FACTSHEET

Debt's climate link

The world faces an unprecedented debt crisis, which is exacerbating the climate emergency in developing countries. As an unfit global financial architecture makes accessing finance more difficult for countries in the developing world, governments are left with the option of either servicing the debt or serving the people.

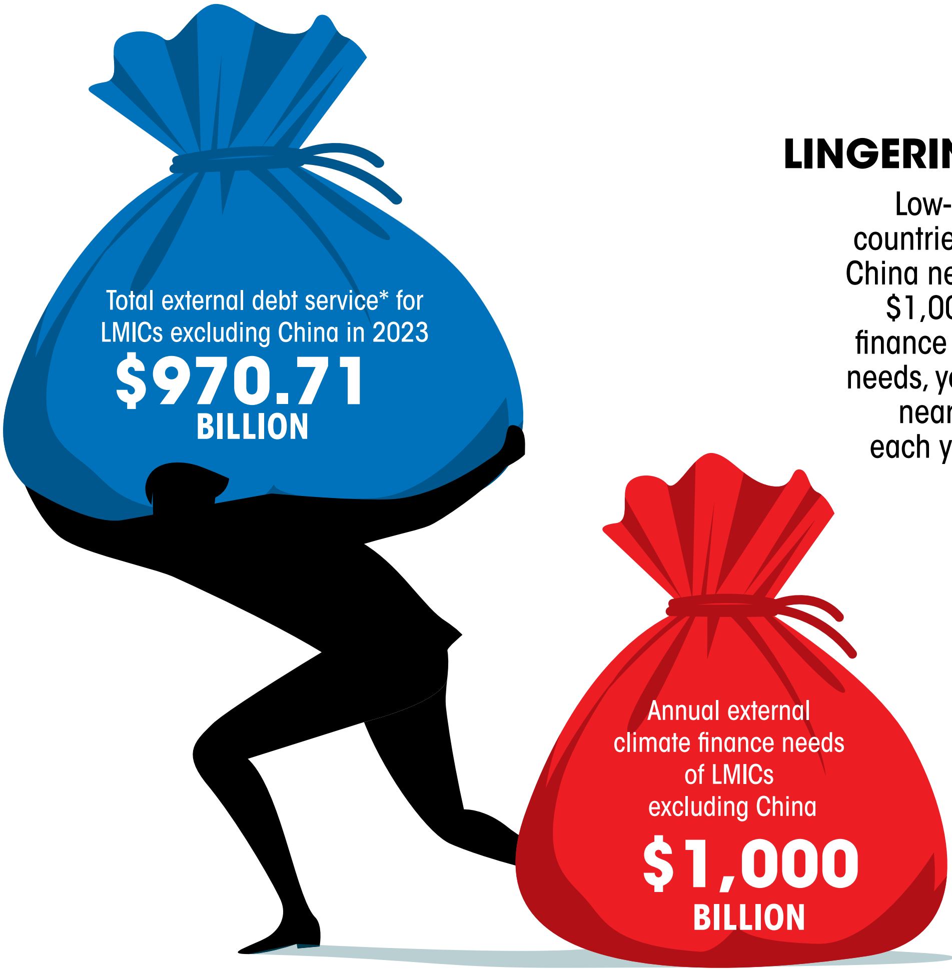
Analysis by **SEHR RAHEJA** and **UPAMANYU DAS**

$105,000. That is the cost of citizenship of Nauru, an island nation spanning just 21 sq km in the southwest Pacific Ocean. The low-lying island is issuing "golden passports" with the aim of raising money to fund climate action. Nauru is the world's third smallest country and its contribution to global greenhouse gases is estimated to be 0.01 per cent. Yet it faces an existential threat from rising sea levels, storm surges and coastal erosion as the planet warms. The government says it lacks the resources to protect itself from the climate crisis and that selling citizenship will help raise the funds needed for a plan to move 90 per cent of the island's 12,500-strong population onto higher ground and build an entirely new community.

Nauru's "golden passport" initiative highlights the dual threats faced by many developing countries, home to 80 per cent of the global population. Amid the escalating climate crisis, these countries are grappling with severe economic and financial hardships. This is making them dependent on borrowings from foreign countries and multilateral institutions, creating a vicious circle that hinders their ability to invest in climate resilience, adaptation and the low-carbon transition. Often, this cycle is forcing these countries to borrow further for disaster recovery, mounting their debt burden.

This has dire consequences. The UN Conference on Trade and Development (UNCTAD), in a 2024 report, warns that the global public debt stock—money borrowed by governments worldwide, from within their country or from abroad—reached record levels of US $97 trillion in 2023. This means that while the average income of an individual in the world has grown by 22 per cent to $13,065 between 2013 and 2023, the individual's share in global debt has increased by an astounding 61 per cent during the same period, reaching $12,034. This unequal growth between public debt per capita and gross national income per capita is troubling, because it means that a significant portion of income is likely to be spent on debt repayment, leaving little room for financing developmental and climate priorities in line with countries' Nationally Determined Contributions (NDCs) to reduce greenhouse gas emissions and adapt to climate change impacts. While the climate finance needs of a citizen of the developing world (low- and middle-income countries excluding China) stand at about $488 annually till 2030, developing countries are also often the most vulnerable to climate change impacts and will require the lion's share of increased investment for climate action.

This reality has grave implications when examined against the current political headwinds, particularly with respect to aid cuts and reduced international cooperation from the developed world. The US' withdrawal from the Paris Agreement has weakened global climate action. The outcome of the New Collective Quantified Goal (NCQG) on climate finance at the



LINGERING PROBLEM

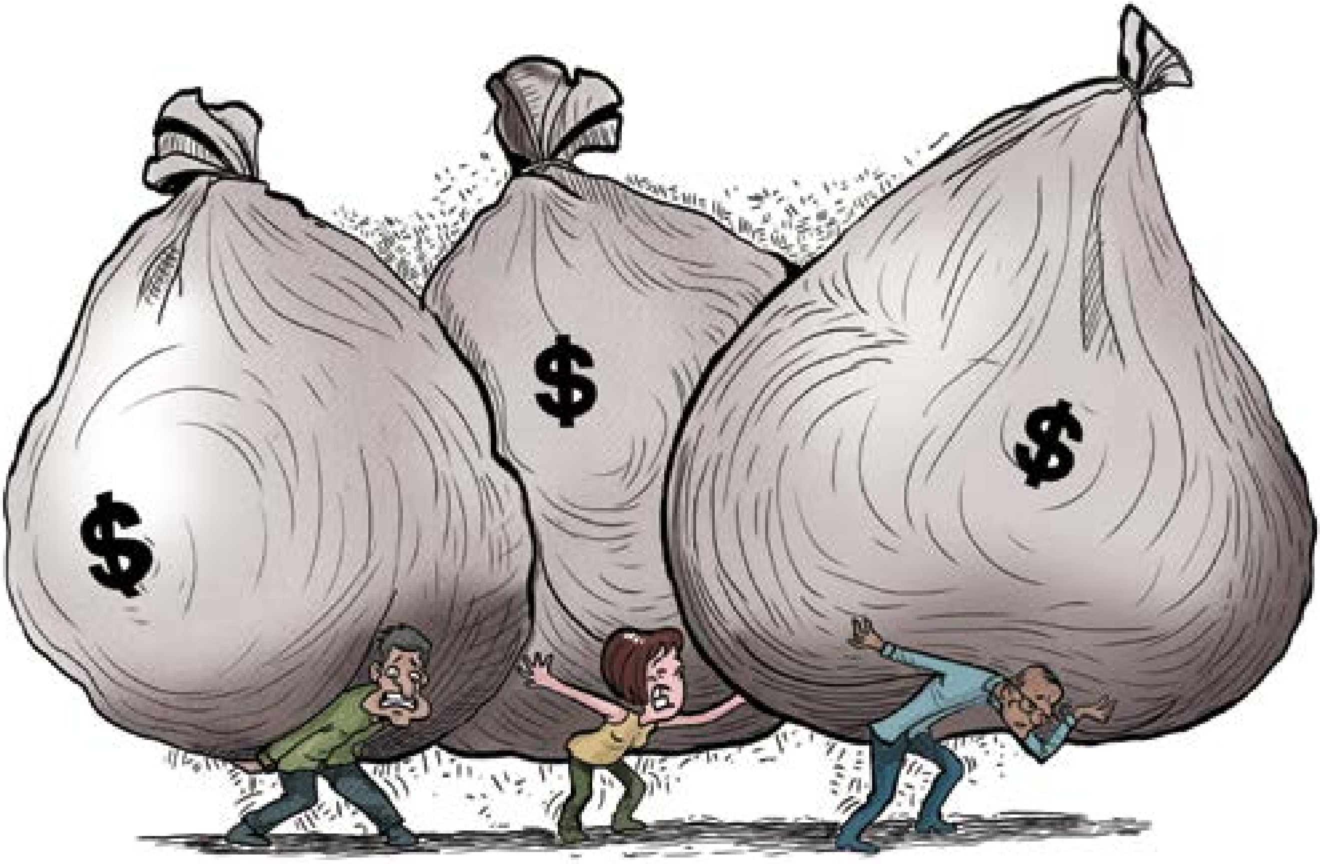
Low- and middle-income countries (LMICs) excluding China need an estimated US $1,000 billion in external finance annually for climate needs, yet they are spending nearly the same amount each year on external debt

