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PARIS CLUB SECRETARIAT CONTRIBUTION TO THE 4TH INTERNATIONAL CONFERENCE ON FINANCING FOR DEVELOPMENT (Sevilla, 30 June – 3 July 2025)

The Paris Club looks forward to the United Nation's upcoming 4th International Conference on Financing for Development (FfD4), to be held in Sevilla, Spain, and stands ready to support the conference's important efforts to create an enabling environment at all levels for sustainable development.

Debt and debt sustainability were a core chapter in the Addis Ababa Action Agenda of 2015, and according to the zero draft of the Outcome document prepared by the UN co-facilitators, the topic will remain a focus with its own dedicated chapter at this conference.

The Paris Club is a group of major sovereign creditors that has provided restructuring operations for almost 70 years, based on negotiations with borrowing countries, transparent and coordinated action with IMF and World Bank, and the integration of comparability of treatment clauses to provide borrowing countries with leverage in their negotiations with other bilateral official and private creditors. The Paris Club secretariat is therefore well placed to provide substantive inputs into debt related discussions for the Sevilla conference, based on the Club's experience and expertise.

This contribution from the Paris Club secretariat: (1) takes stock of financing needs and debt vulnerabilities in developing economies; (2) foregrounds actions taken since Addis Ababa to tackle vulnerabilities; and (3) makes 10 concrete proposals for consideration at the FfD4 Sevilla conference.

This contribution draws on the Paris Club secretariat's observations of the general sentiment of the Club, and as well as its own practical experiences. Paris Club members themselves will negotiate FFD4 text on their own behalf, and this contribution does not commit them to the analysis or proposals herein.

1. <u>Financing needs & sovereign debt vulnerabilities in developing economies</u>

a) <u>The significant financing needs of emerging market and developing economies to address the SDGs will require more debt…</u>

As the Addis Ababa Action Agenda highlighted, borrowing is an important tool for financing investment critical to achieving sustainable development – whether meeting the sustainable development goals (SDGs) or facing the challenges of climate change. Not only does sovereign borrowing allow government finance to play a countercyclical role over the economic cycle, the IMF estimates that \$3 - \$4trn of additional spending is needed annually in developing and emerging economies by 2030 to meet SDG and climate change related financing needs.[1] The Independent Expert Group (IEG) report commissioned under India's G20 Presidency and co-convened by Summers and Singh reinforces this analysis, estimating a broadly similar $3trn a year of additional financing needs for developing economies. The report suggests that $2trn could be met by additional domestic revenue mobilization and local finance, whilst $1trn could come from external financing commitments (principally debt, most of which would be non-concessional).[2] These results have also been corroborated by UNECA's Songwe, Stern and Bhattacharya.[3] Debt financing will therefore remain a key source of funding to meet development and climate priorities in EMDEs going forwards.

b) ...at a time when debt vulnerabilities are elevated

Debt vulnerabilities remain elevated in 2025, and whilst they don't amount to a systemic debt crisis in the short term, solvency and liquidity stress in certain countries will continue to require case-by-case support in order to prevent future debt crises. According to the IMF and World Bank, across 70 low-income countries (LIC), 13% are in debt distress and an additional 37% are at high risk of debt distress. This situation has been stable since 2023, and the same indicators showed greater stress in both 2021 and 2022 respectively.[4] Moreover, a recent analysis by IMF staff places current debt vulnerabilities in a historic context, showing that vulnerabilities in low-income countries on average are less alarming than they were in the mid-1990s, at the cusp of the Heavily Indebted Poor Countries (HIPC) Initiative – with both solvency and liquidity indicators stronger on average than they were then.[5] In 1994, the median public-debt to GDP of a typical LIC was 72%, compared to 55% in 2023-24. The public and publicly guaranteed (PPG) debt to exports of a typical LIC currently stands at 137%, compared to 318% in 1994. Looking at liquidity measures, debt service to revenues stood at 18% in 1994, compared to closer to 10% post-Covid. Chuku et all conclude that the world is not experiencing a systemic debt crisis, and it is possible to avert such a crisis in future via strong macroeconomic policies and reforms.

The Paris Club secretariat broadly agrees with this assessment, whilst noting that averages can mask specific areas of stress, and that the economic situation across both LICs and middle-income countries is hugely varied. Over the last 15 years, following the peak of the HIPC debt cancellation era, debt levels have risen once more and spiked in particular due to countries' need to respond to the Covid-19 pandemic – the median debt to GDP for LICs rose from 34% in 2010 to 55% in 2023-2024. Certain countries are currently experiencing liquidity pressures in particular due to increases in debt service costs and lower flows of new finance. In IDA eligible countries for example, debt service averaged 16.1% of countries' exports base in 2023, and for many the proportion of debt service to government revenues remains high.[6] Since the Addis Ababa conference, higher debt service costs in developing economies have been driven by non-concessional debt dynamics as the role of the private financial flows has increased, the build-up of a larger stock of debt (most notably to respond to the Covid-19 pandemic), the rebound of interest rates from the historically low rates of the 2010s, and finally local currency depreciation against the US dollar. The pass-through of a higher global interest rate environment has also been accelerated by the increasing prevalence of variable loans, which

[1] Carapella et all; How to Assess Spending Needs of the Sustainable Development Goals: The Third Edition of the IMF SDG Costing Tool; 14/12/2023

