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Better Debt Shock Absorbers for Poor Countries

A Proposal

NANCY LEE · LILIANA ROJAS-SUAREZ · SAMUEL MATTHEWS · JAMES REID

Abstract

Our analysis confirms that poor countries are subject to a broad range of exogenous shocks—not under their control and not just those that are climate-related—and that those shocks can have large consequences for growth, debt-carrying capacity, and liquidity. The current major global shock, the Iran war, is the most recent example. Our proposal for temporary suspension of external debt service payments would help prevent liquidity crises from escalating into solvency crisis. By providing immediate fiscal space, it would allow low-income countries to avoid default and undertake countercyclical or reconstruction spending, thereby limiting long-term economic damage and preserving creditworthiness. The proposal has five distinctive features:

- Triggers for DSC activation focus on the magnitude of the shock, not the source.
- Benchmarks for clause activation are simple, standardized, and quantitative. The four-part activation test includes benchmarks for solvency, liquidity, debt service fiscal burden, and growth impact.
- Clause activation would not require creditor approval if triggers are met and verified.
- Clauses would apply to sovereign debt owed to both public and private creditors—to ensure comparable treatment amid the rising public creditor share of poor country debt stocks.
- The issuing country may spend the temporarily freed-up resources as it likes—different from debt for nature or debt for development swaps.

This proposal is meant to complement, not substitute for, ongoing work to deal with liquidity shortages, to make the debt restructuring process more efficient and to explore refinancing options for poor countries' current high-cost debt. The aim is better long-term solutions to strengthen the resilience of poor countries and to help avoid a recurrence of today's pervasive debt strains. We know these countries will continue to be subject to frequent exogenous shocks. A forward-looking approach of building better debt contracts for poor country sovereign borrowing should be a prominent part of the debt relief arsenal.

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Introduction

External debt burdens and risks for poor countries have evolved in important ways in this century. Domestic policy must still play a critical role in maintaining debt sustainability. But two fundamental shifts have made these countries more vulnerable to circumstances beyond their domestic control: (1) as they are more integrated into the global economy—flows of goods, people, and capital—they are more vulnerable to external shocks (pandemics, wars, sharp reversals of global capital flows, large adverse movements of terms of trade); and (2) many of them are exceptionally exposed to increasingly frequent climate-related shocks: storms, droughts, floods, and heat spikes.

We now see widespread debt challenges in poor countries: the IMF reckons that 59 of 68 countries eligible for the Poverty Reduction and Growth Trust (PRGT), its concessional finance window, are either in or at high to moderate risk of debt distress.[1] For many of these countries, debt service obligations exceed social spending as a share of fiscal revenues or expenditures.[2] Their cost of capital for market borrowing is high: The IMF estimates that the spread for low-income country international bonds reached over 500 bps in 2025.[3]

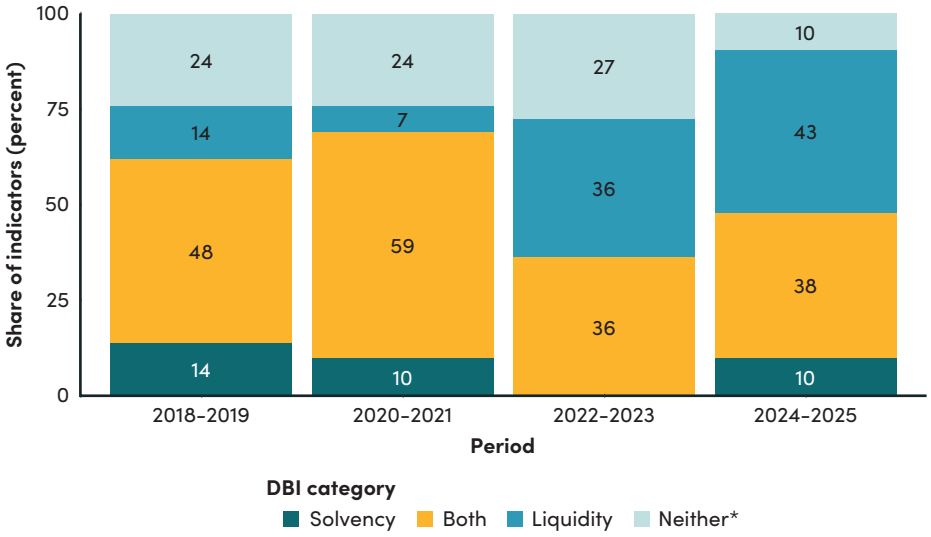
But these countries are generally not "systemic", in the sense of threatening the global financial system or driving regional contagion. Partly as a consequence, we have seen limited progress in efforts to help these countries deal with successive shocks. Others have pushed for reforms to the G20 Common Framework and the Global Sovereign Debt Roundtable to make them function more efficiently, faster, and with better debt sustainability outcomes. In addition, the Africa Expert Panel convened under the South African G20 presidency has proposed a debt refinancing initiative for poor countries supported by official funds and a Sovereign Debt Resolution Mechanism.[4]

But our focus here is not on countries facing insolvency. Rather we target illiquid but solvent countries struggling in what has been termed the "grey zone".[5]

As Figure 1 shows, in recent years, a growing share of poor countries now falls into this category.

1 IMF, 2025e.
2 UNCTAD, 2025.
3 IMF, 2025d.
4 Africa Expert Panel, 2025.
5 Diwan and Harnoys-Vannier, 2025.

FIGURE 1. Triggers for high debt risk: solvency and liquidity debt burden indicators (DBIs)



