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A Real Mosaic of Solutions to Respond to Loss and Damage from Climate Change

Debt Reform

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Introduction

This publication is part of a [series of briefs](#) unpacking the pieces of a fit for purpose “mosaic of solutions” to respond to loss and damage from climate change. This series expands on our earlier work, which presented a [five-year vision for Loss and Damage under the United Nations Framework Convention on Climate Change \(UNFCCC\)](#) to look beyond the international climate regime at catalysing a wider mosaic of solutions.

In the [flagship paper](#) of the series, we unpack the pieces of the mosaic. In these thematic briefs, we dive deeper into existing solutions and how they can be strengthened. We also consider any reforms needed and explore emerging solutions.

This brief unpacks the relationship between loss and damage and debt in developing countries. It provides a succinct overview of the problems developing countries face as a result of sovereign debt and the existing international debt system. It also highlights the inadequacy of existing debt solutions and why a fit for purpose [United Nations Framework Convention on Sovereign Debt \(UN Debt Convention\)](#) must be established.

What is the problem?

Sovereign debt is accumulated by developing countries through borrowing from foreign lenders, international financial institutions such as the [International Monetary Fund \(IMF\)](#) and [World Bank](#), other [multilateral development banks \(MDBs\)](#) such as the [European Investment Bank](#), and private investors.

Developing countries are trapped in a vicious cycle, spending more on debt repayments than essential services such as healthcare and education¹ or climate action.² In 2024 alone, developing countries’ net interest payments on public debt were 921 billion USD³ and in 2025, 38 low income countries were at a high risk of debt distress and 13 faced debt distress.⁴ In the context of responding to loss and damage, debt reform is therefore urgently required for two key reasons:

1. To enable and enhance loss and damage prevention and reduction by increasing fiscal space and the availability of budgetary resources; and
2. To prevent debt crises from occurring in the aftermath of a loss and damage event as a result of borrowing or receiving climate finance in the form of loans and not grants.⁵

What are the existing solutions?

Many of the solutions currently available to developing countries fail to prevent or resolve debt crises. Therefore they should be largely regarded as false solutions or attempts to delay meaningful action, such as debt cancellation. Table 1 unpacks why this is the case.

Table 1: Debt solutions currently available to developing countries.

CURRENT SOLUTIONS	HOW DOES IT WORK?	WHAT ARE THE ISSUES?
Debt for Climate/Nature Swaps	Debt swaps cancel or restructure sovereign debt in exchange for commitments to agreed development goals. Debt-for-climate swaps release funds to be allocated to climate action and debt-for-nature swaps release funds to be allocated to conservation. ⁶	Debt-for-climate and nature swaps do not meaningfully reduce debt levels and can fail to deliver on conservation and climate goals. They also lack transparency and undermine local communities' participation. Often complex, costly, and lengthy to negotiate, they can also legitimise illegitimate debt ⁷ (i.e. loans contracted by a State under unacceptable conditions, which have violated economic, social, cultural and environmental rights), and ultimately distract from the need for debt cancellation. ⁸
Climate Resilient Debt Clauses (CRDCs)	CRDCs are contractual provisions in loan agreements that allow developing countries to temporarily pause or defer debt principal and interest repayments for up to two years following a loss and damage event.	Although CRDCs provide much needed temporary relief, the debt still needs to be paid in the future. CRDCs could be regarded as a distraction from the need for debt cancellation when presented as a solution on their own.
"More Lending" as a Solution	The IMF and World Bank frequently use increased lending as a strategy to manage debt, offering low-cost financing for development and economic shocks. There is also a growing emphasis on using public resources to mobilise more private finance to developing countries.	High-interest private debt combined with increased lending by multilateral institutions will lead to unsustainable, ever-increasing debt burdens in developing countries.
Debt Service Suspension Initiatives	The Debt Service Suspension Initiatives (DSSI) was launched in May 2020 and was active until December 2021. It allowed 73 eligible low-income countries to temporarily suspend official bilateral debt-service payments to focus resources on COVID-19 pandemic relief.	DSSI failed to include multilateral creditors. While private creditors were supposed to participate, they did not. ⁹ It also offered insufficient short-term relief, saw limited participation due to fear of credit rating downgrades, high administrative costs, and very little benefit.