[2] Summers, Singh et all; The_Triple_Agenda_G20-IEG_Report_Volume1_2023.pdf; 07/2023

[3] Songwe, Stern and Bhattacharya; Finance for climate action: scaling up investment for climate and development; 11/2022

[4] Staff of IMF/WB; List of LIC DSAs for PRGT-Eligible Countries - As of March 31, 2025; calculated on basis of all PRGT eligible low income countries

[5] Chuku et all; Are We Heading for Another Debt Crisis in Low-Income Countries? Debt Vulnerabilities: Today vs the pre-HIPC Era; 04/04/2023

[6] Staff of WB; International Debt Statistics | DataBank; data updated as of 03/12/2024

account for 57% of the long-term external debt stock of low- and middle-income countries (excluding China) and 40% of that of IDA-eligible countries. This has meant that in IDA countries for example, government spending on interest payments alone increased to 20% of government revenues in 2023; and compared to export earnings, interest payments on external PPG debt amounts to 2.7% of exports in IDA countries, up by 1.6% compared to 2022. In certain countries this is significantly higher, including for example in Senegal (7.8%), Pakistan (9.1%) and Kenya (10.5%).[7]

At the same time, refinancing has proved more difficult as net debt flows to developing countries remain below pre-covid trends.[8] Net debt flows to low- and middle-income countries turned negative in 2022 (outflow of $54bn) due to a slowdown in new lending from the private sector and emerging creditors. This partially recovered in 2023, with a net inflow to these countries of $221bn driven in part by the partial return of lending from private creditors, but these flows remain markedly below pre-Covid trends when more than $500bn was flowing into these countries annually.[9] There is therefore a liquidity crunch which, if less acute than the negative flows of 2022, mean that liquidity challenges remain.

2. Actions taken since Addis Ababa to address vulnerabilities

a) Delivering the Addis Ababa Action Agenda

The Addis Ababa Action Agenda outlined a framework that Paris Club members have been delivering on - for example, calling on the international community to support remaining HIPC eligible countries working to complete the HIPC process.[10] The Paris Club has put this into action, reaching consensus in 2021 on $14.1bn of debt cancellation for Sudan, following the country reaching its decision point, and providing debt cancellation worth over $2bn for Somalia in 2023 under the enhanced HIPC process, following Somalia's completion point. This reduced the country's external debt to sustainable levels, and allowed Somalia to return to international markets and regain access to new external financing. Somalia was the 37th country to receive a debt cancellation from the Paris Club under the HIPC initiative, and the agreement means that over its history Paris Club agreements have treated debt worth over $616bn.

Debt transparency was also a core part of the Addis Ababa Action Agenda, and improved transparency of debt data is essential to ensuring the sustainability of sovereign debt. Transparency enables borrowing countries and creditors to improve the assessment and prevention of credit risk - and thus supports access to sustainable financing on affordable terms. Transparency also facilitates the faster resolution of debt crises when they do occur. The primary responsibility lies with borrowing countries to disclose their debt arrangements and borrow on transparent terms. However, creditors also have a major role to play, given the accumulation of obstacles including more complex financial tools, the development of confidentiality clauses, and a lack of capacity in many fragile borrower countries. Progress has been made since 2015 in this regard. By publishing highly detailed data on a voluntary basis, Paris Club creditors fully promote transparency.[11] Further, under Japan's impetus,

[7] Staff of WB; International Debt Report; 03/12/2024

[8] Net debt flows defined, per World Bank methodology, as new loan disbursements minus principal repayments.

[9] Staff of WB; International Debt Report; 03/12/2024

[10] HIPC refers to the Heavily Indebted Poor countries (HIPC) Initiative, with analysis of HIPC available from IMF staff at: Debt Relief Under the Heavily Indebted Poor Countries Initiative.

[11] Paris Club Secretariat; Paris Club release of comprehensive data on its claims; Club de Paris; 01/07/2024. Individually, most Paris Club creditors release detailed data loan by loan, including the main parameters

most Paris Club creditors now share loan data bilaterally and directly with the World Bank, which conducts important data reconciliation to improve data quality and increase countries' competence in this area. But further improvements can be made on debt transparency and are proposed in Action VIII below.

Improvements to contractual practices have also been made, with the widespread adoption of Collective Action Clauses (CACs) in sovereign bonds. These clauses allow financial terms to be modified by a qualified majority rather than unanimously. These new clauses promote orderly restructuring and sharply limit non-cooperative behaviour during restructurings.

The Addis Ababa Action Agenda's call for the study of innovative financial instruments, most notably to support countries facing climate risks, has been acted upon. The Paris Club introduced a "hurricane clause" in Grenada's 2015 restructuring agreement – allowing creditors to provide additional debt relief if Grenada was hit by a major natural disaster and requested it**. This type of approach has since been built upon through Climate Resilient Debt Clauses (CRDCs),** which contractually reschedule debt service in the case of a natural disaster, thus providing liquidity relief during a time of economic stress. Such clauses have been adopted by several Paris Club members in their sovereign lending, as well as by MDBs and private creditors. Whilst CRDCs do not necessarily improve short-term debt sustainability, they are a valuable tool to reduce liquidity stress when climate risks materialise. As addressed in Action X below, CRDCs can be integrated into debt contracts more systemically to provide more predictability to creditors and allow borrowers additional fiscal space to respond to a natural disaster.

