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Debt Distress and Development Finance in the COVID-19 Era

YAN WANG, YING QIAN, KEVIN P. GALLAGHER

Executive Summary

The economic shock from the COVID-19 pandemic has set back the development agendas for emerging markets and developing countries. Many developing countries have suffered from severe economic contractions that derailed revenue generation and budget execution and created urgent financing needs. Servicing public debt crowds out fiscal space for investing in a green and equitable recovery. This has exacerbated the triple crises of public health, rising poverty and inequality and climate disasters. How can the Group of 20 (G20) leaders and international financial institutions (IFIs), like the International Monetary Fund (IMF) and the World Bank, act together to restructure debt of developing countries in a concerted manner to prevent and mitigate debt distress so nations can mobilize the financing necessary to achieve their development goals? Leaders around the globe are struggling for answers.

On September 8-9, 2021, the Boston University Global Development Policy (GDP) Center hosted a virtual workshop on "Debt Distress and Development Finance in the COVID-19 Era" that included numerous participants from the Institute of World Economics and Politics at the Chinese Academy of Social Sciences, as well as individuals from across the world and the United Nations Conference on Trade and Development (UNCTAD). The workshop was divided into two sessions, with the first analyzing how debt sustainability can be measured in a more precise manner so policymakers can better understand and design effective investment and development strategies by rethinking and reforming the IMF's Debt Sustainability Analysis (DSA). The second session featured discussions of debt restructuring proposals that would allow key creditor and debtor countries to work together

to reduce debt burdens in a fair and equitable manner, enabling emerging markets and developing countries to have the fiscal and policy space to invest in sustainable growth and development. Ideas were exchanged on topics of debt distress, including asset-based debt sustainability frameworks, debt instruments such as Brady-like bond approaches, debt-for-nature swaps and asset-plus refinancing, as well as China's role in financing development and Chinese approaches to debt restructuring. Six working papers were presented, followed by animated discussions with global experts on financial stability and development finance. The workshop considered questions like:

- How can debt sustainability be measured in a more precise manner so policymakers can better understand and design effective investment and development strategies via rethinking/reforming the DSA framework;
- How can key creditor and debtor countries work together to reduce debt burdens in a fair and equitable manner so that emerging economies and developing countries will have the fiscal and policy space to invest in sustainable growth and development; and
- What can China, a new but significant creditor in developing countries, learn from experiences of the past and coordinate with other creditor countries for concerted and effective action?

The workshop included leading experts with in-depth experience and research in developing country debt issues and China's newfound prominence in the developing country debt market. Key takeaways included:

- The IMF's DSA continues to play a key role in assessing a country's debt situation, identifying potential vulnerabilities in debt structure and examining debt-stabilizing paths in cases of debt distress. But it needs reform to consider the role of public assets and incorporate sustainable development-related issues. With the support of asset mapping and positive cash flow, financial markets and credit rating agencies would be more lenient on the increase of public debt by a particular developing country, particularly if it is being used to build productive assets. Given the difficulty for low-income countries to construct country-level public sector balance sheets, measures of public assets using the estimated value of the completed and ongoing large projects could be useful. UNCTAD's Sustainable Development Finance Assessment (SDFA) framework considers debt sustainability as a long-run solvency issue and helps developing countries identify and implement measures needed for achieving critical Sustainable Development Goals (SDGs), while ensuring compatibility with external finance and debt sustainability.
- As much as 80 percent of loans from China to Africa have been for infrastructure projects. In cases of debt distress, Chinese creditors usually acted quickly with tailored solutions on a project-by-project basis, some following the logic of using public assets to relieve debt repayment burdens. The debt relief provided by China's creditors has complemented debt relief by countries in the Paris Club. Cooperation with the Paris Club will become more important as the share of Chinese loans in developing countries increases in the coming years.
- Risks of a debt crisis due to the COVID-19 pandemic will impact global economic recovery and achievement of the SDGs. High levels of debt service are impeding developing countries' crisis responses and crowding out crucial investments in climate resilience. Thus, debt relief must be linked with building climate resilience. A proposed 'Debt Relief for Green and Inclusive Recovery' scheme, wherein the World Bank provides support through a guarantee facility could provide debt relief while allowing debtor countries to invest in strategic

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areas such as health, education, digitization, sustainable energy and climate-resilient infrastructure. With the guarantee facility, innovative debt instruments in the international capital markets, such as green and climate bonds and sustainability-linked notes (SLNs), could be considered by developing countries to raise funds for sustainable development projects. Other possible proposals included debt-for-nature conservation swaps, wherein international assistance would be rallied to support developing countries to reform policies, develop capacities and build project pipelines for nature conservation.