CURRENT SOLUTIONS	HOW DOES IT WORK?	WHAT ARE THE ISSUES?
The G20 Common Framework for Debt Treatments	Also set up in 2020, the <u>G20 Common Framework for Debt Treatments</u> (CF) is intended to facilitate timely and orderly debt treatment beyond DSSI for countries that are eligible.	The CF has failed to compel the participation of private lenders on fair terms, leading to further bailouts by multilateral institutions and insufficient debt relief. Of the four countries that have requested treatment – Chad, Ethiopia, Zambia, and Ghana—none have completed the process and received adequate debt relief.
Austerity Measures	Austerity measures are government-imposed economic policies designed to reduce sovereign debt and budget deficits. They are also often imposed via conditions included in loans from institutions like the IMF and World Bank. Policies may include reductions in public sector wages, social protection and public infrastructure projects. They can also include increased taxation, structural reforms such as the privatisation of state-owned enterprises, and labor market deregulation.	Austerity measures lead to worsened public health outcomes (e.g. lower life expectancy), increased poverty, higher unemployment, and diminished quality of public services. ¹⁰ They typically increase countries' debt dependency, undermine policies, and reduce fiscal space to respond to loss and damage and address wider needs of societies.
Exploitation of Fossil Fuels or Natural Resources to Pay of Debt	Multilateral and private lenders are trapping heavily indebted developing countries in reliance on fossil fuels to generate revenue that allows them to service and repay debt. This can lead to more debt when expected returns from fossil fuels are lower. ¹¹ It also increases future loss and damage by contributing to global emissions. Resource-backed loans or commodity-prepayment agreements feature clauses designed to prioritise, secure, and accelerate the extraction of natural resources to repay debt obligations, often in volatile markets or as an alternative for high-risk borrowers. ¹²	Increasing fossil fuel extraction and the extraction of other natural resources can increase vulnerability to climate change through cascading environmental impacts that are born by neighbouring communities, not those benefiting from fossil fuel extraction and production. The extraction and burning of fossil fuels and unsustainable use of natural resources will further exacerbate climate change leading to more loss and damage.

CURRENT SOLUTIONS	HOW DOES IT WORK?	WHAT ARE THE ISSUES?
IMF Catastrophe Containment and Relief Trust	The IMF's Catastrophe Containment and Relief Trust (CCRT) provides grants to eligible low-income IMF member countries to service debt owed to the IMF. Grants are available when developing countries face what the IMF categorises as catastrophic natural disasters (e.g. an earthquake) or major public health disasters (e.g. a cholera outbreak). ¹³	Countries only qualify if a "natural disaster" has directly affected at least one-third of the population, is estimated to have destroyed more than a quarter of the country's productive capacity or has caused damage deemed to exceed 100 per cent of GDP. ¹⁴ This means that only the most catastrophic loss and damage events would be eligible. The grants are only to service debt owed to the IMF and cannot be used to service other debt or respond to loss and damage.

What do we need to see?

To prevent debt crises from occurring and increase fiscal space and the availability of budgetary resources, urgent debt cancellation as well as deep reforms to the debt system are needed. The UN Debt Convention is expected to put in place a set of international principles, rules, procedures, and structures to govern both debt crisis prevention and resolution.¹⁵ Table 2 highlights the key reforms that civil society¹⁶ and some developing country governments¹⁷ are calling for under the UN Debt Convention and how they can enhance response to loss and damage.

Table 2: Reforms needed under the UN Debt Convention to enhance loss and damage responses.