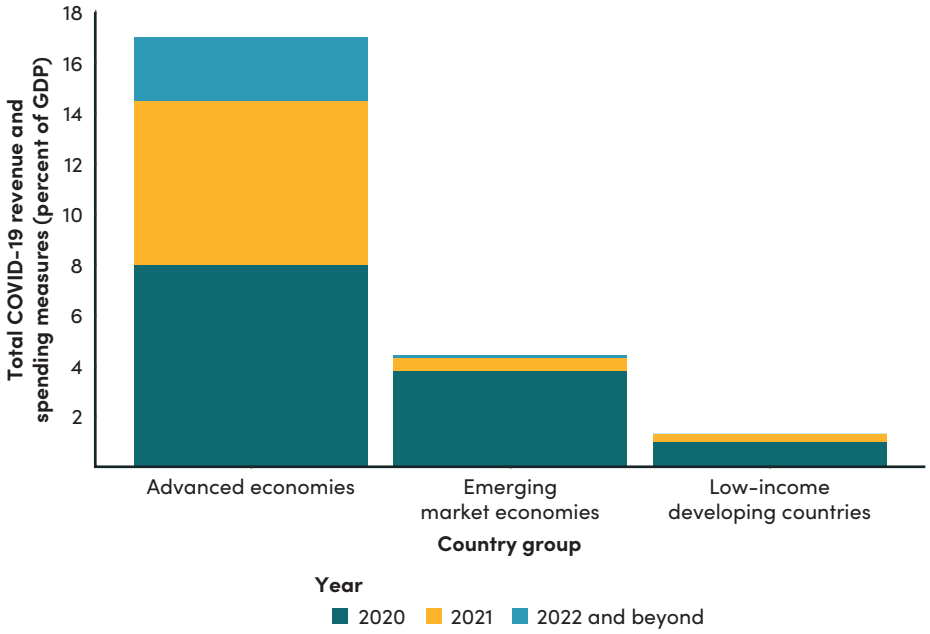
Note: Share of established thresholds breached that trigger an external high-risk rating indicates whether the liquidity debt burden indicators (debt service to revenue or debt service to exports), the solvency DBIs (PV of external debt to GDP or PV of external debt to exports) or both mechanically trigger a high-risk rating. (*) For those cases where neither group of DBIs is breached, the high-risk rating is based on judgment (e.g., long-term considerations).
Source: Figure from IMF, 2025c. Data as of June 2025.

One rapid and sizeable source of relief can come in the form of legal arrangements that permit temporary suspension of external debt payments in response to large external shocks or domestic disasters. The central goal is to prevent a liquidity crisis from turning into a solvency crisis and thereby avert default. Debt default, even with more efficient restructuring, will always do severe damage to countries' growth, investment, and access to fresh capital.[6]

Such pauses in debt service can benefit both creditors and debtors if they provide governments with additional fiscal space to respond to large shocks. This countercyclical role can help diminish the effects of severe temporary economic and social disruption on long-term growth trajectories and poverty reduction progress—developments that ultimately weaken long-term debt service capacity. As we saw most starkly during the COVID-19 pandemic, poor countries lacked the fiscal space to prevent this damage (Figure 2).

6 Asonuma et al., 2019.

FIGURE 2. Fiscal support for COVID-19 responses by country income group



Source: Figure from IMF, 2021. Data based on IMF Fiscal Monitor database of Country Fiscal Responses to COVID-19 and IMF staff calculations.

Research shows that setbacks imposed by the pandemic and other shocks on poorer countries with limited fiscal space are serious and long-term.[7]

Refinancing the existing debt of poor countries with increased lending from international financial institutions (IFIs) would help lower debt service burdens.[8] But IFI concessional resources available to help poor countries refinance high-cost private credits or unsustainable loans from China are tightly constrained.

In any case, even if/as such refinancing proposals move forward, better long-term solutions need to be found to strengthen the resilience of poor countries and help avoid a recurrence of today's pervasive debt strains. We know these countries will continue to be subject to frequent exogenous shocks. A forward-looking approach of building better debt contracts for poor country sovereign borrowing should be a prominent part of the debt relief arsenal.

This paper focuses on one aspect of better debt contracts: provisions to promote resilience to exogenous shocks for poor countries. Poor countries are clearly not the only countries subject to large shocks,[9] but they are the least resilient, in terms of available fiscal resources and international

7 Stemmler et al., 2024.

8 Africa Expert Panel, 2025.

9 Small island developing states (SIDS), for example, are clearly vulnerable to large climate-related shocks but already have the option of deploying the particular type of clause relevant to their needs: Climate Resilient Debt Clauses.

reserves, access to global capital markets, and the impact of financial stress on their capital costs Data for poor countries in this paper refer to countries classified by the World Bank as low-income countries (LICs) and lower middle-income countries (LMICs).[10]

The paper is organized as follows. Section 1 reviews debt suspension initiatives to date. Section 2 looks at how frequently poor countries are subject to large exogenous shocks of different kinds. Section 3 identifies principles that should govern design of temporary debt suspension clauses (DSCs). Section 4 proposes four simple, quantitative tests for activation of DSCs: an insolvency test, a liquidity test, a debt service burden test, and a growth impact test. To set the right bars for the tests, it reviews historical data on the impacts of different kinds of shocks, including the two largest shocks of this century: the pandemic and the global financial crisis. Section 5 offers a summary and conclusions.

1. Recent debt suspension initiatives and clauses

The G20 Debt Services Suspension Initiative (DSSI) was a bold effort to offer such a temporary suspension during the global pandemic to LICs and LMICs. Analysts assess that it had some positive impact: 48 out of the 73 eligible countries participated before it expired in 2021.[11] But it was heavily criticized on multiple grounds: (1) private creditors chose not to participate; (2) finance from the international financial institutions, significant creditors for many of these countries, was not included in the initiative; (3) non-participating creditors objected to the one-size-fits all approach for all DSSI eligible countries, without reference to their particular debt service burdens and circumstances; and (4) there was no agreement on a standardized net present value (NPV) treatment

More recently, we have seen the use of bespoke debt suspension clauses (DSCs), or pause clauses, for countries like Barbados and Grenada at high risk of natural disasters (hurricanes). These two countries included DSCs in their respective restructured bonds. For Barbados, loans from Inter-American Development Bank also now include DSCs. Following Hurricane Beryl in 2024, Grenada and St. Vincent and the Grenadines activated DSCs in their debt agreements with bondholders and the World Bank.[12] Grenada's bond yields were not significantly affected by clause activation.[13]

The World Bank has also extended the coverage of its Climate Resilient Debt Clause (CRDC) to health emergencies like pandemics, as well as to all natural disasters including droughts and floods.[14] Of the 45 countries that are eligible for CRDCs, 14 have included this clause in their loan agreements with

10 But the group of poor countries designated as eligible for use of DSCs could be defined differently, e.g., to include only countries the IMF classifies as LICs to which the LIC Debt Sustainability Framework applies.
11 World Bank Group, 2022.
12 Mustapha, 2025.
13 Song, 2025b.
14 World Bank Group, 2024b.

the World Bank. As more multilateral development banks (MDBs)—which also include the African Development Bank (AfDB),[15] Asian Development Bank (ADB),[16] and European Bank for Reconstruction and Development (EBRD)[17]—and bilateral creditors like the UK,[18] Italy,[19] and Japan[20] are deploying this approach, barriers against including such clauses in official debt are breaking down.

