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Global Sovereign Debt Roundtable

3rd Cochairs Progress Report

October 23, 2024

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Executive Summary

Further important progress has been achieved since the Global Sovereign Debt Roundtable (GSDR) last met at Principals level in April 2024. Ongoing restructuring cases have reached important milestones, both under the Common Framework (CF) and outside. As evidenced by the recent achievements by Ghana and Ethiopia, the Common Framework is delivering faster and more predictable debt treatments. Agreements on Sri Lanka confirm restructuring processes outside the Common Framework are also working better.

There is greater common understanding on key aspects of debt restructuring processes, including on comparability of treatment, information sharing among stakeholders at the different steps of the process, and expected timelines, among others. **The GSDR has contributed to this progress** by providing a platform to discuss and progressively advance this common understanding, while recognizing that individual debt restructurings are undertaken case-by-case and through relevant negotiating processes, including creditor committees. Status of the GSDR discussion since its beginning is accessible through the "**GSDR Compendium of Common Understanding on Technical Issues**", which compiles the successive GSDR Cochairs Progress Reports.

It remains critical to continue this work. Debt vulnerabilities remain elevated, and uncertainties in the global economy are significant. Continuing to further advance and solidify the common understanding on key technical issues, drawing lessons from the experience, is necessary to ensure efficient, timely and predictable restructuring processes are in place for future cases, and to strengthen the debt restructuring architecture.

In addition, supporting countries where debt is sustainable, but where liquidity pressure is high, has become a priority. While solvency risks seem broadly contained, many low-income countries and some emerging markets face significant liquidity pressures. Addressing these liquidity challenges in a timely manner is essential to support growth and development prospects. If unaddressed, these liquidity challenges could morph into a debt crisis.

The IMF and World Bank have proposed a three-pillar approach to help address current liquidity challenges. This three-pillar approach, presented in a joint Bank-Fund non paper, combines structural reforms to boost growth and jobs and mobilize domestic resources, supported by capacity development (Pillar 1); adequate financial support, including from international financial institutions (Pillar 2); and actions to reduce debt servicing burdens, including through greater use of risk-sharing instruments by external partners, where relevant, to incentivize higher inflows from private creditors (Pillar 3). Countries, whose debt is sustainable, but experiencing temporary liquidity pressures, as assessed through debt sustainability analysis, and that are undertaking or committed to structural and fiscal reforms, could make use of this three-pillar approach. While the policies and instruments under each of these pillars are available to all countries, and constitute a "menu of options", the approach would activate a country-specific package, tailored to the country's unique circumstances and needs.

There is broad consensus among GSDR members on the urgency of tackling liquidity challenges and the importance to combine different support mechanisms. Ensuring coordinated efforts, while keeping a bottom-up, country-specific approach, building on experience, as the causes and size of

liquidity challenges may differ significantly from one case to the other, is also understood as essential. GSDR participants underlined, however, that more work is needed and agreed to continue this discussion in the coming months to flesh out further the consensus on how to address these challenges.

The GSDR has also continued its work on technical issues, including the use of state-contingent debt instruments (SCDIs) and the trade-offs associated with collateralized debt from private creditors. SCDIs can help bridge the gap between borrower and creditors in certain restructuring negotiations where uncertainty is high, but they should not be the norm. When used, SCDIs should have well-defined verifiable triggers and be consistent with debt sustainability assessments and IMF program parameters in all scenarios. Depending on the case, there may also be merits to introduce payout caps and mechanisms to ensure that payments can be adjusted both up and down depending on how conditions evolve. Discussion underlined that further work is warranted on these issues, including how to assess and enforce comparability of treatment when SCDIs are used. On collateralized debt, GSDR discussions underlined broad consensus on the importance of ensuring transparency as well as increasing awareness on the benefits and risks of collateralized financing practices, and of helping debtor countries address these issues through training and technical assistance missions.

Going forward, GSDR Principals supported continuing the work on efficient, timely and predictable processes to resolve situations of unsustainable debt; clarifying further the use of SCDIs in debt restructurings, especially the assessment of comparability of treatment when SCDIs are used, including through a specific workshop; advancing operational ways to address liquidity challenges; and deepening the work on ways to build resilience, including through improving debt transparency, debt management and debt reporting. Specific attention should be given to ways to support building fiscal resilience in small states.

