POLICY CENTER FOR THE NEW SOUTH

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COVID-19 & Developing Countries—the Road to Recovery

Hinh T. Dinh

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About the Policy for the New South

The Policy Center for the New South (PCNS) is a Moroccan think tank aiming to contribute to the improvement of economic and social public policies that challenge Morocco and the rest of Africa as integral parts of the global South.

The PCNS pleads for an open, accountable and enterprising "new South" that defines its own narratives and mental maps around the Mediterranean and South Atlantic basins, as part of a forward-looking relationship with the rest of the world. Through its analytical endeavours, the think tank aims to support the development of public policies in Africa and to give the floor to experts from the South. This stance is focused on dialogue and partnership, and aims to cultivate African expertise and excellence needed for the accurate analysis of African and global challenges and the suggestion of appropriate solutions.

As such, the PCNS brings together researchers, publishes their work and capitalizes on a network of renowned partners, representative of different regions of the world. The PCNS hosts a series of gatherings of different formats and scales throughout the year, the most important being the annual international conferences "The Atlantic Dialogues" and "African Peace and Security Annual Conference" (APSACO).

Finally, the think tank is developing a community of young leaders through the Atlantic Dialogues Emerging Leaders program (ADEL) a space for cooperation and networking between a new generation of decision-makers from the government, business and civil society sectors. Through this initiative, which already counts more than 300 members, the Policy Center for the New South contributes to intergenerational dialogue and the emergence of tomorrow's leaders.

Abstract

COVID-19 has ravaged nearly every country in the world, with the globalization of recent decades intensifying its spread. As of mid-2021, the world had spent $16.5 trillion—18% of global GDP—to fight the disease. And that amount does not even include the most important losses such as deaths, mental health effects, restrictions on human freedom, and other nonmonetary suffering. Nearly 90% of this spending was by developed economies, with the rest by emerging market and developing economies. As a result, developed countries are on their way to taming the pandemic. But at just $12.5 billion, or less than 0.001 of the total, coronavirus-related spending by low-income countries amounts to virtually nothing.

This book shows that low- and middle-income countries still have a long way to go to control COVID. To survive the pandemic and restore economic growth, these countries must increase fiscal spending to vaccinate against and treat COVID-19 over the next two years. Because their ability to do so depends on individual country's circumstances, the book examines the fiscal space of selected low- and lower-middle-income countries and finds that most are not in a position to increase fiscal spending without jeopardizing debt solvency and sustainability. Thus, this book concludes that developing countries must bite the bullet and be willing to risk further debt stress to emerge from the crisis. The international community must be willing to accept these exceptional conditions and adopt measures to ease the pain and suffering of the developing world. The book also recommends policies for dealing with the long-term growth issues of developing countries.

Executive Summary

COVID-19 has hit the world economy hard, with global GDP falling more than 3.5% in 2020. The pandemic has inflicted widespread human misery and economic damages since it emerged from Wuhan, China in late 2019. By November 2021, more than 250 million people had been infected worldwide and over 5 million had died. Though the number of new infections has declined in recent months, the rapid spread of variants of the virus has rekindled fears about the reimposition of lockdowns and other measures to contain it.

Unlike previous global crises, COVID-19 spared no country. Both the developed and developing worlds suffered severe harm, creating a self-reinforcing contraction in global demand for goods and services. The more open a country's trade system, the greater the impact on its balance of payments and the deeper the effect on the national economy. Yet, COVID-19's effects on developing countries have been more severe, deepening inequality between the two worlds.

The pandemic arrived when trade tensions were mounting between China and the United States, and the developing world was facing a new wave of debt. Between January 2020 and June 2021 global spending to curb the virus was about $16.5 trillion (18% of world GDP)—which does not even include the most important losses such as deaths, mental health effects, restrictions on human freedom, and other nonmonetary suffering. Nearly 90% of this amount ($14.5 trillion) was spent by developed economies; the rest by emerging market and developing economies (simply referred to as developing countries in this summary). Low-income countries spent just $12.5 billion, or less than 0.001 of the total. COVID-19 has had especially devastating impacts on vulnerable groups including women, young people, poor people, and informal sector workers.