There are also private-sector-led efforts to include DSCs in sovereign bonds issued by EMDEs. The Bondholder Working Group (BHWG) under the London Coalition for Sustainable Sovereign Debt has developed a proposal for broad debt pause clauses.[21] Under this proposal, following an external shock, the borrower would be able to request debt service deferral from bondholders if it has either declared a national emergency or applied for emergency financing from the IMF. The borrower would also have to demonstrate that at least 60 percent of its external debt service will be subject to a similar deferral arrangement. A majority of voting bondholders could vote to block the deferral under the clause's declination option. The proposal also includes a set of transparency clauses to address investor concerns about issuer information-sharing related to the clause. The BHWG is in the process of consulting with market participants and issuers to operationalize the proposal.

To assess the potential relief that such DSCs can provide, CGD colleagues Landers and Aboneaaj (2023). explored case studies of three natural disasters: the 2022 floods in Pakistan, the 2019 tropical cyclone in Mozambique, and the 2021 earthquake in Haiti. They find that:

- Payment relief can be significant if all creditors participate and if the country's debt service burden is significant;
- DSCs are not suitable for countries confronting insolvency and if contracts are structured with large bullet payments.

We lack sufficient evidence at this point to determine whether inclusion of DSCs in bond issuances tends to raise or lower yields.[22] Ex ante arguments can be made in both directions. DSCs in essence offer insurance to issuers which should entail some kind of fee. But for creditors, DSCs should reduce the probability of default and thereby make bond yields with DSCs more attractive in risk adjusted terms relative to the yields of bonds without DSCs—as long as clauses are neutral in NPV terms. Barbados' issuance in 2025 of a bond with a pause clause on the primary market was five times oversubscribed, with a minimal increase in the yield relative to comparable bonds.[23]

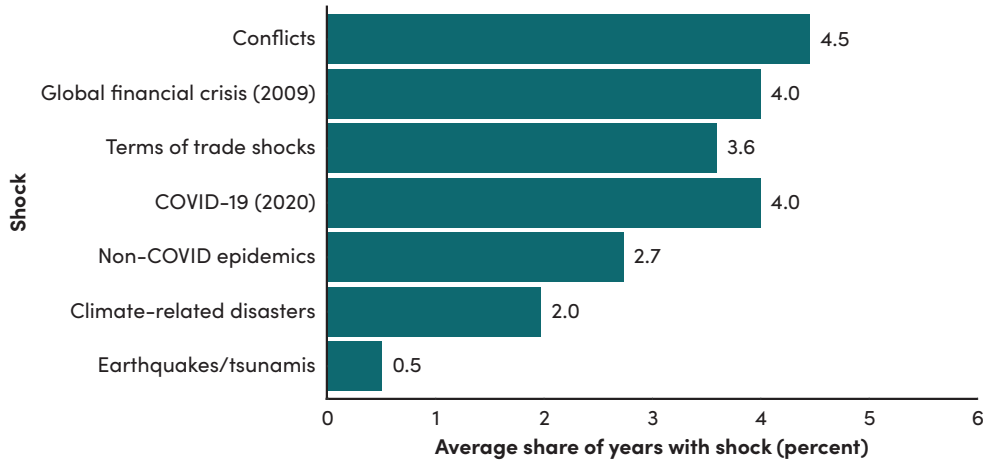
15 AfDB, 2023.
16 ADB, 2026.
17 EBRD, 2023.
18 UK Export Finance, 2023.
19 Reuters, 2026.
20 Japanese Ministry of Finance, 2024.
21 BHWG, 2025.
22 Despite early predictions that Collective Action Clauses (CACs) would raise capital costs, the broad consensus is that this did not happen cf. Gelpern and Zettelmeyer, 2019.
23 Song, 2025a.

2. How frequently are poor countries subject to different kinds of shocks?

Triggers for clause activation for natural disasters and health emergencies are easier to define, although not problem free.[24] But these are not the only shocks that inflict damage on poor countries.

Climate-related disasters have received the most attention in debt suspension initiatives. But it is important to look across different categories of exogenous shocks to get a sense of their relative frequency. Figure 3 shows the results of our frequency analysis across seven different kinds of large exogenous shocks.

FIGURE 3. Frequency of large exogenous shocks in LICs and LMICs (2000–2024)



Note: The number to the right of each bar indicates the average share of years in which the countries in our sample were affected by the given shock. Our sample consists of 79 LICs and LMICs.

Definitions: Exogenous shocks are those not driven by domestically determined economic or financial policies. A country was considered a LIC or LMIC if it fell into either category for at least twelve years over the period. Conflicts are defined as years with more than 1,000 conflict-related deaths. Terms of trade shocks are defined as declines in the terms of trade index two standard deviations below the median. The terms of trade index is defined as the ratio of the import value index to the export value index. Non-COVID epidemics are defined as epidemic disease events for which states of emergency were declared. Climate-related disasters and earthquakes/tsunamis are defined as such events with more than $1 million in associated damages. Climate-related disasters include droughts, extreme temperature, floods, storms, and wildfires.

Source: EM-DAT; UCDP; World Bank, WDI.

Our analysis suggests that the frequency (average share of years with shocks affecting countries in the sample) for conflicts, the global financial crisis (sharp reversal in global capital flows), large terms of trade deteriorations, and the pandemic is roughly double the frequency at which countries were affected by large climate-related shocks (damage >$1 million). The results confirm the importance of designing shock absorbers that mitigate the effects of a broad range of shocks.

24 Mustapha, 2025.

3. Eight principles for designing broadly applicable debt suspension clauses for LICs and LMICs

Designing clauses that serve the interests of both creditors and debtors is obviously challenging, but that should be the objective. Such clauses should: (1) meet recognized legal and transparency norms; (2) be standardized in ways that avoid the transaction costs associated with negotiating clauses issuance by issuance; and (3) facilitate market uptake, as we saw in the case of collective action clauses (CACs). This note outlines one approach for achieving those objectives, beginning with the principles that should shape design.

We propose that clauses be shaped by the following principles to support both issuance and uptake.