*Total external debt service covers public and private borrowings. It is the sum of principal repayments and interest paid in currency, goods or services on long-term debt, interest paid on short-term debt, and IMF repayments (repurchases and charges). Source: World Bank International Debt Statistics, Grantham Research Institute on Climate Change

29th Conference of the Parties to the UN Framework Convention on Climate Change (COP29) in Baku, Azerbaijan, in 2024 has been a failure, especially for developing countries seeking climate justice through the provision of public finance from developed nations. Meanwhile, international financial institutions are quietly stepping away from net-zero alliances and scaling back climate pledges. Major donors, including the US, UK, Belgium, France, Netherlands and Sweden, are slashing their foreign aid budgets, implying a possible 22 per cent decrease in foreign aid (relative to 2023 levels) in the coming year, as per “A generational shift: The future of foreign aid”, released by global management consultancy McKinsey and Company in May 2025. To add to this, public climate finance from developed nations continues to fall short. For much of the Global South, the financial landscape for development and climate looks bleak. One crucial piece of this stalled progress is the growing external debt crisis.

The Fourth International Conference on Financing for Development (FfD4), held between June 30 and July 3, 2025 in Seville, Spain, brought renewed attention to the critical issue of sovereign debt in the context of global development. A key focus was on scaling international financing for the Sustainable Development Goals (SDGs), including climate action (SDG-13), and advancing reforms to the global financial architecture to make it more equitable and responsive to the needs of developing countries.

This fact sheet unpacks the dynamics between sovereign debt and climate change and points to potential solutions for escaping the climate-debt loop.



HOW LARGE IS SOVEREIGN DEBT?

Its burden on developing countries is growing twice as fast as on developed countries

SOVEREIGN DEBT or public debt, as the International Monetary Fund (IMF) describes it, refers to borrowings by governments to confront hardships and invest in public goods and services that support development, such as education, healthcare and energy systems, complementing revenues raised through general taxation. Governments may borrow from within their country or from abroad, with creditors ranging from local private institutions and households to other countries, development banks or multilateral institutions, and private investors. Governments can also "guarantee" debt for private entities, taking on the obligation to repay parts of the loan if the debtor is unable to. Such publicly guaranteed debt is used strategically by governments to lower costs for investments that support their policy objectives.

"Public debt can be a powerful tool for development, enabling governments to finance critical expenditures and invest in a better future for their people," says the 2024 report by UNCTAD, titled "A world of debt: A growing burden to global prosperity". However, when public debt grows excessively or rapidly, it becomes a heavy burden, particularly for developing countries. The report says that there has been an alarming surge in global public debt, and that it has been driven by "cascading crises in recent years as well as the sluggish and uneven performance of the global economy". In 2023, global public debt reached a record level of US $97 trillion—up by a notable $5.6 trillion from the previous year. However, this growth is marked by significant disparities among different economic blocs. Though developed economies account for two-thirds of the global public debt, developing countries, most of which fall under the low- and middle-income countries categorization (LMICS) used by the World Bank, are contending with a staggering $29 trillion in public debt (see 'Unequal spread'). What is more worrying is that since 2010, public debt in developing countries has grown twice as fast in developed economies—with its share in the global total increasing to 30 per cent in 2023, from just 16 per cent in 2010.

OUTSIZED EXTERNAL DEBT

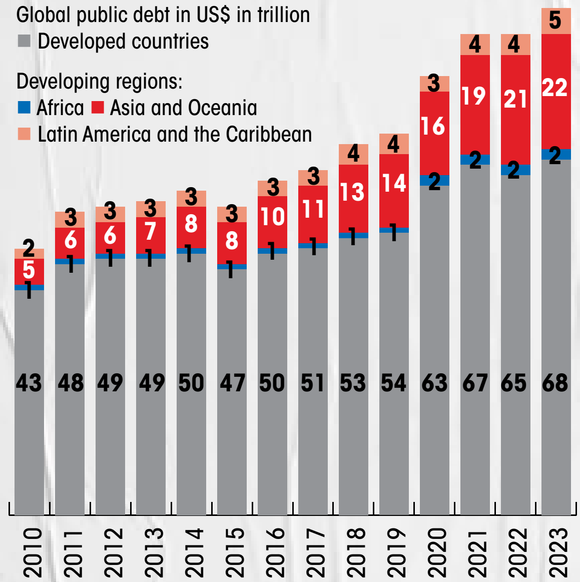
A significant portion of this public debt stock of developing countries is external—borrowed from foreign creditors. It acts as a silent storm, eating into the country's foreign-exchange reserves and increasing its vulnerability to economic shocks, such as currency fluctuations when the domestic currency weakens against the currency of debt. If the country's ability to repay the debt to foreign creditors in foreign currencies is compromised, external debt can even lead to economic crises. Countries like Sri Lanka and Kenya have already experienced such a fallout, with unsustainable external debt levels fuelling economic crises and civil unrest.

According to the analysis "What broke the pearl of the Indian Ocean?", published in the *Journal of Financial Stability* in February 2024, the key crisis in Sri Lanka was large budget deficits financed through foreign borrowings, causing external debt to rise to almost 50 per cent of the central government debt by 2018—the highest in 20 years. In 2020, when the COVID-19 pandemic gripped the world, the country experienced a sudden stop in capital flows. Unable to borrow money from abroad to service foreign debt, the country used its foreign-exchange (FX) reserves to finance the current account deficit. With the continued loss of FX reserves, Sri Lanka eventually defaulted on its external debt in April 2022. The entire economy, and country, came to a screeching halt with ensuing socioeconomic and political turmoil.

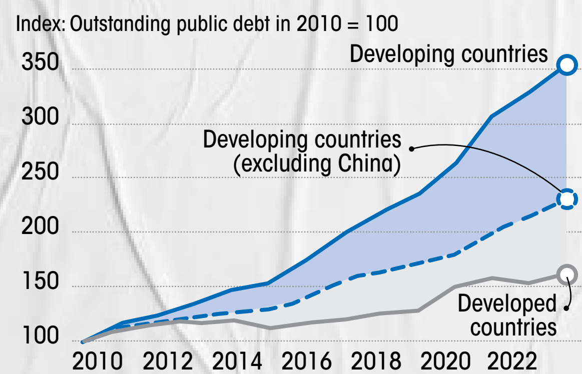
World Bank data shows similar unsettling patterns for many other developing countries. Between 2013 and 2023, developing countries' saw their total

UNEQUAL SPREAD

In 2023, the global public debt had reached a record $97 trillion. Less than a third of this debt burden, or $29 trillion, is with developing countries



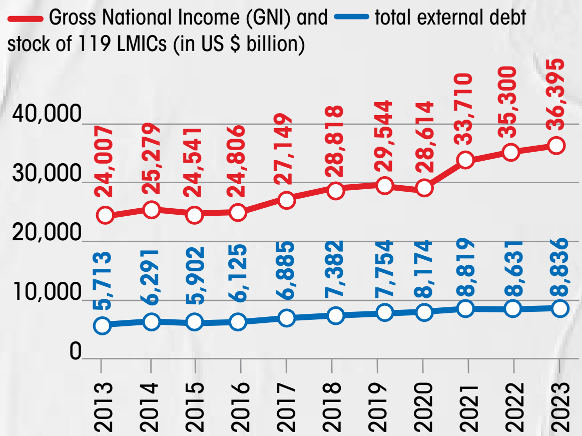
The concern for developing countries is that their public debt burden has grown twice as fast since 2010, compared to developed countries



Source: "A World of Debt", UN Trade and Development

GROWING ON EXTERNAL DEBT

In the past decade, Gross National Income* of LMICs rose by 52%, but their total external debt, repayable in stronger foreign currencies, increased by 55%