Developed countries are projected to see GDP growth of 5.4% in 2021 and 4.0% in 2022, while developing countries are expected to grow 4.4% and 4.2%. But these forecasts assume that annual investment in 2020–22 will exceed that in 2019, especially in China. Excluding China, developing countries will face lower investment and growth. In particular, underlying these growth assumptions is the hope that COVID-19 vaccinations of the global population will be sufficient by the end of 2022 to achieve herd immunity before economic activity fully resumes. As of mid-2021, this hope remains optimistic given halting progress on vaccinations (35% for the world and less than 5% for Africa), emerging variants of the virus, and new waves of infections around the globe.

The countries hit hardest by the pandemic are those that have relied on tourism, services, or commodities for income. Unemployment, already high before COVID-19, worsened—particularly among women and young people—lowering per capita incomes and raising poverty and inequality. Both supply and demand factors have caused the sharp contraction in GDP. On the supply side, the contraction was mainly driven by a sharp decline in the services sector due to the collapse of tourism, reflecting strains on transportation due to closed roads, railroads, airports, ports, and border crossings. On the demand side, consumption and investment have fallen.

COVID-19 caught the world off guard. Emergency measures to save lives included closing borders and introducing lockdowns, quarantines, and stay-at-home orders. To maintain livelihoods, conventional and unconventional policies were developed to support businesses and workers during lockdowns and help them prepare for recovery when lockdowns were lifted. These included fiscal and monetary measures to support healthcare systems, income relief for businesses and households, and liquidity injections to stimulate economies.

All developing countries face a more daunting paradox of choices than before. On the one hand, they need to borrow continuously to manage the lingering pandemic and support their nascent economic recoveries. On the other hand, they face rising debt service costs while their exports slump and their weak economic growth has diminished creditors' confidence. Given the constrained space for budgetary maneuvering, the resulting fiscal deficits are increasingly being financed by central banks through direct advances and holding of more short-term treasury bills and long-term bonds. The fiscal burden on these banks is aggravated by the easing of monetary policies and injections of liquidity.

Until COVID-19 is controlled, near-term prospects for the recovery of developing countries are clouded with risks and uncertainties. Among the greatest likely challenges are the spread of new variants, limited access to or delays in the distribution of vaccines, restoration of supply (especially through global supply chains), and weaknesses in the recovery of consumer and business confidence causing protracted depression of domestic and external demand.

Developing Countries Have Limited Fiscal Space to Respond

Because the pandemic hits both the supply and demand sides of economies, its effects are far more serious than a typical economic shock. On the supply side, lockdowns and quarantines reduce labor supply and firm capacity utilization, while disruptions to global supply chains undermine the provision of inputs—causing shortages and rising costs. On the demand side, the loss of income causes consumption and investment to drop. Workers in services such as tourism and hospitality are hit hardest, and informal workers suffer the most due to the need for close contact with customers. Low-income households fare worst due to limited access to healthcare and financial resources. Commodity exporters and tourism-dependent economies are also vulnerable.

Two types of fiscal measures are being used to support households and businesses during COVID-19. The first are above-the-line policies that directly raise budget deficits, such as cash transfers to low-income households, temporary enhancements of unemployment benefits, and wage subsidies or paid sick and family leave for workers who stay home to care for their children during school closures. These policies also include temporary government cashflow assistance or tax relief for people and firms affected by COVID-19. The second type are liquidity measures that do not directly affect budget deficits. For example, to help firms with liquidity, governments provide cashflow support in the form of loans, umbrella guarantees, and other support. These measures do not show up in budgets immediately but involve contingent liabilities outside budget revenue and spending.

