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A brave new world: the limitations of the G20 debt suspension extension

Blog post by Senior Associate Isabelle Trick, 22 October 2020

At the beginning of the year, many low- and middle-income countries were already struggling with increasingly large debt burdens. Then, these debt levels collided with a global health emergency and an economic crisis – reducing access to finance just when it was needed most. Given the ongoing impact of the pandemic and what looks like an increasingly bumpy and uneven recovery, the Paris Club of official creditors and the G20 just renewed their joint Debt Service Suspension Initiative (DSSI). The initiative now allows some of the world's poorest countries to suspend bilateral debt service payments until mid-2021.

Freeing up these resources to be spent on health and the economy is undeniably a good thing. However, the six-month renewal of the DSSI without major changes highlights some of its limitations.

Since March, many debtor countries have called for the suspension period to be extended until the end of 2021. If not, governments already working to address some of the most severe economic contractions in decades, may be forced into austerity to resume debt service. This would be damaging to their recovery and would compound human suffering in poor countries. A year-long extension right now may have been more appropriate given that the current uncertainty is unlikely to be resolved soon.

Announcing the original DSSI, the G20 "called upon" private sector creditors to participate. This same terminology was used in announcing its extension. With poor countries' private creditor debt service exceeding official bilateral debt service by $2 bn in 2020, there was an expectation that any extension of the DSSI would put more pressure on private lenders to participate. The decision not to rely on the Paris Club's usual MO of "comparability of treatment" clauses which oblige debtor countries to seek comparable terms from all creditors in exchange for debt treatments, lets private lenders off the hook again.

Why does this matter

The present crisis has underlined the need to reform the existing international debt architecture to better suit a world with a more diverse set of creditors and debt instruments.

China, which has emerged as the major bilateral lender to low-income countries, has pledged its participation in the DSSI, but is not used to participating in multilateral debt coordination efforts. Collective action clauses have facilitated smoother restructurings between private bondholders, but there is a large outstanding stock of bonds without them and a significant share of low-income country debt is in the form of loans and other non-bonded debt. Addressing these issues will be crucial in the face of likely looming defaults. Zambia may be a first test case.

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What next

There is a hope that it will be easier to adequately assess debt sustainability in six months. In this case, we may see negotiations for some of the first fully-fledged debt treatments get underway around mid-2021. However, if the economic climate remains volatile, the DSSI may be extended for another six months if for no reason than to ensure that the size of the debt treatments required is sufficiently clear.

More fundamentally, the IMF has released a new report suggesting potential improvements to the current debt architecture. And the G20 have reportedly agreed on a post-DSSI common framework. Once this is made public, likely ahead of the G20 leaders' summit in November, it will be interesting to see whether the international community can agree on how to address some of the fundamental challenges facing debt treatments.