# Breakingviews - Guest view: Debt crisis will delay global recovery

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NEW YORK (Reuters) - The Covid-19 pandemic will spark hugely damaging debt defaults in developing countries, hampering rebuilding and recovery. Many emerging markets borrowed heavily both from official governmental lenders, as well as from international private sector investors, mostly in U.S. dollars. Now they are confronted by rising debt service costs at a time of rising economic difficulties and capital flight. We must start planning for this right away.


World Bank President David Malpass addresses the fall meetings of the International Monetary Fund and World Bank in Washington, D.C., U.S., October 18, 2019.

How can we best mitigate the emerging markets debt crisis? The International Monetary Fund requires additional resources as it now faces immediate requests for fast-disbursing loans from a record 102 countries and will face a deluge of follow-on loan requests in coming months. It estimates 40% of low-income nations are wrestling with debt distress.

The United States has resisted an increase in IMF Special Drawing Rights, which is needed to increase the capital available for lending. That may leave the institution unable to respond on the scale required. President Donald Trump’s administration is forgetting that the fund performs an essential emergency response role at an extremely low cost to taxpayers and is much less costly than permitting crises to cascade or relying on bilateral responses.

The current moratorium on debt payments from an initiative backed by the Group of 20 major economies to the hardest-pressed nations runs until the end of the year. But there is no clear outline for what happens after that. And the IMF says some of the worst-hit are reluctant to participate out of concern it could hurt their credit ratings and future market access.



Today, the debt crisis has commenced in countries such as Argentina, Ecuador, Lebanon and Zambia, but, like the virus itself, it will spread to many more across all the developing and emerging market regions. We have seen major sovereign blowups on a regional scale before, such as in Latin America in the 1980s and East Asia in the 1990s, but never have we seen one with global breadth that we now face.

Historically, the U.S. Treasury and the U.S. Federal Reserve would take leading roles, alongside private lenders working with the Paris Club of major creditor countries. We worry that this time could be different. Solving debt crises is not a zero-sum game. All sides must give ground to succeed. That method worked in prior debt crises. In 2020 we can advance toward a solution, including the private sector, if Washington plays its full part.

Beijing's active participation is also required. China is the largest official creditor in the developing world. Across Africa, Asia, and Latin America, roads and infrastructure have been constructed and repaired through the Belt and Road Initiative, estimated by the Kiel Institute for the World Economy to amount to $520 billion in outstanding loans. As a result of this investment surge, resolving the financial and debt crisis demands Chinese engagement.

China signaled a shift in approach at the current National People's Congress, which runs from May 22 to May 28. The Congress announced a focus on "quality" BRI investments going forward – a small but important recognition that some of the existing investments may be in distress. This could mean China may be willing to engage with other creditors to tackle the looming crisis.

The G20 must work with China to bring it fully into the Paris Club. Part of that process will require the People's Republic to be more transparent about loans and terms. And it will need to agree to substantial debt forgiveness and debt restructuring. Overall, China's stance will be key to an effective emerging market debt solution. As Beijing seeks a leadership role globally, taking a flexible constructive role in debt negotiation is in its interest, will pay diplomatic dividends and underscore a growing influence.

Time is of the essence. The debt crisis is gathering speed. Failure of big creditors to come together will do great damage to confidence in the international financial system. IMF expectations for global growth to rebound to 5.8% in 2021 are optimistic, and will look grossly so if poor countries are hampered by borrowings as they try to manage the pandemic.