Between January 2020 and June 2021 the world spent over $16.5 trillion on fiscal actions related to COVID-19, about $10.4 trillion of which was above-the-line spending (additional spending and forgone revenue) and $6.1 trillion for government loans, guarantees, and capital injections. Again, these COVID costs did not include the most important losses such as deaths, mental health effects, restrictions on human freedom, and other nonmonetary components. The size of financial support has varied by country depending on income level, political willingness, and the extent of the pandemic. Combined, global public debt has approached 98% of GDP. For developed countries the increase in fiscal deficits comes from both higher spending and declining revenue. For developing countries, the increase mainly reflects a collapse in fiscal revenue.

About 88% of this fiscal spending was incurred by the 57 high-income countries. For these economies, half the above-the-line support was devoted to protecting jobs and supporting household incomes. High-income countries spent 14% of GDP on average on COVID-19. Italy led in spending as a share of GDP (more than 46%), though the United States spent the most—nearly $6 trillion.

Low-income countries spent just $12.5 billion to cope with COVID-19, compared with $14.5 trillion by high-income countries, $1.5 trillion by upper-middle-income countries, and $408 billion by lower-middle-income countries. In developing countries as a whole, the most support went to public works and employment protection, though there has been substantial variation in the fiscal measures taken.

In response to the pandemic, and to varying degrees, all developing countries have mobilized resources to boost health spending, provide emergency funds for affected workers and companies in strategic sectors, adopt temporary tax reliefs and holidays, and provide government guarantees for loans from banks or central banks for strategic sectors.

Developing countries face difficult choices between increasing spending to fight the disease and protecting people during a time of fiscal constraints due to lower domestic revenue and external inflows. As a result, in addition to more accommodative monetary policy, countries have had to borrow more—domestically and externally.

Among developing countries, low-income countries face a particularly difficult situation. Faced with contractions in output, drops in commodity prices, and rising debt burdens, these countries could not afford the needed fiscal support, resulting in higher poverty and malnutrition. Many resorted to cutting capital spending, which will make it harder to grow after the pandemic.

In short, the budgetary needs to cope with COVID-19 in developing countries remain large, especially given emerging variants of the virus. In addition to vaccine and treatment budgets, governments are expected to continue to provide social protection—especially cash transfers to vulnerable populations. These needs will pose massive challenges to countries under tight financial constraints, especially those at risk of debt distress.

Thus, the fiscal outlook for developing countries is not promising. Risks are intertwined and reinforcing. The main sources include:

- Protracted economic downturns, such as further lockdowns, delays in vaccine access and availability, and new waves of infections caused by new variants.
- Tighter financing conditions, including rising international interest rates.
- Realization of contingent liabilities, as a significant part of global financial support has been through loans or guarantees, equity injections, and other quasi-fiscal operations.

Other risks include volatile commodity prices and rising social discontent caused partly by mental stress due to lockdowns.

Covid Vaccinations and Treatments are Urgently Needed

Until recently, fiscal spending by developing countries focused on issues unrelated to resolving the two main problems of COVID-19: vaccination and treatment. For the world to return to normalcy, all countries need to continue with vaccination efforts until at least 70% of the population is fully vaccinated. In addition, treatment of infected people needs to continue apace. As of October 2021, just 35% of the global population had been vaccinated—and in the developing world far less. Less than 5% of Africans have been vaccinated. And vaccines are more far more advanced than treatments. Though a variety of effective COVID-19 vaccines exist, developing countries face major challenges in accessing and distributing them. The main issue is ramping up production of these vaccines to satisfy global demand.

