G20 must commit to debt relief

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A photo dated Jan 10, 2024 shows a woman selling items on the streets of Kumasi, Ghana. The World Bank warned in a new report that poor countries will be stuck in economic 'purgatory' without debt relief. (Photo: New York Times)

As G20 leaders met in Johannesburg last month, they faced a grim reality: many developing-country governments are spending more than they can afford on debt service. To keep funds flowing to foreign creditors, policymakers have been forced to cut spending on education, health care, and infrastructure. These countries have so far avoided default, but at the expense of their own development.

The fact that governments across Africa, Asia, and Latin America must close hospitals and cancel school-lunch programmes to service their debt is not only a moral failure; it is also a strategic one. A world where countries cannot invest in sustainable growth and development will struggle to achieve stability, prosperity, and climate resilience.

Five years ago, amid the Covid-19 pandemic, the G20 launched the Common Framework for Debt Treatment to help heavily indebted countries restructure their debts in an orderly, prompt, and equitable manner. But the promised relief has not materialised. According to the International Monetary Fund and the World Bank, 37 out of 67 low-income countries eligible for concessional funding are in or at high risk of debt distress, yet only four -- Chad, Zambia, Ghana, and Ethiopia -- have applied for restructuring under the mechanism. Their experiences have revealed the weaknesses of the Common Framework: it offers far too little relief -- and too late.

In response, the G20 has outsourced the problem to technocratic bodies, tasking them with accelerating the process and increasing relief. While this technical work is important, it is not enough. Debtor countries still fear that the policy is half-hearted. Policymakers now talk less about a "debt crisis" and more about a "debt morass" -- a world where everyone is stuck, waiting for a change that never comes.

Meanwhile, foreign private creditors have been withdrawing their capital from developing economies since 2022. The message is clear: the risks are too high, and no meaningful solution is in sight. When investors leave, governments are left scrambling to borrow from other sources.

Multilateral development banks (MDBs) and the IMF have come to the rescue. As a result, their share of developing countries' external debt has soared, exceeding 75% in around 20 countries. This creates a vicious cycle: when multilateral organisations that don't take a haircut in restructurings hold most of a country's sovereign debt, private creditors become even more reluctant to invest.

To escape the debt morass, G20 leaders must restore confidence in the Common Framework and act with a sense of urgency. That means reassuring debtor countries that applications for relief will be handled quickly, fairly, and generously. The recent G20 leaders' communiqué, and their finance ministers' declaration on debt sustainability, merely reiterated the technical work and thus fell short of what is needed. Stronger commitments must be backed by tangible action.

First, G20 leaders must reduce the stigma of restructuring. When debt becomes a drag on growth, seeking relief and committing to reform should be seen as responsible economic governance.

Second, relief must be meaningful. A token reduction that leaves countries with still-limited fiscal space only prolongs the crisis. G20 leaders must proactively replenish debt-relief funds. While taxpayers in high-income countries, many with their own ballooning debts, may balk at these costs, continuing to bail out private creditors indirectly through MDBs is also expensive. The sooner debt relief is provided, the cheaper it will be.

Third, private creditors should be required to do their part. Based on the comparability-of-treatment principle, every dollar of debt relief from official creditors must be matched by private creditors. G20 leaders must support national legislation that enforces this policy. The self-regulatory approach taken over the past two decades by bondholders has not worked with other private creditors -- and all it takes is a single holdout creditor to scupper a debt-restructuring process.

Some argue that debt relief will make borrowing more expensive for debtor countries in the future. The reality is their borrowing costs are already prohibitively high. Cleaning up their balance sheets would attract investors more quickly than implementing austerity measures. Investors, having incurred losses, will become more discerning and demand risk premiums from countries that fail to improve their debt management -- a welcome incentive for good governance.

The G20 must contend with a confluence of geopolitical, climate, and economic shocks. But the developing world's debt morass cuts across them all. Only by addressing this underlying challenge can we hope to overcome all the others. G20 leaders have already committed to debt relief. Now they need the courage to finish the job.

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