1. *Simplicity and predictability.* Simple and standardized rules, with as little debt issue-specific variation as possible, are important regarding the triggers for invoking the clauses and the nature of the relief offered. For example, relief could be limited to payments due in the 12-month period following invocation of the clause. Deferred interest payments would be capitalized (i.e., added to the principal). For each bond issuance, clauses could be activated only once during the bond tenor. It would be desirable for all future sovereign bond issuances by a given country to include the same DSCs. Over time, as new instruments replace old ones, a growing share of LIC/LMIC debt stocks would include the clauses, much like the gradual adoption of CACs.
2. *NPV neutrality.* The objective is to allow for an orderly, time-bound pause in payments that is NPV-neutral. NPV neutrality ensures that the DSCs function as instruments of liquidity insurance rather than mechanisms for debt restructuring, involving haircuts. The absence of haircuts also reduces concerns about comparability of treatment between official and private creditors, as all creditors are deferring—rather than forgiving—payments. NPV neutrality further supports price transparency since markets find it difficult to price discretionary NPV losses. There are multiple ways to structure the payments of deferred amounts under NPV neutral pauses, ranging from redistribution of payments over the remaining life of the loan to repaying them at maturity. Also, there could be fees associated with these clauses.[25] Although we do not take a specific position on these issues, we believe that the maturity date needs to remain the same to ensure that the overall terms of the original contract are not changed. This implies that the suspension could not be invoked within a year of the debt's original maturity date. The treatment of the deferred amount would partly depend on the debt's remaining maturity after the suspension period.[26]

25 IDB (2021) and the World Bank (2024a) both charge fees of 0.05 percent on the loan balance for their CRDC instruments, though the World Bank fee is recovered from external resources, not the borrower. By contrast, ADB (2026) does not charge fees for including debt deferral clauses in loan contracts.

26 Admittedly, for shocks of long duration, maintaining fixed bond maturities and barring multiple clause activations for given bond issuances diminish the benefits of the DSC. Under these circumstances, other debt relief tools may be required, especially when solvency issues emerge.

3. *Consistent deployment by both public and private lenders.* The benefits of debt payment suspension depend heavily on how much of the debt stock includes these clauses. For LICs and LMICs, we have seen a sharp increase in the share of their external debt stocks owed to international financial institutions (IFIs: MDBs + IMF), as multiple shocks have hit their market access and China has pulled back. The median share owed to IFIs is now 43 percent.[27] To be effective, these clauses must be included in loans from both bilateral and multilateral official lenders. As noted above, we have already seen some MDBs and bilateral lenders adopt some form of these clauses which should spur others to do so. An exception for the IMF might be considered given its lender of last resort mandate. A better focus for the IMF in our view would be to expand the scale of emergency liquidity lending to PRGT countries facing large exogenous shocks through the Rapid Credit Facility (RCF).
4. *Broad applicability across shocks.* In the poly-crisis age, it is essential to account for a wide range of shocks beyond just natural disasters and pandemics. But trying to define a priori all the possible variants of external and domestic shocks covered under DSCs would likely give rise to an excessively long list to cover all eventualities. That could actually encourage overuse of the clauses. Rather the focus should be on developing a common and credible framework to objectively assess the size of the impact of the shock and confirm that it is exogenous, i.e., not driven by domestic economic policy.
5. *Efficient use.* Not all countries facing large exogenous shocks experience major economic damage or need to have their external debt service paused. Much depends on their initial conditions with respect to international reserves and fiscal debt service burdens. Treating all LICs and LMICs the same in this context was one of the principal criticisms of the G20 DSSI. Triggers for activating DSCs must take account of countries' starting points at the onset of the shock.[28] In addition, activation of clauses is up to countries' discretion even if triggers are met: countries may decide not to activate clauses if doing so would worsen their future circumstances, e.g., add to future humps in debt service.
6. *Differentiation from insolvency cases.* DSCs are the wrong tool and potentially harmful in situations where a prompt reduction in debt stock or other forms of debt restructuring is essential to restore debt sustainability. Accordingly, DSCs should include language barring their invocation by countries that have already defaulted on some part of their debt or are in debt distress as judged by the IMF/World Bank Debt Sustainability Analysis (DSA).[29] Strict limits on the duration and frequency of use would also help ensure that the instrument is not used for evergreen forbearance.[30] Finally, invocations of these temporary debt suspension clauses should be clearly differentiated from events of default, so as to avoid triggering sovereign downgrades by credit rating agencies.

27 Diwan et al., 2026.
28 Rojas-Suarez, 2023.
29 World Bank Group, 2026.
30 One example is the proposal to limit relief to payments falling due within the 12-month period following invocation of the clause. More shock analysis is needed to determine the appropriate duration of the pause.

7. *Automaticity.* When creditors purchase a bond or agree to a loan contract that includes a DSC, the triggers are met, and a country decides to activate the clause, the clause should take effect automatically without requiring creditors' approval. The immediate availability of funds is a hallmark of liquidity-support instruments, which differ from mechanisms that address solvency. Accordingly, unlike CACs, implementation of the DSC should not be viewed as an amendment to the contract to approve an asset restructuring, but rather as an option embedded in the contract that preserves repayment capacity. The challenge is to define the triggers with sufficient rigor and objectivity to ensure that creditors are confident that DSCs will not be misused.
8. *Ability to apply and verify triggers objectively, quantitatively, and on a timely basis.* To be credible to creditors, data on initial conditions and the magnitude of the shock must be available quickly and from an authoritative source outside the country. The IMF and the World Bank are the obvious candidates. And the country must be willing to release the relevant data publicly so that all creditors have the same information.

4. Broadly applicable triggers for invoking debt suspension clauses for LICs and LMICs

Following these principles, we can devise four tests based on readily available data and existing IMF assessments of debt distress. DSCs in sovereign debt contracts and in MDB/DFI contracts could be invoked if all four tests are met.

We have suggested particular tests here but there may be better evidence-based alternatives. The important point is to use analysis and assessments already available to establish objective, straightforward benchmarks that set a credible bar, but not so onerous that it would defeat the purpose.

1. Insolvency test

Under the IMF and World Bank Debt Sustainability Framework (DSF) for LICs and LMICs, the IMF and World Bank produce DSAs. A country is classified as being in debt distress if it has already defaulted, is in arrears on its debt payments, or is assessed to be at high risk of imminent default.

> Countries designated in debt distress by the IMF and the World Bank may not invoke a DSC.

2. Liquidity test

A principal goal of DSCs is to address foreign exchange liquidity problems driven or greatly worsened by exogenous shocks. Therefore, the existence of such a problem must first be established. The IMF tracks available liquidity for servicing external debt through its assessment of reserve

adequacy (ARA).[31] The ARA is based on the stock of international reserves relative to short-term debt, imports, and broad money.