Vaccines are extremely effective at preventing severe infections (though fully vaccinated people can still suffer breakthrough infections). Treatments like monoclonal antibodies can keep mild cases from getting worse, but they are expensive, in limited supply, and can be administered intravenously only by medical professionals. Recent announcements by Merck and Ridgeback Biotherapeutics and by Pfizer about the efficacy of their oral medications could be a game changer, if approved by U.S. Food and Drug Administration (FDA). According to the World Health Organization (WHO), effective management of COVID-19 requires four components: vaccines, diagnostics, therapeutics, and health system links. The last component is to deliver vaccines and treatments. Unfortunately, developing countries have no choice in this matter. Economic activities cannot resume unless all four components are obtained and delivered.

Though COVID-19 does not seem to have ravaged Africa as much as it has other continents, its full effects are not yet known. The WHO has found that six of seven COVID-19 infections go undetected in Africa. Underreporting and lack of testing reflect limited healthcare resources, which make COVID tests and diagnoses hard to come by.

Financing large fiscal deficits is especially challenging for low-income countries given their limited market access and restricted ability to increase near-term revenues. Debt levels in these countries are projected to peak in 2021 and continue to climb in some. In 2020 actions were taken under the Group of 20 (G20) Debt and Debt Service Suspension Initiative (DSSI)—the first international effort after the emergence of COVID to help the poorest countries through grants, concessional loans, and debt relief to address the steep rise in their public debt. But these temporary relief actions do not address the root cause of debt problems.

Debt Problems Existed Before the Pandemic

Developing countries faced debt issues long before the pandemic. Over the past decade a growing number of low-income countries had fallen into debt distress. Moreover, the structure of international debt has changed. More private creditors are making loans to poor countries, while the role of official creditors—especially bilateral ones—has shrunk. Both creditors and debtors created this situation. For creditors, high returns and the relatively low debt burdens in low-income countries following the Heavily Indebted Poor Countries (HIPC) initiative created incentives for international lending. For debtors, funding from commercial creditors has become increasingly popular because such loans often come without the conditions usually attached to multilateral and bilateral loans. In addition, syndicated loans and public-private partnership project finance have grown.

Higher borrowing from non–Paris Club and commercial creditors has meant shorter maturities and higher refinancing risks. Since 2013–14 a surge in issuances of 10-year Eurobonds by many African countries as well as non–Paris Club loans (which have shorter maturities than typical multilateral concessional long-term loans) has caused bunching and created sovereign debt liabilities coming due in 2024–25—just as countries are expected to be recovering from the COVID-induced recession. This bunching in maturities elevates risks of debt distress. Developing countries need to begin debt resolution and restructuring negotiations before these risks materialize.

The past decade has also seen an increase in the share of private debt in developing countries' total debt, including private nonguaranteed as well as public and publicly guaranteed private debt. The presence of private creditors has implications for the incentives and ability to provide debt relief. This trend has occurred in both low- and middle-income countries, though more prominently in the latter. Among private creditors, bondholders are diverse and difficult to organize in case debt restructuring is needed.

Prior to the pandemic, the debt problems of developing countries reflected slow growth, unproductive use of debt, and borrowing on commercial terms at high costs and short maturities. The two components that directly affect debt ratios are the primary deficit (budget deficit net of interest payments) and the automatic debt dynamics term (GDP growth and interest rates). The first is more direct and can significantly affect debt ratios. The second can be a potent force if world economic growth slows down or if the international lending environment turns against borrowing countries.

Countries Need Individual Debt Sustainability Analyses

Though it is useful to discuss general debt trends of countries grouped by income level, a deeper understanding of the debt situation in developing countries can be gained only through detailed analysis of debt sustainability at the country level. Thus, this book focuses on the debt situation of Ethiopia and Zambia (two countries currently covered by the DSSI), Egypt, Morocco, and Tunisia. For comparison, it also includes Vietnam, which in 2019 had roughly the same debt and population as Egypt. In addition, the analysis includes Côte d'Ivoire, Ghana, Malaysia, the Philippines, and Thailand, though for brevity complete discussions are not included in the text.

