

Deutsches Institut für German Development Entwicklungspolitik Institute

# **COVID-19: How can the EU support its partner countries to avoid and resolve debt crises?**

DG INTPA InfoPoint, March 19th, 2021 Dr. Kathrin Berensmann, German Development Institute (DIE), kathrin.berensmann@die-gdi.de





- 1. Current debt situation in low-income countries
- 2. Short-term measures: Provision of liquidity
- 3. Conclusion



#### Before the COVID-19 crisis

=> About half of LICs were already highly indebted (IMF/WB)

Main reason:

- Change in the composition of debt from concessional to market-based loans from private and public creditors
- Increased government debt

#### 1. Current debt situation in low-income countries

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#### **COVID-19** pandemic further deteriorates the debt situation in LICs

Public debt increased in LICs

public debt in % of a country's GDP rose: 2011: 29.6 % => 2019: 43.3% => 2021: 49.7%(IMF)

#### Government revenues declined

Government revenues in % of a country's GDP declined: 2011: 17.8 % => 2019: 14.7% => 2020: 13.0 %(IMF)

Reasons: decreases of growth and export earnings

- External official debt in % of a country's GDP increased:
   Example SSA: 2011: 14.0 % => 2019: 23.4% => 2020: 28.1%(IMF)
  - ⇒ Heavily indebted countries are obliged to use scarce financial resources to service their debts
     but: resources needed for sustainable development



- LICs will not be able to cope with the COVID-19 crisis alone.
- => International community = key role in providing financial assistance:
- ⇒ Foremost economically stronger countries such as those of the EU and international financial institutions (e.g. World Bank and IMF)
  Immediate support by IFIs

- WB: US\$ 160 billion to developing countries
- IMF: US\$ 50 billion to developing countries

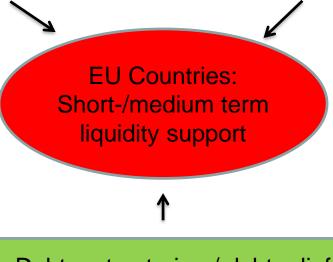
But:

- Countries still lack liquidity
- Loans provided further increase debt

World Bank President: Without immediate financial support the progress that these countries have made in their development over the past decade will be lost.



Debt Moratorium: Participation in Debt Services Suspension Initiative Contribution to IMF's Debt service relief trust



Debt restructuring / debt relief: Participation in Common Framework

#### a) Debt moratorium: "Debt Service Suspension Initiative (DSSI)"

Paris Club / G20 = suspension of debt service payments for LICs from May 2020 to June 2021

main aim: improve the debtor's liquidity position => EU has also committed to participate in the DSSI

Problems:

- DSSI too short
- DSSI only suspension, often debt service relief is needed in the course of COVID-19 crisis

Policy recommendation: EU should

- promote further extension of debt moratorium by at least one year
- discuss debt relief on debt service

#### b) Debt relief on debt service

Catastrophe Containment and Relief Trust (CCRT) IMF

IMF's debt service waiver

EU contribution to the IMF's CCRT: €183 million

But: CCRT is not enough for highly indebted LICs => Grants for debt service under the DSSI

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#### C) Debt restructuring including debt relief

Paris Club / G20 established in November 2020

"Common Framework for Debt Treatments beyond the DSSI"

- Debt restructuring for LICs with unsustainable debt + could in some cases include debt relief
- Case-by-case approach
- Based on IMF/WB Debt Sustainability Analysis
- Broad participation of bilateral official creditors including the call for private creditors participation

=> EU has recognised that LICs with unsustainable debt levels need debt treatments beyond the DSSI and has welcomed the G20 and Paris Club agreement on the "Common Framework"



#### **Challenges of the Common Framework**

- Equal treatment of all creditors: all public and private creditors should participate equally in debt restructuring / debt relief
- Transparency on debt contracts: Ensure that all public creditors and public debtors should disclose their loan agreements as well as private creditors
- Debt restructuring and relief should be tied to economic reforms and earmarking
- ⇒ Use financial resources for sustainable development including social and health sectors and sustainable infrastructure

#### **3. Conclusion**



The international community and in particular those countries with strong economies, such as the EU member states, have a shared responsibility for attaining debt sustainability in the poorest countries of the world.



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### Thank you!

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