- The Brady-like bond modeled after the Brady Plan of 1990s for distressed debt restructuring could work for today's debt distressed countries, particularly with the support of IMF's new allocation of Special Drawing Rights (SDRs), specific facilities at the IMF or new schemes proposed by the G20. Global "Anti-COVID Bonds" issued by creditor countries could be invested and posted as collateral by Brady-like bond issuing debtor countries for credit enhancement. Commodity-linked bonds (CLBs), as one form of a state-contingent debt instrument, could also be used in the Brady-like bond issue. CLBs can offer a natural hedge, thus matching debtor countries' ability to service debt, as many debt-distressed countries are primary commodity producing countries and may suffer from boom-and-bust cycles of economic development.

The following policy brief summarizes the discussion.

Improving the Debt Sustainability Analysis

The Debt Sustainability Analysis (DSA) plays a key role. As one of the pillars of their macroeconomic advisory work, the World Bank and the IMF have developed the DSA framework, first initiated in 2002 and subsequently revised in 2017, aiming to assess a country's debt situation, identify potential vulnerabilities in the debt structure and related policy framework and examine alternative debt-stabilizing policy paths in cases of debt distress (IMF, 2017). Based on the framework, the IMF and other IFIs have played important roles in assisting countries hit by the COVID-19 pandemic, avoiding debt crises and upholding the G20's Common Framework and Debt Service Suspension Initiative (DSSI).

But developing countries and economists have long questioned the adequacy of the framework and its assumptions. For example, the scope of the DSA is often limited to debt repayment capability, rather than debt for economic structural transformation, meaning the assumptions used by the DSA framework are limited. The DSA also does not comprehensively include climate or other sustainability risks or account for crucial investment needs for climate adaptation or achieving the SDGs in low-income countries. Thus, critical revisions and updates are needed. Alternative approaches were discussed, and constructive criticisms were offered from three perspectives at the workshop, including (i) the importance of considering public assets in the DSA, (ii) the reframing of debt sustainability by the UNCTAD and (iii) climate scenarios in the DSA.

Public Assets and Debt Sustainability

The DSA, a useful tool for policymakers to focus on in terms of managing debt since the financial crisis of 2007-08, has largely overlooked the aspect of public wealth. In many debt distressed developing countries, stocks of public assets are larger than stocks of public debt. However, public commercial assets, a segment of wealth vastly larger than any other global asset segment, remains unaudited, unsupervised, almost entirely unaccounted for and often unregulated. A prudent management framework for public assets could help not only tackle the debt problem, but also the war against corruption and thus support sustainable future economic growth.

Specifically, the IMF's DSA does not distinguish debt for capital investments in infrastructure from debt for recurrent expenditures, such as for payments for public civil servant salaries and pension benefits. In fact, if invested effectively, an increase in government debt could be accompanied by government asset accumulation, which could potentially increase the government's net worth over time. Therefore, focusing on debt (as in the case of the DSA) rather than net worth (as would be the case of a public sector balance sheet analysis) cannot provide an accurate measure of debt sustainability and could be misleading and lead to an anti-investment bias.

Governments around the world should create "asset maps" to provide indicative valuations of all public commercial assets within their respective jurisdictions and identify unknown and unmanaged public assets that could generate beneficial fiscal effects. Following that, a holding company could be created to manage the assets in a consolidated and effective way, ensuring positive cashflows are continuously generated from these assets. With the support of the asset map and positive cash flow, financial markets and credit rating agencies could look kinder on the increase of public debt of a government, particularly if it is being used to build productive assets on the left side of the government's balance sheet.

However, there are concerns over how difficult it will be for low-income countries to construct country-level public sector balance sheets, as well as problems with data availability. While countries can benefit from capacity building in the long term, alternative measures of public assets in the short term can be estimated as the value of completed and ongoing large projects.

Reframing Debt Sustainability – the UNCTAD Sustainable Development Finance Assessment (SDFA) Framework

The UNCTAD Sustainable Development Finance Assessment (SDFA) framework, in line with the idea of building public assets for long-term solvency, aims to identify countries' development financing needs for achieving critical SDGs, while ensuring compatibility with external finance and debt sustainability.

In 2018, UNCTAD found it would take an average increase of public debt/GDP ratios from around 50 percent to 185 percent for 30 developing lower-income and middle-income countries in Africa, Asia and Latin America to achieve only the first four SDGs (those on poverty, nutrition, health and quality education) by 2030. This is unless the countries involved achieve an average annual growth rate of 12 percent, which is increasingly unlikely under the constraints of the pandemic. Bearing in mind that a developing country's balance of payment is the most relevant constraint for achieving structural transformation and the SDGs, the SDFA framework views debt sustainability as a long-run solvency issue and adopts the alternative assumption that output is determined by long-run aggregate demand within bounds of external constraints. The SDFA framework also provides various combinations of macroeconomic and development policy suggestions, where fiscal austerity becomes endogenous.

