF loans come with conditionalities, and generally impose austerity measures such as cuts to

41 Mühlich et al. (2022).

health care, education, and food subsidies. In many cases, they have contributed to the weakening of countries' capacity to respond to external shocks, including climate change.[42] Out of the 79 countries currently in or at risk of debt distress, 56 had IMF programs in the last 20 years, most of which (49) had repeat programs.[43]

# 7. The Urgency of Raising Ambition

Increasing debt burdens, combined with the severe effects of the climate crisis in low- and middle-income countries, mean that, without action, these countries "will be forced to implement austerity measures on an unprecedented scale."[44] Immediate measures to alleviate the burden and give countries additional breathing room are needed, along with a fundamental reform of the international financial architecture. Rising external debt burdens, accompanied by growing debt service costs, are leading to increased debt distress in the developing world. Thus, highly indebted developing countries have no path out of the current crisis without a multilateral and global response.

Debt resolution frameworks need urgent updating, and require a reliable platform for rapid and fair debt treatment across all creditor classes along the lines of a decade-old UN proposal.[45] A full suspension of debt payments to creditors is a key element of such proposals, aiming to incentivize creditors to seek a speedy resolution.[46] Additionally, legislative action, along the lines of a bill recently introduced in New York State, can compel private creditors to access the same restructuring terms as those applied to public sector creditors, a measure which would effectively extend the scope of initiatives, such as the CF.[47]

Debt relief can unlock important resources that would otherwise go to debt payments and can be used instead for climate and development needs. A UNDP proposal estimates that a 30 percent haircut of 2021 public external debt stock could lower debt service payments from 2022–2029 by between US$44 billion and $148 billion for the 52 most debt-vulnerable economies.[48]

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42 Ortiz and Cummins (2022).
43 Includes IMF programs from 2001–2022, excluding credit lines and precautionary programs. IMF (n.d.).
44 Crotti and Fresnillo (2021).
45 UNCTAD (2015) and UNCTAD (n.d.).
46 See Jensen (2022) and Ramos et al. (2023).
47 OHCHR (2023).
48 Molina and Jensen (2023).

Another proposal, Debt Relief for Green and Inclusive Recovery (DRGR), also calls for comprehensive debt relief across all creditor classes, including $30 billion in debt suspension and a "Brady bond-like" guarantee facility as an incentive for private creditors.[49]

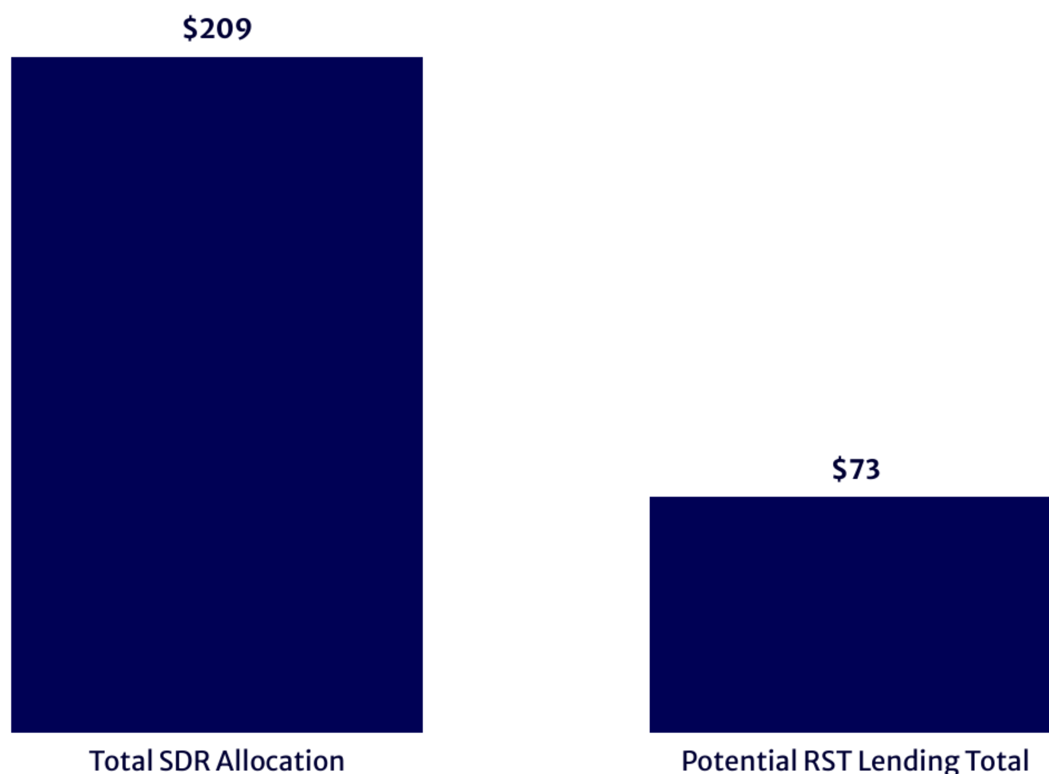
A comprehensive response to the risk of debt crisis, especially for climate-vulnerable countries, would also include significantly more grant-based finance for climate adaptation, energy transition, and other SDGs. Wealthy countries, bearing the lion's share of responsibility for the climate crisis, must take responsibility and allocate appropriate resources to low- and middle-income countries without imposing more debt and perpetuating the vicious cycle. At the UNFCCC, wealthy countries have committed to a "Loss and Damage" Fund to provide such resources; once created, they must provide the fund with the financing to deliver real support to developing countries.[50]

