Article

Developing Countries after the COVID-19 Shock: Inflation, Debt Crisis and Future Outlook

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Abstract In considering human security, it is crucial to examine the implications of downside risks to the economy. The COVID-19 shock triggered profound economic difficulties, resulting in a compounded crisis, characterized by multiple risks chaining and impacting one another, high levels of uncertainty, and the prevalence of policy dilemmas. For developing countries, inflation has mainly been driven by soaring food prices, imposing a particularly heavy burden on low-income groups. Moreover, countries with fiscal and external sector vulnerabilities have experienced challenges in financing their economies after the COVID-19 shock, hampering their debt repayments. Underlying the debt problem is the changing composition of external public debt creditors, a process that has been ongoing since the 2010s. Strengthening economic resilience requires back-to-basics policies in developing countries: sound economic management, improved ability to manage debt risk, and the pursuit of growth opportunities through quality investment. The international community also needs to further develop a framework to cope with these global economic shocks in a coordinated manner.

Introduction

At a symposium held in the aftermath of the Asian currency crisis of the late 1990s, Amartya Sen—a Nobel laureate in economics who significantly shaped the concept of human security—articulated the importance of "growth with equity" and "downturn with security" (Sen 2000).

The global economic crisis triggered by the international spread of COVID-19 from the beginning of 2020 brought about a major global economic shock, surpassing the Asian currency crisis in 1997 and the global financial crisis of the late 2000s. Russia's invasion of Ukraine in February 2022 led to further destabilization, damaging a global economy and society that was still recovering from the economic crisis and the pandemic. Over the past few years, the global economy has witnessed the significant manifestation of the downside risks encompassed by the concept of human security.

This article examines the characteristics of the global economic crisis that has occurred since the global outbreak of the new coronavirus (henceforth referred to as "COVID-19 shock"), paying particular attention to the impact on developing countries. This paper also assesses the outlook for these countries and explores measures to strengthen their resilience. Section 1 provides an overview of the global economic situation after the COVID-19 shock in early 2020 until late 2023, the time of writing, and then summarizes the characteristics of the post-pandemic economic situation—the period marked by compounded crises. Sections 2 and 3 discuss the background of the inflation and debt crisis and their impact on the economies and societies of developing countries based on the previous discussion. Section 4 highlights key aspects of the global economy that require our attention and issues that need to be addressed to support the process of economic recovery in developing countries.

1. Developing Country Economies after the COVID-19 Shock: Experiences of Compounded Crises

1.1. Global economic overview in 2020-23

Following its initial outbreak in Wuhan, China, at the end of 2019, COVID-19 spread rapidly around the world, driven by the frequent movement of people across regional and national borders. The global economy contracted sharply and many countries introduced restrictions on people's movement. The economic outlook also deteriorated and a sharp drop in stock markets was observed in February and March 2020. The IMF Managing Director, Kristalina Georgieva, stated that the economy in 2020 was anticipated to experience "the worst economic fallout since the Great Depression" (Georgieva 2020).

In response to this situation, advanced countries implemented large-scale fiscal policies and monetary easing. The decisions to apply these measures were taken quickly, drawing on lessons learned from the global financial crisis of 2007–2008. By comparison, developing countries had limited capacity to undertake similar large-scale economic measures. By April 2020, not long after the spread of the coronavirus, the number of developing countries that requested IMF support had reached 100. Developed nations, including Japan, and international organizations, such as the World Bank, also provided emergency financial assistance. In addition, 73 countries, mostly low-income countries, became eligible for the suspension of principal and interest payments on their external public debt under the Debt Service Suspension Initiative (DSSI).

Figure 1 shows the annual GDP growth of advanced and developing economies since 1990. It depicts the scale of the economic shock of 2020 in comparison to past economic crises. Despite massive fiscal stimulus and monetary easing, developed economies recorded a negative

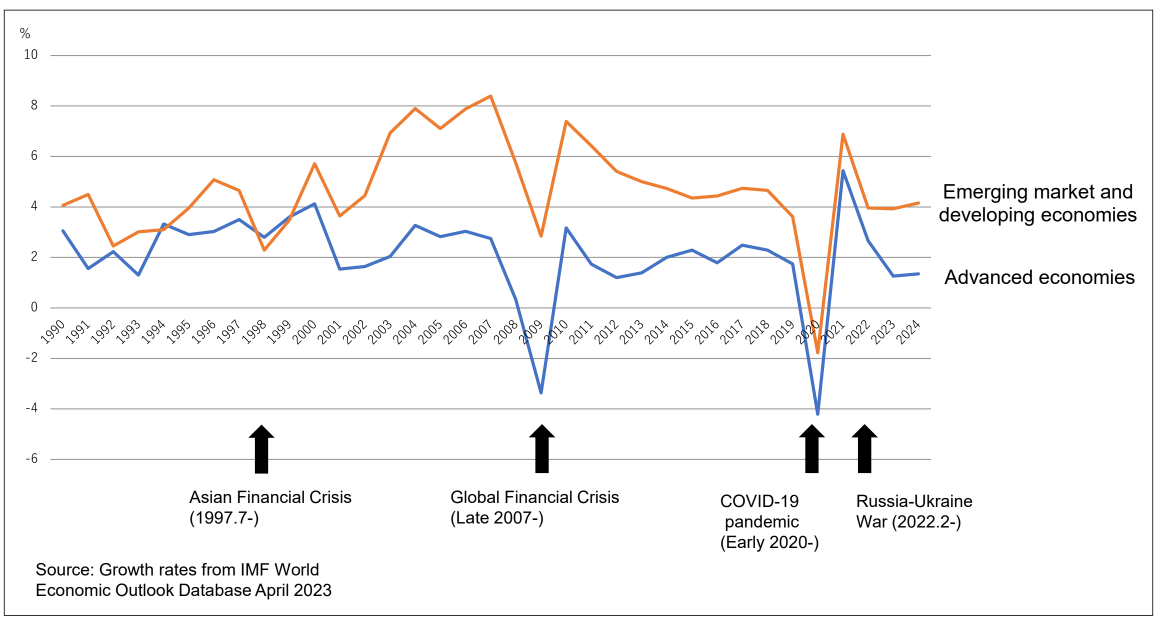

Figure 1 GDP growth rates (advanced and developing countries)

Note: Developing countries are aggregated as "Emerging Markets and Developing Economies" in the source database. 2023 and 2024 are projected figures.

Source: Prepared by the author based on IMF World Economic Outlook Database April 2023 (IMF 2023b) growth of –4.2% in 2020. Developing countries also recorded negative growth of –1.8% in 2020, despite growing at a faster pace than developed countries since the 2000s and maintaining positive growth even during the global financial crisis in the late 2000s.

In 2021, both developed and developing economies rebounded from the previous year, experiencing significant positive growth. The extent of the recovery, however, varied from country to country mainly due to disparities in fiscal capacities and response capabilities, such as the availability of the coronavirus vaccine. In February 2022, Russia's invasion of Ukraine further disrupted the global economy. The imbalance between supply and demand caused by the war accelerated the rise of food and energy prices worldwide. In the same year, the US and Europe moved to raise interest rates and the COVID-19 outbreak was gradually brought under control. While the year 2023 saw no major economic upheaval, as in previous years, many uncertainties remain, including the ongoing war between Russia and Ukraine and a slump in the Chinese economy.