Debt Relief with Chinese Characteristics

In recent years, China has become an important source of finance for many developing countries. Between 2008-2019, China's two state-owned policy banks -- the China Development Bank and the Export-Import Bank of China -- provided a total of $462 billion to development projects around the world, just $5 billion short of the World Bank's sovereign lending during the same period (Ray et al, 2021). While China's lending bridged crucial development finance gaps for many countries, the country has also become the biggest bilateral creditor. Understanding the real impacts of Chinese lending on debtor countries' debt sustainability, sustainable development and China's approaches to distressed debt restructuring will be increasingly important in the coming years.

Consider Africa, where distribution of sources of debts varies widely across the continent. On average, only 13 percent of African country debt is from Chinese creditors and almost 30 percent is from bond markets. According to the Chinese Loans to Africa Database created by the China-Africa Research Initiative at Johns Hopkins University School of Advanced International Studies and managed by the Boston University Global Development Policy Center, 80 percent of China's loans to African governments and state-owned enterprises went to infrastructure sectors, the largest of which are the transport and power sectors during 2000-2019. Of 214 hard infrastructure projects completed with Chinese development finance between 2000-2014, 78 percent of projects addressed African countries' infrastructure bottlenecks for economic development (Gallagher and Wang, 2021). Impact evaluations of debt from these projects will need to consider the contributions to socioeconomic development, creation of state asset values and environmental protection.

Case studies show that when it comes to distressed debt restructuring, Chinese creditors have been quicker to come to an agreement than other lenders. Among Chinese lenders, debt relief usually is negotiated separately by each lender; extending maturity has been common and write-offs are generally only available for interest-free loans, as part of China's foreign aid program. No cases of asset seizures or litigations have been found. A recent study shows debt relief provided by China's creditors complemented debt relief provided by the Paris Club prior to 2010. However, overall debt to Chinese creditors overtook debt owed to Paris Club creditors during 2010–2019 as China became an important player in sovereign debt restructuring. Furthermore, the size of Chinese sovereign debt restructuring has been dwarfed by that from non-sovereign creditors (Gong Cheng et al, 2020).

In terms of debt relief from Chinese creditors, tailored solutions have frequently been sought on a project-by-project basis, depending on whether the concerned project is commercial or developmental. There were debt restructuring cases which have followed the logic of using public assets to relieve debt repayment burdens. For example, there was a $1 billion Chinese loan to the Republic of Congo to build a road between a port city and the capital, the resulting thoroughfare could be considered as a valuable public asset (the road is currently managed by a Franco-Chinese consortium, which assesses tolls for travelers) (Wang and Xu, 2022). The resulting debt, if in distress, could be restructured based on the value generated from the road if it is managed well.

Additionally, there is the concept of "asset+ based refinancing," which treats a debtor country's past repayment of a loan principle as the value of debtor countries equity share in the project and uses it to attract additional financing (Gallagher and Wang, 2020).

Discussion

Given country feedback and reflections on the variety of debt crises in recent years, there is a need for the DSA to improve. Revising the DSA methodology will need to be a continuous process, although the intertemporal consistency of different versions of the DSA is also important. Reforming the DSA requires more than an accounting exercise, it will need complicated economic modeling, as well as consideration of conservative attitudes typical of lenders in times of crisis. Integrating these analyses into a growth framework is essential.

Technical details and sustaining growth momentum during debt restructuring will both be important for the DSA. First, should the interest rate used in the DSA be compatible with the expectation of the institution that runs the exercise, or should it be predicated on the expectations consistent with the market? Secondly, the interaction of monetary and fiscal policies could have significant impacts on results of the DSA and need to be carefully examined. Advanced economies in Europe and emerging markets economies like Indonesia and the Philippines have all used fiscal and monetary policies to stabilize respective economic and financial conditions during the pandemic. Third, an important lesson from the management of the Eurozone crisis was that sustainability needs to be understood differently for debt flows and stocks. Even though the position of overall debt stock will affect funding costs and ratings, for developing countries, there is a strong case to focus on managing debt flows so governments can sustain gross financing needs while concurrently restructuring assets to help strengthen economic sustainability.