- Reserves to short-term debt: For LICs, less than 100 percent is considered risky and less than 50 percent is inadequate.
- Import coverage: Between 3 and 6 months is considered risky and less than 3 months is inadequate.
- Reserves to broad money: Between 5 and 20 percent is considered risky and less than 5 percent is inadequate.

For emerging markets but not LICs/LMICs, the IMF creates a composite metric combining all three called the Ratio of Reserves/ARA metric.[32] Reserves in the range of 100–150 percent of the composite metric are considered broadly adequate. Between 50 and 100 percent is considered risky and less than 50 percent is considered inadequate.

If a LIC/LMIC requests that it do so, the IMF can calculate the composite metric using the 3 ratios above. This composite metric could then be used for assessing liquidity conditions for a country wishing to invoke a DSC.

> To invoke a DSC, a country must—following a shock—have a liquidity ratio (Ratio of Reserves/ARA) assessed by the IMF as being in, or rapidly approaching, the risky or inadequate range.

3. Debt service burden test

The value of debt service suspension is also directly related to the size of a country's external debt service payments relative to its fiscal revenues. The DSF assesses countries' debt-carrying capacities and distinguishes between countries based on their policies, institutions, assets, and macroeconomic prospects.[33] It classifies countries as having strong, medium, and weak capacities and sets thresholds for external debt service as a percentage of revenues for each group of countries as one of the inputs into assessments about risks of debt distress. The threshold for countries in the strong group is 23 percent, 18 percent for the medium group, and 14 percent for the weak group.

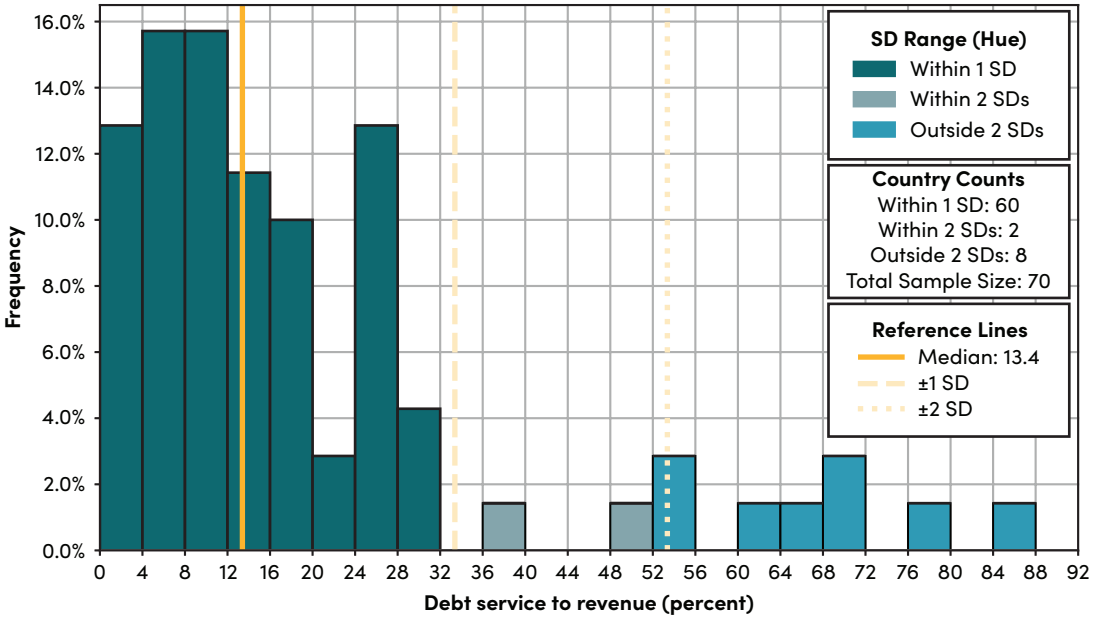
The figures below show LIC/LMIC frequency distributions of external debt service to revenue ratios during the two great global shocks of this century—the COVID pandemic and the global financial crisis (GFC). This comparison is useful in that it shows the impact of two major global shocks that were very different in nature.

31 IMF, 2025a. Special attention must be paid to countries that belong to currency unions to adjust the ARA metric to their particular circumstances.

32 Data published for individual countries is divided by 100.

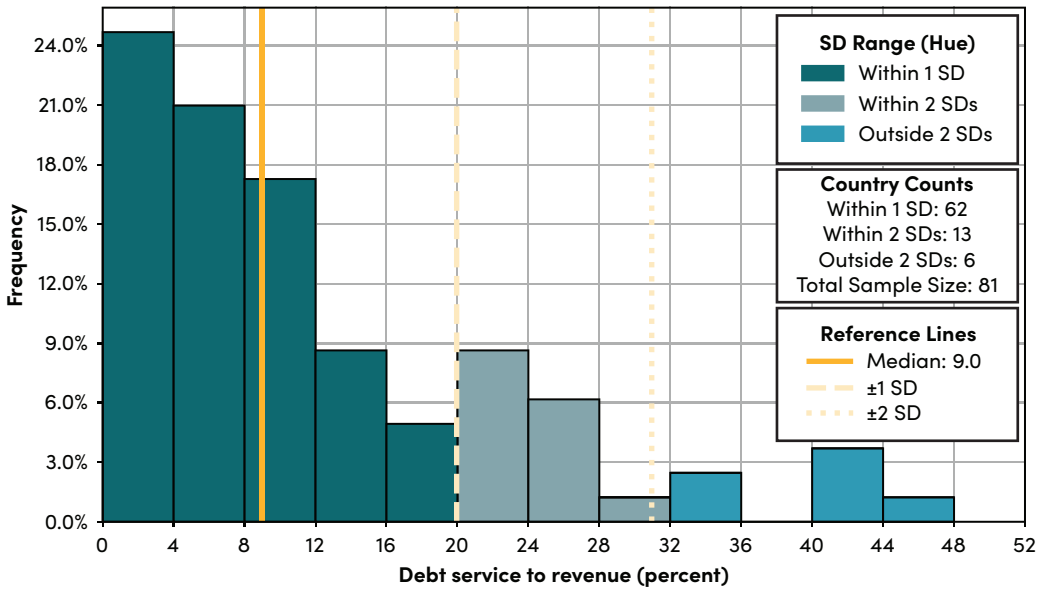
33 IMF, 2025d.