1.2. Characteristics of a compounded crisis

The global economic situation, beginning with the global spread of COVID-19 through Russia's invasion of Ukraine up to the end of 2023, is often described as a "compounded crisis." There are several similar expressions, such as "compounding crises," "multiple crises," and "polycrisis." There is no unified definition of these terms, and what they mean may differ depending on the context or scope of the discussion. However, as **Figure 2** shows, the global economy since the COVID-19 shock has been characterized by various challenges, which collectively make it appropriate to describe the economy so far as being under a "compounded crisis."

The first characteristic of this crisis is that various risks have manifested themselves as a chain of events, where each incident causes the next. One example is the epidemiological shock of the COVID-19 epidemic itself, which led to economic shocks on both the supply and demand sides of the economy. Another example is the chains of risk manifestation, whereby the Russian invasion of Ukraine accelerated the global supply-demand imbalance for food and energy among globally interdependent economies. This has caused international prices to rise, with these higher prices passed on through domestic prices in food and energy import-dependent developing countries. The chain has also been linked to the social unrest that many countries experienced during this period.

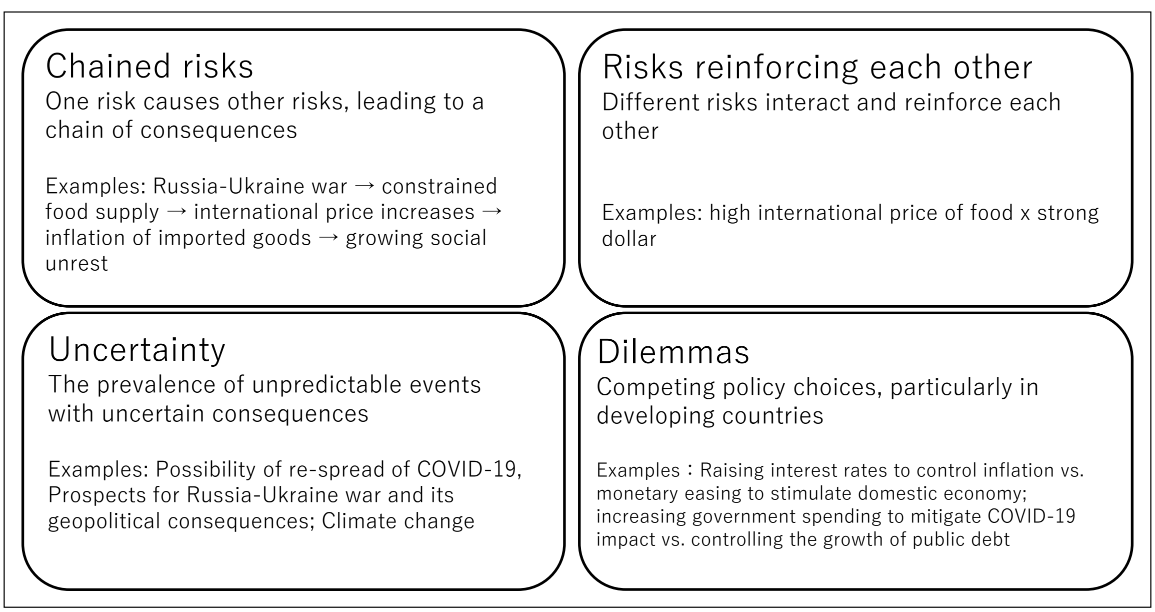

Figure 2 Elements characterizing the "compounded crisis" since the COVID-19 shock

Source: Prepared by the author

Second, different risks often interact, amplifying their collective impact. For example, the rate of increase in international prices for food and energy peaked in mid-2022, as noted in the next section on inflation. On the other hand, the monetary tightening in the United States during the same period caused the US dollar to appreciate against other developed and developing country currencies. The combination of these factors has increased the financial burden on developing countries that rely on imported food and energy.

The third characteristic is uncertainty. In the early days of the COVID-19 shock, it was difficult to accurately predict the spread of the infection and the extent of its socioeconomic impact. Thanks to the development of vaccines, many countries were able to reduce COVID-19 transmission and control its impact, but threats remain, with the possibility of the re-spread of infection and the emergence of mutant strains. Additionally, the Russian-Ukraine war continues at the time of this writing. There are other challenges, such as climate change, whose scope and depth of impact are difficult to accurately predict. Since the COVID-19 shock, governments have increasingly been asked to make policy decisions in uncertain environments.

The fourth characteristic is a policy dilemma that has significantly confronted policymakers in developing countries: governments have been forced to accept increases in government debt to finance spending. This has been necessary to mitigate the economic impacts of the pandemic on households and businesses. After the US tightened monetary policy in 2021 to control inflation, developing countries had to choose whether to raise their interest rates to prevent capital outflows or maintain monetary easing to support domestic economic stimulus.

In the global economic climate outlined in the previous sections following the COVID-19 shock, inflation and debt problems were particularly impactful for developing countries. Each of these aspects will be discussed in detail in the following sections.

2. Inflation

2.1. Trends and characteristics of global inflation

Following the COVID-19 shock, inflation emerged as a significant concern for most countries—and thus, it might be referred to as global inflation. Even before the pandemic, controlling inflation had been an important policy issue in developing countries. By comparison, since the 2000s, inflation has rarely been a concern in developed countries and was sometimes viewed as an issue that had been resolved. In some countries, such as Japan, deflation had become more of a problem. After the pandemic, inflation re-emerged as a major global issue, affecting both developed and developing countries.

A common indicator of inflation is the year-on-year rate of increase in the monthly consumer price index (CPI)—henceforth referred to as the inflation rate in this article (unless otherwise noted). **Figure 3** shows a breakdown of how the price increases of various consumer goods and services contribute to the monthly inflation rate by income group. The original IMF data consists of 12 items of goods and services, from which the most important ones have been grouped as follows: food and non-alcoholic beverages; housing, water, electricity, gas and other fuels; and transportation, while the other items are summarized as "others."

