

# Public Debt and Economic Growth in Developing Countries

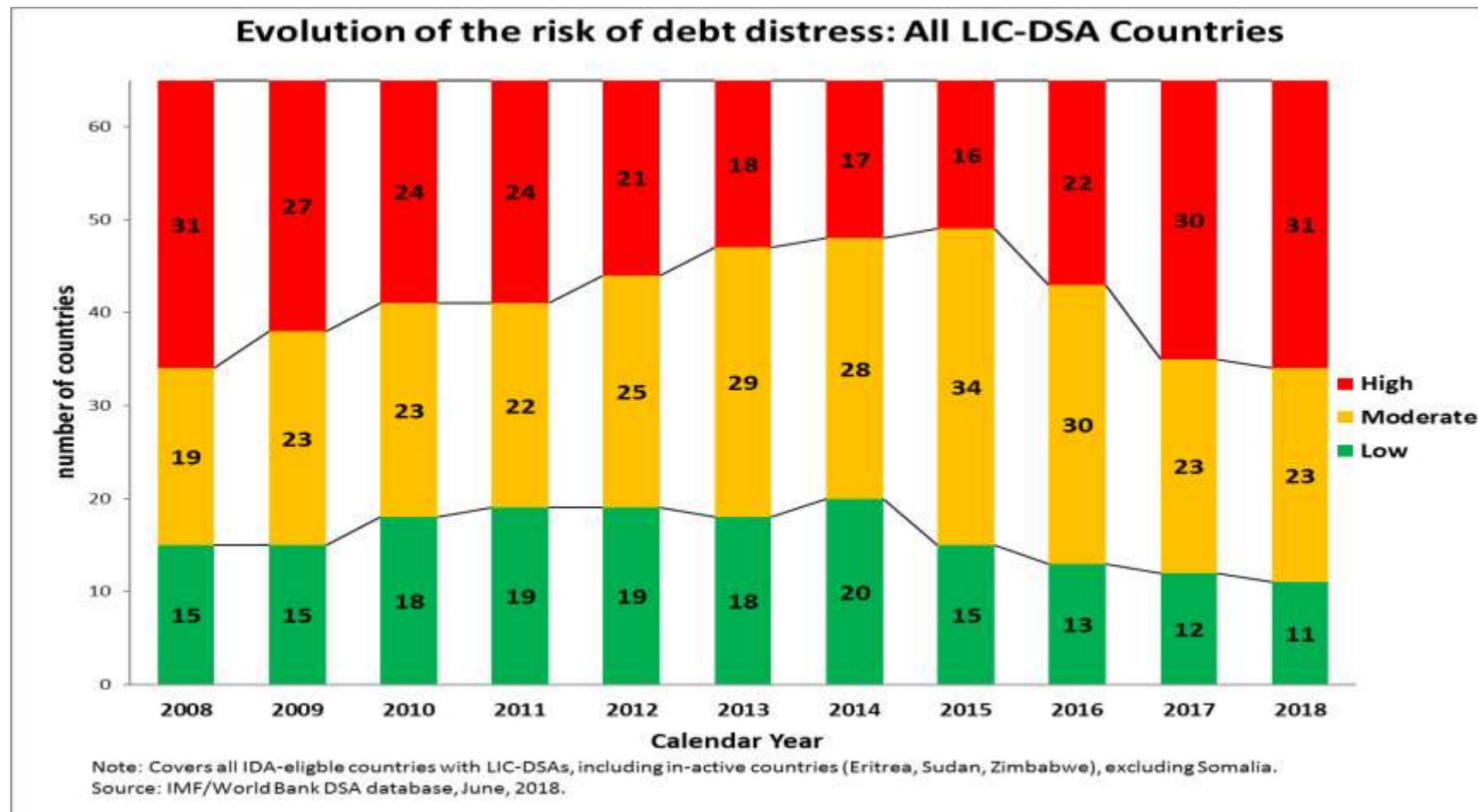
The World Bank/IMF Debt Sustainability Framework



**WORLD BANK GROUP**

Global Knowledge & Research Hub  
in Malaysia

# Developing countries across the world are seeing a rising risk of debt distress



10 countries in debt distress in 2018 vs 1 in 2013

# But why is debt sustainability important?

**Developing countries face significant challenges that often are difficult to reconcile:**

- Meet development objectives (including the SDGs) → need to invest → borrow → debt accumulation → potential for distress or crisis