FIGURE 4. Frequency distribution of country ratios of external debt service to general government revenue for LICs and LMICs in 2020



Note: Two outliers, Liberia and Zimbabwe, were excluded from the sample.
Source: International Monetary Fund, WEO; World Bank, WDI.

FIGURE 5. Frequency distribution of country ratios of external debt service to general government revenue for LICs and LMICs in 2009



Note: One outlier, Liberia, was excluded from the sample.
Source: International Monetary Fund, WEO; World Bank, WDI.

We see median ratios of 13 percent in 2020 and 9 percent in 2009.

We can reasonably assume that LICs and LMICs include many countries classified by the IMF as having weak debt-carrying capacity, corresponding to a threshold of 14 percent.[34] We find 47 percent of countries in 2020 and 35 percent of countries in 2009 had ratios at or above that benchmark. So, for these two shocks, the 14 percent benchmark captures a sizable number, but certainly not all, LICs and LMICs.

That is consistent with the objective: these clauses should be relevant to a significant number of countries but still enable differentiation across LICs and LMICs based on need. Our proposed test therefore depends both on each country's debt-carrying capacity and the effect of the shock on its debt service burden.

> A country may invoke the DSC—following a shock—if its initial or projected external debt service-to-revenue ratio meets or exceeds the threshold associated with its assessed debt-carrying capacity under the LIC-DSF (e.g., 14 percent if classified as "weak", 18 percent for "medium", 23 percent for "strong").

4. Growth impact test

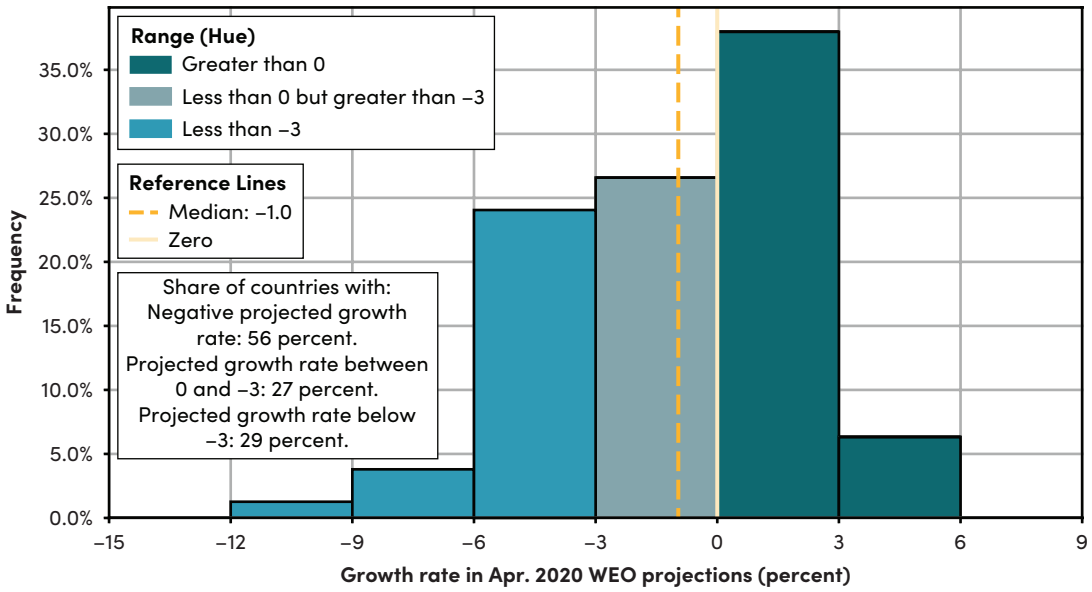
Major exogenous shocks have a wide range of effects on economies, financial systems, and individual and social wellbeing, but one consequence can reasonably be argued as common to all of these shocks: they significantly reduce growth. We see this for natural disasters, pandemics, epidemics, conflicts, sharp reversals of terms of trade, and global financial crises. The magnitude of the effect depends on the magnitude of the shock and the country's exposure to the shock, but as we see more shocks that are global in scope, we see poorer countries increasingly affected. Below, we examine the growth effects of different kinds of shocks.

The pandemic and the global financial crisis (GFC)

The two figures below show frequency distributions for LIC/LMIC projected growth rates in 2020 and 2009 (the year when the global financial crisis had the largest effect on real economies). Growth rates shown were projected by the IMF to take into account the effects of the shock. We explore one possible benchmark for meeting the growth impact test: countries must experience negative growth (economic contraction of any magnitude) as a result of the shock.

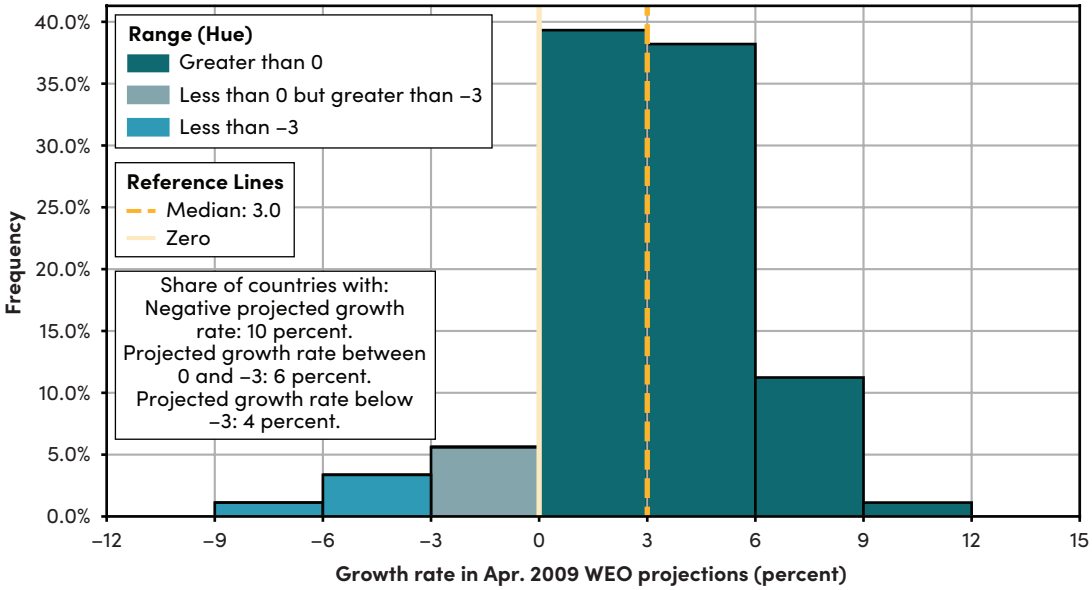
34 The World Bank Independent Evaluation Group found that 38 percent of low-income countries had weak debt-carrying capacity in 2022–23 (World Bank Group, 2023).