Beyond The DSSI and Common Framework: Innovative Schemes for Addresssing the Debt Problem for a Green and Inclusive Recovery

The impact of financial market turmoil and large-scale withdrawal of international capital from developing and emerging economies during the outbreak of the COVID-19 crisis has somewhat been counter-balanced by the temporary relief driven by the rise of primary commodity prices and more favorable bond market conditions. However, risks of a debt crisis continue to loom large, and for some countries a new round of debt issuances may further undermine their debt sustainability. Protracted recoveries due to insufficient fiscal stimulus and slow progress in vaccination have undermined development prospects in the Global South. The existing high levels of debt services impede the crisis response, threaten achievement of the SDGs and crowd out crucial investments in climate resilience. The IMF is concerned the recovery in advanced economies may lead to overheating and subsequent interest rate hikes that could trigger capital outflows and exchange rate depreciation in developing countries, which could balloon already worrying levels of external debt across developing countries (IMF, 2021).

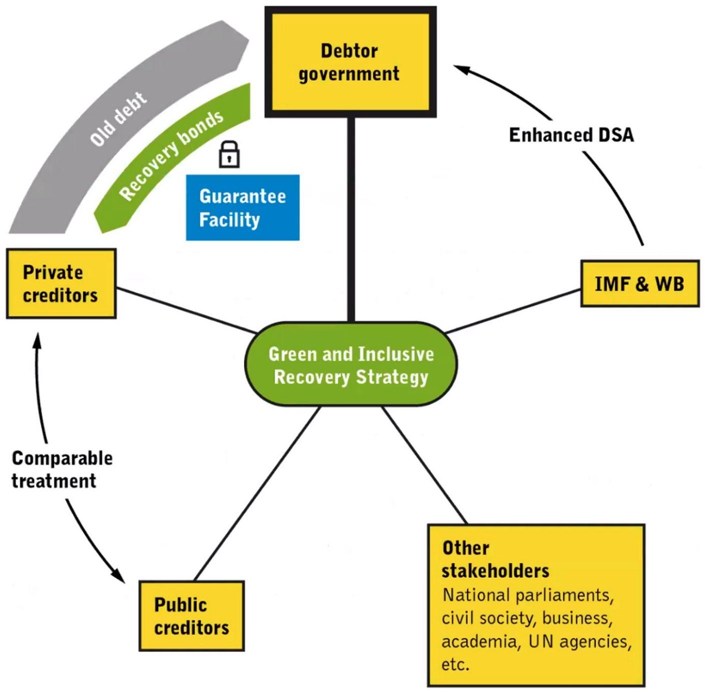
Debt relief must be linked with building climate resilience. Creditor and debtor countries alike need to align newfound fiscal space with globally agreed-upon development and climate goals and incentives need to be designed to ensure private creditors' participation in debt restructuring. Additionally, innovative debt restructuring instruments need to be devised to enable coordination among creditors where debt relief is granted in exchange for greater assurance of collectability and linked with policy reforms.

This section of the workshop discussed proposals for green and inclusive debt relief, like the creation a guarantee facility by the World Bank or the IMF which could be used for debt restructuring transactions similar to the Brady Plan introduced during the Latin American debt crisis of the 1980-90s. Other proposals included variations of Brady-like bonds with the use of state-contingent instruments or green and climate change bonds.

Debt Relief for a Green and Inclusive Recovery

The Debt Relief for Green and Inclusive Recovery proposal was presented, wherein debtor countries seeking haircuts from bilateral sovereign creditors would be required to seek commensurate relief from private creditors. Incentives would be designed, with both guaranteeing and regulatory mechanisms, to ensure private creditor participation. A "Guarantee Facility for Green and Inclusive Recovery" would be created at the World Bank to provide a partial guarantee of the principle, as well as 18 months' worth of interest payments that automatically renew until the debt is fully serviced. The proposal is modeled after the Brady Plan of 1990s, with financial resources such as guarantees for new loans or bond issuances and includes private creditors in the restructuring process. Figure 1 shows how it would work. Additionally, regulatory incentives offered together with the guarantee facility may include tax relief or regulatory capital relief for creditor banks participating in the debt relief. The IMF, financial authorities of major advanced economies and China, could play a critical role in persuading private creditors to accept and implement debt reductions for developing countries.

Figure 1: A Guarantee Facility for Green and Inclusive Recovery



Source: Volz, Jones and Gallagher, 2021.

Debt relief should not only provide temporary breathing space but should empower debtor country governments to lay the foundations for sustainable development by investing in strategic areas such as health, education, digitization, sustainable energy and climate-resilient infrastructure. An agreement on debt restructuring should require the debtor country to commit to reforms that align its policies and budgets with the SDGs and the Paris Agreement. The proposed "Guarantee Facility for Green and Inclusive Recovery" at the World Bank should ensure debtor country's commitments with involvement of policymakers and in consultation with stakeholders, including bilateral and private creditors, civil society, academics and international development partners including IFIs. The development priorities should reflect the needs and concerns of the country.