Countries of different income levels have shown different inflationary paths since 2020. In high-income countries, inflation rates remained subdued throughout 2020. This suggests that in the early stage of the pandemic, their economies were more affected by demand-side decline due to restrictions on mobility rather than constraints on the supply of goods and services. **Figure 4** shows global price trends for energy and food. International prices for energy initially fell in 2020, which reduced the contribution of "transportation" items, including gasoline, leading to negative inflation rates in developed countries, as shown in **Figure 3**. In 2021, international energy prices began to rise globally, driving price increases in the "transportation" and "housing, water, electricity, gas, and other fuels" items. The contribution

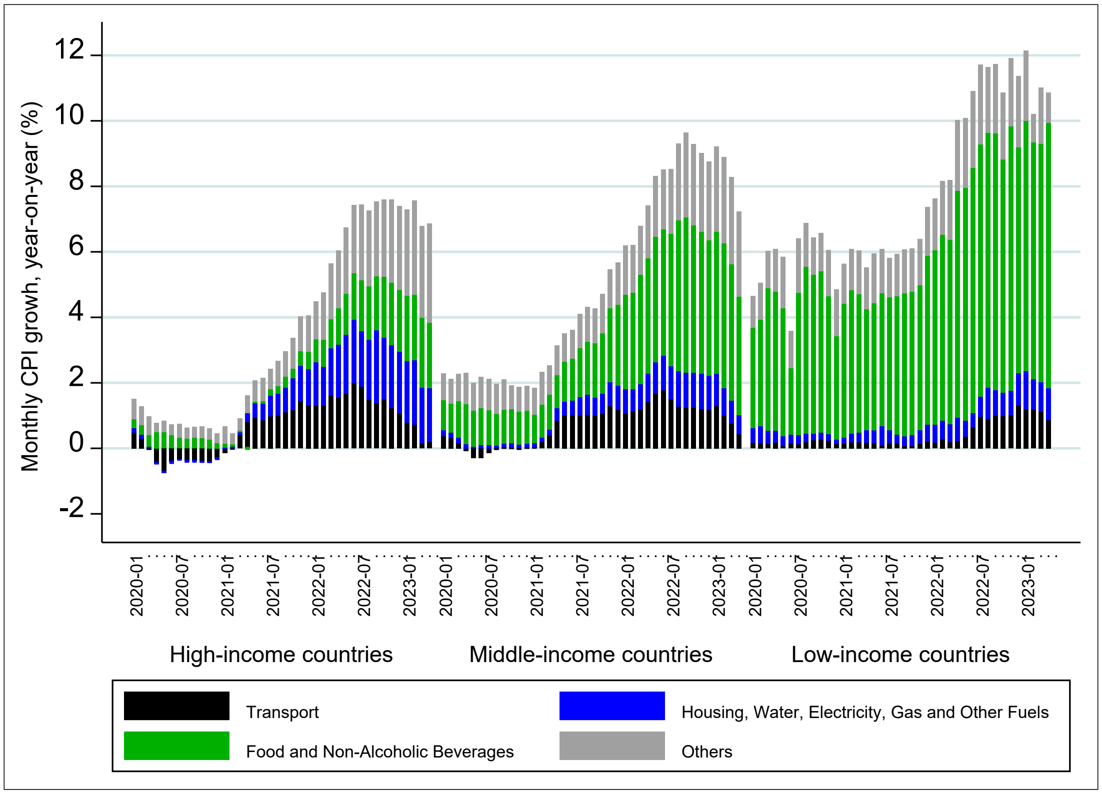

Figure 3　Contribution of each item to consumer price index increase by income group

Note 1: Income groups are based on World Bank standards. High-income countries are those with a GNI per capita of US$13,846 or more, middle-income countries are those with a GNI per capita of US$1,136-13,845, and low-income countries are those with a GNI per capita of US$1,135 or less.

Note 2: Medians within income groups are shown as the contribution of “Transportation,” “Housing, Water, Electricity, Gas, and Other Fuels,” “Food and Non-Alcoholic Beverages,” and “Others”; totals of each category do not necessarily correspond to the percentage increase in the CPI by income group.

Source: Prepared by the author based on IMF Data, Consumer Price Index (IMF 2023a).

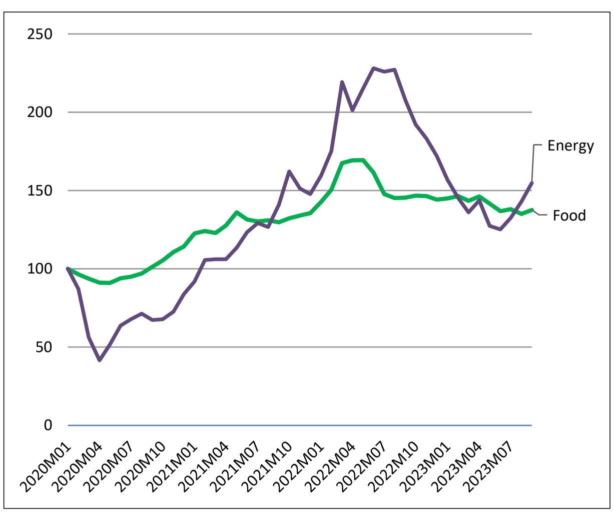

Figure 4　Food and energy price trends

Note: Changes in relative levels from January 2020–July 2023. January 2020 is set as 100.

Source: Prepared by the author based on World Bank, 2023b

of “food and non-alcoholic beverages” also began expanding, especially in 2022, leading to a further increase in the inflation rate. Subsequently, the contribution of “others” has also been increasing.

Inflation rates in low-income and middle-income countries have consistently been higher than those in advanced economies. Traditionally, “food and non-alcoholic beverages” have contributed significantly more to inflation in low-income countries because of the large share of household expenditure on food items. Although to a lesser extent than low-income countries, middle-income countries also have a higher contribution of food prices to inflation rates than advanced economies.[1]

[1] Low- and middle-income countries place a higher weight on food in the calculation of the CPI, reflecting its significance in consumption expenditures.

International food prices have been on an upward trend since mid-2020 after the COVID-19 shock. The war between Russia and Ukraine in 2022, both of which are important producers and exporters of wheat and other grains, pushed up grain prices globally and accelerated food inflation. With this background, the rise in prices of "food and non-alcoholic beverages" contributed significantly to the overall increase in the price level, especially in low- and middle-income countries. Compared to high-income countries, the contribution of energy price increase on inflation from "transportation" and "housing, water, electricity, gas, and other fuels" has been relatively small in low- and middle-income countries. However, higher energy prices may have caused indirect impacts on food prices through higher production and transportation costs for agricultural and other products.

Figure 5 depicts regional trends in inflation, showing median value and variation in rates. Note that countries with extremely high inflation rates are excluded from the graph as outliers in each region. The emerging Asian economies maintained relatively controlled inflation after the COVID-19 shock, with inflation rates held below 10% in most countries. In Mongolia and some island countries, inflation rates rose above 10% after 2022. The inflation rates for Sri Lanka and Laos may be considered outliers and are not included in this graph. Sri Lanka experienced a debt crisis in 2022—discussed in the next section—and its inflation rate exceeded 60% at one time. Similarly, Laos experienced an inflation rate of over 40% in late 2022.