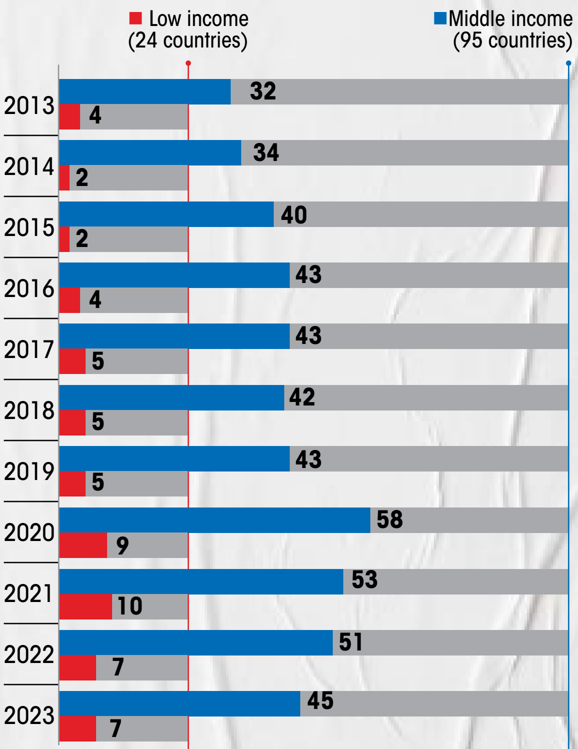


*Gross National Income is the total income earned by a country's residents. It includes net income from abroad and the Gross Domestic Product
Source: World Bank International Debt Statistics

UNSUSTAINABLE BURDEN

In 2023, at least 52 LMICs had total external debt exceeding 50% of their GNI—up from 36 in 2013

Number of countries with total external debt stock exceeding 50% of GNI



Source: World Bank International Debt Statistics

external debt stock (which includes public and private borrowings) rise by 55 per cent—from \$5.71 trillion to \$8.84 trillion. Further analysis shows that the total external debt stock is increasing at a rate higher than the gross national income (GNI), which grew at 52 per cent over the 10-year period (see 'Growing on external debt'). A majority of the external debt has been borrowed by public sector bodies in developing economies.

An assessment of total external debt stock-to-GNI ratio, which indicates the share of debt in a country's income and the government's capacity to repay the debt, shows that in 2023, the ratio stood at 36.44 per cent for low-income countries and 24.06 per cent for middle-income countries. The number of low- and middle-income countries (LMICS) whose total external debt stock exceeded 50 per cent of their GNI almost doubled, growing from 36 to 52 between 2013 and 2023 (see 'Unsustainable burden').

For instance, Mozambique's total external debt in 2023 was 350 per cent of its GNI—the highest among all LMICS. Similarly, Mongolia's total external debt was 189 per cent of its GNI and Mauritius' was 128 per cent of its GNI. Such high levels of external debt increase repayment pressure and can push countries towards economic crises.

A regional analysis of the public component within external debt—or external public debt—shows that the Asia and Pacific region has consistently borne the highest external public debt stocks over the past decade within the Global South. Between 2013 and 2023, the region's external public debt stocks almost doubled—from \$829 billion to \$1.63 trillion. Even if one excludes China from the analysis—which has the highest public debt in the world after the US—the debt stock increases by 1.7 times, from \$676.7 billion to \$1.16 trillion. The external public debt stock of Latin America and the Caribbean rose by 1.6 times from \$574 billion to \$940 billion. In Africa, external public debt stocks doubled, reaching \$689 billion in 2023. More countries now face high debt burdens, especially in Africa.

THE REAL COST OF BORROWING IN THE GLOBAL SOUTH

Biased sovereign credit ratings and steep interest push developing countries into deeper debt

THE SOVEREIGN debt burden of developing countries is rising sharply—not because they borrow more recklessly, but because they borrow more expensively. Much of this is due to high interest rates and structurally biased sovereign credit ratings that inflate borrowing costs. Countries in Africa, Asia, and Latin America are disproportionately penalized by financial markets, often paying 2–12 times higher interest than developed nations. As a result, debt servicing is crowding out essential public spending and delaying recovery from global crises, especially in low- and middle-income countries.

HIGH COST OF BORROWING

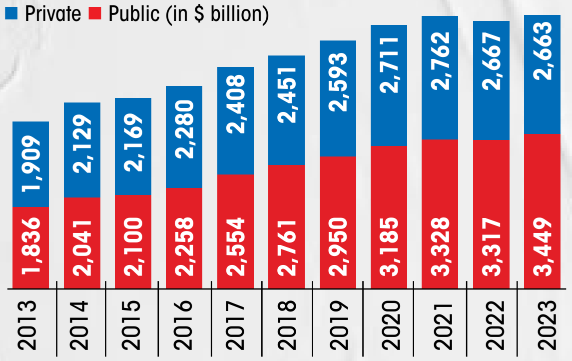
Developing countries spent a record $1.4 trillion to service their total external debt as their interest costs climbed to a 20-year high in 2023, says the World Bank's "International Debt Report", released in December 2024. "Currently, more than half of developing countries allocate at least 8 per cent of government revenues to interest payments, a figure that has doubled over the past decade. The rising pressure of interest payments is substantial across regions, particularly in Africa and Latin America and the Caribbean," says United Nations Conference on Trade and Development's (UNCTAD's) "A world of debt" report. According to the report, in 2023, of the total number of countries analysed in the report, a record 54 developing countries or 38 per cent of the total, allocated 10 per cent or more of government revenues to interest payment, with nearly half of them in Africa. Developing countries' interest payments are not only growing fast, but they are outpacing growth in critical public expenditures.

The annual external public debt service in LMICs has doubled over the past decade, reaching $368 billion in 2023 from $182 billion in 2013 ('Uncomfortably high'). This becomes clearer still when one looks at the share of each dollar of GNI earned by a country that goes towards external public debt servicing. For one dollar of GNI

EXTERNAL PUBLIC DEBT SURGE

In LMICs, external debt held by private entities rose by 39% over the past decade, while external public debt surged by 88%

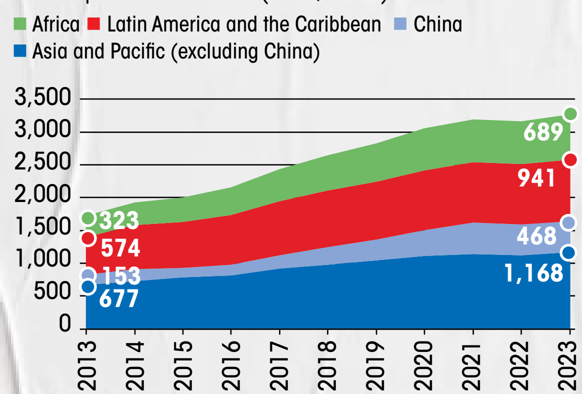
Composition of long-term external debt stock for LMICs



CLEAR REGIONAL DIVIDE

LMICs across Asia and Pacific hold the largest share of external public debt, but Africa's debt burden has doubled over the past decade

External public debt in LMICs (in US$ billion)

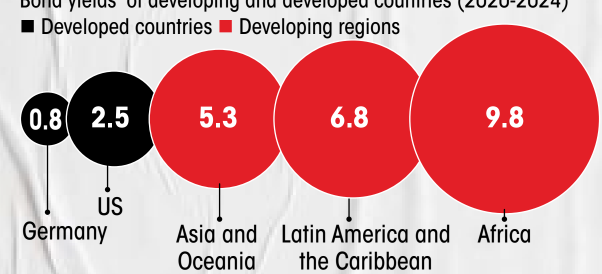


Source: World Bank International Debt Statistics

FAVOURING THE RICH

Borrowing costs of developing countries are higher than those of developed ones (in %)

Bond yields* of developing and developed countries (2020-2024)



*Illustrative comparison of the average JPM EMBI Global Diversified USD bond yields per region with the 10-year bond yields of Germany and the US from January 2020 to May 2024.

Source: "A World of Debt", UN Trade and Development

earned, the average developing economy spent 1.6 cents on external public debt servicing in 2013, which rose to 2.5 cents in 2023. For MICS, the figure increased from 1.8 cents in 2013 to 2.8 cents in 2023.