Section 1: Update of developments since April 2024

Ongoing debt restructuring cases have further advanced:

Ongoing restructurings have continued to progress since last April, both under the Common Framework (CF), with the cases of Ethiopia, Zambia and Ghana, and outside, with the cases of Sri Lanka and Suriname.[1] In particular:

- Ghana has reached an agreement in principle with its international bondholders in June and completed the 2nd Review of its Fund-supported program shortly after, on June 28. It has finalized its Eurobond exchange in October.
- Sri Lanka has reached a final agreement with the OCC and China EXIM in June, and an agreement in principle with its international bondholders in September. Meanwhile, the 2nd Review of its Fund-supported program was completed on June 12.
- Ethiopia has reached a key milestone under the Common Framework. After reaching staff-level agreement with the IMF in May, the OCC (co-chaired by China and France) met in July and provided the financing assurances paving the way for the presentation of the Fund-supported program to the IMF Board. The program was approved by the IMF Board on July 29 and the first review approved on October 18.

	Common Framework				Non-Common Framework	
	Chad	**Zambia**	**Ghana**	**Ethiopia**	**Suriname**	**Sri Lanka**
Date of SLA 1/	January 27, 2021	December 3, 2021	December 12, 2022	May 7, 2024	April 29, 2021	September 1, 2022
Paris Club / OCC assurances	June 16, 2021	July 30, 2022	May 12, 2023	July 11, 2024	November 30, 2021	February 7, 2023
Program approval	December 10, 2021	August 31, 2022	May 17, 2023	July 29, 2024	December 22, 2021	March 20, 2023
AIP reached with PC or OCC	November 11, 2022	June 22, 2023	January 12, 2024	-	June 22, 2022	November 29, 2023
1st review 2/	December 22, 2022	July 13, 2023	January 19, 2024	-	June 14, 2023	December 12, 2023
2nd review 2/	December 22, 2022	December 20, 2023	June 28, 2024	-	December 15, 2023	June 12, 2024
Number of months passed between: -						
SLA & program approval	10.5	8.9	5.2	2.1	7.8	6.6
program approval & 1st Review 3/	12.4	10.4	8.0	-	17.7	8.8
SLA & 1st review	22.9	19.3	13.2	-	25.5	15.4

1/ For Ethiopia, there was no formal announcement of the SLA. The table shows the date when agreement was made between IMF staff and the Ethiopian authorities on policies.
2/ For Chad, the 1st and the 2nd Reviews were combined. For Suriname, the dates are for the 2nd and the 4th EFF reviews respectively since their reviews occur on a quarterly basis.
3/ The protracted timeline for Suriname was not only owed to difficulties in the restructuring process, but other country-specific circumstances.

[1] The case of Malawi, where the debt restructuring does not involve the creditor coordination challenges that have been the focus of the GSDR work so far, is of a different nature.

In parallel, policy work at the GSDR or of interest for the GSDR have included:

- **The G20 has continued its work to address debt vulnerabilities**, including meetings at working group, Deputies, and Ministers and Central Bank Governors level, and has made important progress on drawing the lessons learned from the first cases of implementation of the Common Framework for Debt Treatment as well as on building understanding on the use of climate-resilient debt clauses and debt swaps.
- The IMF and the World Bank have published in August their **Supplementary Guidance Note on the Debt Sustainability Framework for Low-income Countries (LIC DSF)**, complementing the existing guidance to staff on how to implement the current LIC DSF to help address issues that have become more prominent. The supplement provides further guidance and practical examples on how to account in a more structured way for risks stemming from climate change and domestic public debt vulnerabilities, and on the use of the LIC-DSF in debt restructuring situations. The IMF and the World Bank have also further advanced their work on the **comprehensive review of the LIC DSF**, as part of the regular review of existing frameworks.
- The IMF is finalizing a **Guidance Note on the Fund's sovereign arrears and financing assurances policies**, and the IMF's role in debt restructuring situations. This will be the first comprehensive operational guidance on these IMF debt policies, replacing guidance that was so far available through different documents.
- The IMF and the World Bank staff published end-July a **note on "*Stepping Up Domestic Resource Mobilization: A New Joint Initiative From the IMF and World Bank*"** and a **note on "*Debt for Development Swaps: An Approach Framework*"**. The World Bank has also published a technical note on the potential role of the World Bank in such transactions.
- **A technical workshop on comparability of treatment (CoT) was organized on June 26 by the Brazilian G20 Presidency and the Paris Club**. Lessons were drawn to enhance coordination and support more parallel negotiations between official and private creditors, along with earlier information sharing. The Paris Club published in June its detailed position on CoT.
- **A GSDR Technical Meeting on state contingent debt instruments (SCDIs) and on collateralized financing practices was held on July 8.** The meeting discussed the potential use of SCDIs in particular in restructuring contexts, focusing on the costs and benefits of such instruments, and characteristics they should have when used. The meeting also discussed the use of collateralized financing from private creditors and the specific challenges it can pose.
- **An Open GSDR Workshop on liquidity challenges was held on September 16**, focusing on the situation faced by many low-income and some emerging market economies where debt is sustainable, but debt service and refinancing needs are high. The workshop discussed both the assessment of the situation and potential policy options, with participation of all GSDR members, G20 members, Paris Club members and a large representation of private creditors, borrowers, multilateral development banks (MDBs), civil society organizations (CSOs), and debt experts.
- **GSDR Deputies met on October 9 to review and further advance the technical work and prepare the meeting of GSDR Principals on October 23.**

Section 2: Building Further Common Understanding on Debt Restructuring Challenges

Further supporting efficient, timely and predictable restructuring processes

Significant progress has been achieved to make restructuring processes more efficient, timely and predictable. As evidenced by the recent achievements by Ghana and Ethiopia, the Common Framework is delivering faster and more predictable debt treatments. Agreements on Sri Lanka confirm restructuring processes outside the Common Framework are also working better. There is now greater common understanding on key aspects of debt restructuring processes, including on comparability of treatment, information sharing among stakeholders at the different steps of the process, and expected timelines, among others. The GSDR has contributed to this progress by providing a platform to discuss and progressively advance this common understanding, while recognizing that individual debt restructurings are undertaken case-by-case and through relevant negotiating processes, including creditor committees. Status of the GSDR discussion since its beginning is accessible through the "GSDR Compendium of Common Understanding on Technical Issues", which compiles the successive GSDR Cochairs Progress Reports.

It remains critical to continue this work. While the need for debt restructuring appears contained at this stage, debt vulnerabilities remain elevated, and uncertainties in the global economy are significant. Continuing to further advance and solidify the common understanding on key technical issues, drawing lessons from the experience, is necessary to ensure efficient, timely and predictable restructuring processes are in place for future cases, and to strengthen the debt restructuring architecture.

State Contingent Debt Instruments

State-Contingent Debt Instruments (SCDIs) are debt instruments with cash flows that differ according to future states of the world. Typical SCDIs are value-recovery instruments (VRIs), which provide for additional payments (upside) in a state of the world associated with a higher capacity to repay by the debtor. These include warrants linked to GDP or commodity prices. Most recently, climate resilient debt clauses (CRDCs) have become more prominent. CRDCs typically provide liquidity relief in the case of a natural disaster (downside), automatically reprofiling cash flows in an NPV-neutral fashion.

SCDIs have only been used in a few past debt restructurings but there seems to be renewed interest. Earlier examples of the use of SCDIs in debt restructurings include the GDP warrants issued to private creditors in Argentina (2005/10), Greece (2012) and Ukraine (2015), an upside instrument linked to Citizenship by Investment revenues in Grenada (2015), and "value recovery rights" linked to GDP, oil prices and measures of the terms of trade in many of the Brady restructurings of the 1980s and 90s. More recently, Suriname's 2023 restructuring with international bondholders has included a value recovery instrument (VRI) linked to future oil revenues. New triggers have been considered in more recent cases, for example in Zambia (SCDI linked to future debt carrying capacity or exports) and Sri Lanka (SCDI linked to future GDP or governance improvements). On the flipside, Ghana's debt restructuring did not include any SCDI, while being completed relatively quickly.