FIGURE 6. Projected growth rates for LICs and LMICs during the pandemic



Source: International Monetary Fund, WEO; World Bank, WDI.

FIGURE 7. Projected growth rates for LICs and LMICs during the global financial crisis (2009)



Source: International Monetary Fund, WEO; World Bank, WDI.

In both cases, a subset of LICs and LMICs saw negative projected growth rates as a result of the global shock: 44 out of 79 in 2020 (56 percent), and 9 of 90 LICs and LMICs in 2009 (10 percent).[35]

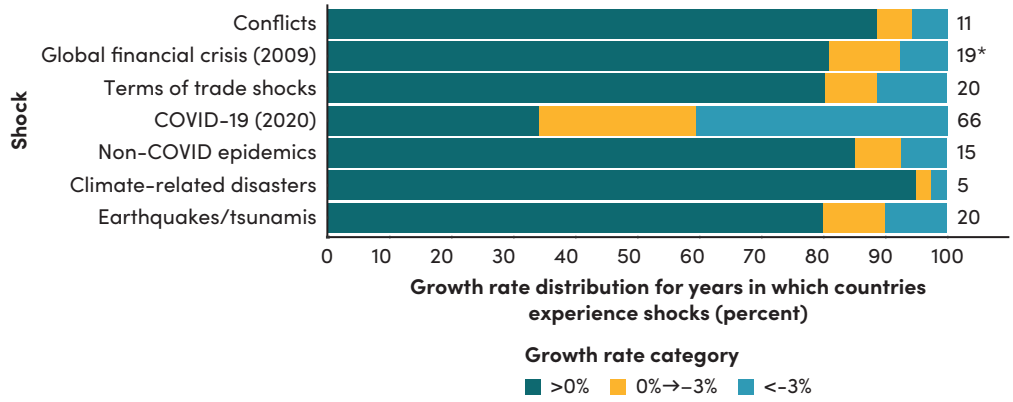
35 As country incomes grew, the total number of LICs and LMICs fell from 2009 to 2020.

Three takeaways are useful from this evidence. First, growth effects differ greatly depending on the nature and magnitude of the shock. Second, for those economies that had projected economic contractions during these two shocks, the size of the projected growth effect was large. For 89 percent of these economies, projected negative growth rates were –1 percent or less in 2020. For 78 percent of shrinking economies in 2009, projected negative growth rates were –1 percent or less. Third, the growth impact also depended on the degree of exposure of LICs and LMICs to the shock, which was considerably less in 2009 than in 2020. This supports application of DSC criteria that treat LICs and LMICs differently according to their circumstances, exposure, and the size of the shock—that is, avoiding the one-size-fits-all approach criticized for the DSSI.

Growth impacts of other major shocks

We can also compare growth effects of other major shocks to those of the pandemic and the GFC. Figure 8 compares shock-affected GDP growth rates for different types of shocks: significant conflicts, large declines in terms of trade, non-COVID epidemics, major climate-related events (droughts, extreme temperature events, floods, storms, wildfires), and earthquakes.

FIGURE 8. Growth rate frequencies by shock type in LICs and LMICs (2000–2024)



Note: The growth rate distributions were calculated using the sample of countries experiencing both that shock and a growth rate within that range during a given year. The number to the right of each bar indicates the share of years with negative growth for that shock.

Definitions: A country was considered a LIC of LMIC if it fell into either category for at least twelve years over the period. Conflicts are defined as years with more than 1,000 conflict-related deaths. Terms of trade shocks are defined as declines in the terms of trade index two standard deviations below the median. The terms of trade index is defined as the ratio of the import value index to the export value index. Non-COVID epidemics are defined as epidemic disease events for which states of emergency were declared. Climate-related disasters and earthquakes/tsunamis are defined as such events with more than $1 million in associated damages. Climate-related disasters include droughts, extreme temperature, floods, storms, and wildfires. (*) The total share for the global financial crisis differs from that found in Figure 7 because (a) this figure uses actual growth rates and (b) there is a sample size difference.

Source: EM-DAT; UCDP; World Bank, WDI.

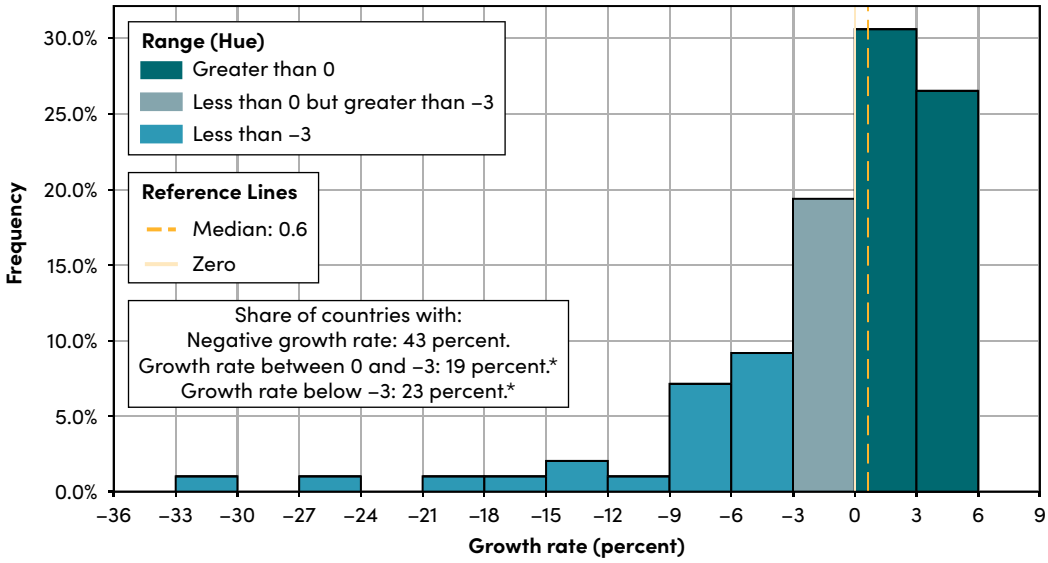
Negative growth was much more prevalent for the COVID-19 shock. It is relatively rare for countries confronting climate-related disasters. But growth was negative in 10 percent or more of years in which countries were affected by other shocks: conflicts, terms of trade shocks, non-COVID

epidemics, and earthquakes/tsunamis. This again supports the application of DSCs to a broader range of shocks than only those that are climate related.