RISING, UNFAIR INTEREST RATES

A key reason for such high debt servicing cost is the high interest being charged by creditors. The UNCTAD report shows that developing regions borrow at rates that are 2-4 times higher than those of the US and 6-12 times higher than those of Germany. "The burden of this debt varies significantly, with countries' ability to repay it exacerbated by inequality embedded in the international financial architecture," states the report. This is in part because developing countries have higher perceived risks, and thereby face higher cost of borrowing. Sovereign credit ratings are meant to be independent measures of a country's ability to pay its debts. Such ratings are important because they determine the interest rates a country faces in the global financial market and, therefore, its borrowing costs. Unfortunately, a growing body of literature suggests that sovereign credit ratings are negatively biased towards the Global South. The 2023 report by the United Nations Development Programme (UNDP), "Reducing the Cost of Finance for Africa", estimates that unequal country ratings have cost African states more than $24 billion in excess interest and over $46 billion in forgone lending.

For instance, Cameroon and Ethiopia's credit ratings were slashed after they requested relief from the Debt Service Suspension Initiative (DSSI)—a G20 initiative launched in May 2020 to help eligible low- and lower-middle-income countries recover from the economic impact of the COVID-19 pandemic. Instead, the rating downgrade increased the costs of Cameroon and Ethiopia's debt, prolonging recovery by straining their budgets, explained Ramya Vijaya, professor of economics and global studies at Stockton University, US, in an interview with Danish Development Research Network in March 2025, on sovereign credit ratings and wider implications of unequal access to finance for developing countries. It is crucial to investigate the long-term effects of country ratings because they determine how much money governments—particularly Global South countries with lower tax revenues—can afford to spend on healthcare, education and other important areas for development, said Vijaya.

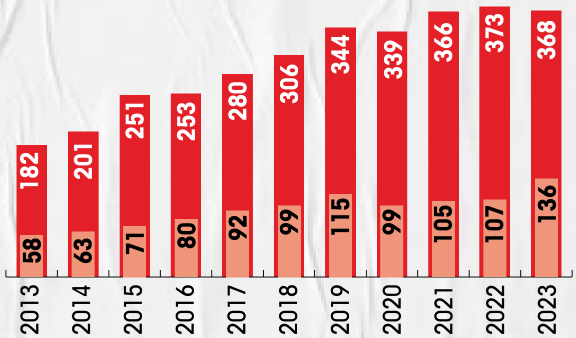
A report by the International Monetary Fund (IMF) shows Global North countries averaged 12 per cent of GDP on pandemic-related spending. The numbers for emerging market and low-income economies were 6 per cent and 3 per cent of GDP respectively. Yet, emerging and developing states accounted for 95 per cent of sovereign rating downgrades in 2020. This highlights how developed economies get additional leeway from rating agencies to ramp up spending or cut taxes during downturns to stimulate growth. Consequently, these countries can recover more quickly from crises. Global South nations, meanwhile, cannot increase government expenditure due to the threat of rating downgrades. Such systems embedded in the international financial architecture exacerbate the debt problem.

It can be seen that Africa has had the highest rise in interest payments on external public debt, increasing by 3.2 times from $7.8 billion in 2013 to $25.1 billion in 2023. The Asia and Pacific region has seen a similar rise, with external public debt interest payments more than tripling in value from $20.9 billion in 2013 to $64.1 billion in 2023—accounting for the highest share of interest paid in 2023 at 48.7 per cent. Latin America and the Caribbean saw a slower rise in interest payments of 1.6 times over this period.

UNCOMFORTABLY HIGH

In 2023, LMICs spent 134% more on interest payments on external public debt than in 2013, accounting for 37% of external public debt service costs

Interest payments and external public debt service costs (interest and principal payments) for LMICs (in $ billion)

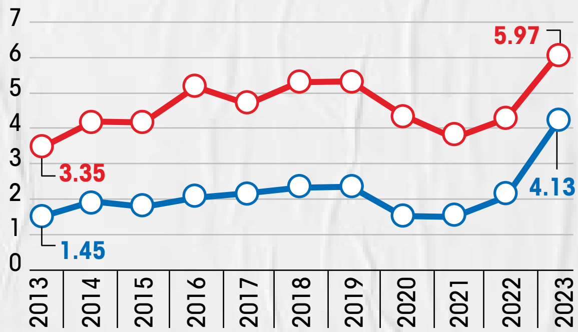


UPWARD MARCH

After a dip during the COVID-19 pandemic, interest rates on external debt for LMICs have risen sharply, surpassing pre-pandemic levels

Average interest rate on new external debt commitments* for LMICs

Official Creditors Private Creditors (in %)



*The average interest rate on all new government and government-guaranteed loans contracted during the year

Source: World Bank International Debt Statistics

WHO GAINS FROM BALLOONING DEBT?

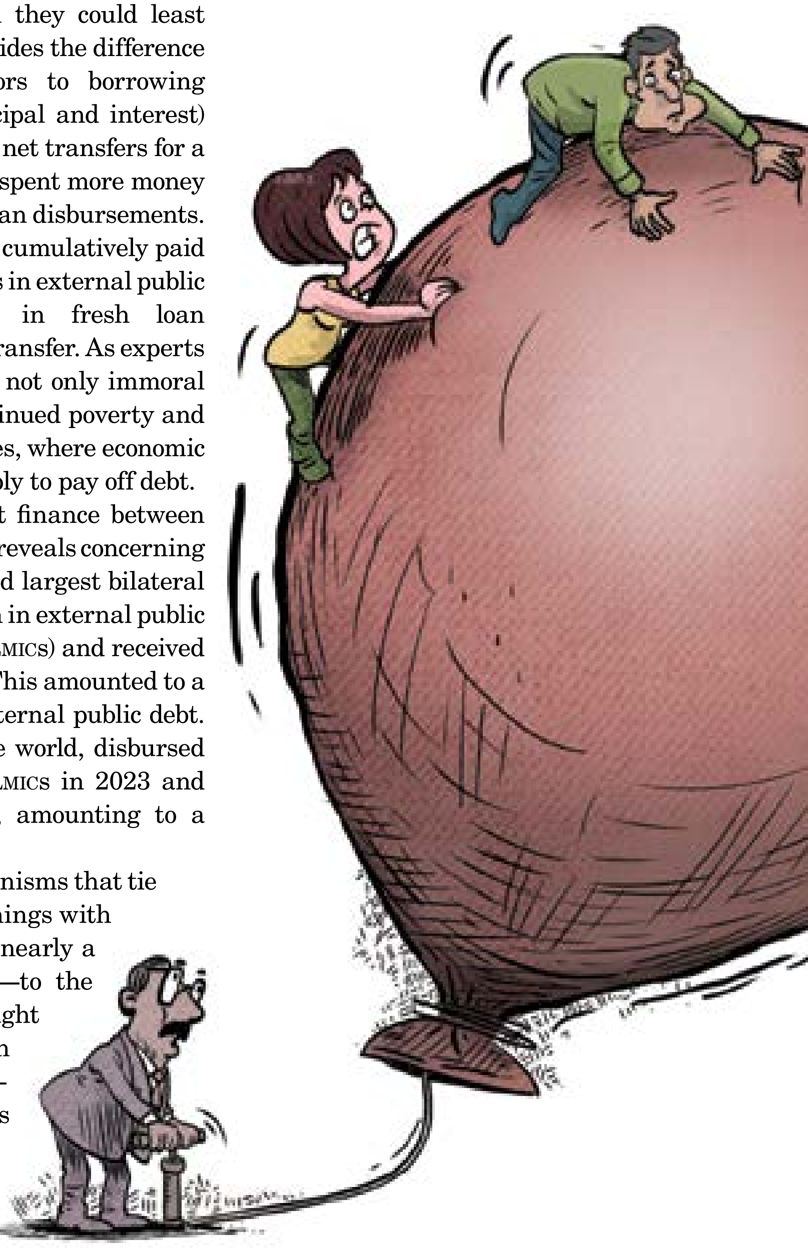
Rising interest and falling exchange rates are driving capital back to developed nations—and closing the doors to credit for developing countries

THE MOUNTING debt burden of the developing world has reached a stage where it has completely reversed the North-South resource flows. According to the World Bank International Debt Statistics, developing countries experienced a net resource outflow when they could least afford it. Net transfer on external debt provides the difference between total disbursements by creditors to borrowing countries and the total repayments (principal and interest) made by the borrowing countries. Negative net transfers for a particular year implies that the borrowers spent more money on debt repayments than they received in loan disbursements.