Similarly, the understanding of the two types of debt swaps has greatly advanced, with swaps that leverage the private-sector becoming more mainstream. Paris Club agreements have included debt-swap mechanisms since the 1990s, as an additional bilateral debt relief option, and members' therefore have experience of these tools. For borrowers, an official-sector debt swap reduces debt service payment which can be redeployed towards an agreed area of spending. For creditors, debt-swaps are in effect bilateral debt cancellations, supported by a governance process to agree with the borrower where newly released funds will be spent. For creditors, such swaps often carry the same budgetary costs as the provision of new grants, but with additional transaction costs and need to be considered against other forms of support. Official-sector swaps do not tend, in general, to significantly impact debt sustainability due to their historically limited transaction sizes and because additional fiscal space is only created if the proceeds of the debt swap are used to fund projects already within the borrower's budget (which is not often the case). However, they can provide targeted thematic or project support in areas of interest to the creditor and debtor alike. Private-sector debt swaps are a more recent innovation, leveraging the increased role of private debt in developing economies. Transaction sizes have tended to be larger, with a noticeable uptick in transactions since 2020 with successful issuances from Belize, Barbados, Ecuador, and Gabon amongst others.[12] Such swaps generally take the form of debt buybacks with some support (often partial guarantees) from the official sector. Whilst the bespoke and complex nature of the transactions can increase associated costs, such swaps have served as useful debt management operations, and have in some cases redirected savings to environmental or development projects. More can be done in this space, as advocated in Action X below, whilst noting the recent G20 Presidency note on the topic which summarises that "swaps are not considered suitable for addressing debt vulnerabilities, unsustainable debt, or fiscal and balance

(amount, maturity, grace period, interest rate, etc.) on a dedicated website or on the OECD Credit Reporting System (CRS) – at least for concessional loans.

[12] Example transactions include: Belize (2021, $553m), Barbados (2022, $151m), Gabon (2023, $500m), Ecuador (2024, $1.628bn). See Albinet, Chekir & Kessler, FDL_Policy-Note_D2S_June-2024.pdf ; 06/2024.

of payments crises. They cannot replace conditional concessional funding/grants, or comprehensive debt restructuring […] Swaps can serve as a useful debt management instrument in specific circumstances, but their effectiveness is limited [and] financing obtained through swaps could also be attained through conditional concessional loans or grants."[13]

b) Reshaping responses to debt vulnerabilities for the 21st century

Whilst significant progress has been made on the 2015 Addis declaration, the creditor landscape has also evolved substantially over the last decade, bringing new challenges. After the large-scale debt cancellations of the 2000s – principally through the Heavily Indebted Poor Countries (HIPC) and Multilateral Debt Relief (MDRI) initiatives - we now see a greater plurality of bilateral creditors alongside the traditional Paris Club members. The proportion of private sector debt in developing economies (notably Eurobond debt) has significantly increased as debtors took advantage of a historically low interest rate environment to issue on the markets, many for the first time. The share of non-Paris Club creditor to LICs has almost tripled from 8% to 20%, and private sector debt has more than doubled from 8% to 19%. Finally, domestic debt as a percentage of GDP has markedly increased, with the IMF estimating a tripling of domestic debt between 1993 and today from 8% to 24%.[14]

The Paris Club has continued to work effectively alongside the G20, IMF, World Bank and other stakeholders to tackle existing debt vulnerabilities and ensure responses are fit for this 21st century landscape. The first step forward was taken at the onset of the Covid-19 pandemic in April 2020, through the Debt Service Suspension Initiative (DSSI). This agreement across the G20 and Paris Club, provided additional fiscal space to countries under stress during the pandemic, by allowing for a deferral in debt service repayment.[15] It was implemented at speed and at scale to respond to the urgent pressures of the Covid-19 pandemic. From a total of 73 eligible countries, 48 participated, with the initiative suspending $12.9bn of debt service.[16] The DSSI was also complemented by significant emergency finance from the international financial institutions.

This first step was then built upon in November 2020, with the G20 and Paris Club members agreeing the Common Framework for debt treatments beyond the DSSI.[17] This landmark agreement established a new model for coordinated debt restructurings, bringing together Paris Club creditors, non-Paris Club G20 creditors, and any other willing official bilateral creditor, under a single official creditor committee (OCC). In short, it offers a mechanism to provide DSSI eligible countries with orderly and coordinated debt restructuring, with broad creditor participation and with the objective of contributing to putting a country back on a sustainable external public debt trajectory within the context of an IMF programme. The G20 Common Framework for debt treatment note endorsed by the G20 during the Saudi Arabian presidency, and also agreed by the Paris Club, presents the main principles of this coordinated approach: a case-by-case approach, where the process is initiated at the request of a debtor country; the need for a debt treatment, and the restructuring envelope that is required, being based on an IMF-WBG Debt Sustainability Analysis (DSA) and the participating official creditors' collective assessment, all consistent with the parameters of an upper credit tranche (UCT) IMF-supported program; and a requirement for the borrower to seek from all its other official bilateral creditors and private creditors a treatment at least as favourable as the one provided by the OCC under the Common Framework (i.e. the comparability of treatment principle).