Inflation rates in sub-Saharan Africa vary significantly from country to country, with numerous outliers across the region. One example is Zimbabwe, which has recorded year-on-year hyperinflation of more than 800%. This is more due to the country's poor economic management than the economic shocks of COVID-19 and the Russia-Ukraine war. High inflation rates can also be observed in Ghana, Zambia, and Ethiopia—countries experiencing debt crises. Central

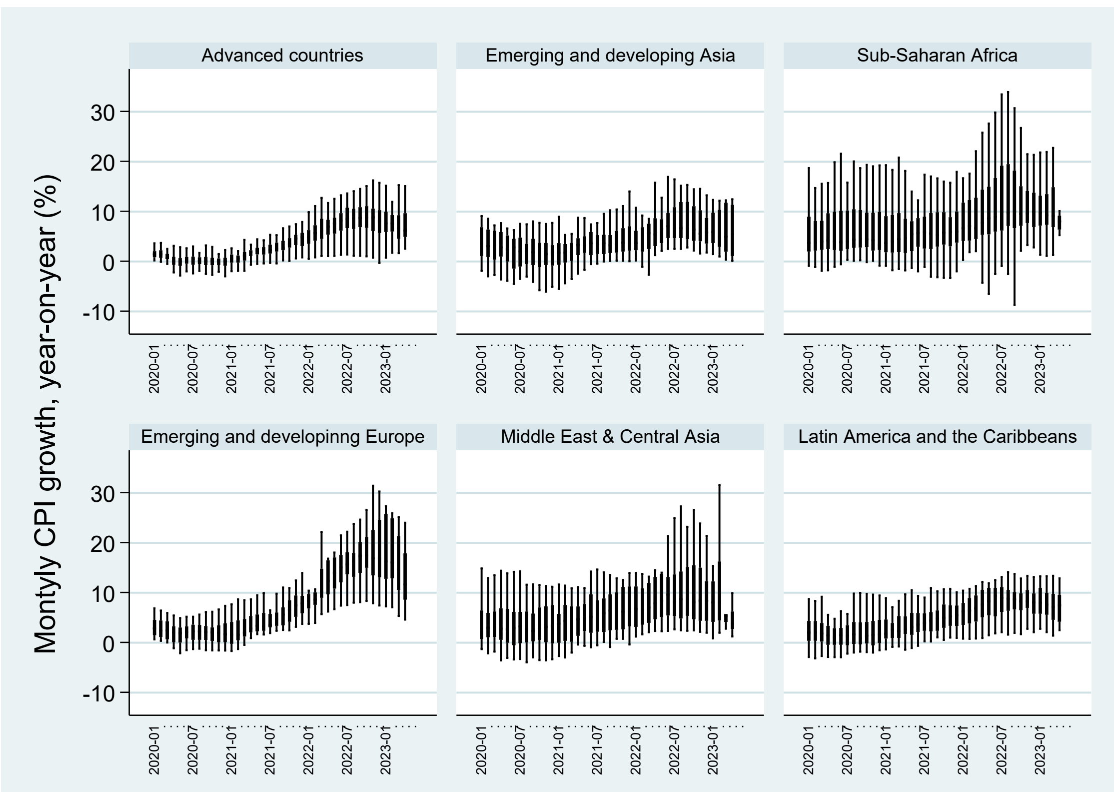

Figure 5 Inflation trends by region

Source: Prepared by the author based on IMF Data Consumer Price Index (IMF 2023a)

Note: Observations situated above the third quantile at a distance of 1.5 times the length between the first and third quartiles or below the first quantile by the same distance are treated as outliers and are not shown in this graph.

and Eastern Europe were the most inflationary regions, with many countries recording inflation rates of around 20% in 2022. Turkey and Moldova are outliers, with inflation rates soaring above 80% and 30%, respectively, in 2022.

The Middle East and Central Asia, as well as Latin America and the Caribbean regions, recorded median inflation rates of up to 10%. The Middle East and Central Asia show significant differences between countries, with outliers Lebanon and Sudan recording inflation rates of over 200% and 400%, respectively. Iran, Egypt, and Pakistan also experienced high inflation rates. Outliers in the Latin America and Caribbean region, such as Argentina, Haiti, and Suriname, are perennially inflationary countries. Argentina, for example, has experienced an inflation rate of more than 100% since 2023.

Entering 2023, price levels in many developing countries have settled down compared to the previous year. However, due to continuous price increases, the absolute level of prices has risen significantly compared to the pre-pandemic level. Inflation remains particularly high in some countries that have had difficulties in repaying public debt or are at high risk of failing to do so.

We should also pay attention to the global trend of US dollar appreciation: US policy rates and long-term interest rates have risen as a result of monetary tightening in the US beginning in 2022. As a result, funds once invested in developing countries in search of higher yields have tended to leave these countries, contributing to the dollar's appreciation. Under these circumstances, even if the international price level of food prices stabilizes, the price of imported food products in developing countries may remain high due to the depreciation of the local currency. In Egypt, for example, the exchange rate, which was at 15 Egyptian pounds per dollar in 2021, has exceeded 30 pounds since the beginning of 2023. Egypt has traditionally experienced large fluctuations in portfolio investments from abroad. The US tightened monetary policy after the end of 2021 and the impact of the Russia-Ukraine war on Egypt—which heavily depends on these countries for wheat imports—has led to an outflow of funds from Egypt, depreciating the value of its currency. As a result, in August 2023, Egypt's inflation rate remained high at 37.4%.

2.2. Impact of inflation on livelihoods

Next, this article examines how inflation has affected the livelihoods in developing countries. Since the beginning of 2022, the term "Cost of Living Crisis" has been used in the media to describe the consequence of inflation. This term was initially used to discuss the inflationary impact on the lives of people in the United Kingdom and other European countries where record-high inflation, triggered by high energy prices, exceeded wage growth. The impact of inflation, however, has also been significant for households in developing countries. In particular, global food price increases resulting from the imbalance between supply and demand—due to the Russia-Ukraine war and other factors after the COVID-19 shock—caused food price inflation in developing countries where the weight of food in the consumer price index has been high. In addition, the surge in energy prices may have also affected food prices through increased production and transportation costs, as mentioned in the previous section.

Figure 6 provides a comparison of food expenditures as a percentage of total expenditures by country. Countries with lower incomes and smaller absolute expenditures on food spend more on food as a percentage of their total spending, suggesting that higher food prices have a greater impact on people's lives in these countries.

Inflationary impacts may be less serious if wage growth exceeds price growth. According to the ILO's Global Wage Report 2022–2023 (ILO 2022), however, real wage growth worldwide was negative at –0.9% in 2022. The report indicates that inflation's adverse effects on the level of real wages that year were significant.