In 2022 and 2023, developing countries cumulatively paid $38.5 billion more to their external creditors in external public debt repayments than they received in fresh loan disbursements, resulting in a negative net transfer. As experts point out, this reverse flow of resources is not only immoral but it is a major contributing factor to continued poverty and environmental degradation in poor countries, where economic resources have to be exploited quickly, simply to pay off debt.

Further assessment of the flow of debt finance between creditors and developing country borrowers reveals concerning trends. In 2023, the Netherlands—the third largest bilateral creditor in the world—disbursed $9.9 billion in external public debt to low- and middle-income countries (LMICS) and received $17.02 billion from them in debt servicing. This amounted to a negative net transfer of $7.12 billion on external public debt. China, the largest bilateral creditor in the world, disbursed $12.07 billion in external public debt to LMICS in 2023 and received $24.14 billion in debt servicing, amounting to a negative net transfer of $12 billion.

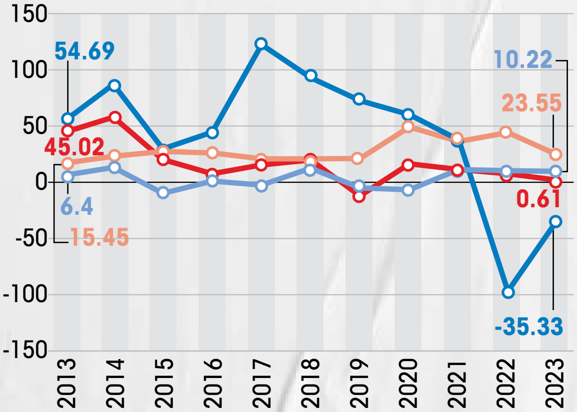
Often, creditors also employ debt mechanisms that tie in a country's natural resource export earnings with debt repayment. For instance, Chad owes nearly a third of its external debt—$1.45 billion—to the Swiss oil giant Glencore. In 2020, Chad sought debt restructuring under the G20 Common Framework. In November 2022, a debt re-profiling deal was reached, which continues



WHAT REALLY COMES IN

Since 2022, LMICs have paid $38.5 billion more in external public debt servicing than they received in new loan disbursements

Net transfers (disbursements minus debt servicing) on external public debt by external creditors ● Bondholders ● Commercial banks and other private creditors ● Bilateral ● Multilateral (figures in $ billion)



Source: World Bank International Debt Statistics

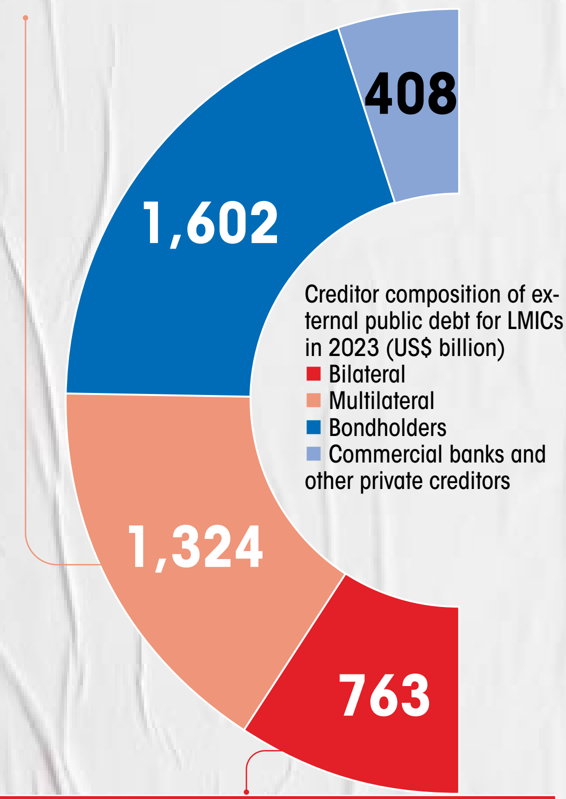
using oil revenues to service the loan, but extends payment schedules beyond 2024, providing the country temporary relief. Similarly, Zambia, which relies on copper for export earnings, defaulted on its external debt repayment in 2020—as COVID-19 hurt exports. It then faced pressure from private and bilateral lenders to prioritise copper export revenues for debt servicing. Further, a Zambian state mining firm inherited a $1.5 billion debt to Glencore in 2021 when it took full control of Mopani Copper Mines, in a deal that required repayments through a share of copper revenue. The arrangements ensured that much of Zambia's copper earnings flowed outward. Such examples show a pattern of resource extraction from developing countries on the pretext of debt repayment.

WHO ARE THE MAJOR LENDERS TO LMICS

Multilateral and bilateral lenders hold nearly half of LMICs' external public debt; the rest comes from costlier bondholders and commercial banks

Multilateral creditors

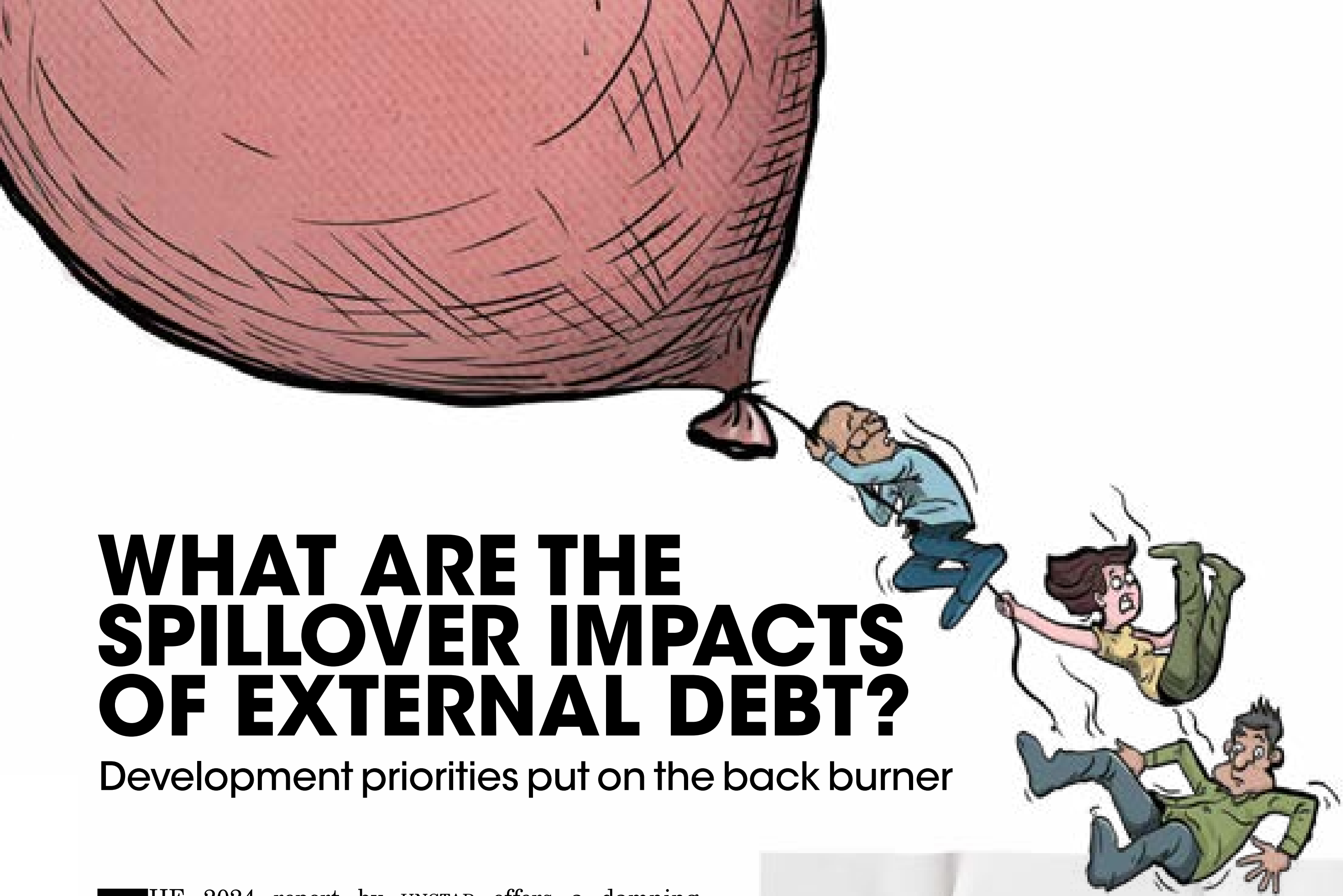
- **438** World Bank
- **383** IMF
- **146** Asian Development Bank
- **98** Inter-American Development Bank
- **45** African Development Bank
- **35** European Investment Bank
- **23** Corporacion Andina de Fomento
- **18** Islamic Development Bank
- **18** Asian Infrastructure Investment Bank
- **10** Central American Bank for Economic Integration
- **10** African Export-Import Bank
- **9** New Development Bank
- **93** Other Multilaterals



Bilateral creditors

- **190.77** China
- **120.73** Japan
- **71.16** Netherlands
- **52.68** France
- **40.47** Germany
- **34.79** European Union
- **30.36** United States
- **29.58** Russia
- **27.87** United Kingdom
- **21.67** Saudi Arabia
- **19.89** UAE
- **13.93** India
- **109.27** Other Bilaterals

Source: World Bank International Debt Statistics



WHAT ARE THE SPILLOVER IMPACTS OF EXTERNAL DEBT?