At the IMF, the Resilience and Sustainability Trust (RST) was established to provide long-term loans for countries seeking to invest in climate resilience and pandemic preparedness.[51] The facility was set up in response to a call from G20 countries to create a facility through which advanced economies could "re-channel" parts of their SDR allocations to developing countries, pledging $100 billion worth in funding.[52] However, countries can only access this facility in parallel with a traditional conditional IMF program, and regular access to the RST is limited to the equivalent of 75 percent of a country's IMF quota or SDR 1 billion, whichever is lower.[53]

49 Ramos et al. (2023).
50 UNFCCC (2022).
51 IMF (2022).
52 G20 Italy (2021).
53 IMF (2022).

## Figure 13

## Resources from a New SDR allocation vs. Potential Lending from the RST




Source: IMF (2021), (2022), and (2023b). Authors' calculation.
Note: Includes 153 countries potentially eligible for RST lending under Normal Access, on the condition of having an existing IMF program. The exchange rate SDR 1 = 1.33282 USD was used to calculate potential RST lending. The exchange rate SDR 1 = 1.42426 USD was used to calculate the total 2021 SDR allocation.

As shown in **Figure 13**, despite the uneven distribution of SDR allocations, which allots a large share to advanced economies, developing countries would still immediately receive far more financial support from a new general allocation, equivalent to $650 billion, than from what they would be able to potentially borrow, over 20 years, from an RST program.

In the short term, a new allocation of Special Drawing Rights (SDRs) would serve as a quick way to provide relief to all developing countries, giving climate-vulnerable and debt-constrained countries more breathing room. The IMF took an important step in August of 2021 by issuing $650 billion in SDRs — which come with no strings attached, no cost to taxpayers, and are ready

for immediate use — to its member states to help them address the economic fallout of the COVID-19 pandemic.

The August 2021 allocation provided low- and middle-income countries with immediate, effective fiscal relief, allowing countries to address balance of payments constraints, decrease exchange rate risk, improve borrowing terms, and better respond to the external shock of the pandemic.[54] In 79 of the 105 countries that have used their allocated SDRs, a total of $10.9 billion was used to pay down debt owed to the IMF.[55] Calls for a new SDR allocation have been made by civil society and political actors from around the world. They have urged the IMF, the Biden administration, and the US Treasury Department to rapidly act to authorize a new allocation.[56]

In addition to a new allocation of SDRs, the IMF should once and for all eliminate surcharges — punitive fees on borrowing countries, which increase interest rates by two or three percentage points and are projected to cost borrowers $2 billion per year.[57] Meant to incentivize early repayment, IMF surcharges instead create an undue burden for middle-income countries that are already struggling to provide basic public services and respond to increasingly severe climate disasters, at the very time when these countries have the most liquidity constraints.[58] Two of the countries most burdened by surcharges, Pakistan and Egypt, are facing recovery from climate catastrophe and a soaring food price crisis, while paying $142 million and $306 million in surcharges per year, respectively.[59] Ukraine, in the midst of war, will pay $316 million each year.

# 8. Conclusion

The combined burdens of the climate crisis and increasing debt troubles, exacerbated by an unfair and inefficient global financial architecture, are a recipe for continued economic, social, and environmental devastation across the globe. Climate disasters will continue to strike with greater force and frequency, forcing low- and middle-income countries to choose between servicing debt and saving lives.

