Debt Swaps
Resetting global SDG 2 development agenda and building back better from the impact of Covid-19 pandemic
April 2021

Introduction and background

At the third UN Conference on Financing for Development in Addis Ababa in 2015, world leaders committed to take decisive measures to mobilize sufficient resources to meet the ambition of the UN’s Sustainable Development Goals (SDGs), with a particular focus on the poorest and most vulnerable countries.

Improvements in tax policies, the adoption of new financial instruments such as blended finance and rapid rise in sustainable commercial investments are among key positive developments generating new resources towards the SDGs. However, much more needs to be done to mobilize and channel sufficient finance to countries and sectors that need it most. For example, Foreign Direct Investment (FDI) flows have declined for many low and middle-income countries since 2015, remittance transfer costs remain too high, and Official Development Assistance (ODA) has stagnated and remains far from the UN target of 0.7% of GNI for advanced economies. Against this backdrop, the COVID-19 pandemic has now made the financing for development outlook bleaker, unless the international community can come up with new approaches to address the challenge.

One key factor adversely impacting SDG financing, is the large increase in public and private external debt across developing countries over the past decade. This increase has led to a rise in debt distress and debt sustainability challenges. Economic growth recorded by many developing nations over the past decade was funded by debt and mostly, non-concessional debt. For instance, sub-Saharan African countries saw their debt rise on average by 9.4% annually between 2010 and 2020 as many low-income countries gained access to global debt markets for the first time. Even prior to the COVID-19 pandemic, 44% of countries in this category were classified as either at ‘high risk’, or already in ‘debt distress’. That figure had further risen to 51% by February 2021. Moreover, the COVID-19 pandemic has increased borrowing needs (and costs) as countries have seen public spending needs rise, while revenues have declined sharply. Concerns over a potential debt crisis in developing countries as a result of COVID-19 led the G20 to announce the Debt Service Suspension Initiative (DSSI) in April 2020. While the DSSI has provided eligible countries with valuable debt service relief in the short-term, ensuring a return to long-term debt sustainability for most developing countries will likely require deeper and more permanent debt relief solutions.

As the international community looks to support a sustainable and inclusive recovery from the pandemic, and simultaneously deal with mounting concerns over debt distress, WFP advocates for increase in the use of debt relief measures such as debt swaps.
Debt swaps

A debt swap is the foregoing of repayment of public debt by a creditor, under condition that the borrower ‘invests’ the money in mutually agreed development projects. Debt swaps aim to reduce external public debt of a country and allow the debtor government to grow its fiscal space by repurposing funds previously earmarked for debt servicing, towards spending on national economic and social development programmes.

**Figure 1: Debt swap illustration**

Covid-19 and the urgent case for debt-for-food swaps

Since the SDGs were adopted in 2015, there has been a chronic underinvestment in SDG 2 (zero hunger). The pandemic has also unfolded at a time when the number of acutely food insecure people around the world had been rising steadily, increasing by almost 70% over the four years prior to the pandemic, with conflict and climate change as key drivers of this increase. The pandemic is further increasing the number of food insecure people as jobs are lost, the flow of remittances slows and food systems are further stressed or disrupted. WFP and FAO data on food security show that the number of people facing acute hunger globally reached 270 million at the end of December 2020. This is a more than 80% increase from pre-COVID levels. As the world appears to be on the cusp of a “hunger pandemic”, other key risks such as new conflicts are likely to emerge. Food crises are known to aggravate structural vulnerabilities and pre-existing grievances, potentially leading to widespread instability and conflicts.

The COVID-19 pandemic has exposed the devastating impacts of chronic underinvestment in SDG 2, as weak food security and social protection schemes have struggled to meet citizens’ basic needs. In several countries, the pandemic has led to a near complete reversal of gains made over the last decade on food security and poverty alleviation. Unlike other development goals where significant increase in investment in future years can reverse the effects of underinvestment in earlier years, lives are lost to hunger and human capital development potential that is unrealised due to inadequate food and nutrition is hardly recovered.

As countries deal with the urgent need of ending the Covid-19 pandemic and ‘build back better’, debt-for-food swaps can play a key role of ensuring sustained spending on SDG 2.
WFP’s experience with debt swaps

Germany—Egypt

WFP has partnered several times with Germany and the Government of Egypt to implement programmes funded by contributions stemming from debt swaps agreed between the two countries. The latest debt swap agreement among the three parties, valued at EUR 15 million, was part of EUR 80 million debt relief granted to Egypt by Germany in June 2020. The contribution comes from Germany’s Federal Ministry of Economic Cooperation and Development via the German Development Bank (KfW) and is being used for resilience, nutrition and education programmes in Upper Egypt governorates. The ‘Investing in Human Capital in Rural Upper Egypt’ project will build the resilience of 136,000 poor families to cope with the social and economic impacts of the COVID-19 pandemic and provide income generation opportunities for women and youth.

Italy—Egypt

In 2009, WFP began implementing a USD 15 million five-year project funded by resources stemming from an Italy-Egypt debt swap. Successfully concluded in 2014, the project was implemented in the governorates of Fayoum, Menia and Beni Suef, and provided children with daily nutritious snacks. The snacks provided children with 25% of their daily nutritional needs and helped increase the pupils’ level of concentration in classes. The project also encouraged parents to enrol their children by providing take-home rations to the families of children regularly attending school. A final evaluation of the project reported significant gains in nutrition and education outcomes.