Development priorities put on the back burner

THE 2024 report by UNCTAD offers a damning indictment of how rising sovereign debt costs are hindering developmental priorities of low- and middle-income countries (LMICS). It says that today, 3.3 billion people live in countries that spend more on interest payments than on health, and 2.1 billion live in countries that spend more on interest payments than on education.

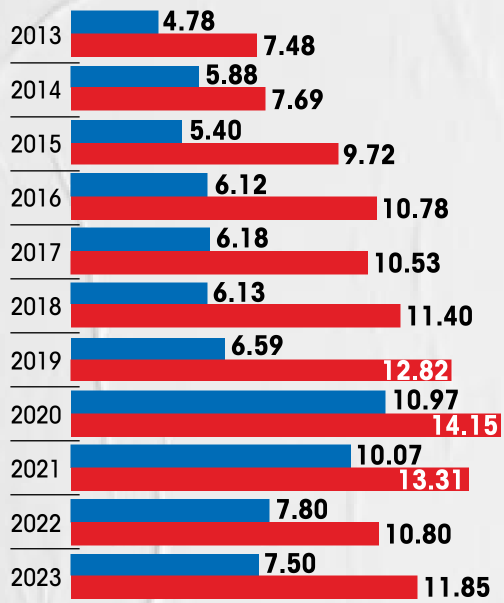
Since 2015, gross capital formation (or fixed assets of the economy such as schools, hospitals and plants) in low-income countries has stalled at just 22 per cent of GDP—well below the 33 per cent average for middle-income countries, highlights “The Jubilee Report”, a Vatican-backed report by 30 prominent economists commissioned by Pope Francis. To emerge from their poverty and to catch up with middle-income countries, they should be investing a larger, not a smaller, percentage of GDP towards developmental priorities. The report adds: “Interest payments on public debt are crowding out critical investments in health, education, infrastructure, and climate resilience. Governments—fearful of the political and economic costs of initiating debt restructuring—prioritise timely debt payments over essential development spending. This is not a path to sustainable development. Rather, it is a roadblock to development and leads to increasing inequality and discontent.”

The implications of rising debt repayments and the

COST OF EXTERNAL DEBT

In the past decade, external public debt service has taken up a growing share of government revenue in LMICs

Average external public debt service as a share of government revenue by income group ■ LICs ■ MICs (in %)



Source: World Bank International Debt Statistics, IMF World Economic Outlook resulting burdens on a country's financial health are worrisome. Comparing external public debt service costs as a share of GDP with governments' health and education expenditures as shares of GDP reveals startling results. The past decade has witnessed an increase of over 47 per cent in the number of countries where external public debt service is crowding out education and health spending. In 2013, nine countries saw their external public debt service as a share of GDP exceed their education expenditure as a share of GDP, while 35 countries saw their external public debt service as a share of GDP exceed their health expenditure as a share of GDP. By 2023, these numbers had risen to 17 and 45 respectively.

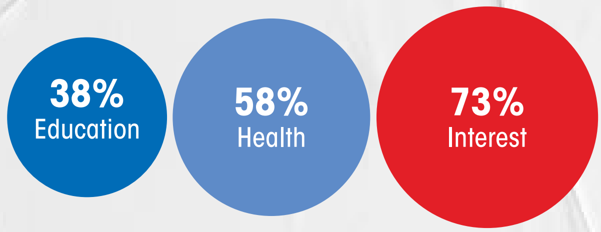
Moreover, in 2023, 11 countries saw their external public debt service as a share of GDP exceed government education expenditure as a share of GDP by over 1 percentage point. For Indonesia, the difference was 2.1 per cent, for Maldives it was 5.1 per cent, for Angola it was 5.9 per cent while for Mongolia, it was 8.2 per cent. Similarly, 21 countries saw their external public debt service as a share of GDP exceed government health expenditure as a share of GDP by over 1 percentage point. In 13 of these countries, the difference was over 2 percentage points. The difference was 1.6 per cent for Indonesia, 3 per cent for Cameroon, 4.7 per cent for Congo, 4.9 per cent for Jordan, and 6.4 per cent for Angola. This highlights the growing precarity of developmental spending in the Global South—driven, at least in part, by the unfolding sovereign debt crisis.

A 2023 report by international non-profit ActionAid states such high debt service costs are locking countries into a negative spiral, forcing governments to not only cut public spending on vital public services but also investing in things that are not good for the climate to pay back their debts. Countries like Ghana are even cutting funds to vital public services like health and education to keep up with debt repayments.

TRAPPED IN DEBT CYCLE

Interest payments for external public debt for developing countries are growing faster than other public expenditures

Nominal change (%) in public expenditure categories in developing countries between 2010-2012 and 2020-2022

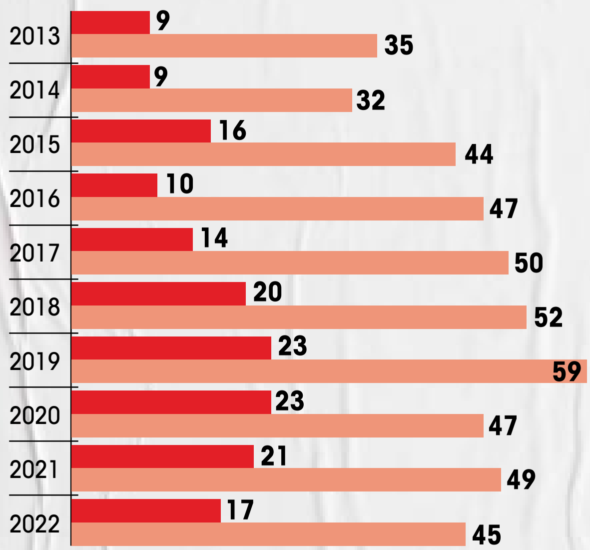


Source: "A World of Debt", UN Trade and Development

In 2022, external public debt service exceeded health expenditure in 45 LMICs and education expenditure in 17

Number of LMICs where external public debt service exceeds health expenditure or education expenditure

■ Debt service exceeding education expenditure and ■ Debt service exceeding health expenditure (as shares of GDP)



Source: World Bank International Debt Statistics, World Bank World Development Indicators and World Health Organization

WHAT IS THE DEBT AND CLIMATE LINK?

Over half of the low- and middle-income nations with high climate vulnerability are either already in debt distress or at high risk of it

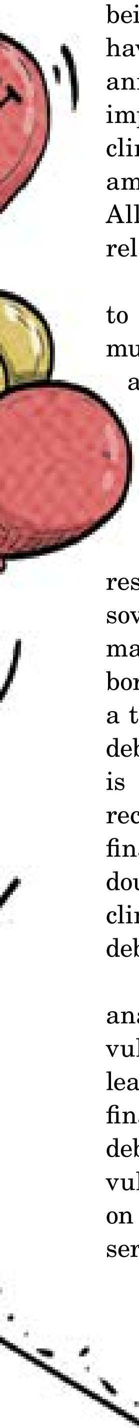
FOR A growing number of developing countries, debt and climate crises are coming together in a vicious circle. A study by United Nations Environment Programme (UNEP) and School of Oriental and African Studies, UK, found that climate change has already raised the average cost of debt by 117 basis points (1 basis point is equal to 0.01 per cent) for a sample of developing countries.

For several of the most vulnerable countries, the costs of addressing climate change, as reported by them, amount to costs of damages for isolated climate-induced/climate-worsened weather events. For instance, past hurricanes are a primary reason that Dominica and other Caribbean countries are heavily indebted. When Dominica was hit by Hurricane Erika in 2015, the damages amounted to up to 90 per cent of their total GDP. More recently, several small island countries, at greatest risk of sea level rise caused by climate change, have rallied together to call for debt relief in the face of mounting physical and economic impacts of climate change. Haiti, among the most vulnerable and severely indebted, faced damages of at least $432.38 million in 2023 alone from "climatological" natural disasters alone. These vulnerabilities reinforce each other, demanding that debt and climate finance be addressed together.