Growth patterns for countries using the IMF Rapid Credit Facility

Finally, we can examine growth patterns for the countries that made use of the IMF's RCF, its instrument launched in 2010 for providing rapid liquidity to poor countries. The RCF has both an exogenous shocks window and a window for countries facing an urgent balance of payments need. RCFs, which entail minimal conditionality, are small relative to regular IMF programs. The cumulative access limit is 150 percent of quota. (For large natural disasters, the cumulative limit is 183.33 percent.)

FIGURE 9. Growth rates in RCF recipient countries in the year the country received relief (2010–2024)



Note: *Values do not add to 43% due to rounding.
Source: International Monetary Fund, IMF Financial Data.

Forty-three percent of countries that gained access to the RCF in the last 15 years experienced negative growth, affirming the relevance of this benchmark for countries that the IMF deems in need of urgent relief. During the pandemic, 59 percent of countries receiving RCFs had negative growth.

The projected growth threshold and data source

If the benchmark for meeting the growth impact test is defined as negative growth, this analysis suggests that it would benefit countries that are severely affected by different shocks but avoid excessive resort to DSC activation. That is a result that could be argued as desirable for both creditors and debtor countries. The debt relief would be well targeted and quickly available to the countries that need it most. But the four-part test is sufficiently stringent to protect creditors from overuse.

We have an authoritative source for revisions to country growth projections due to exogenous shocks: the IMF. It already responds rapidly to country requests for such revisions to growth and other macroeconomic variables in cases where countries are seeking RCFs to respond to exogenous shocks. Under this proposal, the country may ask for the revised growth projection with or without an associated request for an RCF through the exogenous shock window. The IMF would have to affirm that the revision to projected growth is driven by an exogenous shock.[36]

> To invoke a DSC, a country's real growth, as revised by the IMF due to the shock, must be negative for the year following the onset of the shock.

5. Summary and conclusions

Our analysis confirms that poor countries are subject to a broad range of exogenous shocks—not under their control and not just those that are climate-related—and that those shocks can have large consequences for growth, debt-carrying capacity, and liquidity. Our proposal for temporary suspension of debt service offers poor countries an opportunity to avoid default and pursue countercyclical or reconstruction spending to mitigate long-term economic damage and maintain creditworthiness.

The proposal has five distinctive features:

- Triggers for DSC activation focus on the magnitude of the shock, not the source.
- Benchmarks for clause activation are simple, standardized, and quantitative. The four-part test includes benchmarks for solvency, liquidity, debt service fiscal burden, and growth impact.
- Clause activation would not require creditor approval if triggers are met and verified.
- Clauses would apply to sovereign debt owed to both public and private creditors, to ensure comparable treatment amid the rising public creditor share of poor country debt stocks.
- The issuing country may spend the temporarily freed-up resources as it likes—different from debt for nature or debt for development swaps.

The proposal provides the opportunity to free up resources quickly, a critical advantage for poor countries with very limited fiscal space and international reserves. Because debt suspension clauses and terms of activation would be clearly delineated in debt contracts, invocation of DSCs can be distinguished from an event of default or distressed operation under the methodologies of credit rating agencies.

The activation process would be relatively straightforward. Countries would obtain the relevant data and shock-driven growth projections from the IMF, make the information public with IMF verification, and activate the DSC, which would permit suspension of their external debt payments

36 It would make little sense for the IMF to withhold a response in cases where RCFs are not sought on the grounds that the request is not related to IMF finance. Both the IMF and the country gain if other actors contribute to helping countries grapple with temporary debt strains and avoid default.

in the twelve months following the shock for eligible issuances that include the DSC. The deferred interest would automatically be added to the outstanding principal.

The relief would be large in relation to the alternatives available to heavily impacted countries. Jamaica offers a recent example of relative magnitudes (though it is a UMIC). It will receive a $150 million payout from its catastrophe bond due to Hurricane Melissa (October 2025).[37] Jamaica also borrowed $415 million in January under the IMF's Rapid Credit Instrument for large natural disasters (80 percent of quota).[38] But if its total 2026 debt service for Eurobonds and MDB debt were temporarily suspended, the freed-up resources would amount to $1.1 billion. Jamaica suffered an estimated $8.8 billion in damage from the hurricane, equivalent to 41 percent of GDP.[39]

It is important to acknowledge that the proposal has an important limitation. It applies only to new issuances, which will initially represent a small portion of countries' total debt stocks. As a result, the impact on debt service will initially be limited. However, precedents in Barbados and Grenada show that DSCs can be added to debt contracts during restructurings. Finding a way to add such clauses to existing issuances is worth pursuing, despite the legal challenges.

The proposal is meant to complement, not substitute for, ongoing work to make the debt restructuring process more efficient and to explore refinancing options for poor countries' current high-cost debt. The aim is better long-term solutions to strengthen the resilience of poor countries and to help avoid a recurrence of today's pervasive debt strains. We know these countries will continue to be subject to frequent exogenous shocks. A forward-looking approach of building better debt contracts for poor country sovereign borrowing should be a prominent part of the debt relief arsenal.

A crucial aspect of better debt contracts is transparency. Both debtors and creditors gain when obligations under sovereign debt contracts are fully disclosed, articulated in standardized language, and available for all outstanding debt.[40] It is especially important for contracts with DSCs to be transparent, given understandable initial uncertainty from creditors and stakeholders in issuing countries about how this innovation would work. Any contract with these DSCs should be published in full on sites readily available to the parties and to the public.

The role of the official sector will be critical in advancing this approach. Including DSCs in the loan contracts of the MDBs and bilateral DFIs (including China's) would go a long way toward addressing the comparability of creditor treatment disputes that hampered the DSSI effort. It would ensure consistent and timelier debt relief for countries that borrow heavily from these sources. Building momentum and ensuring the cooperation of the IMF, World Bank, and other MDBs will require strong support from the G20, G7, and finance ministries of both major creditor countries and poor countries.

37 CNBC, 2025.
38 IMF, 2026.
39 World Bank Group, 2025.
40 E.g., IIF, 2019.

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