**In a debt crisis, countries can experience:**

- Sharp deterioration in living standards (sharp fiscal adjustments, exchange rate revaluations, collapses in consumption...)
- Negative spillover effects, through financial and trade channels
- Permanent negative effects on social and human capital
- Social tensions

# What is debt sustainability?

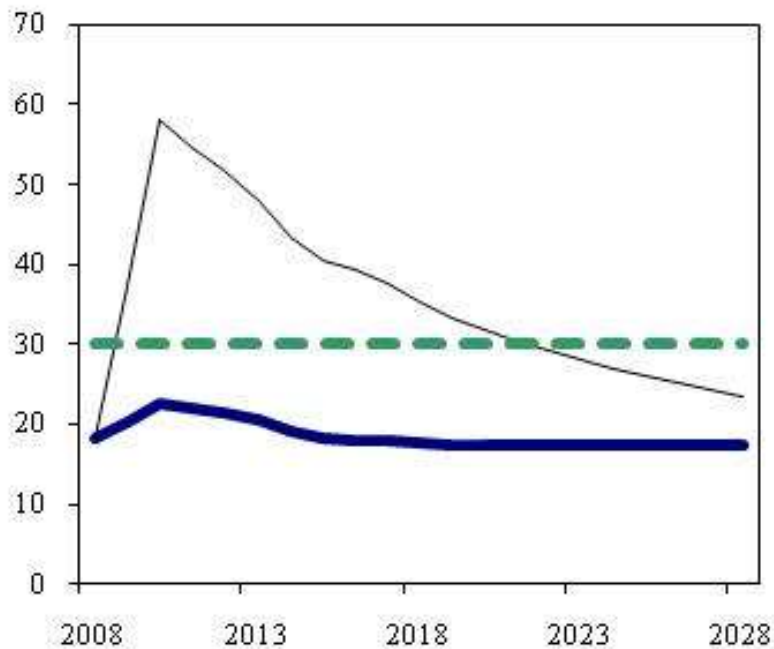
Capacity to meet future financial obligations without sharp adjustments in:

Income and expenditure patterns, fiscal policy

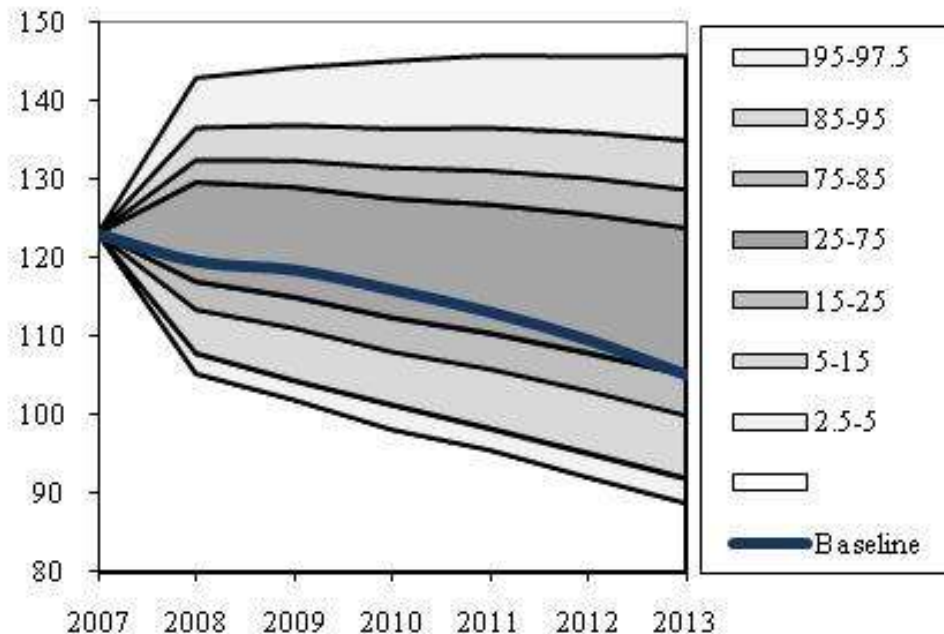
Financing decisions

# But assessing debt sustainability is as much an art as a science

So we use a variety of tests to assess the risk of debt distress using a joint World Bank/IMF Debt Sustainability Framework



Deterministic



Stochastic

...and use different thresholds depending on judgements as to the strength of a country's debt carrying capacity