SCDIs involve costs to the debtor. SCDIs are not "free" and change the balance of risks around the baseline. Depending on their design, costs to the debtor could be unjustifiably high as the debtor governments in crisis may risk selling off their future revenues to creditors. Even if the country can afford the payments in the "good states" it will limit its ability to rebuild buffers. Depending on how the triggers are designed, it may also be the case that the higher SCDI pay-offs get triggered in a situation where the capacity to repay is actually low—thereby reducing the country's ability to stay current on its debt service.

For their part, investors have typically shunned and undervalued VRIs, due to their complexity, lack of liquidity, limited correlation with conventional fixed-income portfolios, and susceptibility to government influence. From the borrower's perspective, VRIs have been limited in effectiveness due to undervaluation by creditors, lack of payout caps, indexation lag, political incentives for overly generous terms, moral hazard problems, and the potential to introduce uncertainty regarding the country's future debt path. Capacity challenges in monitoring VRIs on an ongoing basis and calculating the required debt service are also a concern, especially for LICs.

Participants in the July 8 GSDR Technical Meeting and subsequent October 9 GSDR Deputies meeting agreed that SCDIs can help bridge the gap between borrower and creditors in certain restructuring negotiations where uncertainty is high, but they should not be the norm in debt restructurings. In general, agreeing on a fully defined debt treatment early on brings certainty to the creditors and investors and is more efficient than a contingent restructuring. There may be cases, however, when uncertainty around the economic outlook and future capacity to repay of the country is so high that it is difficult for the debtor and its creditors to find a common ground in a timely manner, while delaying the negotiations until uncertainty dissipates is costly for all. In such circumstances, SCDIs can help bridge debtor-creditor differences. This is particularly the case when major assumptions on the future of the economic prospects of the debtor country impact significantly the restructuring envelope (e.g. assumptions on new sources of revenues such as new oil fields, significant evolution of the debt carrying capacity etc.).

When used, SCDIs should have well-defined verifiable triggers and be consistent with debt sustainability assessments and IMF program parameters in all scenarios. Depending on the case, there may also be merits to introduce payout caps and/or mechanisms to ensure that payments can be adjusted both up and down depending on how conditions evolve. If SCDIs are used to facilitate debt restructuring negotiations, their design should involve the following: (i) a careful selection of verifiable triggers that best reflect increased repayment capacity by the borrower country, (ii) ensuring that the payments associated with the use of the SCDIs do not compromise the borrower's debt sustainability prospects (for instance by setting payout caps), and (iii) the use of market friendly design to the extent feasible, such as one-time tests and shorter-maturity instruments to limit uncertainty, subject to debt sustainability risks being adequately managed.

SCDIs also pose CoT challenges which need to be taken into account for the restructuring timeline. Assessing CoT is further complicated by the presence of SCDIs, given the inherently higher uncertainty over cash flows, and lack of agreement at this stage on whether CoT should be assessed on an ex ante (are official and private creditor SCDIs comparable?) or ex post basis (through revision or clawback clauses in official creditor agreements). That problem is exacerbated when private and official creditors have different SCDIs (or when only one creditor group has SCDIs), possibly requiring additional

iterations across creditor groups. These factors should be taken into account when considering the use of SCDIs as they may impact the timeline of the restructuring. Early engagement across creditor groups can facilitate the common understanding on the trade-offs and best path forward. GSDR members supported bringing further clarity on the treatment of SCDIs in CoT assessments through a specific workshop.

Collateralized financing from private creditors

The benefits and risks of collateralized borrowing depend on the specific terms of the financing. Collateralized financing of projects where future revenue streams are directly linked to debt repayment under adequate disclosures that mitigate the risk of mispricing for both unsecured and secured creditors has the highest potential for benefiting the borrower and protecting the longer-term development relationship with creditors. Conversely, collateralized financing can cause more harm than good when one or more of the following criteria are met: (i) it does not improve borrowing terms; (ii) it weakens debt sustainability; (iii) it is inadequately disclosed; or/and (iv) it does not respect negative pledge clauses.