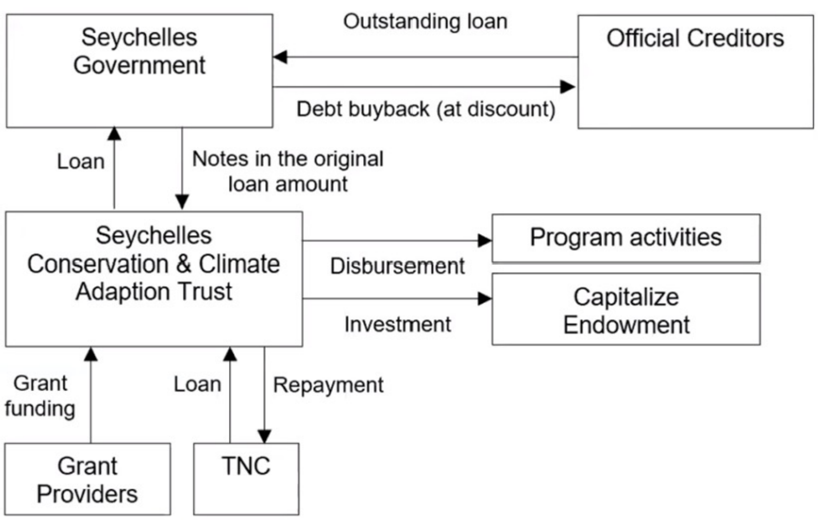
To form a common ground for a debt restructuring plan in which a debtor country government and public and private creditors agree, debtor country governments are suggested to advance their own green and inclusive recovery strategy (GIRS), building on the country's existing national vision, strategy and plans, including its Nationally Determined Commitments submitted under the Paris Agreement. The GIRS should highlight the government's policy priorities for the recovery, along with a set of key performance indicators and a spending plan, guided by a set of principles to ensure the recovery is in line with the SDGs and the Paris Agreement. The draft GIRS should be based on the latest scientific knowledge regarding the unfolding sustainability crisis and undergo a public consultation process. Principles applied should include that (i) no public financial resource or guarantee should be used to finance fossil fuel supply; (ii) fossil fuel subsidies of the past should be shifted towards the provision of clean and affordable energy; (iii) economic recovery should not sacrifice the integrity of country's ecosystem and its biodiversity in line with global biodiversity targets which should be maintained; and (iv) public policies should be consistent with low-carbon transition targets.

A delegated "Fund for Green and Inclusive Recovery" could be established in the country for management of the envisaged GIRS spending. A portion of the restructured debt repayments would be channeled to the Fund and the government would be free to decide how to spend the money from the Fund, with the spending in line with the goals set out in the GIRS. A steering group would monitor the implementation. Governments would also commit to enhancing debt transparency, adopting sustainable borrowing practices and to strengthening public debt management capacity and domestic resource mobilization. (Ulrich Volz, et al, 2021).

Innovative debt instruments in international capital markets, such as green and climate bonds and sustainability-linked notes (SLNs), could be considered to raise funds for sustainability projects. The challenge is meeting global standards by debtor countries, but so far, there is virtually no certified green and climate bonds issued by DSSI countries. In the case of SLNs, the barriers of entry may be lower since such arrangements only require interest payments be linked to key performance indicators (KPIs) with a designated quantifiable SDG.

Notably, the distressed debt buybacks can also be linked with conservation or climate adaptation programs (Qian, 2021), as in the case of the Seychelles in 2015, when a Special Purpose Vehicle (SPV) was set up to raise grant and loan capital for a debt-for-nature conversion swap. In exchange, the Seychelles government committed to improve policies and use the recycled funds to invest in marine conservation and climate adaptation projects. However, sufficient international assistance is needed to reform policies, develop capacities and build project pipelines.

Figure 2: An Illustrative Transaction Structure for Distressed Buybacks with Green Finance



Source: Qian, 2021.
Note: TNC = The Nature Conservancy.