It is essential to note that the degree and direction of the impact of food inflation in developing countries varies significantly across the affected groups. Lower-income groups, who spend a higher proportion of their income on food, are generally more adversely affected by food inflation within the same country. However, increases in international prices for agricultural commodities can be desirable for farmers and producers. In response to increases in imported food prices, rural households may switch to agricultural products they grow for their own consumption. Conversely, the urban poor are likely to be unable to take such measures and are generally more vulnerable to price hikes. Dairy and

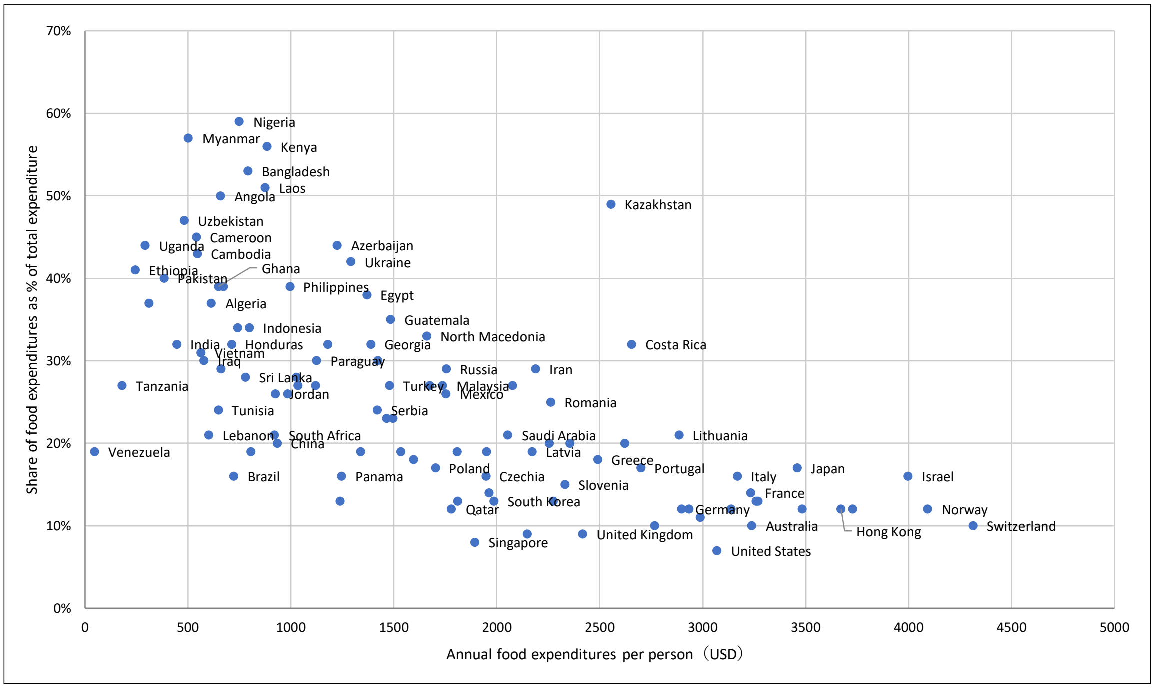

Figure 6 International comparison of food expenditure as a percentage of total per capita expenditure

Source: Prepared by the author based on Richie (2023)

poultry farmers may be vulnerable if they depend on imported feed.

The cost-of-living crisis in developing countries has led to changes in behavior among the most affected populations, with many being forced to eat less often or choose cheaper but less nutritious foods. It has been reported that after the COVID-19 shock, 102.2 million more people faced hunger compared to 2019 (FAO, IFAD, UNICEF, WFP and WHO 2023). The burden of daily spending may result in families sacrificing the funds needed for education and other long-term needs. In Lao PDR, it was reported that the rising cost of living, inflation, and devaluation of the country's currency have collectively impacted students' access to higher education, and in 2023, university enrollment fell to the lowest level recorded since 2018.[2]

Economic crises necessitate policy responses, particularly in situations where there are limited means for individual households to mitigate the impacts. Accurate identification of the most vulnerable groups is vital for the implementation of such policies, but determining those most in need can be challenging. For example, estimating the base poverty level through a large-scale national survey requires time and resources and cannot always be conducted frequently. The World Bank estimated in 2022 that the number of people living in poverty will increase from 648 million in 2019 to 719 million in 2020 (World Bank 2022a), but this figure for 2020 remained an estimation. While individual countries may have more recent data on the magnitude of the impact of the COVID-19 shock and the subsequent economic crisis on households, adjusting the data quickly for international comparison is another challenge. Given these constraints, researchers have attempted to understand the magnitude and diversity of the impacts in a more timely manner by using additional methods, such as targeted telephone surveys.[3]

2 https://laotiantimes.com/2023/08/15/laos-records-decline-in-university-enrollment-across-the-country/ Accessed September 29, 2023.

3 One example is the World Bank's COVID-19 Household Monitoring Dashboard.

3. Debt Crisis

3.1. Increase in public debt during the COVID-19 shock

In addition to global inflation, the problem of debt has attracted international attention in the aftermath of the COVID-19 shock. This section discusses public debt—or government sector borrowing—has been a serious issue for developing countries. IMF (2023c) data show that the ratio of public debt to GDP grew from 105.4% in 2019 to 124.4% in 2020 in advanced countries, from 55.7% to 65.8% in emerging economies and 42.9% to 48.5% in developing countries. The level declined slightly after 2021 in each region but remains higher than pre-pandemic levels.

It should be emphasized that it is prudent to increase public debt during serious epidemiological and economic emergencies, such as the spread of COVID-19. It can help to provide necessary economic measures and social services, thereby preventing more serious social breakdown. Advanced countries were able to increase their public debt while minimizing their negative impact through low-interest policies and central bank bond purchases as non-traditional monetary policies. However, for developing countries, it was difficult to secure sufficient fiscal resources, as many of them had to contend with weak debt sustainability positions. Several countries faced problems in servicing their past debt or repayments during the economic downturn following the COVID-19 shock.

Table 1 shows the defaults on public debt by developing countries for the period 2020–2022, based on the definitions of a private rating agency. Since 2020, the number of defaults on public debt has significantly increased compared to previous periods.

As of the time of writing, the IMF has rated the debt sustainability of 26 low-income countries as "high risk" and ten countries as "in debt distress," the most severe rating. The debt problem remains an issue that requires careful attention.

3.2. Background to the debt crisis

To understand the dynamics of public debt crises since the COVID-19 shock, we first summarize the relations between government deficit and public debt. As shown in **Figure 7**, the difference between government revenue and expenditure for a given year is the "fiscal balance," with a negative value indicating a fiscal deficit. The fiscal deficit for each year plus the principal repayments needed during the year to repay past government debt is referred to as the government's gross financing needs, for which new borrowing may be required.[4]

This borrowing can be domestic or foreign. The major form of domestic borrowing is the issuance of government bonds, which are typically purchased by domestic banks and other financial institutions.[5] However, due to their underdeveloped domestic financial system and the need for foreign currency, developing countries often rely on external borrowing, i.e., borrowing from sources other than their own country.

However, external borrowing entails additional risk, such as whether sufficient foreign currency is available when the

[4] Other financing measures such as the sale of government assets have been omitted from the discussion for simplicity.

[5] The proportion of domestic debt held by foreign entities is also high in some countries and can be a destabilizing factor for the economy, but we will not analyze this in depth in this article.

Table 1　The record of defaults by developing country governments, 2020-2022

Year 2020	Argentina (February), Lebanon (March), Ecuador (April), Suriname (July), Belize (August), Zambia (November)
Year 2021	Belize (September)
Year 2022	Russia (March), Sri Lanka (April), Belarus (July), Ukraine (August), El Salvador (September), Ghana (December)

Note: The table shows cases in which the rating agency Moody's has identified defaults that occurred from 2020–2022. It includes countries that have already resolved their default status through the completion of debt restructuring negotiations and other means.