[13] G20 Brazilian Presidency; G20 Presidency Note on Debt for Development Swaps; 10/2024
[14] Chuku et all; Are We Heading for Another Debt Crisis in Low-Income Countries? Debt Vulnerabilities: Today vs the pre-HIPC Era; 04/04/2023
[15] Staff of WB; Debt Service Suspension Initiative (DSSI); data update as of 02/12/2024
[16] Staff of WB; Debt Service Suspension Initiative brief; 10/03/2022
[17] Paris Club Secretariat; Club de Paris Common Framework brief; as at 31/01/2025

Several points follow from such a coordinated approach, but two in particular warrant attention. **The magnitude of the debt treatment is not set by bilateral official or private sectors, but by the parameters of the IMF supported program:** bilateral and private creditors then work with the borrower country on how to share debt relief that fills the financing gap identified in the DSA. Proposals to improve the DSA are explored in Action IV of this contribution**. The Common Framework also depends on the debtor initiating the process.** This is important as the timing of a debt treatment carries significant economic implications. The sooner a debt treatment is carried out, the quicker the country is able to look to the future, including accessing new financing on a sustainable basis. Yet getting to that point is not simple. First, a request for an IMF programme must be made, followed by negotiations with IMF staff on the programme parameters. In parallel, a Common Framework request can be made when necessary, where creditors then need to coordinate effectively amongst themselves, as well as with the debtor country and the IMF and World Bank. Initiating such a process and effectively declaring default can carry political, reputational and financial risks for a debtor country, which can lead some to delay. Borrower countries often need to take policy and technical ownership of their restructuring, and work alongside the IMF, official creditors, and commercial creditors in order to achieve timely results. Often doing so requires technical capacity and effective debt management operations.

c) Lessons learnt from initial cases

On the creditors' side, the implementation of the Common Framework by official bilateral creditors was initially too slow. As shown in the G20's lessons learned note, this was due to a myriad of substantive issues including: the need to establish new ways of working between emerging creditors and Paris Club creditors, including building trust and understanding between creditors; conducting significant data reconciliation and debt mapping to build a commonly accepted analytical base on which to proceed with the restructuring; solving complex technical issues such as the treatment of non-resident holders of domestic debt, or loan guarantees backed by export credit agencies; and finally due to complex and lengthy internal approval procedures for some creditors.[18]

However, the Common Framework has delivered concrete results – leading to agreements across a greater set of official creditors. Progress under the Common Framework has enabled borrower countries to access timely and vital IMF and MDB resources, which depend on progress in both the debt restructuring and the debtors' IMF programme. In the cases of Chad, Zambia and Ghana, the Common Framework has delivered agreements between the debtor country and its main bilateral creditors, grouped in OCCs:

- In the Chad case, while a surge in the oil price closed the financing gap during the IMF programme, the OCC agreed to address any request for debt relief should macroeconomic conditions deteriorate once more and a new financing gap materialize. In parallel, Chad's main private external creditor agree to defer repayments due during the IMF programme period.
- In June 2023, Zambia and the OCC agreed a restructuring of the \$6.3bn bilateral debt stock, which consisted of an almost total reduction of debt service over the IMF programme period (2023-25), a lowering of interest rates, an extension of average maturity duration by over a decade, and a review clause to assess Zambia macroeconomic performance in 2025.
- In January 2024, Ghana and its OCC agreed on rescheduling 100% of the debt service due to official creditors during the IMF programme (2023-2026), with interest rates reductions and repayments of these maturities not restarting before more than a decade and a half.

[18] G20 IFA Working Group Publications; G20 2024 Finance Track documents hub: see G20 Note on the lessons learned from the first cases treated by the Common Framework; 10/2024

- In Ethiopia, bilateral creditors were able to provide a debt suspension to Ethiopia over 2023-2024 ahead of an agreement with the IMF on a programme, providing the county with breathing space to prepare its updated homegrown economic reform agenda. Now an IMF programme is in place, the debt restructuring itself is ongoing and moving faster as creditors build on previous cases.

The Common Framework process has become faster and more effective with each case. The debt treatment process for Ghana was quicker and information sharing with all stakeholders richer than it was for Zambia. Concretely, for Chad it took 23 months to proceed from a Staff-Level Agreement (SLA) to the agreement on the main parameters. In Zambia this delay was 20 months. In Ghana this took 13 months. In Ethiopia the equivalent will have taken 8 months.

Agreements with bilateral creditors under the Common Framework have also supported Zambia and Ghana in reaching agreements with sovereign bondholders. The Common Framework includes the Comparability of Treatment (CoT) principle which ensures that the financial effort made by private creditors in their specific debt treatment is at least as favourable to the borrowing country as that granted by bilateral public creditors. Compliance with the principle of comparability of treatment ensures that the efforts made by bilateral creditors (and thus their taxpayers) is comparable to the efforts made by the private sector, whilst integrating the different needs of different creditor classes. The CoT principle also provides the borrower with leverage to negotiate and come to timely agreements with non-OCC creditors, as the borrower commits to remaining in arrears to creditors until a CoT compatible agreement can be reached – meaning it is in the interest of all parties to reach such an agreement. The application of comparability of treatment meant that Zambia and Ghana were able to negotiate deals with bondholders and other private external creditors soon after the OCC deals. As of February 2024, both countries had effectively restructured more than 85% of their respective external bilateral and private debt thanks to the application of CoT. This isn't always simple - as Zambia's initial negotiations with its bondholders proved, whereby the first agreement with bondholders was rejected as it was not coherent with debt sustainability and the CoT principle - but the end result is a fair debt restructuring across all key creditor classes, and which in Zambia's case structurally reduces its debt vulnerabilities. Similarly in the Chad case, the CoT principle ensured that the main private creditor was part of the restructuring exercise. Here also negotiation dynamics are picking up speed, as negotiations with the private bondholders, be they in the Common Framework like Ghana, or outside of it like Sri Lanka, were much quicker.