For each country we first assess the current debt structure and the base case (before COVID-19) for key macroeconomic variables based on assumptions by international institutions. We then add the additional fiscal spending needed for COVID vaccination and treatment in 2021–23, together with non-health spending for the pandemic, to see how this spending will affect macroeconomic stability. This case is called Scenario 1. In addition, we examine a Scenario 2 in which the international environment worsens in the form of falling GDP and rising interest rates.

The debt analysis of these selected low- and lower-middle-income countries demonstrates two key points. First, the external debt of developing countries rose significantly in 2020 after COVID-19 emerged. Yet this increase is only the beginning because more fiscal spending will be needed to acquire and deploy vaccines and to treat infected populations. Most low- and lower-middle-income countries will be under debt stress, with the ratio of debt to GDP exceeding 65%. A few countries will experience liquidity problems, but most will face solvency problems that require addressing their debt burdens.

Second, developing countries face a stark choice between avoiding a collapse through vaccination at any cost and risking further debt distress. The debt situation will be made worse if global economic growth slows while borrowing costs rise as a result of tighter monetary policy in developed economies. Most developing countries will face serious debt difficulties if this combination of events occurs.

COVID-19 has increased external vulnerabilities and markedly reduced external buffers. The containment measures implemented to slow the pandemic's spread significantly eroded fiscal space. The shift in debt structure from official bilateral to private creditors—mainly Eurobond and commercial sources—to finance budget and current account deficits has raised the costs of debt service and made it more sensitive to movements in interest and exchange rates. Some economies will have insufficient liquidity to meet financial obligations as the pandemic continues beyond 2021.

Fiscal spending by developing countries to cope with COVID has been much lower than in developed ones because of resource constraints and lack of access to vaccines and treatments. But until COVID-19 is under control, these countries will have no way to recover. So, spending on COVID vaccines and treatments will be a priority in 2022–23. In addition, priority has to be placed on protecting workers, especially informal ones.

Should governments borrow domestically or externally to finance this extra spending? In countries with nascent capital markets, policymakers may not have many choices but to borrow from abroad. Developing countries should take advantage of the International Monetary Fund's new Special Drawing Rights allocation for COVID-19, which countries do not have to repay, supplemented by loans from international organizations that offer longer maturities and lower borrowing costs. A large portion of the potential increase in fiscal spending should be used for cash transfers to help vulnerable groups hit hardest by COVID-19: poor people and informal workers (especially in services) who cannot avoid physical contact with customers.

Policies to Ensure Strong, Sustainable, Inclusive Growth

Many policies in place or designed before COVID-19 are no longer valid. Developing countries should focus on priority policy actions covering the short term (2021–23), to survive the pandemic, and the medium term (2023–25), to ensure full economic recovery. And the groundwork should be laid to address long-term growth issues (beyond 2025).

To manage COVID-19, the top priority for policymakers is to control its spread by acquiring the best vaccines and vaccinating at least 70% of their populations, and acquiring and distributing medications to treat it. Along with adequate testing and decent health system links, these policy actions are not negotiable. In the medium term, efforts should focus on reforming healthcare systems, particularly decision making and implementation and delivery mechanisms.

The second area of urgency is to resume domestic production, especially for global supply chains requiring exports. Lockdowns have decimated the labor force in many countries, leading many migrant workers to return to rural areas. The first step is to bring workers back to factories by providing incentives such as relocation bonuses, housing subsidies, and transport grants. Such efforts obviously need to be combined with policies that reduce administrative restrictions on or impediments to workers' movement. Governments should work with private firms to ease any constraints they are facing to get back to output levels prior to COVID-19.

In the medium term, governments should encourage the development of personal protective equipment and medical industries, improve worker skills through training and technical assistance programs, provide incentives for domestic companies to link with foreign ones, and review laws on foreign direct investment to foster higher-value activities. Some countries might also need to implement stimulus packages for nontradable goods and services, since most unskilled workers are informal—especially in services and domestic trade. Such packages could provide grants to all households and reduce or delay charges and taxes for small and medium-size enterprises.