Russia—Mozambique

WFP signed an agreement with Mozambique and Russia in 2017 for the implementation of a school meals programme targeting 150,000 children in Mozambique over a 5-year period, funded by a USD 40 million debt swap. The school meals programme is an investment in Mozambique’s education sector and represents an important safety net. It is also a powerful means of alleviating poverty and hunger in the most vulnerable households. The debt swap and WFP’s school meals programme also represent significant investment in the broader local economy, with all food procurement taking place at the local level, including from neighbouring smallholder farmers. The programme therefore has a strong economic multiplier effect. The provision of daily school meals incentivizes children to attend schools regularly, thereby contributing to reducing absenteeism and drop-outs. Assessments of the programme often note significant improvement in students’ concentration levels and overall learning outcomes. WFP is committed to supporting the Government of Mozambique transition towards a nationally owned, funded and managed home-grown school meals programme over the next few years and increase opportunities for Mozambican children to thrive. This debt-to-development partnership has been pivotal in this respect.
The impact of debt servicing on SDG 2

Many low-income countries are dependent on food imports for most of their national food requirements and the effect of COVID-19 on trade and balance of payments is turning out to be another key driver of reported increases in global hunger. For most developing countries, debt service costs represent the highest proportion of their governments’ hard currency spending, presenting a direct trade-off between debt servicing and a country’s capacity to import adequate food in constrained resource environments. Because debt service costs and other external commitments are often fixed and not linked to prevailing economic conditions, when a developing country’s foreign currency earnings or government revenue decline, the impact often directly translates to food insecurity and/or underinvestment in SDG 2, overall. For these reasons, WFP is advocating for bilateral creditors and private/institutional creditors to consider debt-for-food swaps in debt relief resolutions.

Benefits of debt-for-food swaps to key stakeholders

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<th>Creditors</th>
<th>Debtors</th>
<th>WFP</th>
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<td>• Opportunity to increase ODA without making new resource outlays.</td>
<td>• Immediate reduction in foreign currency denominated debt, creating fiscal space to reprioritize the use of scarce foreign exchange resources.</td>
<td>• Increase in predictable resources towards SDG 2 priority areas jointly identified with creditors/donors and debtor governments.</td>
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<td>• Unlocks new ways of development cooperation with debtor countries and development agencies.</td>
<td>• Opportunity to increase or sustain domestic spending on SDG 2 within a multi-stakeholder environment.</td>
<td>• Unlock opportunities for increased and/or new ways of cooperation with creditors/donors and national governments.</td>
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<td>• Provides means for creditor/donor countries to ensure that resources freed-up through debt relief are transparently used to finance priority programmes under SDG 2.</td>
<td>• Provide platform and incentive to strengthen debt and fiscal management practices in cooperation with creditors and development agencies.</td>
<td>• Chance to contribute to dialogues on debt and fiscal management, helping countries develop integrated approaches to SDG 2 financing.</td>
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Partnership for the Goals through debt-for-food swaps

While debt swaps are agreed bilaterally between creditor and borrower governments, implementation of the development programmes into which debt repayments flow is often assigned to third parties, such as United Nations agencies and non-governmental organizations. These third parties typically have capacity to complement national efforts, while maximizing efficiency, effectiveness, transparency and accountability over use of resources.

WFP offers such capacity on supporting SDG 2 programming and has effective systems to ensure transparency and operational excellence in implementation. Success stories presented on Page 3 highlight WFP’s capacity to effectively and efficiently operate and manage development projects and programmes funded through debt swaps.

Attributes that position WFP favourably as a preferred implementing agency on SDG 2 include:

- Scale of existing operations and programmes, both humanitarian and development.
- Alignment with national priorities and the 2030 Agenda, and highly regarded as a trusted partner and advisor to national governments on SDG 2.
- Beneficiary reach, trust of communities and experience implementing various types of development and humanitarian programmes at scale in the context of SDGs.
- Demonstrated commitment to results, transparency and accountability.

Resources mobilized through debt-for-food swaps can be directed towards various development or humanitarian programmes linked to SDG 2. WFP sees great potential impact from debt-for-food swaps in the context of ‘building back better’ from school meals, nutrition, social protection, climate change mitigation, asset creation and other resilience building programmes.

All of WFP’s activities on SDG 2 and its country strategic planning process places national governments and their priorities at the centre. This is often achieved through national Zero Hunger Strategic Reviews (ZHSR) which are carried out under the leadership of governments themselves, with support from WFP. ZHSR aim to establish a hunger baseline, determine gaps in the national food security and nutrition response and identify priority actions needed to achieve SDG 2. The findings of Zero Hunger Strategic Reviews inform the plans of national and international stakeholders, including WFP and other UN agencies.

The consultative and integrated planning process adopted by WFP ensures that it consistently offers its programmatic and operational assistance to governments and partners, including donors, in complete alignment with national priorities and the SDGs. This strategic alignment on priorities, WFP’s historical performance and its operational capacity, scale and accountability tools, help to ensure the organization is a preferred partner for national governments, development institutions and donors on implementation of SDG 2 programmes, including those resourced through debt-for-food swaps.

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