Debt Restructuring for Developing Countries: An Upgraded Version of the Brady Bond Plan

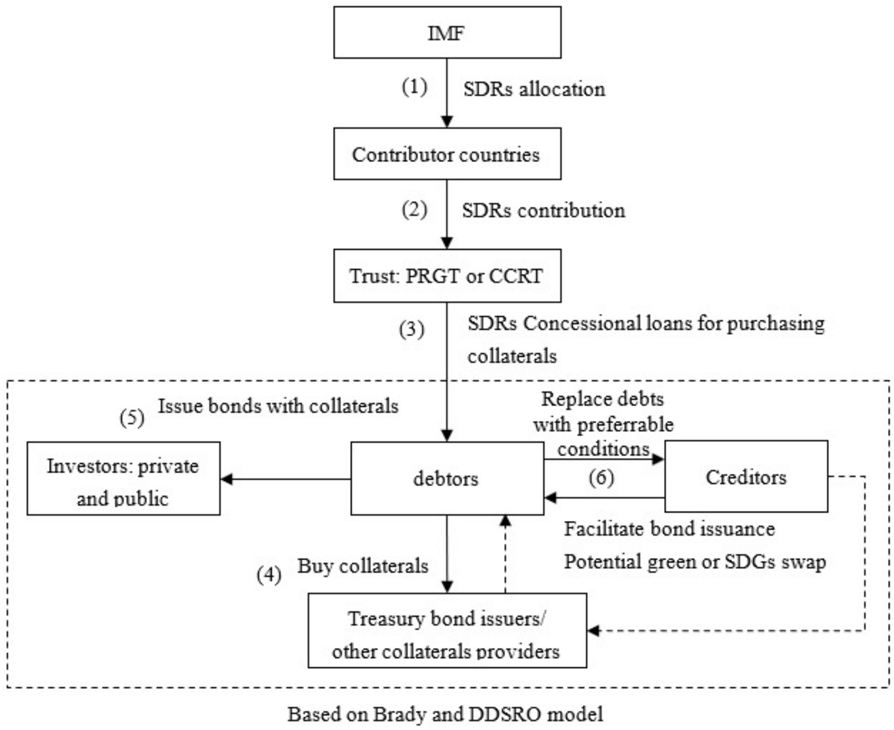
A newly proposed Brady-like bond for today's debt restructuring would work well with the IMF's new allocation of SDRs and existing facilities like the Poverty Reduction and Growth Trust (PRGT) and Debt- and Debt-Service-Reduction Operation (DDSRO), and possibly the nascent Resilience and Sustainability Trust (RST) proposed by the G20. The SDRs and resources from these facilities could be used to purchase sovereign bonds with high credit ratings as collateral for credit enhancements on Brady-like bonds issued by debtor countries.

The IMF's new SDR allocation of $650 billion is expected to enhance member countries' capacity to respond to the pandemic. It was suggested that major creditor countries and donor countries contribute their SDR allotments to the PRGT or the Catastrophe Containment and Relief Trust (CCRT), in the form of lending as currently practiced in PRGT, with low or zero interest rates to debtor countries. Using proceeds from these concessional loans, debtor countries could purchase treasury bonds from major creditor countries with high credit ratings and use them as collateral to ensure successful new Brady-like bond issuances. Investors, particularly those in the corresponding creditor countries, would then be encouraged to invest in the Brady-like bonds, due to strong recognition of their own sovereign debt and generally favorable risk treatment on their balance sheets.

With such a credit enhancement, each or several creditor countries could negotiate with debtor countries and issue sovereign "Anti-COVID Bonds" in national or international capital markets. In the past, debtor countries typically issued Brady bonds in the forms of fixed and discounted rate par bonds and market rate floating bonds with long tenors, but structuring was flexible. The proceeds, with longer maturity and more favorable coupon rates to debtor countries to replace the original loans or debts, could be designated for green purposes and the SDGs. Creditors participating could include banks, non-bank financial institutions, corporations or other types of private or public creditor institutions, thus ensuring restructured terms for both public and private sector creditors are on comparative terms.

Creditors and debtors are also encouraged to apply other innovative designs for debt restructuring transactions and submit their applications to the IMF or the PRGT. For debt restructuring purposes, the development finance concept might need to be expanded to include both the narrower concept of aid, concessional lending and the broader concept of export buyers' credit, infrastructure loans and equity finance. Figure 3 shows a Brady-like restructuring with IMF support using thematic bonds for credit enhancement.

Figure 3: Brady-like Restructuring with IMF Support and Thematic Bonds for Credit Enhancement



Source: Qiyuan Xu and Tailei Wang, Chinese Academy of Social Sciences, 2021.