To understand the overlap of debt and climate vulnerability, it is important to examine the countries most at risk from climate impacts and most burdened by debt. Over half of the low- and middle-income countries (LMICS) with high climate vulnerability, or 36 countries, are either already in debt distress or at high risk of it (see 'Threat from all corners' *p*42). Their experiences offer a sharp lens into how debt burdens shrink fiscal space, deepen climate vulnerability, and how international climate finance still falls short of addressing this imbalance.

CLIMATE FINANCE MUST NOT BE LOANS

Developing countries need scaled-up finance to enable climate action. Those most vulnerable—to both climate and economic shocks—need non-debt climate finance. The countries in this analysis have together received $78 billion



over 11 years (2012-2022) as development finance with a climate component. This is a generous estimate, given the varying degrees of actual climate aspects at the project level, and the fact that the figures are only available for the commitments made by donor countries—actual disbursements might vary. It has been noted in the past that climate finance has a much lower disbursement ratio than overall development finance; sometimes, even as much as only half the amount being disbursed. On an annual basis, they have together received $7.17 billion per annum. The total costed needs for implementing these countries' national climate plans per year, on the other hand, amounts to $79 billion—the gap is massive. All the while, damages from climate related disasters continue to pile up.

When we add the lens of sovereign debt to this situation, the picture becomes murkier. These countries are either already at high risk of debt distress or in debt distress. The World Bank and the International Monetary Fund (IMF) explain debt distress as a situation where a country is "unable to fulfil its financial obligations and debt restructuring is required." In the event of a sovereign debt default, countries lose market access and face even higher borrowing costs. These 36 countries spent a total of $13.24 billion on external public debt service payments in 2022 alone. This is 1.8 times more than what they have received as climate-related development finance in a year—they have spent nearly double the amount of what has flowed in for climate action on servicing external PPG debt alone.

Of the 36 countries highlighted in this analysis, one-third have the highest vulnerability to climate change with the least preparedness. Examining the climate finance needs, flows and external public debt service, it is revealed that climate-vulnerable countries are under-supported on finance, yet overburdened with debt servicing, often spending more on debt than on education or health. While the situation varies given the unique circumstances of each country, it is reflective of the broader debt-development-climate nexus.

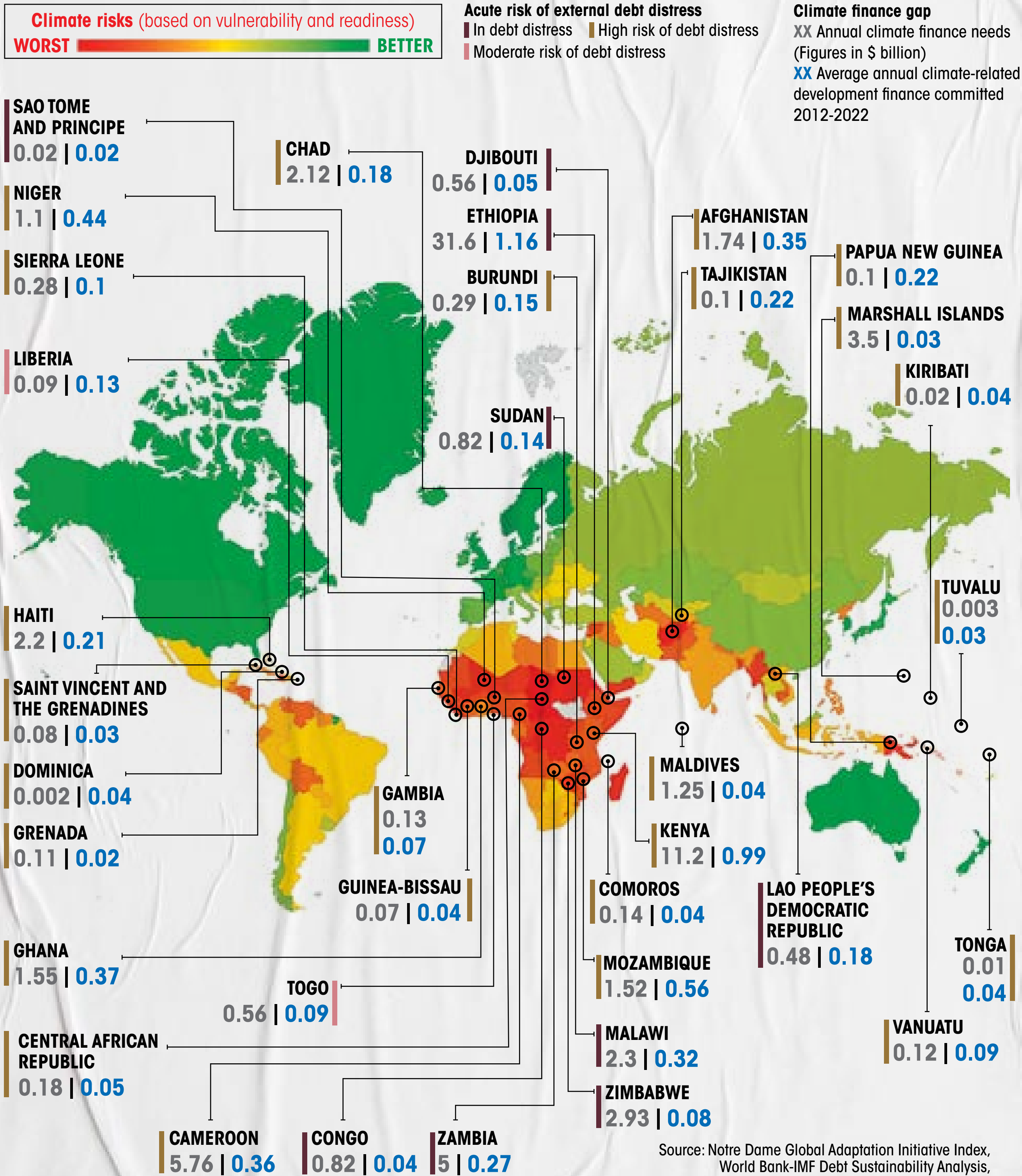
In many countries, external public debt service outweighs either climate finance received or basic social spending as a share of GDP. For instance, debt service is higher than climate-related development finance flowing in Chad, Guinea-Bissau, Haiti and Sierra Leone. In Chad, Guinea-Bissau and Haiti, debt service also exceeds social spending.

Of the 36 countries in this sample, reliable data on losses from climate related disasters was available for 25. For these 25 countries, nearly 70 per cent have paid more in external public debt service in 2022 than the average annual losses from climate disasters. In four of these countries, Zambia, Ghana, Cameroon and Tajikistan, the external public debt service exceeds the losses from climate by over 50 times. It comes as no surprise that two of these, Ghana and Zambia are also countries that have attempted to have their external debts restructured under the G20 Common Framework—to limited avail. While climate-related losses may be episodic and debt service is a recurring fiscal obligation, this contrast reveals the structural imbalance in how public finances are allocated. It underscores that even without a disaster occurring, a significant portion of a vulnerable country's fiscal space is already pre-committed to creditors—often far exceeding what they typically lose from disasters. This leaves little-to-no room to respond when an actual climate crisis strikes. The comparison is not to equate the two, but to expose how rigid and unfair financial commitments can crowd out the capacity to prepare for or recover from the far less predictable—but potentially catastrophic—shocks of climate change.

