Briefing: Support debt restructuring for lower-income countries

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Debt Justice calls on MPs to write to the Chancellor to raise the failure of BlackRock to cooperate with debt restructuring under the G20 Common Framework.

- Fifty-four countries are in debt crisis globally, up from 31 in 2018. The economic stress of the last few years has pushed more and more countries into debt. Debt levels for lower-income countries are at their highest for over 20 years.
- Zambia is currently in debt crisis, and one of the first countries to go through a new G20 restructuring process called 'The Common Framework'. But they are being blocked by their biggest bondholder, the asset manager BlackRock, who could make up to 110% profit if paid back in full.
- Right now, Zambia is in negotiations with their lenders. They UK government is a key part of these negotiations and UK law governs all of Zambia's bonds.
- The government must encourage BlackRock to restructure Zambia's debt, introduce legislation to require bondholders such as BlackRock to take part in internationally agreed debt relief and support debt relief for countries in distress.

Summary

Lower income countries have been plunged into a debt crisis that is preventing them from addressing the pandemic or the climate emergency. There is an urgent need for debt relief, but private creditors are blocking restructurings of unsustainable debt by demanding to be paid in full. Since the start of the pandemic, the G20, the UK Government, the IMF and the World Bank have all been calling on private creditors to participate in debt restructurings, but their pleas have been ignored.

The UK is in a strong position to close the loopholes that are allowing private creditors to evade responsibility, since the vast majority of lower income country debt contracts are governed by English or New York law. This means that the UK could pass legislation to ensure that minority hold-out creditors cannot undermine collectively agreed restructurings. This would benefit all creditors, allowing private creditors to do the right thing without fear of losing out to competitors. There is an opportunity for the UK to provide global leadership in addressing this crisis.

There is growing support for legislation in the UK and the US. The World Bank President David Malpass has said that "Major jurisdictions may need to look to legislative changes to support faster progress if private creditors aren't able to move forward on their own.[1]" IMF Managing Director Kristalina Georgieva has said "We also are pressing for some of the changes, legal changes that need to happen in New York, in London, to close loopholes for vulture funds and others to prevent debt resolution."[2] Proposals for legislation have been made in New York to make it harder for private creditors to avoid internationally agreed debt restructuring.[3]

[1] https://www.reuters.com/article/us-g20-worldbank-debt-idUSKBN2801YO
[2] https://www.imf.org/en/News/Articles/2022/04/21/tr220421-transcript-of-the-imfc-press-briefing
[3] https://www.nysenate.gov/legislation/bills/2021/S6627 and https://www.jubileeusa.org/new_york_taxpayer_and_international_debt_crises_protection_act?utm_campaign=pr_ny_bill&utm_medium=email&utm_source=jubileeusa

Zambia is in debt crisis, with its debt payments higher than healthcare, education and social protection, combined. Right now, the Zambian government is negotiating with its lenders, and BlackRock, their biggest bondholder, is refusing to cancel or suspend any debts. It's set to make huge profits of up to 110%, if paid in full.

The debt crisis and private creditors

Lower income countries have been facing increasingly unsustainable debt since the 2008 financial crisis. The economic shocks imposed on lower income countries from the pandemic have significantly exacerbated the situation. For the 69 countries they assess, the IMF say 39 are in debt distress or at high risk of being so.

In December 2020, the G20 introduced a new mechanism to help address the crisis, the Common Framework. Although it requires private creditors take part, it lacks a process to compel them to do so. Progress has been painfully slow: only three countries have so far applied, Chad, Ethiopia and Zambia, and none have yet seen any debts restructured. The lack of cooperation of private creditors appears to be both blocking progress on the countries that have applied and discouraging others from applying.

The participation of private creditors in debt restructuring is critical: 47% of lower-income country external debt repayments are due to private creditors in 2022, compared to 27% to multilateral institutions, 12% to China and 14% to other governments. Debt restructurings have to involve all creditors on a fair and equitable basis, recognised in the Common Framework in the principle of comparability of treatment. If private creditors refuse to participate, governments are rightly reluctant to grant debt relief that would simply allow private creditors to continue being paid, effectively using public money to bail out the risky (and usually higher interest) lending of banks and hedge funds.

Zambia defaulted on interest payments to foreign currency bondholders in November 2020 when private creditors refused to suspend debt payments. In February 2021, Zambia applied for a debt restructuring through the G20 Common Framework, but no progress has been made on the negotiations as large private creditors have so far refused to restructure the debt. Blackrock is the largest of a number of creditors who are refusing to cancel Zambia's debt, despite lending to the country with interest rates as high as 9%.

What reform is needed?

The UK has a unique opportunity to strengthen the legal framework to ensure the participation of private creditors, as 90% of bonds issued by countries eligible for the Common Framework are governed by English law. There is a precedent for UK legislation to facilitate debt restructuring processes: the 2010 Developing Countries Act prevents a private creditor suing a borrowing government for more than it would have received if it had taken part in the Heavily Indebted Poor Countries process, the previous major debt relief initiative.

The UK could introduce new legislation which would make a debt restructuring binding on all private creditors if agreed by 66% of them or more for loans provided under English law. It would ensure that, when at least two thirds of private creditors vote to agree to a restructuring, it would be binding on the minority who voted against, as is the case in corporate debt renegotiations. This would prevent private creditors taking borrowing governments to court to sue for the full amount they are owed as they would be tied into a debt restructuring.

Alternatively, the UK could replicate the 2010 Act and legislate so that no creditor could sue for more than they would have got if they took part in the Common Framework, or any other internationally agreed debt restructuring.

The key benefits of the legislation would be to:

- Ease the debt restructuring process by undermining the ability of minority creditors to hold out on an agreement, reducing risks of default
- Facilitate financial settlements for debtor governments in distress
- Increase the speed of restructuring processes, reducing uncertainty for debtor countries and creditors and enabling borrowing governments to access capital markets again more quickly (as has been shown by the IMF's own research)
- Address the power imbalance between the single debtor country and often large number of creditors.

The UK government could also help Zambia negotiate a debt restructuring with BlackRock and other private lenders by following the IMF lending into arrears policy and saying 1) Zambia should be supported to default on any creditor who refuses to take part in the Common Framework debt restructuring and 2) it will restructure the debt Zambia owes the UK in line with the Common Framework, as long as Zambia remains in default on any creditors who refuse the restructuring.

For more information contact Jerome Phelps jerome@debtjustice.org.uk.