The Global South Is On The Brink Of A Disastrous Debt Crisis. Reform Is Urgent.

Ilene Grabel – ilenegrabel.com Photo: © Tommy Collier Productions

12-16-2024 ~ *The coming debt crisis will surpass that of the 1980s and disproportionately impact women, economist Ilene Grabel warns.*

Countries across the Global South are experiencing climate, poverty and development crises — all made worse by the unbearable costs of debt servicing. Indeed, according to Development Finance International, "Citizens of the Global South now face the worst debt crisis since global records began." Low-income countries, which have seen the amount paid on foreign debt payment increase by 150 percent since 2011, are being hit especially hard.

In the exclusive interview for *Truthout* that follows, Ilene Grabel, a leading economist in global finance and global financial governance, sheds light on the roots of the Global South debt crisis and offers specific strategies for easing the debt burden of developing countries. She argues that the obstacles to debt relief are purely political and ideological, as the global financial architecture is "morally bankrupt" and was designed to serve the interests of the rich at the expense of the poor. Grabel is Distinguished University Professor at the University of Denver and Professor of International Finance at the Josef Korbel School of International Studies of the University of Denver. She has conducted commissioned research for various United Nations agencies and NGOs, and is the author of the multi-award-winning book, *When Things Don't Fall Apart: Global Financial Governance and Developmental Finance in an Age of Productive Incoherence* (MIT Press).

C. J. Polychroniou: The debt crisis in the Global South is not a new phenomenon, but has been exacerbated since the outbreak of the COVID-19 pandemic to the point that many experts regard it as the worst debt crisis ever. Now, you have studied extensively the Global South debt crisis, so what's your take on this critical issue? Why are so many developing countries facing rising debt burdens this decade? And why is the Global South paying so much more to service its debt than it receives?

Ilene Grabel: A debt crisis of epic proportions is emerging in the Global South. Some have referred to this as a "silent debt crisis." But it's loud and clear. We are poised on the cusp of a new "lost decade" with vast debt overhangs, widespread debt distress, demands for austerity by lenders, and severe economic slowdowns just some of the legacies of this crisis. The term "lost decade" was used to describe the crisis of the 1980s — the last time the Global South faced a debt crisis.

The total external debt stock of low- and middle-income countries (LMICs) reached an historic high of $8.8 trillion in 2023. (Except where noted, data drawn from the World Bank.) In 2023, LMICs (excluding China) paid a record $971 billion toward debt service (i.e., principal and interest). That's the highest level since 1973. It was more than double the amount a decade ago. Interest payments by LMICs increased by a third to $406 billion in 2023. For the poorest countries, interest payments have quadrupled since 2013 and reached an all-time high of $34.6 billion in 2023. The UN reports that in the last three years, over a dozen governments have defaulted on their debt and over 30 of the world's poorest countries experienced "debt distress." This is greater than the number of defaults in the previous two decades.

The combined effects of high interest rates in the Global North (despite recent rate reductions) and a strengthening dollar have increased the cost of servicing debts. Fifty-seven percent of all long-term external debts held by LMICs (excluding China) and 40 percent of the debt held by the poorest countries are at variable interest rates tied to rates in the Global North. And more than 80 percent of public- and publicly-guaranteed debt in LMICs is repayable only in dollars, which means that the dollar's appreciation increases debt service costs. The strengthening of the dollar since the U.S. election has made matters worse.

Foreign private creditors largely pulled out of lending to Global South countries starting in 2022 as debt distress accelerated and interest rates in the Global North rose in 2022 and 2023. Indeed, since 2022 foreign private creditors have received nearly $141 billion more in debt service payments from governments than they've disbursed in new loans. That was the first time since 2015 that private lenders withdrew more funds from the Global South than they disbursed.

Many, including yourself, believe that the current debt crisis is not only more serious than the debt crisis of the 1980s, but that its consequences will also be far more traumatic. Why is that? And why is it, as you have argued, that the burdens of today's debt crisis in the Global South are borne disproportionately by women?

The lost decade of the 1980s serves as a powerful warning of what's to come. That period witnessed economic collapse under radical austerity programs, untold human suffering and setbacks to human development (including women's equality), compounding intergenerational social and economic losses; and environmental degradation as natural resources were sacrificed to the burdens of debt service. The miseries of that period amplified already existing deficits in the care economy, increasing the burdens and threatening the life chances of women and girls the world over.