Source: Moody's (2023a)

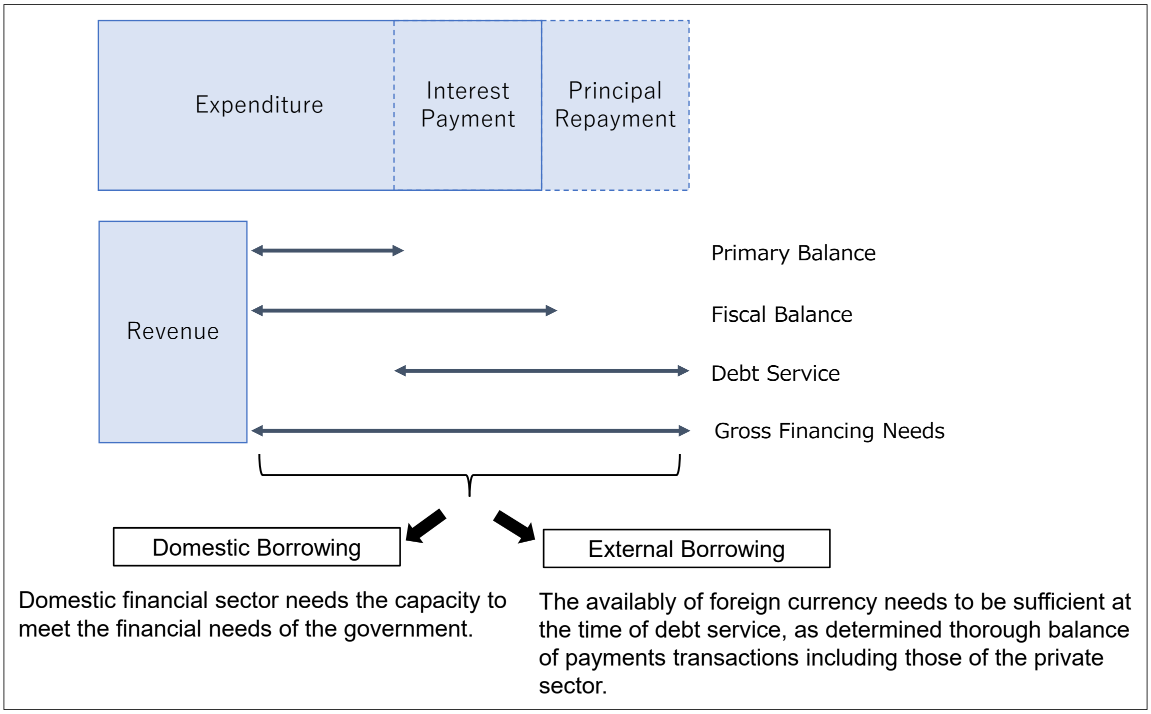

Figure 7 Relationship between government finances and public debt

Source: Prepared by the author

government needs to service the debt. If a country has competitive export industries and is able to export sufficient goods, or if it has sufficient foreign currency inflows from new borrowing or investment from abroad, foreign currency funding is unlikely to be a problem. However, the government may face difficulty in servicing foreign debts and the settlement of import payments when the outflow of foreign currency outpaces the inflow and the foreign reserves of the government become insufficient.

The debt crises of developing countries after the COVID-19 shock were often triggered by such difficulties in financing external debts.

The contributing factor behind this debt crisis is the substantial change in the composition of the external public debt of developing countries since the 2010s. **Figure 8** shows the outstanding external public debt in low-income countries and lower-middle-income countries by creditors.

We can see that since the mid-2000s, outstanding external public debt for low- and middle-income countries has increased rapidly. This trend is not surprising given the high growth rates experienced by developing economies and significant expansion in their GDPs since the 2000s. If a country is growing at 7%, for example, its GDP will double in 10 years and quadruple in 20 years. A country's public debt sustainability is often assessed based on the debt-to-GDP ratio rather than the absolute amount of debt. A country with a larger GDP generally has a larger economic base that can be taxed, which means that the absolute amount of public debt the country can bear is greater.[6] As GDP grows, the government's spending correspondingly increases to meet the growing needs of government policies, such as social security spending, which remained undeveloped when the country's level of development was low. Therefore, the increase in the absolute amount of debt outstanding in developing countries is to be expected when they experience high economic growth.

It is important to note that the composition of creditors for external public debt of developing countries has changed drastically since the last decade. **Figure 8** shows that since the 2010s, there has been a particular increase in the number of bondholders, i.e., borrowing through the issuance

6 There may be cases where tax collection capacity is not maintained at the same pace as the increase in the economic base.

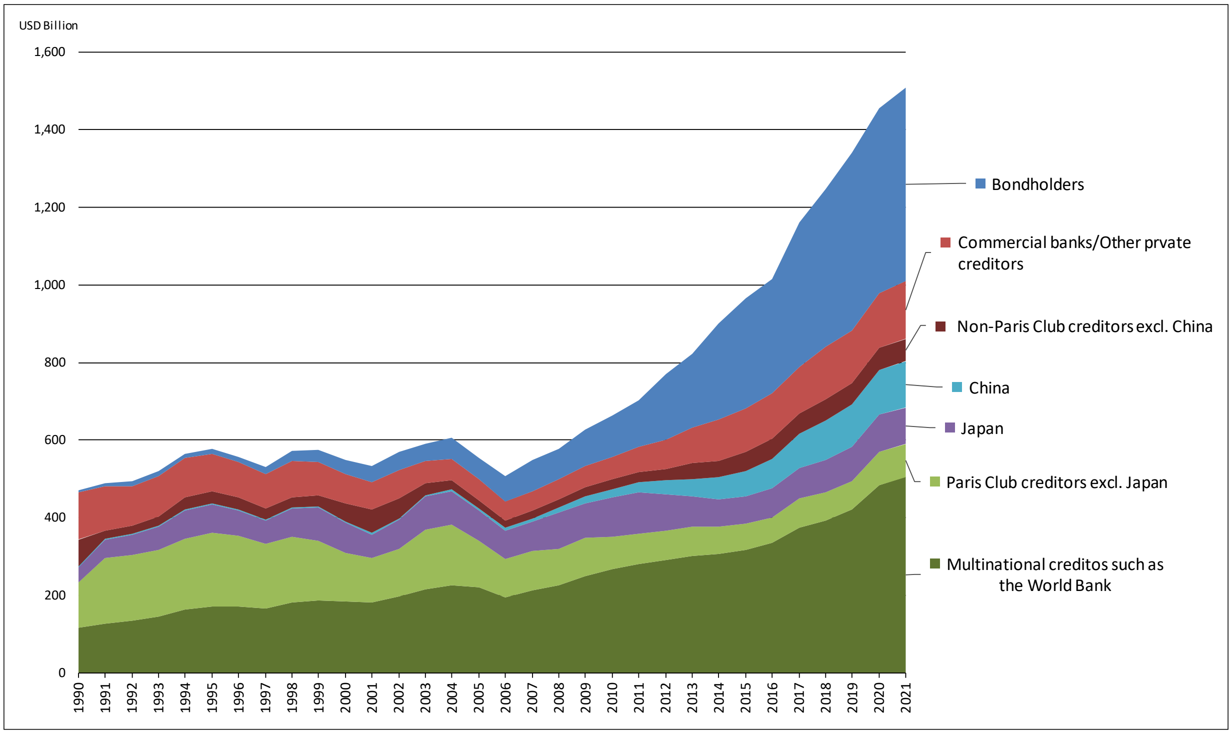

Figure 8 External outstanding public debt among low-income and lower-middle-income countries by creditor-type

Note 1: Low- and middle-income countries are those with GNI per capita of between US$1,086 and 4,255, and low-income countries are those below US$1,085.