Collateralized lending, in particular from private creditors, poses important challenges in restructuring cases. Collateralization may provide a creditor with de facto seniority on its claim. On the official sector side, coordination mechanisms such as the Paris Club or the Common Framework, or informal coordination where formal processes are not in place, anchor the negotiation primarily around the objective of achieving fair burden sharing even if some official claims are secured with collateral. The political will to find a solution, or the absence thereof, is a more determining factor than the presence or absence of collateral. The situation is different on the private sector side, where the presence of private collateral can lead to an impasse. Official bilateral creditors may not stand ready to provide more debt relief to compensate a lower contribution of private creditors with collateralized claims than what would be consistent with the principle of comparability of treatment. In such situations, the IMF may not be in a position to provide financial support given the lack of prospects of a successful debt restructuring to restore debt sustainability. In some cases, the specific features of certain resource-backed loan contracts can also make the use of the IMF's Lending into Arrears Policy (LIA) impossible because, in practice, the debtor country cannot run arrears to its creditor.

There was broad consensus among participants to the July 8 GSDR Technical Meeting and subsequent October 9 GDSR Deputies meeting on the importance of increasing awareness on the benefits and risks of collateralized financing practices. The IMF and World Bank underlined the findings and policy considerations included in their 2020 note on "*Collateralized Transactions: Key Considerations for Public Lenders and Borrowers*" and 2023 note on "*Collateralized Transactions: Recent Developments and Policy Considerations*", which can help countries assess these benefits and risks, and adopt mitigating measures where needed, including on transparency and disclosure. There was also general support on the importance to help debtor countries address these issues through trainings and technical assistance missions.

Section 3: Addressing Current Liquidity Challenges

While solvency risks seem broadly contained, many low-income countries (LICs) and some emerging markets (EMs) face significant liquidity pressures. The series of major shocks since 2020, rise in global interest rates and large refinancing needs have all increased gross financing needs. The reversal of debt flows from bilateral and private creditors have brought considerable liquidity pressures to LICs and EMs. Private and bilateral net flows to IDA countries peaked in 2014 at US$1.8 billion, or 73 percent of total net flows, and declined to less than US$200 million in 2022, with private net flows turning negative. Concurrently, these countries require substantial investments to advance toward the Sustainable Development Goals (SDGs), including adapting to climate change. Large debt repayments due in the coming period further heightens these vulnerabilities in a range of countries.

The IMF and World Bank have proposed a three-pillar approach to help LICs and vulnerable EMs address current liquidity challenges. Countries, whose debt is sustainable, but experiencing temporary liquidity pressures, as assessed through debt sustainability analysis, and that are undertaking or committed to structural and fiscal reforms, could make use of this three-pillar approach. While the policies and instruments under each of these pillars are available to all countries, and constitute a "menu of options", the approach would activate a country-specific package, tailored to the country's unique circumstances and needs. The pillars include:

- **Pillar I: Structural reforms and domestic resource mobilization, supported by technical assistance, capacity development and policy advice**. Governments themselves must be willing to tackle underlying imbalances exacerbating debt challenges. This pillar thus entails undertaking structural reforms to boost growth and job creation, mobilizing fiscal revenues to meet priority needs, improving the efficiency and effectiveness of public spending, strengthening the business environment to foster the domestic private sector as well as foreign direct investment, and developing domestic financial markets to enhance access to financing.
- **Pillar II: External financial support, including from the international financial institutions.** Structural reforms and resource mobilization will take some time to deliver on their potential. In the meantime, mobilizing sufficient international support will be needed to help countries meet their financing needs and provide net positive flows, particularly in low-income countries. Support from bilateral and multilateral development partners will be needed, including through the provision of concessional loans and grants, consistent with the strength and ambition of the domestic reform agenda and the needs of the country. The IMF and World Bank are important parts of this collective effort, including through their catalytic role. For countries engaged in a Fund-supported program, official bilateral creditors could contribute by aiming at maintaining, where possible, their exposures over the program period.
- **Pillar III: Crowding-in more private finance and reducing debt servicing burdens where relevant.** Crowding-in higher and more affordable inflows from private creditors and investors is a key part of the package. Improvements in the business environment and progress on the domestic reform agenda will help in this regard. In addition, new solutions could be introduced to support countries that do not have solvency problems but need to manage high debt servicing burdens. This could include greater use of risk-sharing instruments by bilateral and multilateral