Finally, value-recovery instruments (VRIs) have also been a feature of several recent debt restructurings, both inside and outside the Common Framework. In Suriname, bondholders requested a VRI indexed on oil revenues from an oil-field project which was not included in the IMF macroeconomic assessment. Official creditors ultimately integrated a similar clause in their agreement with Suriname. In Zambia, private creditors asked for a VRI based on the country's debt carrying capacity, as Zambia was close to the threshold between low and medium debt carrying capacity, as defined by the IMF. Again, official creditors also ended up including a similar "upside" clause in their agreement with Zambia. In both these cases, VRIs were therefore included across both private and bilateral official creditors, justified by an exceptional external factor impacting the debtor's debt payment capacity. Whereas, in the Sri Lanka case, bondholders proposed a macro-linked bond, based on diverging macroeconomic assumptions from those of the IMF. Official creditors did not include such an option in their agreement with the country. The design of VRIs is highly complex and can carry unwanted side effects for creditor and the borrower countries alike: without a cap to limit the additional debt service, creditors may capture all of the revenues associated with the improvement of the macroeconomic situation; the trigger depends on reliable data from the debtor country; VRIs are not always attractive for investors as such instruments may not be liquid on the secondary market; and VRIs can complicate the assessment of the CoT principle. From the Paris Club perspective, whenever possible, it is preferable not to introduce a VRI in debt restructuring, for both private and bilateral official creditors. However, when such instrument is introduced, it should be based on a specific external factor (such as future commodity revenues) which can significantly improve the debt payment capacity of a country, rather than any open-ended instrument which effectively claws-back from the debtor any macroeconomic outperformance.

3. Concrete proposals for FfD4

A lot has been achieved since Addis Ababa. But there is much work still to be done. The Paris Club is fully engaged with the international debt reform agenda, and proposes below a 10-point action plan to improve the way in which the international community addresses debt vulnerabilities. This 10-point plan aims to respond to requests for the international financial architecture to be more open and inclusive to a range of voices including critically borrower countries, to provide swifter debt treatments when they are required, and to better support countries facing debt vulnerabilities.

I. Action I – Strengthening macroeconomic and institutional fundamentals

Sustainable borrowing depends on a broad base of country-owned policies including public spending efficiency, domestic resource mobilisation, strong governance and institutional capacity, structural reforms to drive inclusive growth, and stable, transparent and predictable macroeconomic policy environment to catalyse investment. As the Summer and Singh report shows, domestic resource mobilisation is a crucial component, as it is estimated to represent the largest single financing source to meet financing needs - $2trn annually.[19] The IMF and World Bank have also shown there is significant untapped potential in this space – with estimates that on average lower income developing economies could increase their tax revenue by 6.7% of GDP to help meet SDGs financing needs, whilst emerging market economies could raise an additional 5% in GDP in tax to finance development spending.[20] Moreover, a working paper from the IMF supports the link between effective domestic resource mobilisation and growth, showing that countries with a tax-to-GDP ratio below 15% are less likely to be able to meet their spending needs in a manner that is consistent with price stability and fiscal sustainability—and thus, they tend to grow slower than countries with a ratio above 15%.[21] There are 41 out of 75 IDA countries with tax revenues below 15% of GDP. The Paris Club secretariat supports initiatives that aim to strengthen macroeconomic and institutional fundamentals, including country-led reforms which can be worked-up with the IMF and World Bank and other sources of relevant multilateral and bilateral assistance, as well as through initiatives such as the joint IMF and World Bank initiative to step up domestic resource mobilisation, while addressing social acceptability for policy changes.

Action I: reiterate the importance of strengthening macroeconomic fundamentals, to help meet financing needs and drive inclusive growth while securing social acceptability for policy changes, and highlight the initiatives in place from the likes of the IMF and WB to support this objective.

[19] Summers, Singh et all; The_Triple_Agenda_G20-IEG_Report_Volume1_2023.pdf; 07/2023

[20] Staff of IMF/WB; Stepping up domestic resource mobilisation: a new joint initiative from the IMF and WB; 06/2024.

[21] Gaspar et all; Tax Capacity and Growth: Is there a Tipping Point?; 2/21/2016

II. Action II – Taking an evidence-based analytical approach

The conference should continue to highlight the ongoing importance of debt financing in meeting the SDGs and climate needs, as one of a range of financing options to be complemented by others. The growth in global external liabilities also means that absolute debt statistics are likely to continuing growing, in line with global economic growth. FfD4 would do well to draw on leading debt analysis, from the likes of the IMF and World Bank amongst others, to prepare a clear-eyed and nuanced view on debt vulnerabilities globally, where the picture is heterogenous.

Action II: encourage an evidence-based analytical approach in assessing debt vulnerabilities.