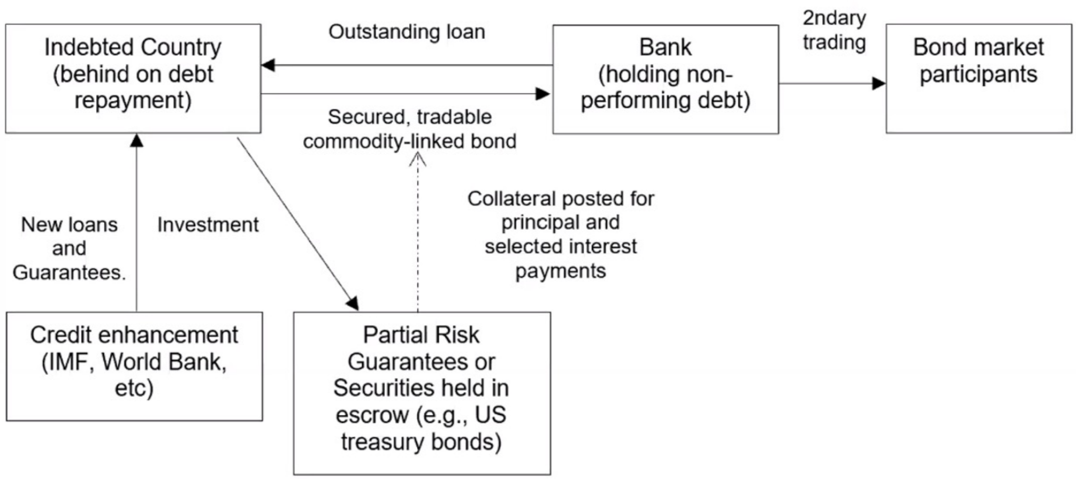
Using concessional loans has an advantage over having donor countries donating their SDRs to debtor countries, as (i) the loan structure could avoid protracted negotiation between countries on how to allocate the SDRs and who donates what amount; (ii) political obstruction could be eased, as the donation of SDRs will fundamentally change the landscape of SDR distribution among countries, affecting the next SDR allocation which will be based on the outstanding number of the current allocation; and (iii) the loan structure could hopefully help avoid moral hazards that may come with donation arrangements (Qiyuan Xu and Tailei Wan, 2021).

Brady Bonds and the Potential for Debt Restructuring in the Post-Pandemic Era

Developing countries are vulnerable to boom-and-bust cycles of economic development. A state-contingent debt instrument is an arrangement that has its interest payments linked to growth rates of GDP, stock index, wages and state-owned enterprise (SOE) revenues, among others, to create a natural hedge in the bond structure and reduce credit risks. When the contingent indicator is performing well, the interest payment is higher, matching the country's ability to pay; when the country's economic conditions are not doing well, its interest payment burden would be reduced.

Specifically, commodity-linked bonds (CLBs) could be a good option, as many developing countries are primary commodity producers and commodity prices are not subject to reporting errors and moral hazards. For distressed debt restructuring, CLBs have the advantage of potentially requiring less collateral and guarantees. Compared with a debt-equity swap (fixed to variable income streams), CLBs are more standardized, transparent and can be priced accurately. Creditors may also enjoy a natural hedge if they are importing a concerned primary commodity. Theoretical and empirical evidence has shown benefits of CLBs, which were used in Mexico's Brady bond placement in the 1990s (Qian, 2021). Both Mexico's par and discount bonds included an "oil price recapture" clause. The instrument helped Mexico achieve macroeconomic stability and regain investment grade status in the early 2000s (Qian, 2021). Other contingency instruments to explore include disaster damages with a quantifiable indicator. Figure 4 shows a potential transaction structure using CLBs.

Figure 4: An Illustrative Brady-like Transaction Structuring Using a State Contingent Instrument (Commodity-linked Bonds)



Source: Qian, 2021.

Discussion

Compared to the 1990s when Brady bonds were first introduced, bond markets for developing countries are now much deeper and diversified, with greater availability of resources to support distressed debt restructuring. In addition to the IMF and the World Bank, many other regional development finance institutions and bilateral initiatives have also allocated funds for post-pandemic support. Additionally, more streamlined and transparent processes have been established, like the IMF's DSA framework for market-access countries, which despite the issues previously discussed, conducts regular monitoring and issues early warnings for effective preemptive action.

But the current market environment makes the Brady-like transaction more complicated than it was 30 years ago. Since par bonds in the Brady Plan used reductions in interest rates to ensure debt sustainability, there may be little space in the current market for further interest rate cuts. Additionally, more debt is now in currencies other than the US dollar. Chinese creditors have started playing a much larger role in debt restructuring negotiations, but there may be a lack of coordination among traditional creditors and Chinese creditors. Given that a significant haircut of about 40 percent might need to be taken, a leading party will need to coordinate the various official and private creditors. There is a need for planning and sharing the burden in a truly multilateral manner, especially between Chinese official creditors and Western private creditors.