partners to incentivize new or higher inflows from private creditors, as well as liability management operations such as debt for development swaps and debt buy backs.

The GSDR Open Workshop held on September 16, and subsequent GSDR Deputies meeting on October 9, helped advance the consensus on these issues, while recognizing further work is needed. There is now broad consensus on the urgency to address liquidity challenges that impact the growth and development prospects of many LICs and some EMs and which, if unaddressed, could morph into a debt crisis. There is also broad consensus on the importance to combine different levers, including supporting countries' efforts to define and implement an ambitious set of domestic reforms, such as measures to enhance growth and job creation, mobilize public revenues and develop domestic capital markets, and improve spending efficiency, public financial management and governance more broadly; and providing adequate external financial support from the IFIs and mobilization of the official bilateral and private creditors, possibly using credit enhancements where relevant. The importance of coordinated efforts, while keeping a bottom-up, country-specific approach, building on experience, as the causes and the size of liquidity challenges may differ significantly from one case to the other, is also understood as essential. Participants underlined, however, that more work is needed and agreed to continue this discussion in the coming months.

Specific attention should also be given to the situation of small island developing states (SIDS), whose particular vulnerabilities call for special efforts. In addition to robust efforts to expand domestic revenue mobilization, there is a need for stronger fiscal discipline in SIDS, which can be supported by well-designed fiscal rules with flexible fiscal anchors.

Section 4: Next Steps for GSDR Work

Following the Annual Meetings, the work will focus on:

1- **Further supporting efficient, timely and predictable processes to resolve situations of unsustainable debt.** This could include following up at Technical Group level on the implementation of key improvements observed in recent months, including with regards to information sharing, comparability of treatment and coordination across creditor groups, and perimeter and parameters of the debt restructuring. This could also include further exchanges on the ongoing review of the LIC DSF.

2- **Clarifying further the use of SCDIs in debt restructurings, including with regards to comparability of treatment.** This could include a specific workshop, which could be organized by the Paris Club and G20 Presidency, to help clarify further how to establish clear and verifiable triggers for SCDIs used in a debt restructuring context to ensure they reflect borrowers' repayment capacity, and how comparability of treatment should be assessed and enforced when SCDIs are used.

3- **Further advancing the work on ways to address liquidity challenges.** This could include additional discussions on the developments in international financial conditions and on the respective roles of multilateral, bilateral and private sector partners to address liquidity challenges, and further work on liability management operations, such as debt swaps and debt buy backs. Discussions may include the appropriate role of credit guarantees and deepening the understanding of rating implications of such operations.

4- **Building resilience.** This could include discussion at Technical Group level or/and an Open Workshop on ways to increase debt transparency and improve debt management and reporting, including through increased countries' technical capacity. Specific attention should be given to the ways to support building fiscal resilience in small states. The discussion could also include ways to foster investor/debtor relations, enhance awareness raising on the risks and benefits associated with collateralized financing from private creditors, and promote a greater use of tools such as majority voting provisions in syndicated loans to improve private creditor coordination in case of a restructuring. Work on transparency could include discussion on adopting transparency clauses (whereby borrowers and creditors commit to heightened disclosure levels) to restructuring agreements, as well as identifying measures to improve the exchange of loan information between creditors, borrowers and international financial institutions, with a view to increase transparency data accuracy, and reduce the time required for debt reconciliation in cases of restructuring.

Several of the topics indicated above may warrant further engagement with credit rating agencies, as appropriate, including with regards to SCDIs, liability management operations, or timelines for rating upgrades once a restructuring is sufficiently advanced.