Riders on the storm

How debt and climate change are threatening the future of small island developing states

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european network on debt and development

EXECUTIVE SUMMARY

The oceans are scattered with small islands, dots on the world map that have too often been ignored. Yet they are home to 65 million people. Small Island Developing States (SIDS) are among the countries that are under the greatest threat from the multiple crises that the world is facing today, particularly the climate emergency and the wave of debt in which many countries in the Global South are drowning. The sustainable development of SIDS is constantly jeopardised by their structural weaknesses, including their small size, remoteness, reduced resource base, exposure to adverse climate events and limited diversification of the economy. Together with the Covid-19 shock, global inflation and spillovers of the war in Ukraine, these multiple crises and vulnerabilities are not only threatening the stability of the SIDS' economies and harming the wellbeing of their people, but have also resulted in greater exposure to public debt problems. This report looks at the twin challenges of debt and climate change facing SIDS and suggests calls to action to help tackle these challenges.

Table 1: Which countries are SIDS?

	Asia and the Pacific	Latin America and the Caribbean	Sub-Saharan Africa
Low income			Guinea-Bissau*
Lower middle income	Kiribati* Micronesia Papua New Guinea Samoa Solomon Islands* Timor-Leste* Tonga Vanuatu	Haiti*	Cabo Verde Comoros* São Tomé and Príncipe*
Upper middle income	Fiji Maldives Marshall Islands Palau Tuvalu*	Belize Cuba Dominica Dominican Republic Grenada Guyana Jamaica Saint Lucia St Vincent & the Grenadines Suriname	Mauritius
High income	Bahrain Nauru Singapore	Antigua and Barbuda Bahamas Barbados St. Kitts & Nevis Trinidad and Tobago	Seychelles

*Also Least Developed Countries (LDCs)

Sources: Eurodad based on UN and World Bank.

Waves of austerity in SIDS

SIDS urgently need to increase their fiscal space to tackle the multiple challenges and crises facing them. However, high debt levels are leading many governments to adopt austerity policies in order to pay for their debt commitments. In 2019, the average government expenditure was 39.4 per cent of Gross Domestic Product (GDP) in SIDS, but in 2025 this spending is expected to be reduced to 37.95 per cent (1.45 points less). International Monetary Fund (IMF) projections show that 20 out of 37 SIDS are expected to have lower government spending in relation to their GDP in 2025 than they had before the Covid-19 pandemic. **Government expenditure as a percentage of GDP is predicted to decrease in 31 out of 37 SIDS between 2022 and 2025.** This will not only exacerbate poverty and inequality, but rapid fiscal consolidation can also hinder economic recovery.

Tides of debt in SIDS

This austerity push in SIDS is being implemented to respond to worsening debt sustainability assessments. Eurodad examined three different debt risk assessments – IMF and World Bank Debt Sustainability Analysis, and two civil society analyses by Debt Justice UK and Jubilee Germany. We found that **81 per cent of SIDS have been identified by one or several of these assessments to be facing different levels of debt difficulties. Twelve countries have been assessed by all three methodologies as facing a potential debt crisis or as being in debt crisis already.** These include: Belize, Dominica, Grenada, Guinea-Bissau, Haiti, Maldives, Papua New Guinea, Saint Vincent and the Grenadines, Samoa, São Tomé and Príncipe, Suriname and Tonga.

Our own calculations show how **public debt rose from an average 65.9 per cent of GDP in 2019 up to 82.5 per cent in 2020, to remain over 70 per cent of GDP until 2025.** This is above the average in emerging and developing countries in Asia, Latin America and the Caribbean and sub-Saharan Africa. Half of the countries have ratios above the SIDS average and, for 10 of them, the debt ratio remains above 100 per cent of GDP for several years.

In this situation, an increasing portion of government revenue is dedicated to meeting debt obligations. Between 2020 and 2023, countries like Belize, Cabo Verde, Dominican Republic, Jamaica, Maldives, Grenada and Papua New Guinea are **allocating between 15 per cent and up to 40 per cent of their government revenue to pay their external creditors.**

Debt rose in SIDS particularly with the Covid-19 shock due to an increase in lending. Disbursements on external public debt almost doubled with the pandemic, increasing from US$8.5 billion in 2019 to US$16.2 billion in 2020. The IMF went from having programmes with three SIDS in 2019 to lending to 20 small island countries between 2020 and 2021.

The vicious circle of debt and climate emergencies in SIDS

Small islands are amongst the most vulnerable countries to climate change, despite their limited contribution to it. Mitigation, adaptation and loss and damage strategies require consistent and regular resources, which should be funded through non-debt creating public climate finance. However, financing needs for climate resilience – and particularly reconstruction costs after a climate-extreme event – lead to additional borrowing, which usually comes at higher costs for climate-vulnerable countries.