Note 2: Paris Club creditors are mainly OECD member countries (22 countries are members, including Japan) who were major bilateral creditors. Non-Paris Club creditors are emerging bilateral creditors such as China, India, Saudi Arabia and the UAE.

Source: Prepared by the author based on World Bank (2023a) International Debt Statistics 2022

of government bonds (mainly dollar-denominated) in international capital markets, commonly referred to as Eurobonds, as well as borrowing from China. Up to the early 2000s, external private sector funding mainly comprised syndicated loans by private financial institutions, but bond issuance in international markets has been increasing since then. One reason for this is that interest rates in the US and other developed countries remained low in the 2010s, and investors seeking higher yields actively purchased bonds issued by developing country governments with higher interest rates. The increase in China's credit was, on the other hand, driven by "One Belt, One Road" initiatives proposed by President Xi Jinping in 2013.

These new sources of external financing are extremely important to support developing countries that have sustained high growth since the 2000s. However, these funds entailed particular risks that were different from those of traditional creditors, including international financial institutions such as the World Bank and members of the Paris Club, like Japan and other advanced Western countries. The interest rates of international bonds are higher than those of concessional financing sources. In addition, the principal repayment tends to be large, with a lump-sum redemption of the principal five or ten years after issuance. These funds are also subject to instability, as changes in the market sentiment can suddenly make it difficult or more costly to issue new bonds. Chinese loans, on the other hand, face significant controversy about their transparency and profitability, as well as the appropriateness of the specific projects that these loans finance.

The new risks brought by the changing structure of creditors were manifested during the post-pandemic period. The case of Sri Lanka, which fell into a debt crisis in April 2022, provides a valuable example. Sri Lanka's economy had been growing at a high rate since the end of the civil war in the late 2000s, but the country also experienced chronic fiscal and trade deficits for many years, even before the COVID-19 shock. Regarding public finances, basic social services such as healthcare and education were provided free of charge, and the country has a large number of ministries, agencies, and state-owned enterprises, which led to structurally oversized government spending. On the other hand, the revenue base, including tax revenue, remained weak. The country's main exports were clothing and tea, while it relies mainly on imports for daily commodities and industrial products, leading to a large deficit in the trade of goods. As a result, the current account balance remained chronically negative, although it was partially compensated by the service trade surplus from tourism.

Despite these fiscal weaknesses and the economy's weak ability to obtain foreign currency, external borrowing from emerging sources of funds progressed steadily in the 2010s. The ratio of central government public debt to GDP increased from 71.6% in 2010 to 101.2% in 2020. What stands out is the increase in the share of external public debt from bond issuance in the international markets: the country issued new international bonds almost every year in the 2010s, and the share of debt from international bond issuance in total external public debt increased rapidly. During the same period, borrowing from the Chinese public and private sectors also increased. These external borrowings did not resolve the structural weakness of the Sri Lankan economy but rather contributed to the preservation of a fragile structure. Since the late 2010s, the weak state of the economy began to show more clearly. In 2017, the country was unable to repay its debts to the Export-Import Bank of China for the development of the Hambantota port in southern Sri Lanka, resulting in a long-term lease of the port's operating rights to China.

The serial bombing incidents in the country in April 2019 and the COVID-19 pandemic after 2020 had a major impact on the country's economy, affecting the tourism sector in particular. As tourism income plummeted, international capital market sentiment worsened, making it difficult to issue new international bonds after 2020. Under these tighter constraints on external borrowing, the only option was to increase domestic borrowing, which normally requires a higher interest payment burden. In addition to the effect of the pandemic, a significant tax cut introduced in 2019 resulted in a sharp decline in revenue in 2020, and interest expenses on public debt rose to 70% of government revenue.

The level of Sri Lanka's foreign exchange reserves has declined rapidly since 2020, with limited new foreign currency inflows. By the end of 2021, its reserve was less than one month's worth of the country's import value. The Sri Lankan government allowed the exchange rate to fluctuate in March 2022, but this did nothing to improve the situation. The country declared a state of emergency in April 2022 and suspended the payment of its external debt.

Similar cases have also been observed in other countries, such as Zambia and Ghana in sub-Saharan Africa. These countries also increased their dependence on borrowing from international capital markets in the 2010s. After the COVID-19 shock, they found it difficult to issue new bonds in the international market, hampering their ability to pay the principal and interest on the external debt they had previously accumulated.

3.3. Consequences of the debt crisis

What are the impacts of government defaults on external public debts on the economy, and what are the consequences for society? First, there will be a depreciation of their currencies and a spike in the inflation rate. The countries will face challenges in procuring goods, especially those that are dependent on imports. Exchange rate depreciation often occurs even before default events. When defaults occur, the credibility of each affected country is further eroded. This accelerates capital outflow and the sell-off of the local currency, leading to further currency depreciation. This results in higher prices for imported products in nominal currency terms, which in turn leads to higher inflation. When foreign currency reserves become physically scarce, the countries may experience problems importing even daily necessities.

In the case of Sri Lanka, the value of their currency depreciated from 200 rupees per dollar before the debt crisis to 360 rupees by mid-2022 after the country defaulted in April 2022. The year-on-year inflation rate reached 72 percent in September 2022. In particular, imports of gasoline and other fuel became constrained immediately after the debt crisis. It was reported that there were long lines of people waiting to refuel at gas stations and sales of gasoline were strictly rationed.[7] Inflation also peaked in Zambia and Ghana after the debt default, reaching up to 50% and 25%, respectively.

Second, after a debt crisis, it becomes difficult to raise additional funds from abroad, especially before the completion of debt restructuring negotiations. The declaration of default on external public debts does not mean that their debts are forgiven. Negotiations between creditors and debtor countries take place to discuss whether or not their payment obligation can be deferred or how much it can be reduced. Debtor countries cannot expect new inflows of money through borrowing or inward foreign investment until the debt restructuring negotiations are concluded. In the past, the main creditors of external public debt, especially those of low-income countries, were public sector bodies, such as governments of OECD countries, and international organizations. Credits often took the form of concessional loans, and their loans often took the form of aid. Debt restructuring negotiations were relatively smooth, as most creditors shared similar positions and ideas. Since the 2010s, however, creditors have become more diverse and now include bilateral lenders such as China, India, and Saudi Arabia, as well as private bondholders. This has made debt restructuring negotiations more complex. After the COVID-19 shock, the "Common Framework" was created to facilitate debt restructuring negotiations among various creditors for the most affected countries. Despite this, negotiations can still take years to reach a conclusion. Such prolonged processes can restrict government access to new financial sources, substantially limiting government spending.

