NARRATIVE on the G7 Campaign 2022 by erlassjahr.de

The debt situation of countries of the Global South is coming to a head. Measures taken so far are not enough to alleviate the situation. States continue to pay their debt, although they have to cut public spending to do so - all this in the middle of the pandemic. A timely, comprehensive and fair solution to the debt crisis can only work if all creditors participate in debt restructuring negotiations. But private creditors refuse to grant debt relief. The G7 countries have the responsibility to make private creditors participate in debt restructuring and relief. On the occasion of the German G7 presidency, the German debt and development coalition erlassjahr.de, together with more than 500 member organisations throughout Germany, calls on the German government to take concrete steps to finally hold private creditors accountable.

THE CONTEXT

Even before the Covid-19-pandemic, the debt of low- and middle-income countries had already reached an all-time high - also due to the climate crisis. As a result of the pandemic, the debt situation in countries of the Global South has further worsened. 135 out of 148 countries have at least one debt indicator in the critical range at the beginning of 2022. **Compared to before the pandemic, more than three times as many countries are already in a debt crisis or directly threatened by over-indebtedness.** The measures for debt restructuring[1] taken by the G20 countries and the IMF in the context of the pandemic has not provided substantial debt relief.

Overdue reforms of the debt architecture have not been addressed. This missed opportunity will be felt at the latest when central banks stop pumping new liquidity into the capital markets and raise interest rates, and when countries have to repay the debt service deferred with the G20 countries during the pandemic on top of the already high regular debt service. In **this situation, the IMF warns of a widespread economic and social collapse in the absence of debt relief.**

Already, many countries can only continue to service their debt on time because they prioritise the rights of creditors over the economic and social rights of their people. In 2021, 83 countries in the Global South have cut public spending at home. By 2023, 115 countries are expected to do so. This is despite the fact that even before the pandemic, spending in some social sectors was at dangerously low levels.

Time and again, countries of the Global South have themselves put forward proposals for measures that would offer them an effective way out of the debt crisis. For example, the Alliance of Small Island States (AOSIS) or the Vulnerable20 Group. But a large number of the affected states are excluded from the decision-making forums, e.g. the G20. Their proposals and demands have so far been ignored by the creditors.

[1] The IMF waived the debt service due to 31 low-income countries between April 2020 and January 2022. In total, the initiative cancelled interest and principal payments amounting to approximately 850 million US dollars. The G20 countries offered 73 low-income countries the temporary suspension of debt service under the *Debt Service Suspension Initiative* (DSSI). In November 2020, they also created the *G20 Common Framework on Debt Treatments beyond the DSSI*, which aims to make debt restructuring possible for countries that cannot easily resume servicing their debt.

PRIVATE CREDITORS INFLUENCE ON INSUFFICIENT DEBT RELIEF

Private creditors hold more than 60 percent of all debt claims on countries in the Global South. In order to reduce debt in critically indebted countries to a sustainable level, the participation of private creditors in debt restructuring and debt relief is crucial. However, the G7 countries have so far made too little use of their regulatory options - not least due to intensive lobbying by private creditor[2] institutions.

Private creditors have repeatedly used the **narrative that debt relief is ultimately not in the interest of the debtor country, as it would deprive it of access to new funds on the capital market. Empirically, however, this is not true.** On the contrary, timely and comprehensive debt relief promotes economic recovery and thus also facilitates raising new loans at reasonable conditions in the long run. Rating downgrades and exclusion from the capital market, on the other hand, are usually relatively short-lived, if they even occur. In many debtor countries, however, the threat scenario worked: instead of actively seeking debt relief, they preferred to continue paying their debt. But even in the short term, this strategy did not pay off for many: 58 countries of the Global South repaid more in interest and principal payments to external private creditors in 2020 than they received in new loans from them in the same period.

At the same time, **both the financing of the crisis with public money, and the debt relief provided by the G20, enabled governments to continue to meet their payment obligations to private creditors.** While public creditors deferred claims amounting to approximately 10.3 billion US dollars between April 2020 and June 2021, private creditors collected approximately 14.9 billion US dollars in interest and principal payments from the countries concerned during the same period.

Within the G20 *Common* Framework, debt restructuring is conditional on comparable treatment by private creditors. But the difficulty of negotiating this with private creditors is shifted unilaterally to the debtor states. Negotiations - and much-needed relief - can and are therefore blocked by uncooperative private creditors.