Policy dialogue with governments and regulatory authorities is also needed. As Chinese creditors may face regulatory constraints at home in taking haircuts as part of debt restructuring, policy discussions between stakeholders and banking regulators are needed to ensure haircuts for the new Brady-like bonds are sustainable. To create a conducive policy environment, China may need to designate a targeted share of its Official Development Aid (ODA) in Gross National Income (GNI) to a level that is commensurate to its per capita income and count debt relief as part of its ODA. On the global scale, rather than continuing with the current ad hoc and country-specific approach, a centralized global debt authority might need to address the lack of coordination on debt management among creditor countries and between public and private creditors.

Debtor countries' perspectives need to be respected. Distressed debt restructuring and management must consider what debtor countries need, not simply what creditors are prepared to give. Debtor countries might be sensitive towards policy conditionalities due to sovereignty or market reaction concerns. These issues should always be dealt with in a sensitive and cautious manner. While performance benchmarks and monitoring mechanisms are necessary, they must be established in a way that respects debtor countries' sovereignty and uses agreed-upon international best standards. While the conditionalities of the IMF have improved in recent years, more can be done towards "pro-development conditionalities," such as those in areas of asset management requirements and sustainable and green finance. Sector-specific conditions more frequently used by other development banks including the Asian Development Bank and the African Development Bank could also be introduced at the IMF for debt restructuring. Regionally, a potential African Brady Plan was discussed at the United Nations Economic Commission for Africa (UNECA) in 2020, but implementation is still awaited (Soto, 2020). In the meantime, a Liquidity and Sustainability Facility was established by UNECA. More research needs to be done to assess how the facility could be used to support an African Brady Plan.

The World Bank and the IMF can be involved through different angles. One angle is credit enhancement, and based on technical and political considerations, the debtor country could either use SDRs or take a direct loan from the IMF. In the latter case, the loan could be channeled through the PRGT or the RST. In addition to the loan for collateral, the World Bank could also provide guarantees directly. The IMF and other IFIs are facing a situation that is unprecedented, with a worldwide challenge on public health, climate and biodiversity and green and sustainable development. The IMF and IFIs need to play a more relevant role in helping debtor countries respond to the challenges of today and tomorrow. Whichever approach allows them to play a more efficient and effective role should be prioritized. The international community should be open-minded about employing innovative financial instruments and arrangements and debtor country perspectives need be to front and center of discussions.

Conclusion

At the time of publication, the IMF's DSA framework for market-access countries incorporating climate impact has come into effect. From May 2020 to December 2021, the G20's DSSI suspended $12.9 billion in debt-service payments owed by participating countries to creditors, according to the latest estimates (World Bank, 2022). The DSSI expired at the end of December 2021, leaving the G20 Common Framework as the only multilateral mechanism for debt relief in 2022. As the global pandemic protracts, IFIs and the G20 have a narrowing window to steer the world away from a more severe debt crisis. The important aspects and policy options discussed during this workshop will hopefully support policymakers around the world in addressing these challenges.

Policy recommendations:

- **Multilateral institutions and IFIs need to assume more critical roles in debt restructuring.** Despite significant improvement of international financial markets, the current low-interest market environment makes Brady-like transactions more complicated than they were 30 years ago. In addition, Chinese creditors have started playing a much larger role in debt restructuring negotiations. Intellectual support, policy dialogue and coordination among debtor and creditor countries and among different stakeholders is needed. The IMF and IFIs can be effectively involved in debt restructuring through the DSA and policy dialogue at the macro-level, donor and creditor coordination on the mid-level and selection of the most appropriate transaction structure for debt restructuring at the micro-level.

- **Debtor countries' perspectives need to be fully considered.** Developing countries involved will be sensitive towards policy conditionalities due to sovereignty or market reaction concerns. While benchmarks and monitoring mechanisms are necessary, these must be established in a way that respects debtor countries' sovereignty and uses agreed-upon international best standards. More initiatives can be linked directly towards "pro-development conditionalities," such as public asset management, sustainable development and green finance.

- **Lowering debt burdens should be accompanied with commitments towards the SDGs and the Paris Agreement.** As part of the debt restructuring and economic recovery process, stakeholders both in debtor and creditor countries can work together in line with the SDGs, including Nationally Determined Commitments submitted under the Paris Agreement. Innovative approaches can be deployed as green and climate bonds and sustainability-linked notes (SLNs), as well as debt-for-nature swaps to help expedite the process.

- **Proven and innovative approaches can be considered for debt restructuring.** Leveraging public assets, utilizing natural hedges through state-contingent instruments including CLBs, debt buy-backs with green and climate finance, debt-for-nature swaps and various forms of credit enhancements have all proven to be effective in helping debtor countries reduce distressed debt overhangs, raise credit worthiness and meet challenges on public health, climate, biodiversity and green and sustainable development. However, effectively using these tools will require creditor countries and development partners to help debtor countries improve their policy frameworks, technical know-how and financial market infrastructures.

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