IMF, World Bank debt revamp process needs a relook

Of particular concern is the IMF's delay in putting together a package for financially-stressed nations

Neeraj Kumar

The recent Global Sovereign Debt Roundtable (GSDR) meeting held on the sidelines of the IMF and World Bank Spring Meetings on April 17 offered a ray of hope for low- and middle-income countries (LMICs) burdened by mounting debt. The IMF and World Bank acknowledged significant progress in tackling global debt vulnerabilities.

However, a key challenge remains: expediting debt restructuring processes and ensuring fair treatment across creditors. The world faces a daunting challenge: global debt reached a staggering $235 trillion in 2022, with low-income developing countries particularly vulnerable.

According to Unctad's Least Developed Countries Report 2023, the total external debt of Least Developed Countries hit a record $570 billion in 2022 — more than four times higher than in 2006. As a result of this growing debt burden, they are spending five times more on debt servicing than a decade ago.

In the past three years alone, the number of sovereign debt defaults in these countries has surged to 18, outstripping the total of the previous two decades. The situation is particularly dire for Low-Income Countries, with over 60 per cent currently in debt distress or having defaulted on their obligations.

This unsustainable debt situation creates a vicious cycle. LMICs often rely on borrowing to finance crucial infrastructure projects and social programmes. However, excessive debt can become a major drag on economic growth. High debt servicing costs divert resources away from productive investments, hindering long-term development prospects.

The IMF and World Bank through tools like Debt Sustainability Frameworks (DSFs), assess a country's ability to repay its loans. They also offer financial assistance and policy advice to help countries implement reforms that promote economic stability and growth.

THE TIMEFRAME

One of the key issues addressed at the GSDR was the lengthy timeframe associated with debt restructuring processes. Delayed resolutions not only create uncertainty for debtor countries but also exacerbate economic hardship.

The delay in finalising IMF programme and debt restructuring package for

IMF. Working on debt sustainability REUTERS

Ethiopia under the G20 Common Framework for debt treatments has caused particular concern. Stakeholders have specifically sought clarification over the efficacy of the IMF's Ethiopia package and the reasons for its delay.

Such transparency would not only benefit Ethiopia but also strengthen confidence in the IMF's role as a facilitator of debt resolution.

The GSDR discussions proposed a potential solution: setting a target of programme approval within 2-3 months for future debt restructuring cases, including under the G20 Common Framework for debt treatments. This would require streamlining communication and information sharing between debtor countries, official bilateral creditors (government-to-government loans), and private creditors. Another critical aspect of debt restructuring is ensuring comparability of treatment (CoT) between different creditor groups. This principle dictates that all creditors holding similar claims should receive comparable treatment in terms of debt relief. Inconsistent CoT can create an uneven playing field, potentially undermining the overall debt restructuring effort.

The GSDR discussions emphasised the need for enhanced information exchange and coordination between official bilateral creditors and private creditors. This would allow debtor countries to negotiate with full knowledge of how CoT will be assessed, facilitating a more efficient and equitable resolution. While the GSDR meeting represents a step forward, significant challenges remain. The IMF and World Bank must continue to play a proactive role in facilitating communication, promoting transparency, and advocating for faster and fairer debt restructuring processes.

Neeraj Kumar is an IES officer, currently serving as Joint Director (Bilateral Cooperation) at the Ministry of Finance.

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Uncertain times

Global inflation fears return

To observers of global economy and finance, the air of apprehension at the recently concluded Spring meetings of the IMF and World Bank was not surprising at all. Two factors are currently playing out to unsettle world trade, public finances and capital markets: first, the spat between Israel and Iran and, second, the fiscal, and thereby inflationary impact of over 80 countries including India going to polls this calendar year.

The meetings as well the three reports released last week — the IMF's Global Financial Stability Report, its Fiscal Monitor and the Bank's World Economic Outlook — draw succour from the 'resilience' of growth amidst generally declining inflation since 2022. But there is no mistaking the elephant in the room — sticky inflation, and its fallout on financial stability and growth. The Fund-Bank reports clearly say that since the "progress towards inflation targets has somewhat stalled since the beginning of this year", the Fed is expected to hold rates "higher for longer". US consumer inflation in March at 3.5 per cent was above the target of 2 per cent. The reports recommend that "central banks should avoid premature monetary easing" — clearly an effort to check volatility in capital flows in emerging economies. While inflation was the main theme at the meetings, public debt and "fragmentation" of global trade as medium term risks to inflation and growth too emerged as key takeaways.

Today's global inflation stems from many sources: commodity shocks; disruption to trade arising out of protectionism and emergence of 'geo-economic' enclaves; rising cost of labour in the developed world (particularly the US) as a result of social safety nets; and a vicious cycle of public debt (led by US and China) and inflation feeding into each other. High public debt is believed to crowd out private investment, hurting growth and taxes, leading to more debt in the absence of spending cuts. A weak medium-term outlook on global growth is linked to this debt-inflation overhang. There are two notable issues here: first, US debt has become a global worry; and second, it has become difficult to roll back spending undertaken during crisis years.

The US's fiscal deficit jumped to 8.8 per cent of GDP in 2023 from 4.1 per cent in 2022 (it was 11.1 per cent in 2021). China's fiscal deficit was 7.1 per cent of GDP in 2023, against 7.5 per cent in 2022, while India's (general government) was 8.6 per cent of GDP (9.2 per cent). The Fund-Bank duo is worried over whether US growth will be robust enough to offset rising debt. China's tanking property sector could impact all asset classes, growth and trade. But the biggest challenge for multilateral bodies is to overcome fragmentation of trade. Trade blocs have been carved out along geo-political lines, with more trade taking place within blocs than between them. This could create untold inefficiencies, besides inflation.

FROM THE VIEWSROOM.

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The battle against plastics

GREEN AGENDA. Reduction and recycling of plastics must be taken up to save the planet

Apart from banning non-essential plastics, manufacturers must be held accountable for the entire life-cycle of their products — collection, recycling, and disposal of plastic waste

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