**Table 6. PPG External Debt Thresholds**

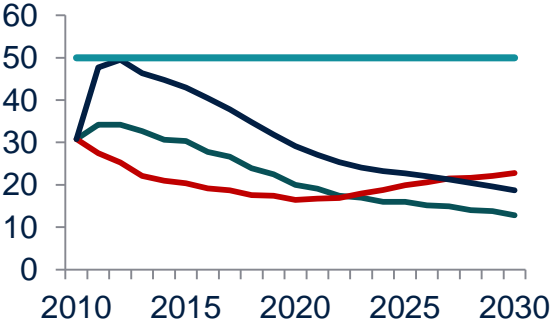
Debt carrying capacity (CI classification)	PV of PPG external debt in percent of		PPG external debt service in percent of	
	GDP	Exports	Exports	Revenue
Weak	30	140	10	14
Medium	40	180	15	18
Strong	55	240	21	23

**Table 7. Total Public Debt Benchmarks**

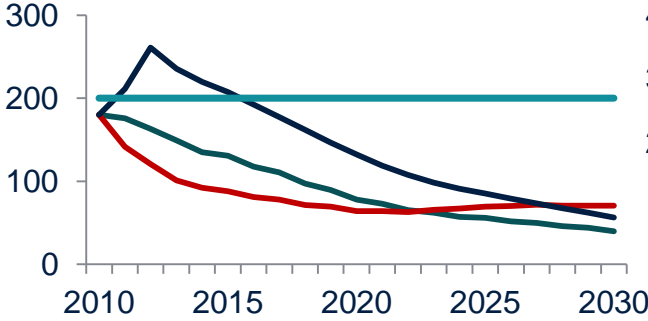
Debt carrying capacity (CI classification)	PV of total public debt
	GDP
Weak	35
Medium	55
Strong	70

# ...and then apply a battery of stress tests to see if those thresholds are at risk of being breached

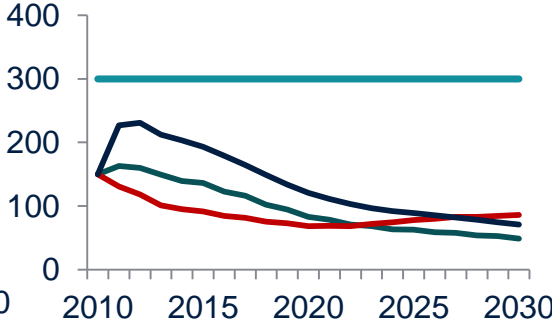
**PV of External PPG Debt to GDP**



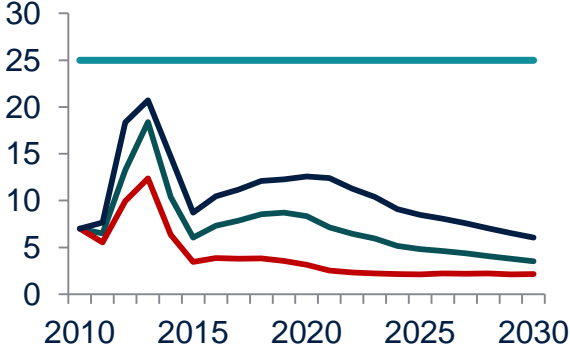
**PV of External PPG Debt to Exports**



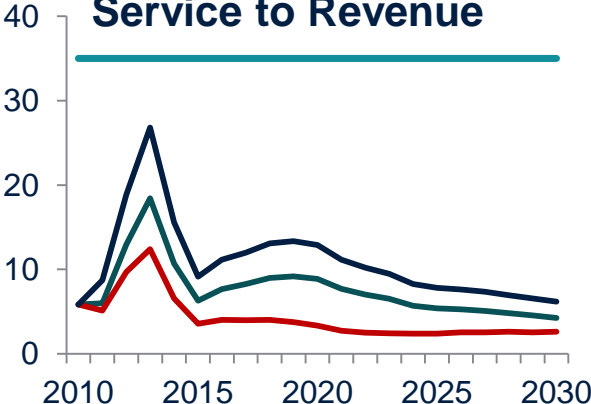
**PV of External PPG Debt to Revenue**



**External PPG Debt Service to Exports**



**External PPG Debt Service to Revenue**



- Baseline scenario
- Historical scenario
- Stress test
- Threshold

# Summary of the debt sustainability framework for low-income countries

Figure 1. Structure of the Reformed LIC DSF