There's no question that we are at the start of a debt crisis that's certain to worsen dramatically in the coming years. Debt service obligations to multilateral, bilateral and private creditors directly reduce available funding for already under-resourced shock absorbers, social protections (including those that support women's workforce participation and caring labor), public investment and investments in physical and social infrastructures that support growth and gender equality. Moreover, as in previous financial and debt crises, support from the Bretton Woods institutions (BWIs) is conditioned on austerity programs that entail, among other things, fiscal consolidation, public expenditure reductions, increased consumption and value-added taxes, user fees (that can restrict educational access for girls), and measures that contract public sector employment.

Constraints on fiscal space are already being felt anew across the Global South.

Deeper constraints surely lie ahead. Indeed, there's ample evidence that the austerity agenda has arrived, and it appears likely to be more severe than that associated with the crisis of the 1980s. Constraints on fiscal space and economic crises are always borne disproportionately by women, as per decades of research by feminist economists.

The current debt crisis is and promises to be much worse and harder to address than the debt crisis of the 1980s. Chief among the reasons is that today's lending landscape has far more bilateral, multilateral and private players. This includes the traditional cast of characters, but also and importantly China, India and petrostates. This crowded creditor landscape makes coordination, overcoming deadlocks and bringing relevant actors to the table difficult, especially in a world in which multilateral institutions and democracy are under threat. Today's debt and broader financial architecture is not only crowded, it's also more noxious. The greater toxicity stems from financialization and the power of the financial community, including the credit rating agencies and vulture funds. The deficient BWIs are at the apex of a failed global financial architecture. Moreover, the weakened fabric of multilateralism — coupled with the densely populated debt architecture — makes addressing the debt crisis simultaneously more urgent and complex than in the 1980s.

As if the debt crisis weren't enough, it's unfolding in a world of crises. These include food, refugees and climate crises; wars and other humanitarian disasters; and a backlash to democracy.

Many see the global financial architecture as dysfunctional. What's your take?

I agree, and indeed would go further. I share the view of UN Secretary-General António Guterres, who rightly indicted the global financial system, calling it "morally bankrupt" as it is a "system created by rich countries to benefit rich countries" and "to punish the poor."

The global financial architecture is anti-developmental, crisis-prone and unfit to address the development and climate challenges of our time. It reflects the power and economic realities of a long-gone post-WWII environment. The financial architecture is characterized by asymmetries that include the exorbitant privilege enjoyed by the U.S. and other northern economies. This privilege allows them to borrow and lend in their own currencies, while also giving them the ability to borrow on global markets at far lower rates than countries of the Global South. It also allows them to pursue monetary policies without regard for the global spillover effects. And it permits them to exercise undue influence and veto power at the BWIs, institutions that operate under outdated, rigid, exclusionary rules and norms. International Monetary Fund (IMF) practice exhibits severe dysfunction and inequities. For instance, interest rates on loans from the IMF have long been higher than they should be in view of the capacities of their clients. High surcharges on IMF loans to middle-income borrowers disadvantage borrowers at a time when needs are greatest.

Global South debt reform is a hot and controversial topic. What strategies do you recommend for easing external debt burdens and supporting sustainable development? Is there an economic and moral imperative for the cancellation of external debt for heavily indebted poor countries and those on the front lines of climate change?

It's essential that bold, comprehensive steps be taken — and quickly. In a paper commissioned by UN Women and the International Labour Organization, I consider strategies to ameliorate external debt burdens. I draw on approaches advanced by scholars, think tanks, policy makers and civil society advocates. In what follows, I outline a few key approaches.

One avenue involves new approaches to the IMF's Debt Sustainability Analyses (DSAs). DSAs are produced annually as part of the IMF's routine monitoring. More importantly, they are also produced when a country applies for assistance, during surveillance of an existing IMF program and during debt restructuring negotiations. DSAs should incorporate assessments of social markers (such as human rights) and climate commitments; introduce a Sustainable Development Goals (SDG) "carve out" that exempts public investment in SDG-related goals from counting toward a country's debt-to-GDP calculation; and not a DSA, but a "Sustainable Development Finance Assessment."

Another strategy involves the development of a Sovereign Debt Restructuring Mechanism (SDRM). There's a pressing need for an international legal framework for a SDRM that's comprehensive, consistent, binding, timely and transparent — and available to LMICs. An SDRM must incentivize or force all creditors to come to the table together in good faith. Participation of private lenders in restructuring negotiations might be forced or incentivized through debt exchanges for longer maturities or lower interest rates.