At the same time, it is crucial that developing countries restore the long-term growth potential of their economies by completing ongoing infrastructure investments, especially in roads, ports, and the like; accelerating reforms in education and training systems, with a view toward replacing traditional teaching methods with online services; undertaking digital transformations to foster innovations; cutting red tape in economic decision making; placing annual budgets under medium-term frameworks so that unexpected spending can be made in any period without jeopardizing macroeconomic stability; and boosting labor productivity, which dropped in developing countries between the 2008 global financial crisis and the arrival of COVID-19—partly due to the reallocation of labor to services. Pandemic-induced economic disruptions have reduced productivity even more, especially in Sub-Saharan Africa. Policies to raise agricultural productivity—such as strengthening infrastructure and land property rights—would likely pay large dividends.

Equally important are policies to support structural transformation, which could contribute even more to Sub-Saharan productivity growth. Facilitating structural transformation in the region's low-income countries requires creating jobs in modern, industrial sectors. The binding constraints on African competitiveness in manufacturing are limited industrial land, input industries, finance, trade logistics, worker skills, and infrastructure. Solutions drawn from East Asia's experiences could help ease these constraints.

Middle-income countries in general face different issues. They need to create jobs for unskilled and semiskilled workers as well as jobs that create more added value in global value chains. They also need to actively promote innovation to move to the next stage of economic development.

A comprehensive and coordinated approach to deliver the above policy agenda includes three types of policy reforms: short-term, medium-term, and long-term actions.

Short-term actions

- Quickly acquire and deploy reputable COVID-19 vaccines for at least 70% of the population and acquire and deliver medications for treating the disease. No country can be considered safe without these efforts, along with adequate testing and health system links.
- Restore domestic supply—especially global supply chains for exports—to the levels before the virus emerged.
- Continue social distancing and other practices such as mask wearing, hand washing, and restricting large public gatherings.
- Avoid premature reopenings or stop-start containments, which undermine productivity because furloughs and reduced working hours tend to lead to permanent job losses.
- Implement demand stimulus packages if needed.
- Protect lives and livelihoods by extending social safety nets and protection programs through cash transfers, food aid, unemployment assistance, and free treatment for informal workers, women, youth, and poor people.
- Ensure the liquidity of the financial system and timely support for firms.
- Search and raise funding for large additional, unplanned fiscal spending. Institute debt management systems that foster long-term debt sustainability through debt reprofiling or restructuring.
- Develop capacity for debt sustainability analysis that can publish debt reports at fixed intervals, working with multilateral institutions and with bilateral and private creditors to promote prudent decision making by borrowers and lenders alike.
- Strengthen coordination of fiscal, monetary, and exchange rate policies to monitor the direction, speed, and magnitude of capital flows and their economic effects.
- Conduct thorough public expenditure reviews to establish a core protected group of investment projects needed to restore economic growth, and focus on making capital projects more efficient through procedures that enhance project identification and implementation.

Medium-term actions

- Provide fiscal support and introduce policies to formalize the informal sector through training for workers and businesses to narrow mismatches in skills.
- Adapt education systems to have a technological bias. Investing in science, technology, engineering, and mathematics (STEM) fields and problem-solving skills will groom the workforce for the future. Such investments will also trigger the adoption of new technology and the emergence of new service industries to support diversification.
- Invest in network infrastructure that expands internet connectivity economywide so that everyone—children, adults, workers, businesses—can benefit from online learning. Doing so will also boost managerial and production productivity in small and medium-size enterprises through technological and financial innovation, and more efficient trade through ecommerce and financial inclusion across all sectors. In addition, it will create a lot of jobs and could disproportionately benefit youth and women. Digital transformation is already the hallmark of most upper-middle-income countries. Lower-middle-income countries could invest in it to leapfrog and catch up.
- Deepen domestic bond markets while taking into account the risks of foreign ownership of treasury bills and bonds, reflecting the "on and off" impacts of market sentiment that may lead to capital flight under changing market conditions such as interest rate changes in developed countries. Capital flows should be carefully managed and create incentives for more stable, long-term flows such as foreign direct investment.
- Closely monitor and review guarantees, subnational debt, financial liabilities of state-owned enterprises, and other contingent debt. An inability of state enterprises or subnational governments to roll over maturing principal debt obligations may require central governments to step in.
- For middle-income countries, invest in more functional, efficient healthcare systems to cope with future pandemics and ease government burdens. Unlike most low-income countries, where affordability and implementation are major constraints, middle-income countries could consider universal health insurance to cut government spending.