III. Action III – Supporting sustainable lending and borrowing practices

Given the need for continued debt financing to meet financing needs, the international architecture needs to foster sustainable borrowing and lending practices. The Paris Club supports initiatives that aim to foster better borrowing and lending practices, including the G20 sustainable finance principles, the OECD sustainable lending practices, the UNCTAD principles of promoting responsible sovereign lending and borrowing, and the IIF principles for stable capital flows and debt restructuring amongst others. Rather than drawing up another round of principles, priority should be placed on putting existing principles in place, identifying common ground, and delivering on them, with a consensus on agreed monitoring and evaluating mechanism. The IMF and World Bank could also consider these principles as part of their overall surveillance work, in their analysis of debt vulnerabilities, and in programme design, as well as creditors and debtors conducting voluntary self-assessment. In all cases, any new work should consolidate what has come before and be led by the likes of the IMF and World Bank.

Action III: call on all stakeholders to engage in a dialogue on, consolidate and put into practice existing principles on responsible sovereign lending and borrowing, and set a process for monitoring their implementation, with one example being the IMF and World bank integrating into their ongoing surveillance work and programme design.

IV. Action IV – Improving debt sustainability analysis frameworks

As the lender of last resort and trusted, independent third party, the IMF, along with the World Bank, play a fundamental role in the sovereign debt architecture. The IMF provides borrowing countries with balance of payment support and helps set a stable long-term macroeconomic trajectory, which instils confidence - catalysing additional finance from the official and private sectors. Moreover, IMF and WB debt analysis (DSA) is central in assessing countries' debt sustainability – providing a comprehensive analysis of country’s debt risks including across external and domestic debt inclusive of local currency financing, helping countries to take corrective action when vulnerabilities reach a critical level, and triggering a resolution mechanism and treatment when debt is no longer sustainable. In the latter case, the depth of any debt treatment is a function of the DSA. The IMF and WB debt sustainability frameworks are consequently a central global public good, whose parameters are set by the IMF and WB boards, where all member states are represented, and then put into practice in an independent manner by IMF and WB staff.

The IMF and WB have already launched a review of their debt sustainability framework (DSF) for low-income countries, which amongst other elements will consider how to better integrate climate risks and analyse debt risk signals depending on their appearance on the time horizon of the LIC DSF. Progress can already be seen, with supplementary guidance published in the summer of 2024 on the integration of climate risks in DSFs.[22] The Paris Club supports this review, to ensure the LIC DSF remains fit for the challenges faced by low-income countries, whilst maintaining the clarity and credibility of its analysis. But in preparing DSAs for both low-income countries and market access countries, the IMF and WB could go further in their stakeholder engagement, to ensure they hear from a broad range of perspectives and actors and they adequately take into account the potential of the reforms undertaken by the countries. Whilst ultimately the IMF and WB need to independently set their DSA analysis as a global public good, the preparation of DSAs would be enriched by actively hearing the broadest possible perspectives. The DSF review could also explore adapting DSA thresholds dynamically, to ensure countries that are pursuing high ambition macroeconomic reforms are rewarded, and have the fiscal space against debt targets to pursue high quality investments.

Action IV: support timely completion and operationalisation of the LICs DSF review, and encourage the IMF and World Bank to broaden consultations and stakeholder engagement on DSAs as they are being developed, whilst emphasising that as the independent arbiter providing a global public good only the IMF and WB can set final DSAs.

V. Action V – Improving the Common Framework & debt restructuring cases

There is room for improvement to step up the implementation of the Common Framework, and the Paris Club fully supports the G20 *Note on the lessons learned from the first cases treated by the Common Framework* and is ready to go further. This note sets out a series of specific areas where improvements can be made including: streamlining or speeding up internal procedures for approval of treatments by public creditors; clarifying the main stages in the restructuring process and actions to be taken by the various parties including indicative timelines for debtor countries to reduce uncertainty; improving transparency on the part of public creditors on the progress of negotiations and other non-confidential information; encouraging private creditors to form joint private creditor committees; developing creditors' debt data transparency.[23] Paris Club creditors are committed to the full implementation of the G20's Lessons Learned note.

The Lessons Learnt note also highlights how further assessment is warranted on debt service suspensions (i.e. debt standstills) from official bilateral creditors during the negotiation of a debt treatment, building on the experience with Ethiopia. A simple and effective way of implementing such an approach would be a semi-automatic provision of a debt service suspension by OCC creditors, upon request for a debt treatment under the Common Framework. Bilateral creditors could agree to remain in arrears during the restructuring period without charging late interest, conditional on the borrower being fully committed to negotiating and implementing an IMF programme. Such an approach would ensure that the borrower does not bear any additional costs from the time it takes to conduct the restructuring, provide short-term liquidity support, and ensure greater clarity on repayment expectations during the restructuring.

Moreover, the Common Framework does not cover all countries, even though effective coordination between bilateral creditors is also required in cases of vulnerable middle-income countries that also find themselves in default. Whilst there is not yet a G20 consensus on this, many Paris Club creditors

[22] Staff of IMF and WB; Supplement to 2018 Guidance Note on the Bank-Fund Debt Sustainability Framework for Low Income Countries in: Policy Papers Volume 2024 Issue 039 (2024); 05/08/2024
[23] G20 IFA Working Group Publications; G20 2024 Finance Track documents hub: see G20 Note on the lessons learned from the first cases treated by the Common Framework.; 10/2024

deem that the Common Framework could be improved by broadening its scope to vulnerable middle-income countries also, on a case-by-case basis. In the meantime, the lessons learnt from initial Common Framework cases should also be applied in non-eligible cases, to maximise as much as possible shared understanding and coordination across all bilateral creditors – as in the Sri Lanka case, where an official creditor committee was formed with co-chairmanship between India, Japan and France as chair of the Paris Club, and the OCC conducted light-touch informal coordination with China to support the smooth conclusion of the debt restructuring across all bilateral creditors.