While all SIDS together only received US$1.5 billion in climate finance between 2016 and 2020, in the same period 22 SIDS paid more than US$26.6 billion to their external creditors – almost 18 times as much. There is no firm commitment about the climate finance flows to be received by SIDS in the upcoming years, but we can be sure that the flow of money towards official and, particularly, private creditors will continue.

Unsurprisingly, public debt goes up in the aftermath of climate-extreme events. This report looks at how, **during the two or three years after a climate-extreme event, there is an increase in debt-to-GDP in many cases.** Debt vulnerabilities in SIDS also make them more vulnerable to climate change. Countries with unsustainable debt tend to have fewer resources available to invest in climate resilience or to face the impacts of climate events.

Table 2: Total damages in recent climate-extreme events in SIDS and debt-to-GDP changes

			Total Damages		General Government Debt-to-GDP			
Country	Name & year	Year	Billion US$	% GDP	Year of event	Plus 1 year	Plus 2 years	Plus 3 years
Dominica	Hurricane Maria	2017	1.60	259%	81.90	84.63	94.23	107.33
Grenada	Hurricane Ivan	2004	1.27	148%	94.69	87.31	92.92	89.06
Saint Kitts & Nevis	Hurricane Georges	1998	0.66	110%	77.42	89.18	96.48	105.18
Dominica	Hurricane Erika	2015	0.55	90%	68.87	75.30	81.90	84.63
Bahamas	Cyclone Dorian	2019	3.60	27%	59.62	75.07	102.81*	91.25*
Tonga	Cyclone Harold	2020	0.12	24%	43.25	44.68*	42.91*	50.22*
Saint Lucia	Hurricane Elsa	2021	0.03	2%	95.00	92.40*	91.22*	90.56*
Fiji	Cyclones Josie & Keni	2018	0.06	1%	45.77	48.68	62.04	79.18*

*IMF projections

Source: EmData and IMF WEO.

A financial system not fit for purpose

The existing international financial system offers very few options for resolving the risks of a debt fallout in SIDS. Even with debt distress imploding in many countries in the Global South, the international community has not been able to make any advances – either in the systemic reform needed, or in short-term solutions that work. The limitations of the Debt Service Suspension Initiative (DSSI) and the Common Framework (CF), approved by the G20 to address debt problems in 2020, are today more evident than ever, particularly for SIDS.

Sixteen SIDS are not eligible for the G20 debt relief initiatives, some of them at high risk of debt distress or already in debt crisis. For those that were eligible for the DSSI and applied for a debt payment moratorium, **the temporary savings were less than US$975 million – around 35 per cent of the total payments made by those countries between 2020 and 2021.** These temporary savings are to be paid from 2023 onwards, added to existing and new debt commitments.

The uncertainties and lack of clarity regarding the implementation of the CF remain high. The timeline for the framework is unclear; private creditor participation remains voluntary and countries are supposed to keep paying their debts during the lengthy negotiations. Unfortunately, the G20 Common Framework does not offer any guarantees for a timely and orderly debt restructuring for SIDS.

Calls to action for a fair resolution of the debt and climate crises

A fair response to the multiple crises in SIDS should start with a recognition of climate, ecological, social and historical debts that western countries owe to countries and communities in the Global South. This is a debt that started with slavery and colonialism, and that continued with neo-colonial resource pillage and unfair trade, financial and political relations that have lasted for centuries.

Such unequal north-south relations are at the root of the accumulation of climate debt by countries in the Global North due to their disproportionate contribution to carbon and other greenhouse emissions. In this historical context, climate finance commitments and debt cancellation should be part of a wider set of structural and financial reparations that should also include ecological restoration, phasing out fossil fuel subsidies, ending extractivism and shifting to decarbonised modes of production, distribution and consumption.

Beyond the profound change that we need to see in the world and economic system in order to redress the climate emergency and the unsustainable debt accumulation, there are other possible responses that go beyond what the existing international financial architecture has to offer. We call for policies and reforms that governments and international institutions could pursue and that would support SIDS in tackling the existing multiple challenges facing them, including:

Actions for immediate implementation

1. Immediate and unconditional debt cancellation of all unsustainable and illegitimate debts, to all countries in need, by all creditors.
2. Immediate access to non-debt creating or concessional climate finance that is new and additional to existing international commitments, including on ODA.
3. Introduction of multidimensional vulnerability indicators to define access to concessional finance and debt relief.

International financial architecture reforms

1. Create a permanent multilateral sovereign debt resolution framework that, under the auspices of the United Nations, 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.
2. Establish an automatic mechanism for a debt payment moratorium and comprehensive restructuring in the wake of catastrophic shocks.
3. Agree on common and binding principles on responsible borrowing and lending, and ensure compliance with them.
4. Review debt sustainability frameworks to incorporate climate vulnerabilities, risks and impacts, and human rights and development impact assessments.
5. Establish a global public debt transparency registry, with mandatory rules that require all lenders and borrowers to disclose information on loans and other debt-creating instruments

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