Third, economic restructuring of the defaulting countries is typically carried out in accordance with the economic program agreed upon with the IMF, which also provides financial support. Austerity policies to reduce budget deficits and secure foreign currency are often pursued if the chronic budgetary deficits and foreign currency shortages are the cause of the crisis. These economic restructuring plans were often criticized as "painful" for the citizens of developing countries. The IMF has been encouraging developing country governments to ensure spending continues for vulnerable groups. However, the burden placed on the people tends to be heavier compared to pre-crisis levels, with higher taxes or the reduction of subsidies frequently adopted. This process is often inevitable when correcting the mismanagement of the economy and putting the country back on a stable track.

4. Global Economy and Developing Countries in the Post-pandemic Era: Building Resilience

Since mid-2023, inflation and economic fluctuations in the major advanced economies appear to be subsiding. However, the Russia-Ukraine war still continues and new concerns have arisen, such as the economic downturn in China. In addition to these individual events, it is essential to consider the following factors that will affect the economies of developing countries.

The first factor of concern is the level of global interest rates. For advanced economies in particular, the trend in interest rates is important due to their significant impacts on capital flows to developing countries. In the short term, the US and other major advanced economies will need to determine when to ease monetary policies that were tightened to curb inflation in the post-pandemic period. In the longer term, the funding conditions for developing countries will differ significantly. Much will depend on whether the era of low interest rates in advanced countries during the 2010s returns, triggering an inflow of money to developing countries, or if interest rates will remain high even as the global economy stabilizes after the disruptions resulting from the COVID-19 shock.

The second factor is the extent of the "scar" left by the economic crisis. The scarring effect is related to the possibility of economic losses being sustained by the negative aftereffects caused by the economic recession or crisis, which make it difficult for economies to return to their original growth paths. Particular attention needs to be paid, for example, to the learning losses of children due to school closures during the

[7] The refueling cap was eliminated in September 2023.

pandemic and the loss of skills for workers due to prolonged unemployment, as well as how this will affect the economy in the long term. Such effects may be more severe in developing countries, as they were unable to respond fully to the COVID-19 shock and subsequent economic downturn through fiscal policies and other measures compared to more advanced countries. This could set back a country's potential economic growth and cause extended suffering for the affected individuals. This situation should also be closely monitored from the perspective of human security.

The third factor is the extent to which the behavioral patterns of firms and households will change in the post-COVID-19 era. Various behavioral changes have been observed since the COVID-19 shock, including the relative increase in demand for goods relative services triggered by mobility restrictions, changes in working patterns, such as remote work, and decreases in the labor supply due to voluntary turnover since the pandemic—observed mainly in the United States and other developed countries. There have also been remarkable advances in AI technology over the past few years. These may bring about fundamental changes in future economic activities and industrial structures, not only in developed countries but also in developing countries.

The fourth factor is the extent to which the acceleration of economic blocs and the fragmentation of trade and investment will continue. Since the COVID-19 shock, the fragility of global supply chains has been recognized. Food and energy security risks have emerged in those countries that excessively depend on imports for such products. Buying up of COVID-19 vaccines by some countries sparked another controversy. Attention must be given to the possibility that each country will promote self-centered policies and that anti-globalization sentiment will increase.

Human security is particularly threatened during economic downturns. The words of Sen, quoted at the beginning of this article, also suggest the need to be well prepared for such economic downturns. Drawing lessons from the economic crisis since the COVID-19 shock, it is crucial to emphasize the following as options for developing countries to enhance their resilience.

The first suggestion is the need to pursue sound macroeconomic management and fiscal discipline even during periods of relative stability. Discussions of human security tend to focus on safety nets for individuals, such as health and education. However, the financial resources for such safety nets can only be available when sound and stable economic management is maintained when economic conditions are positive so that governments will be able to respond during times of crisis using the reserves they have accumulated. Another issue observed during the COVID-19 shock and subsequent economic downturn was that a lack of fiscal discipline puts the economy in a difficult position in times of recession. Social spending and protective policies cannot be sustainable if they are implemented without sufficiently considering various macroeconomic constraints, such as revenue and foreign currency availability.

Secondly, there is a need to strengthen risk management practices for public debt. As discussed above, the external financing environment for developing countries has changed significantly since the 2010s, and even in low-income countries, private financing through the issuance of foreign currency-denominated bonds and the importance of new creditors, including China, has increased. Amid the enormous funding needs for development, it is imperative to build a proper debt management capacity where governments pay close attention to interest rate levels and repayment schedules that differ substantially from those of conventional aid funds and contribute to the uncertainties related to the continuous inflow of funds.

Thirdly, opportunities for sustained growth should be created. Stable economic growth is essential for developing countries, many of which still experience high population growth. In the process of development, demand for imported goods tends to increase, and it is necessary to improve their ability to earn foreign currency to meet the import demand. Industrial diversification is vital to enhancing resilience to international price instability. In addition, public investment should be appropriately selected and implemented for projects that can contribute to the improvement of productive capacity.

The role of the international community is also important for maintaining international support mechanisms that can quickly and flexibly assist vulnerable countries and put them on the road to recovery in the event of an economic shock, such as the COVID-19 pandemic. Decision-making on international assistance after the COVID-19 shock was fairly rapid, considering the lessons learned from past crises, and financial support and debt suspension were provided immediately. Issues that require additional consideration include how the international community can work together effectively to support the recovery of countries whose economies have been severely disrupted since the COVID-19 shock and how debt restructuring can be smoothly negotiated. These are significant agenda items from the perspective of human security.

Conclusions

In considering human security, the deterioration of economic activity on which people's livelihoods depend has significant implications. This article examined the characteristics of the global economic crisis since the COVID-19 shock and how it has affected developing countries in particular. It has outlined the prospects and challenges for recovery and resilience enhancement in these countries.

The recent economic crisis as a compounded crisis is characterized by a chain of multiple risks, their mutually reinforcing impacts, a high degree of uncertainty, and related policy dilemmas. Inflation in developing countries is mainly affected by food price hikes. While the degree of inflation varies by region and country, the negative impacts may be particularly high in low-income countries and among low-income social classes and groups. Regarding the debt problem, it is noted that the increase in debt levels after the COVID-19 shock is inevitable. In the rapid changes in the composition of external public debt creditors since the 2010s, multiple countries with fiscal and external sector vulnerabilities experienced difficulties in managing their debts after the COVID-19 shocks.

While there is still much uncertainty about how the global economy will fully recover, developing countries require back-to-basics policies. This entails seeking growth opportunities through quality investment while conducting sound economic management and improving their debt management capacity. The international community also needs to further develop a framework to tackle these enormous shocks through the cooperation of various parties. The crisis triggered by the COVID-19 shock was devastating, but it is essential to learn from the experience and prepare for the future.

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