Both inside and outside the Common Framework, VRIs should be treated on a case-by-case basis and with caution. A GSDR-Paris Club workshop on VRI is planned in March 2025 to analyse their recent use and identify best going forwards when introducing VRIs in debt restructuring.

Box 1 – Multilateral sovereign debt mechanism - The zero draft of the FfD4 outcome document calls for the exploration of a multilateral sovereign debt mechanism. The added value of such an approach and how it would work in practice is unclear and therefore Paris Club members do not support a new multilateral sovereign debt mechanism. At best the envisaged mechanism risks tortuous discussions to agree the precise shape of such a mechanism, which would then in effect duplicate the existing debt architecture already in existence, undermine the independent governance, authorities and mandates outside the UN including international financial institutions, and increase confusion as to how to treat debt vulnerabilities. At worst, such a mechanism risks impeding the flow of new financing from private and official sector creditors out of concern that the politization of debt treatments, particularly if such a restructuring mechanism were housed at the UN, will lead to creditors being forced to take losses beyond what is judged necessary in the IMF/WB DSA to put debt on a sustainable path – at a time when debt flows are needed to meet financing needs.

Ultimately, debt restructurings require charting a difficult course through very different and sometimes diametrically opposed interests – with the aim of finding an acceptable agreement which supports the debtor's long-term sustainability. It is a delicate balancing act, which creditors choose to engage with on the basis of clear independent economic analysis from the IMF and World Bank, and effective coordination mechanisms like the Common Framework or Paris Club. To be effective, coordination mechanisms need to be led by actors with "skin in the game", which builds trust and helps bilateral creditors find the balance between supporting the borrower country and doing right by their own taxpayers and domestic constraints. As explored in this contribution, there is more work to be done to move faster and more effective, and to be more responsive to debt vulnerabilities. But reform and improvements should build on what has come before and worked successfully, rather than proposing new initiatives which are at best at a conceptual stage.

Action V: step-up implementation of the Common Framework in a predictable, timely, orderly and coordinated manner and produce a User Manual to enhance clarity for debtor countries; fully implement the recommendations of the G20 Lessons Learned note; provide semi-automatic debt standstills upon request for a Common Framework debt treatment; improve the transparency of debt restructuring cases; and open a discussion on expanding Common Framework eligibility to vulnerable middle income countries.

VI. Action VI – Better supporting countries facing liquidity stress

Recognising ongoing debt service challenges, coordinated and effective responses to support solvent countries facing short-term liquidity pressures is more relevant than ever. The Paris Club has a long history of providing both stock and flow debt relief when appropriate, with flow relief via debt reschedulings an option for countries experiencing liquidity stress.[24] The Common Framework can also act to support borrowers' facing both liquidity and solvency issues.

However, a debt treatment is not always appropriate when a country has a viable medium-term debt profile, but is facing large, bunched upcoming repayments and financing needs to meet the SDGs. Over the last year, the Paris Club has supported multilateral discussions on how to support these sets of countries, drawing on its experience, and hosted think-tanks such as the Financing for Development Lab in presenting their response ideas.[25] The IMF and World Bank have effectively brought together this thinking and progressed the discussion by developing a three pillar approach, centred on : i) domestic resource mobilisation, to generate the fiscal space necessary to boost growth and jobs; ii) international financial support; iii) reducing debt servicing burdens, including using mechanisms from multilateral and bilateral partners to leverage in the private sector via credit enhancements to support transactions akin to debt swaps on private debt.[26] Implementing such an approach would directly address liquidity challenges equitably, with all stakeholders playing a role. For their part, bilateral creditors could contribute, on a voluntary basis, to making their "best efforts" to provide new financing, with the ambition to provide net positive flows on aggregate level (i.e considering all flows from IFIs, bilateral official and private creditors) during a time of illiquidity for the borrower.

Action VI: support the timely implementation of IMF-WB efforts on liquidity support for countries that demonstrate strong performance on domestic revenue mobilization and improving their investment climate through reforms. Such efforts could be supported, on a voluntary basis, by creditors making "best efforts" to provide new financing that contributes to providing net positive debt flows to a borrower country facing a period of illiquidity.

VII. Action VII – Fostering better coordination on debt issues across international stakeholders

Whether the focus is improving how debt restructurings work, or considering approaches to support countries facing large debt service repayments in the short-term, effective collaboration, coordination and partnership across relevant actors is key.