THE G7'S RESPONSIBILITY: HOLDING PRIVATE CREDITORS ACCOUNTABLE

Although today global financial and debt issues are largely discussed in the G20, the ball is in the court of Western countries with regard to the binding involvement of private creditors: **A large number of private creditor institutions are based in Western countries, and a large number of contracts are concluded under London or New York law.** Therefore, the Western states have both the opportunity and the responsibility to agree - for example, in the circle of the G7 - on measures and goals that can guarantee the binding inclusion of private creditors.

The governments of the G7 - including the German government - recognise that the non-participation of private creditors is one of the main obstacles to solving the debt crisis. However, instead of using their powers to legislate, they are unilaterally relying on moral appeals with little success so far. Instead, they could **introduce national legislation** that make it impossible for private creditors to undermine multilaterally agreed debt restructuring.

It is to be welcomed that the G20 countries want to avoid public concessions financing the bail-out of private creditors in debt restructurings under the *Common Framework* and therefore insist on the equal participation of private creditors. Instead of allowing the process to be blocked by uncooperative private creditors, however, the G20 countries should already grant relief when the debtor country suspends repayments to non-cooperative private creditors. This would **significantly increase the pressure on**

[2] On the lobbying of private creditor institutions see Vander Stichele, M. (2021): The IIF and debt relief.

private creditors, since they would have to fear a total loss if they continue to refuse to agree to comparable relief.

Also with regard to a more confrontational attitude of the G20 towards private creditors, the willingness of the Western states - organised in the G7 - is central, as they have so far shown little progressiveness within the G20 in this regard. Within the framework of the debt moratorium of the G20 states, more than half of the relief was granted by China. China, which obviously can have little interest in financing the bail-out of private, mainly Western, creditors through public relief, has already announced that it is not prepared to grant further relief as long as private creditors are not included in a binding manner.

Since default is the lever to force private creditors to provide debt relief, governments in the Global North should actively encourage debtor countries to do so and support them politically and financially in the confrontation with creditors unwilling to restructure. To this end, they could, for example - as already suggested by the Vulnerable20 - make the granting of public bridging loans by the IMF dependent on debt restructuring or the suspension of payments to private creditors. Under its *Lending into Arrears Policy,* the IMF is also able to issue loans even if the debtor country is still in arrears with individual creditors. If the IMF were to make more frequent use of this policy, the negotiating power of debtor countries vis-à-vis uncooperative creditors could be decisively strengthened. At the same time, it would prevent the granting of publicly subsidised loans from merely financing the bail-out of private creditors.

WHAT TO DO NOW

In the context of such a momentous global crisis, it is imperative that the burden of adjustment be shared equally between debtors and creditors. The **top priority must be to stabilise the health, economic and social situation in the affected countries as quickly and comprehensively as possible and to enable sustainable investments in climate protection measures and the achievement of the United Nations Sustainable Development Goals (SDGs).** If we want to set the necessary course to achieve the climate and sustainable development goals, anything less would be a considerable loss.

Instead of waiting to see whether the G20's attempts at regulation in their current form will eventually bear fruit, decisive political action is urgently needed to finally set the course for creating sustainable solutions to the global debt crisis. **The German government has created the political basis for this in its coalition agreement. There, the German government commits to the goal of creating a codified sovereign debt workout mechanism and implementing debt relief for particularly vulnerable countries.** The German G7 presidency offers an important opportunity to put words into action.

WE THEREFORE DEMAND FROM THE GERMAN AND OTHER G7 GOVERNMENTS:

1. Put the unresolved debt crisis on the G7 agenda

As part of its G7 presidency, the German government should put the unresolved global debt crisis on the agenda of the G7 in 2022. The G7 countries should also recognise that the debt crisis has not been solved for either low-income or middle-income countries and that extensive debt relief is needed to solve it.

2. Increase pressure on private creditors

The G7 countries should send a clear signal in their communiqué that they will fulfil their responsibility for the binding inclusion of private creditors. They should explicitly declare their willingness to support debtor countries politically and financially in their confrontation with creditors unwilling to restructure and to motivate them to stop payments to uncooperative private creditors.

3. Secure legal protection of debt restructuring agreements

Within the framework of the G7, the German government should advocate for legal safeguards for debt restructuring by initiating the coordinated implementation of national legislation that makes it more difficult to undermine multilateral debt restructuring agreements (along the lines of the UK's Debt Relief Act 2010, for example, which enforced Heavily Indebted Poor Countries debt relief on private creditors).

4. Consult with affected states

As part of its G7 Presidency, Germany should specifically seek dialogue with groups of states and governments that are also committed to fair and efficient debt relief procedures. Further decisions on debt relief should not be taken without consultations with affected governments to ensure that all highly indebted countries are given a chance to receive debt relief.