Long-term actions

- Promote economic and export diversification through trade policy reforms and fiscal investments in public goods and industrial clusters for non-extractive goods and services. Doing so is key to inclusive, sustainable growth and large-scale job creation in economies dependent on natural resources.
- Improve economic resilience to exogenous shocks and future challenges including climate change and food and water security.
- Invest in public goods needed to reduce regional disparities and foster inclusive growth. Formalizing informal businesses, expanding digitization, and developing skilled workforces in the medium term will help narrow regional disparities in middle-income countries.
- Deepening regional integration in the context of the African Continental Free Trade Area (AfCFTA) agreement.

Considerations for the International Community

- The Debt Service Suspension Initiative (DSSI) was the first attempt to help the poorest countries confront COVID-19. It suspended debt service payments from 73 low- and lower-middle-income countries to bilateral official creditors between May 2020 and June 2021. But this temporary relief did not fundamentally address these countries' debt issues—though it provided more time to assess and address debt sustainability for each country.
- Private creditors have not yet participated in the DSSI and are reluctant to accept lower payments from debtors. Concerns deterring debtor countries from requesting private creditors to participate include reputation issues, credit rating downgrades, and legal risks. Participation by private creditors would enhance DSSI benefits for participating countries, but a requirement for comparable treatment from private creditors could stunt such participation. The lack of private creditor participation in the initiative raises concerns that official debt service suspension would partly benefit private creditors. This issue is particularly important if DSSI support would defer the recognition of unsustainable debts. The G20 could consider options to mitigate such concerns in the context of the DSSI.
- The DSSI is insufficient to deal with the magnitude and urgency of the

debt problems facing developing countries. First, because it provides only temporary relief, the problems will come back. It could even make them worse if more countries are downgraded and fall into debt crises. The total amount of relief provided by the DSSI is just $5 billion. Second, the initiative fails to distinguish appropriately between countries with liquidity problems and those with solvency problems. Third, serious debt service problems also will likely also occur in middle-income countries. Finally, the DSSI does not address the liquidity problems of the public sector or of private businesses in developing countries—essential to resuming growth as soon as possible.

- Africa's debt issues cannot be resolved without addressing the debt owed to China by African countries such as Ethiopia and Zambia. During 2000–19, the Chinese government, Chinese banks, and Chinese companies lent more than $150 billion to Africa. About 10 African countries have debt problems with China even though Chinese lending was concentrated in Angola, Djibouti, Ethiopia, Kenya, and Zambia. All these countries face serious debt issues. Chinese lenders are opportunistic in modifying standard contract tools to maximize their repayment prospects and to protect a broad range of Chinese interests in borrowing countries. The terms and conditions of Chinese lending are opaque, and contracts are confidential.

- The only feasible way to deal with Africa's debt problem is to have a concerted effort by all lenders—bilateral and commercial, Chinese and non-Chinese—under the leadership of an international institution like the IMF or the World Bank to agree on a common, orderly framework for debt workouts. Doing so will require more transparency in sovereign lending, including but not confined to loans between governments. This will also require that private and emerging creditors are open to accepting haircuts on loan repayments.