54 Arauz and Cashman (2022).
55 Arauz and Cashman (2022).
56 Shalal (2022); CPC (2022); Muchina and Woods (2023).
57 Amsler and Galant (2023).
58 Amsler and Galant (2023).
59 Amsler and Galant (2023).

As this report has demonstrated, the sharp increase in external public debt is a direct obstacle to a country's ability to respond to climate catastrophes and invest in climate adaptation as well as to finance basic services and long-term development needs. This year, total debt service is estimated to exceed climate investment needs for 39 countries and non-climate-related SDG investment needs for over 100 countries around the globe. Interest payments alone amounted to about 4 percent of export revenue on average for low-income countries in 2021 and 10 percent if principal payments are included. The erosion of foreign currency reserves threatens balance of payments stability, as well as countries' ability to cover the cost of necessary imports. Further, the significant lack of grant-based climate finance from wealthy countries means that low- and middle-income nations have little choice but to borrow in order to cover the increasing cost of climate disasters, thus becoming more indebted and perpetuating a vicious cycle that blocks countries' progress on the SDGs and perpetuates their inability to adequately address climate change.

Highly indebted developing countries have no path out of the current crisis without a robust multilateral and global response; thus far that response has been wholly inadequate. A fundamental reform of the international financial architecture, as well as far-reaching debt restructuring measures, debt relief from all creditor classes, and more grant-based finance from wealthy countries, are imperative to ending the vicious cycle. In the immediate term, a new SDR allocation would provide immediate, effective support to climate-vulnerable and debt-constrained countries, providing them with much-needed additional fiscal space for taking urgent action.

# 9. Methodology

External Public Debt

External public debt stocks, principal, and interest payments are calculated using the World Bank's International Debt Statistics. External public debt covers public and publicly guaranteed debt denominated in a foreign currency and not issued under domestic law. This category includes the external obligations with maturities longer than one year of all public sector debtors, including the state-owned enterprises, and the debt held by multilateral, bilateral, and

private creditors. Credit outstanding to the IMF, without counting SDR allocations, is added to this data under multilateral debt.

IMF and UNDP Debt Risk Analyses

The IMF uses a debt sustainability framework that "classifies countries based on their assessed debt-carrying capacity, estimates threshold levels for selected debt burden indicators, evaluates baseline projections and stress test scenarios relative to these thresholds, and then combines indicative rules and staff judgment to assign risk ratings of external debt distress."[60] Debt burden indicators include the present value of debt to GDP, present value of debt to exports, debt service to revenues, and debt service to exports.

The 54 countries identified in the UNDP analysis include "all low- and middle-income countries with an average numeric credit rating of less than six, or if no credit rating a DSA-risk rating of either 'in distress' or 'high risk of distress' or countries with sovereign bond spreads trading at more than 10 pp to US Treasury bonds." The analysis also includes countries which are "on the brink of being included among the most vulnerable as per their average credit rating."[61]

Climate Vulnerability

The number of countries which are "highly vulnerable" to climate change is calculated using ND GAIN's climate "vulnerability" indicator, which measures the "propensity or predisposition of human societies to be negatively impacted by climate hazards" by assessing "six life-supporting sectors: food, water, health, ecosystem services, human habitat and infrastructure," on a scale of 0–1.[62]

SDG and Climate Investment Needs

Estimates for global SDG and climate investment needs in 2023 are reproduced from Ramos et al. (2023)'s recent analysis and compared with external public debt service per country.