In addition to an SDRM, comprehensive debt relief on bilateral, multilateral and private debt is unambiguously essential. It must involve creditor haircuts and debt cancellations on some portion of outstanding debt, particularly in the poorest countries and those most immediately vulnerable to climate change. Without debt relief, we consign countries to austerity and constrain their policy autonomy. Barbados's Prime Minister Mia Mottley recently called for cancelling the debts of countries on the front lines of climate change. There are important precedents for debt relief, such as the BWI's Heavily Indebted Poor Countries Initiative of 1996.

In today's conflicted, multipolar world and complicated debt architecture, collective action by debtors may make a difference when it comes to debt cancellation. In this context, the formation of a "debtors' cartel" is overdue. In this scenario, a group of countries collectively agree to stop servicing the debt owed to public and private creditors until they agree to a set of terms that enable essential domestic spending. Coordinated action by creditors is not unprecedented. After all, that's what the Paris and London Clubs of creditors involve.

In certain contexts, debt standstills may be a useful stopgap. In such cases, the costs of a standstill must be clear to the borrower up front and preferably borne by the creditor. Credit rating agencies must be brought on board at the outset of standstill discussions. The World Bank includes a "debt-pause clause" in new and existing lending agreements with 45 small island states and states experiencing "qualifying events." This provision should be extended to all borrowing countries and represents a model on which other lenders should build. Also important is the introduction of "multi-year suspension clauses" for external shocks, including climate catastrophes and pandemics. Barbados has introduced such clauses into its loans. These might be included in agreements with all lenders. Credit rating agencies should be precluded from downgrading debt when such clauses are activated.

Several of the debt mitigation strategies I've discussed depend on institutional and governance reforms at the BWIs that expand the voice and vote of the Global South. Debt reprofiling by the BWIs is an important tool that should be utilized, especially in crises. This could involve extending maturity structures, including meaningful grace periods in loan agreements that could be activated during crises, and lowering borrowing costs (e.g., though lending rate caps). Surcharges on IMF loans should be eliminated permanently, well beyond the modest, inadequate steps taken on surcharges in November 2024.

Many have argued for new, annual, large-scale issuance of special drawing rights (SDRs). SDRs are an international reserve asset that the IMF creates electronically, by fiat, and at no cost to the institution. This is the single most potentially impactful, virtually cost-free way to provide the liquidity support necessary to shoulder the debt crisis, avoid cuts in much needed social spending, make support available for SDG-related and especially climate finance, and increase global inclusion. Countries of the Global North should also be encouraged to lend or preferably donate unused SDRs to countries that can use them to advance economic and human development and sustainability.

The current moment does not feel propitious when it comes to progress on the fronts you identify — your thoughts?

We are standing on the brink in so many respects. During the 1980s debt crisis, Tanzania's former President Julius Nyerere said, "[T]he world's children do not have to starve to pay the debts of those who came before." It was true then. It's true now. It was true then. It's true now. It was true then. It's true now.

The task ahead involves creating, exploiting and widening openings for the implementation of the strategies I've discussed. This necessitates sustained engagement, advocacy, coalition building, and a firm grasp of the facts in the face of ideological blinders. The chief obstacles are not the absence of workable economic strategies. The obstacles are political and ideological. It's my hope that in the coming years the multilateral cooperation that's in such short supply today can be reinvigorated, made more inclusive and supportive of social and environmental goals, and made more permissive of national policy choices and innovations in the service of improving lives and the health of our planet. In the meantime, there is much work to do — and quickly.

In these exceedingly difficult times, we can and should embrace what Albert Hirschman termed "possibilism." Possibilism involves a hard-headed appreciation of the profound challenges we face, while not letting ourselves be overwhelmed by "futilism." We have to look for and exploit all openings for change and coalition building, even if — as seems likely in the next four years — these openings will be small. There's too much at stake and no time to waste for the world to remain stuck on the shores of what cannot be done.

It's impossible not to acknowledge the rise of illiberal governments and the hollowing out of multilateralism. In this dismal landscape, it might be more realistic to think about medium-term rather than short-term strategies. At best, the Trump administration will be so preoccupied with vengeance, chaos and personal gain that actors committed to decency and progress on the debt and climate crises — *a coalition of the willing* — will not be weighed down by the traditional commitment to maintaining retrogressive U.S.-led multilateralism. Admittedly, that was far less toxic than what's to come. But even previous U.S. administrations were obstacles to progress. And perhaps there will be space for action created by the void in the multilateral landscape that's sure to be widened by Trump. It's conceivable that leaders outside the U.S. who seek to reshape multilateralism to make it more permissive, create new multilateralisms, or step into the brink to serve their own interests will at least buy indebted countries some breathing room. Time will tell.

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