Box 2 – Paris Club outreach - *The Paris Club invites observer countries to attend its monthly Tour d'Horizon meetings, to horizon scan upcoming debt risks with a view to collaborating in preparing solutions; has organised several open workshops to discuss technical debt restructuring issues like the Comparability of Treatment Principle; and organises the annual Paris Forum between official and private creditors, IFI, borrowing countries, academics and NGO, as well as the annual meeting of the Paris Club and the Institute of International Finance (IIF) to encourage greater collaboration and information sharing across different stakeholders across the broad suite of debt issues. The Paris Club acts as a forum where creditors, debtors, and civil society organisation can debate the key debt issues of the day.*

The Paris Club strives to foster better common understanding on debt and debt treatment negotiations between creditors - both within and beyond the Paris Club – debtors and all stakeholders. It does this through set-piece events like the annual Paris Forum, by being an active participant in other multilateral platforms, and by publishing contributions on its website and its annual report. Dialogue and a clear understanding of debt issues are essential to better understand country situations, to

[24] Paris Club secretariat staff; Flow and stock treatments explained; 04/02/2025
[25] Diwan et al.; An Updated Bridge Proposal | Policy Note ; 23/07/2024
[26] Pazarbasiglu & Saavedra; Now Is the Time to Help Countries Faced with Liquidity Challenges ; 01/08/2024

explain and improve debt restructuring processes which are often complex, and to anticipate possible future difficulties. But there is always more that can be done, in particular to anchor the United Nations' (UN) thinking on debt policy issues, and in this vein the opportunity for a**n annual dialogue at the UN could be explored, between countries facing debt vulnerabilities issues, the Paris Club, other official creditors, and with the IMF and World Bank also participating.** The terms of reference for such an annual dialogue could be discussed between UN/DESA, Paris Club and other interested stakeholders.

Action VII: consider the opportunity for an annual dialogue to be set-up across UN institutions and countries facing debt vulnerabilities, the Paris Club, other official creditors, and the IMF and World Bank.

VIII. Action VIII – Bettering transparency

Data transparency from all creditors, including emerging and private creditors, and debtors is in the common interest of the international financial community, supporting analysis of debt vulnerabilities globally; ensuring at the country-level that debt sustainability analyses by international institutions and other actors is comprehensive; acting as a marker and signal of good domestic governance and debt management practices; and supporting faster debt treatment resolutions when needed by speeding up data reconciliation. The publication of detailed line-by-line data by all creditors should remain the ultimate goal. However, given the current state of the debate and national legal constraints and procedures, this is realistically a long-term objective, which can best be achieved through incremental steps forward. At this juncture, the most effective next step would be for all major creditors to share their data directly with the World Bank International Debt Statistics (IDS), which is *de facto* the single global central debt data registry, for reconciling data reported by debtors to the World Bank. The international financial community should leverage the technical architecture and expertise already in existence via this global public good from the World Bank. Creditors who remain reluctant to publish detailed data could share their data directly with the World Bank as a trusted and independent third party, under a specific protocol – at the very least for LICs. This would further improve the quality of WB IDS and LICs data, which could be published at the aggregate level on the database – therefore preserving the required level of confidentiality some creditors have. Any such approach would also need to be consistent with creditors' national laws and internal procedures.

Action VIII: promote better information sharing from creditors and borrowers alike; as a first concrete step launching a data-sharing protocol negotiation across creditors under the G20 or GSDR, with the aim of agreeing improved creditor data-sharing through the World Bank's IDS platform, and encourage the World Bank to stand ready to receive greater flows of creditor debt data for data reconciliation.

IX. Action IX – Supporting higher contractual standards

The widespread adoption, since Addis Ababa, of Collective Action Clauses (CACs) in bonds has meaningfully improved the speed of debt restructurings by limiting non-cooperative behaviour. However, CACs only apply in bond contracts, yet in 2023 bondholders made up just under half of all private creditor debt stocks in low- and middle-income countries.[27] The other half is held by banks and other private creditors. Extending the sort of contractual provisions seen in CACs to the syndicated loan market ("majority voting provisions") would therefore further the progress made.

[27] Staff of WB; International Debt Report; 03/12/2024, p.4

Action IX: extend collective action provisions to commercial loans in the form of Majority Voting Provisions (MVPs).

X. Action X – Bolstering systemic deployment of climate resilient debt clauses (CRDCs) in debt contracts & standardise debt swaps

CRDCs directly respond to the risk that the frequency and severity of natural disasters can impair the debt repayment capacity of borrower countries, providing for temporary liquidity support which can help reduce the risk of default when a natural disaster hits. Significant progress in the adoption of CRDCs has been made, buoyed by several initiatives including the UK's private sector working group, the "call to action" held during the 4P Paris summit of 2023, the active leadership of multiple MDBs, and the Brazilian G20 presidency's note on this topic.[28] This G20 Presidency note also highlighted the range of choices and challenges in incorporating such clauses into debt instruments including defining precise triggers, evaluating financial impacts, ensuring robust legal enforceability, and fostering market acceptance. These clauses have now been adopted by several Paris Club members in their sovereign lending, as well as by multiple MDBs. But the effectiveness of CRDC's hinges on their widespread adoption by diverse creditors, and so creditors should assess whether they can integrate these clauses into their lending instruments. The G20 could also map the creditors using CRDCs to bolster transparency on their integration into lending instruments and identify problems they face in its application.

Given the increasing size of private sector debt, debt-swaps on private debt present significant promise in supporting borrowers' debt and liability management operations. However, the costs and bespoke nature of these types of debt-swap transactions can lessen their impact. Standardising approaches to debt-swaps across borrower countries could have a significant impact in increasing their use and effectiveness, whilst lowering associated transaction fees.

Action X: encourage further evaluation and uptake of CRDCs in lending instruments, and ask the G20 to conduct a mapping exercise on the current use of CRDCs by creditors; call for the WB to set-up a taskforce to produce replicable examples i.e. principles/best practice/standardise as far as possible) for debt-swap transactions on private debt.

[28] G20 Brazillian Presidency; G20 Presidency note on climate resilient debt clauses; 10/2024