60 IMF (2018).
61 Jensen (2022).
62 Chen et al. (2015).

# 10. Appendix

## Appendix 1.1

## The 79 Low-and Middle-Income Countries in or at Risk of Debt Distress

| Country | IMF Risk (2023) | UNDP Risk (2022) | Interest/Exports (2021) |
|---|---|---|---|
| Afghanistan | High | High risk of distress | N/A |
| Argentina | N/A | 3.7 | 2.9% |
| Belarus | N/A | 1.3 | 1.7% |
| Belize | N/A | 4.5 | 1.6% |
| Benin | Moderate | N/A | 2.7% |
| Bhutan | Moderate | N/A | 5.7% |
| Burkina Faso | Moderate | 5 | 0.7% |
| Burundi | High | High risk of distress | N/A |
| Cabo Verde | Moderate | N/A | 2.2% |
| Cameroon | High | N/A | 3.7% |
| Central African Republic | High | High risk of distress | N/A |
| Chad | High | In distress | N/A |
| Comoros | High | High risk of distress | 1.0% |
| Congo, Dem. Rep. | Moderate | 5.5 | N/A |
| Congo, Rep. | In debt distress | 4.7 | N/A |
| Côte d'Ivoire | Moderate | N/A | 4.4% |
| Cuba | N/A | 2 | N/A |
| Djibouti | High | High risk of distress | 0.4% |
| Dominica | High | High risk of distress | 5.5% |
| Ecuador | N/A | 5 | 5.1% |
| Egypt, Arab Rep. | N/A | 7.3 | 6.8% |
| El Salvador | N/A | 3.3 | 8.1% |
| Ethiopia | High | 4 | 4.9% |
| Gabon | N/A | 5.5 | N/A |
| Gambia, The | High | High risk of distress | 7.4% |
| Ghana | In debt distress | 4 | 8.2% |
| Grenada | In debt distress | 1 | 3.7% |
| Guinea | Moderate | N/A | 0.5% |
| Guinea-Bissau | High | High risk of distress | 16.4% |
| Guyana | Moderate | N/A | 1.4% |

## Appendix 1.2

# The 79 Low-and Middle-Income Countries in or at Risk of Debt Distress

| Country | IMF Risk (2023) | UNDP Risk (2022) | Interest/Exports (2021) |
|---|---|---|---|
| Haiti | High | High risk of distress | 0 |
| Iraq | N/A | 5.7 | N/A |
| Kenya | High | 7.3 | 8 |
| Kiribati | High | High risk of distress | N/A |
| Kyrgyz Republic | Moderate | 6 | 1 |
| Lao PDR | In debt distress | 3 | 2 |
| Lebanon | N/A | 1 | 0 |
| Lesotho | Moderate | N/A | 16 |
| Liberia | Moderate | N/A | 1 |
| Madagascar | Moderate | N/A | 1 |
| Malawi | In debt distress | High risk of distress | 1 |
| Maldives | High | 5.5 | 2 |
| Mali | Moderate | 4 | 1 |
| Marshall Islands | High | High risk of distress | N/A |
| Mauritania | Moderate | High risk of distress | 2 |
| Micronesia, Fed. Sts. | High | High risk of distress | N/A |
| Mozambique | High | 4.7 | 1 |
| Nicaragua | Moderate | N/A | 2 |
| Niger | Moderate | N/A | 4 |
| Nigeria | N/A | 6.7 | 2 |
| Pakistan | N/A | 6 | 5 |
| Papua New Guinea | High | N/A | 1 |
| Rwanda | Moderate | N/A | 3 |
| Samoa | High | High risk of distress | 2 |
| São Tomé and Principe | In debt distress | In distress | 1 |
| Senegal | Moderate | N/A | 6 |
| Sierra Leone | High | High risk of distress | N/A |
| Solomon Islands | Moderate | 5 | 0 |
| Somalia | In debt distress | In distress | N/A |
| South Sudan | High | High risk of distress | N/A |

## Appendix 1.3

# The 79 Low-and Middle-Income Countries in or at Risk of Debt Distress

| Country | IMF Risk (2023) | UNDP Risk (2022) | Interest/Exports (2021) |
|---|---|---|---|
| Sri Lanka | N/A | 1.3 | 8.9% |
| St. Lucia | Moderate | N/A | 2.7% |
| St. Vincent and the Grenadines | High | N/A | 5.0% |
| Sudan | In debt distress | N/A | 25.5% |
| Suriname | N/A | 1.7 | N/A |
| Tajikistan | High | 6 | 1.9% |
| Tanzania | Moderate | N/A | 3.3% |
| Timor-Leste | Moderate | N/A | 0.7% |
| Togo | Moderate | N/A | 1.9% |
| Tonga | High | High risk of distress | 0.8% |
| Tunisia | N/A | 4.5 | 3.0% |
| Tuvalu | High | High risk of distress | N/A |
| Uganda | Moderate | N/A | 4.1% |
| Ukraine | N/A | 3.3 | 2.5% |
| Vanuatu | Moderate | N/A | 1.6% |
| Venezuela, RB | N/A | 1 | N/A |
| Yemen, Rep. | Moderate | N/A | N/A |
| Zambia | In debt distress | 1.3 | 0.7% |
| Zimbabwe | In debt distress | In distress | 0.4% |

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