PROPOSED REFORM	HOW WILL IT WORK?	HOW DOES IT RELATE TO LOSS AND DAMAGE?
Multilateral Sovereign Debt Resolution Mechanism	Establish a Multilateral Sovereign Debt Resolution Mechanism that ensures: • The primacy of human rights over debt service; and • A rules-based approach to orderly, fair, transparent, and durable debt crisis resolution, in a process convening all creditors. This mechanism would act as an independent institutional body and deal with the resolution of debt crises by responding to countries in default and/or in need of debt restructuring and cancellation.¹⁸	This would help enable developing countries to free up fiscal space and increase the availability of budgetary resources to respond to loss and damage.

PROPOSED REFORM	HOW WILL IT WORK?	HOW DOES IT RELATE TO LOSS AND DAMAGE?
Binding Principles on Responsible Sovereign Lending and Borrowing	Upgrade the United Nations Conference on Trade and Development's (UNCTAD) Principles on Promoting Responsible Sovereign Lending and Borrowing to a set of binding rules and principles and defining tools to track implementation and ensure compliance. ¹⁹	This would help to ensure that developing countries avoid debt traps if they have no choice but to borrow to finance loss and damage responses.
Automatic Mechanism for Debt Payments Cancellation	Establish an automatic mechanism for debt payments cancellation in the wake of external catastrophic events such as a loss and damage event followed by enhanced debt restructuring and cancellation.	This would immediately increase the availability of budgetary resources that can be used by an impacted developing country to respond to loss and damage rather than service existing debt. It would also kick start the process to restructure or cancel sovereign debt.
Mandatory inclusion of Climate Resilient Debt Clauses (CRDC)	Mandate the mandatory inclusion of CRDCs in lending contracts from public lenders (governments, MDBs, the IMF and other official lenders), that are tied to climate, geological, health, and economic shocks.	This would ensure that developing countries have the option to temporarily pause or defer debt principal and interest repayments for up to two years following a loss and damage event while debt cancellation is in progress.
Global Debt Registry	Establish a global debt registry to promote transparency that includes all debt operations and that applies to all types of lenders and current holders of outstanding debt including commercial lenders. By making registration binding for all debt-creating operations, debt not included in the registry should not be enforceable by national courts.	Increasing debt transparency will help to advance debt cancellation for developing countries, thereby enabling enhanced responses to loss and damage.

PROPOSED REFORM	HOW WILL IT WORK?	HOW DOES IT RELATE TO LOSS AND DAMAGE?
Comprehensive Review of Approaches to Debt Sustainability	Agree on a comprehensive review of approaches to debt sustainability. This is needed to evolve towards a more adequate debt sustainability model, one that is delivered independently from creditors and includes human rights and other social, gender, climate, and development considerations at its core.	Current debt sustainability frameworks, particularly those of the IMF and World Bank, rely on overly optimistic growth projections ²⁰ , fail to integrate climate ²¹ and environmental ²² risks and promote austerity ²³ that hinders sustainable development. This means the need to respond to loss and damage is not taken into consideration. Therefore, a review will help to ensure that developing countries have fiscal space to respond to loss and damage.

Civil society and supporting governments aim to introduce the debt convention to the UN [General Assembly](#) by 2027. It will then take time to negotiate and operationalise. Therefore, developing countries should continue to push creditors to agree to debt cancellation, while ensuring that all new loan agreements contain CRDCs.

At the same time, to accelerate debt cancellation, creditor countries should introduce new laws that would ensure that private creditors participate in debt restructuring deals on fair terms. This is needed to undermine their ability to delay negotiations, seek maximum payment or threaten to take countries to court for full payment.²⁴ The UK and New York are key jurisdictions for this as nearly all of the external private debt of developing countries is governed under English²⁵ and New York law.²⁶

The [Borrowers' Platform](#), launched on the margins of the IMF and World Bank Spring Meetings on April 15, 2026 in Washington, DC, also presents an opportunity for developing countries to strengthen cooperation among borrowers.²⁷ This will be done by enabling developing countries to share experience and knowledge through the Platform that could improve debt sustainability and aspects of the international financial architecture, and ultimately enhance loss and damage response.²⁸

Endnotes

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