Chad, one of the world's most climate-vulnerable countries, faces a stark imbalance between its climate needs and

THREAT FROM ALL CORNERS

While most low- and middle- income countries are climate-vulnerable, at least 36 of them also face acute external debt and a severe climate finance gap. Together, they need $79 billion annually, but received just $7.17 billion per year in commitments between 2012 and 2022

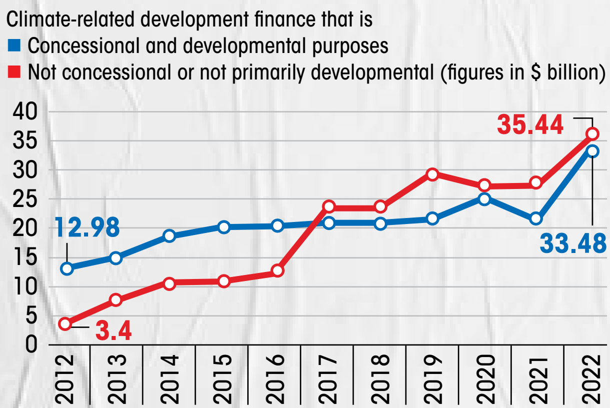


Source: Notre Dame Global Adaptation Initiative Index, World Bank-IMF Debt Sustainability Analysis, Nationally Determined Contributions of countries, OECD Climate Related Development Finance database financial realities. With over $2.1 billion needed annually to implement its climate plans, it has received just $177 million per year in committed climate-related development finance over the past decade—barely 8 per cent of its actual requirements. Meanwhile, the country suffers annual average climate-related damages of around $29 million, further compounding its vulnerability.

Yet, Chad spends far more on debt repayment than on addressing climate or development needs. In 2022, the government paid $393 million in external public debt service—more than double the amount it receives on average per year in climate related development finance, and more than seven times what it spent on health as a share of GDP. Debt servicing also consumed a staggering 19.15 per cent of total government revenue; the country is classified at high risk of debt distress. This also underscores the urgent need for creating non-debt climate finance and fairer financial rules for frontline nations.

AN EXPENSIVE BARGAIN

Although climate finance to LMICs has grown in the past decade, non-concessional finance now exceeds the preferred concessional finance



Concessional or developmental finance refers to funding from developed countries aimed at supporting economic development, often offered on generous terms such as low interest rates and long repayment periods.
Non-concessional or non-developmental finance includes funding that is not primarily intended for development or lacks favourable terms—such as loans at or near market interest rates
Source: Organisation for Economic Co-operation and Development

MORE CONCESSIONALITY

Several countries delineate the requirement of international assistance for climate finance in their nationally determined contributions (NDCs), ranging from 75 per cent to 90 per cent of overall needs. The Organisation of Economic Cooperation and Development (OECD) collates data on flows of Climate Related Development Finance (CRDF), of which Official Development Assistance (ODA) towards developing countries is a large part. These flows comprise the bulk of tracked international assistance for climate finance flowing to developing countries around the world. Though it is important to note that CRDF is closely related but distinct from the flows that comprise climate finance, tracked as part of the erstwhile $100 billion goal.

The growing share of non-concessional, less development-focused climate related development finance suggests a shift away from equitable, need-based support. The data shows around 2015, the share of non-concessional flows overtook concessional flows, and the trend continues till 2022. The gap may be reducing, but for countries with small economies, the need for majority concessional finance, particularly for climate, is imperative. OECD's latest report tracking overall climate finance flows highlighted that of the $115.9 billion provided/mobilised by developed countries in 2022, some 69 per cent were in the form of loans.

For countries grappling with climate shocks, low readiness, and high debt, this triple bind leaves little space for investment in adaptation or recovery. These are not isolated or theoretical mismatches—they are systemic and structural failures of the global financial system. The analysis underscores the need for a justice informed lens on climate and debt to ensure that those facing the brunt of climate breakdown are not punished twice.

FIX DEBT TO FUND THE CLIMATE FUTURE

Reforming the global debt architecture is key to unlocking climate finance, enabling vulnerable nations to invest in resilience and development

THE MOUNTING debt crisis in developing countries is often portrayed as a failure of fiscal prudence or governance. But "The Jubilee Report", released recently, shows that this narrative is both misleading and incomplete. The truth is, today's crisis is a systemic failure—of global financial architecture, creditor behaviour and neglect.

Debtor governments borrowed beyond their means, often under poor terms and short maturities. Creditors, including private investors and multilateral institutions, knowingly extended excessive and risky financing in the greed for better returns. International financial institutions enabled the spiral by delaying hard conversations, offering band-aid solutions, and propping up a system that privileges short-term returns over long-term resilience.

At the root of the problem lies a gaping hole in the global economic order: there is no international mechanism to deal with sovereign debt distress. Unlike corporations that can declare bankruptcy and restructure, countries in crisis are left to navigate a complex maze of fragmented, creditor-dominated negotiations—with no framework for timely, fair or equitable outcomes. Meanwhile, the deep asymmetries that define the global financial system continue to widen. Countries like the US and France—whose public debt now exceeds 100 per cent of GDP—are considered safe borrowers. Zimbabwe and Chad, with far lower debt-to-GDP ratios, are penalised with exorbitant interest rates and harsh borrowing conditions. This is because wealthy countries borrow largely in their own currencies, enjoy favourable credit ratings, and are perceived as "low risk." Developing countries, in contrast, borrow in foreign currencies, face high currency volatility and are often punished by credit rating downgrades during crises—raising the cost of capital just when they need it most.

If the world is serious about enabling climate action, it must first fix its broken financial system. First, debt resolution must be fair, fast and fit for purpose. "The current creditor-led approach thwarts developing countries' maneuvering potential at the worst possible moment during a crisis," says an expert from UNCTAD, requesting anonymity.

At the Fourth International Conference on Financing for Development (FfD4) in Seville, Spain, developing countries pushed for a UN-led multilateral sovereign debt workout mechanism. However, to their dismay, language on the intergovernmental debt process was watered down in the final outcome document, following strong resistance from several Global North countries during the negotiations. While the weakened text fell short of expectations, civil society organisations and many developing nations remain hopeful that it provides an entry point to continue mobilising efforts toward a fairer debt architecture in the decade ahead, recognising that unresolved sovereign debt challenges threaten both development and climate goals.

Several policy options have also emerged in recent years, each offering pieces of the larger systemic solution. While arrange-ments such as the G20 Common Framework—a global initiative endorsed by the G20 and the Paris Club of creditors (of mostly Western nations)—is meant to facilitate government debt restructurings, other more climate-specific proposals are emerging as well. One such tool is debt-for-climate swaps, a version of debt-for-nature swaps, where creditors agree to forgive a portion of a country's external debt in exchange for commitments by the debtor country to direct the savings towards policy actions and investments in climate resilience or conservation. Such swaps have been used in Seychelles, Belize, Cabo Verde and Barbados, among others, with some positive results. However, they remain small in scale, slow in uptake and ad-hoc in nature—rather than being an integral component of sovereign debt relief pathways.

They have been critiqued for many reasons including the fact that 37 of the world's most severely indebted countries together account for just 0.5 per cent of global emissions. The debt relief from swaps is also too little, amounting to a total of just $3.7 billion till date and creating minimal fiscal space for poor countries.

According to the Centre for Global Development, a US-based think tank, more effective approaches would include reducing reliance on borrowing, improving debt management and accountability, and reforming how debt is structured and handled.

Another emerging innovation is the introduction of debt pause clauses or climate-resilient debt clauses in government debt contracts. These clauses allow debtor countries to temporarily suspend repayments in the wake of an extreme climate event. This provides temporary liquidity in the face of a disaster. Barbados, Grenada and Bahamas are among countries where this approach has been utilised. But civil society has critiqued such clauses in their present form as being inadequate. The fundamental problem is that interest continues to accrue as payments are suspended, thereby not offering any real reductions in the overall amount of debt. Further, since it is not mandatory and not all creditors have such clauses in place, the possibility of freed-up resources from one contract being used to repay another creditor is high.

"The Expert Review on Debt, Nature and Climate", jointly established by Kenya, Colombia, France and Germany, has put forward suggestions that address the systemic roots of the climate-debt nexus. They call for a reform of the World Bank-International Monetary Fund Debt Sustainability Frameworks which assess developing countries' debt conditions and are critical for countries' ability to borrow internationally. Their proposed solutions speak about the inclusion of climate risks, nature-related risks and the use of different climate scenarios to make these analyses more robust and climate-relevant.

Most importantly, debt cancellation must be on the negotiation table. "The Jubilee Report" argues that stopping negative net transfers—where countries pay more in debt than they receive in aid or investment—is fundamental. Aid and climate finance will remain inadequate if every dollar received is cancelled out by two dollars sent to creditors.

DEBT'S CLIMATE LINK

The Global South has contributed the least to the climate crisis but bears its harshest impacts. Climate finance remains inadequate, while sovereign debt burdens rise, limiting the ability of the Global South to respond to its developmental and climate needs. As these twin crises converge, this factsheet highlights the urgent need for equitable climate action and fair, systemic reform of the global financial architecture, particularly on sovereign debt. Addressing both crises together is essential to ensure that vulnerable countries are not left behind in the transition to a climate-resilient future and sustainable development.

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