- A change in the financial architecture is also needed so that a long-term resolution of the debt problem can be found. This would provide more certainty to the macroeconomic and investment policies needed to restore economic growth in developing countries. For those that are insolvent, there is no way out except for creditors to take a substantial reduction in debt principal. It is not clear that innovative debt workouts such as auctions to buy debt at below-face-value prices, or debt-nature swaps, would work for private creditors such as bondholders or commercial banks. And unlike with official creditors, the broad distribution of bondholders and investors makes it hard to reach timely decisions.

- The international community needs to fully recognize the desperate situation of indebted countries and take prompt, decisive actions to help restore growth. Another round of the Heavily Indebted Poor Countries (HIPC) initiative may be needed. Debt relief could be linked directly to acquisition and deployment of COVID-19 vaccines and treatment medications. As noted, one important resource is the IMF's recently allocated Special Drawing Rights (SDRs) worth $650 billion to support the global recovery from COVID-19.

- Multilateral development banks must provide additional liquidity, perhaps through higher leverage in capital markets, and bilateral creditors need to do their share. Commercial creditors could take a longer view of the debt situation: by allowing more debt relief now, prospects are better for getting money back in the long run.

- Given the dire, urgent need for additional fiscal spending by developing countries to deal with COVID-19, it is essential for international organizations to be far more flexible and understanding when using traditional debt burden and debt service ratios when lending.

- The shift to Eurobond issuances by developing countries has raised the question of how to prepare for debt restructuring should the need arise. A collective action clause allowing for a supermajority of bondholders to agree to debt restructuring that is legally binding on all holders of the bond—including those who vote against the restructuring—is needed to avoid holdouts. Most bondholders opposed such clauses in the 1980s and 1990s, fearing that it gave debtors too much power. But after the experiences of Argentina and Ecuador, collective action clauses have become more common because they are now seen as potentially warding off more drastic action while facilitating coordination among bondholders. In this context it is crucial to share experiences aimed at fostering collaboration and voluntary exchange of information with creditors.

- There is a need for a debt workout framework for the middle-income countries. No such framework exists at the moment. Such a framework would require efforts from all sides. From creditors, continued support to help lower-middle-income countries overcome COVID-19—including, where relevant, debt relief linked to COVID-19 vaccines and treatment medications as well as investment in the health sector. Debtors need to develop and implement a medium-term debt framework to ensure continued sustainability of both domestic and external debt. Over the long term, governments of these countries should develop the skills needed to be more engaged with issuance advisers in managing bond negotiations for lower interest rates. They should also be more active in exercising their choice of accepting or rejecting investors' bids.

COVID-19 & Developing Countries—the Road to **Recovery**

COVID-19 has ravaged nearly every country, with the globalization of recent decades intensifying its spread. As of mid-2021, the world had spent $16.5 trillion—18% of global GDP—to fight the disease. And that amount does not even include the most important losses such as deaths, mental health effects, restrictions on human freedom, and other nonmonetary suffering. Nearly 90% of this spending was by developed economies, with the rest by emerging market and developing economies. As a result, developed countries are on their way to taming the pandemic. But at just $12.5 billion, coronavirus-related spending by low-income countries amounts to virtually nothing. This book shows that low- and middle-income countries still have a long way to go to control COVID. To survive the pandemic and restore economic growth, these countries must increase fiscal spending to vaccinate against and treat COVID-19 over the next two years. Because their ability to do so depends on individual country circumstances, the book examines the fiscal space of selected low- and lower-middle-income countries and finds that most are not in a position to increase fiscal spending without jeopardizing debt solvency and sustainability. Thus the conclusion is that developing countries must bite the bullet and be willing to risk further debt stress to emerge from the crisis. The international community must be willing to accept these exceptional conditions and adopt measures to ease the pain and suffering of the developing world. The book also recommends policies for dealing with the long-term growth issues of developing countries.

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