

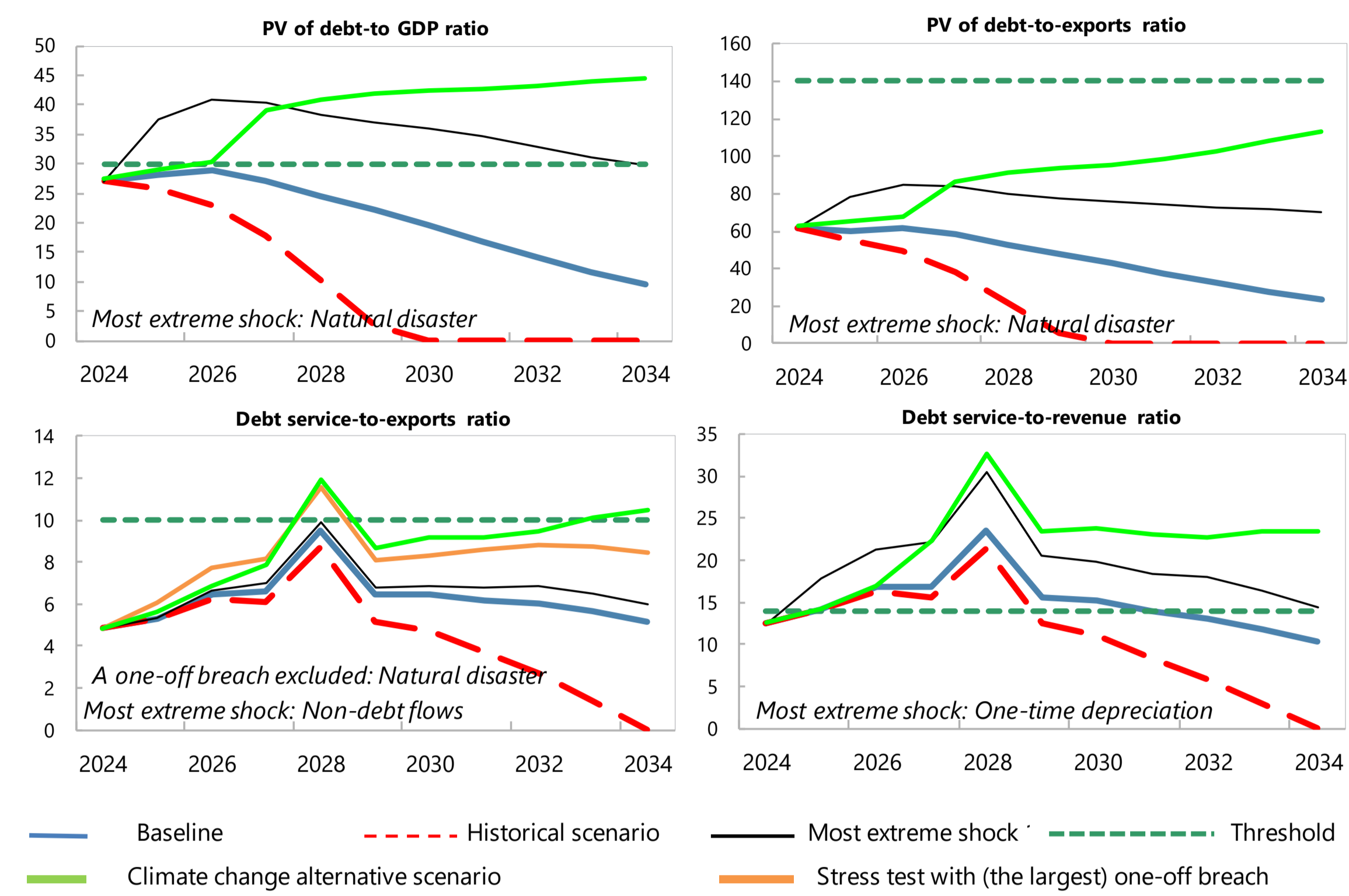
1. Introduction

- The IMF and World Bank's prepares regular joint Debt Sustainability Analyses (DSA) for Low-Income Countries (LICs) to assess debt vulnerabilities and guide borrowing and lending decisions.
- The DSAs coverage of climate risks and policies has been evolving with the increasing recognition of their macro-criticality.
- The 2024 Supplementary Guidance Note (SGN) provided structured guidance on their incorporation in the baseline or in alternative scenarios, and stress tests.
- The SGN also provided guidance for the inclusion of innovative climate finance instruments like green and catastrophe bonds, swaps and CRDCs.

2. Alternative Climate Scenarios in DSAs

SGN introduced a New Climate Change Alternative Scenario feature in LIC-DSF

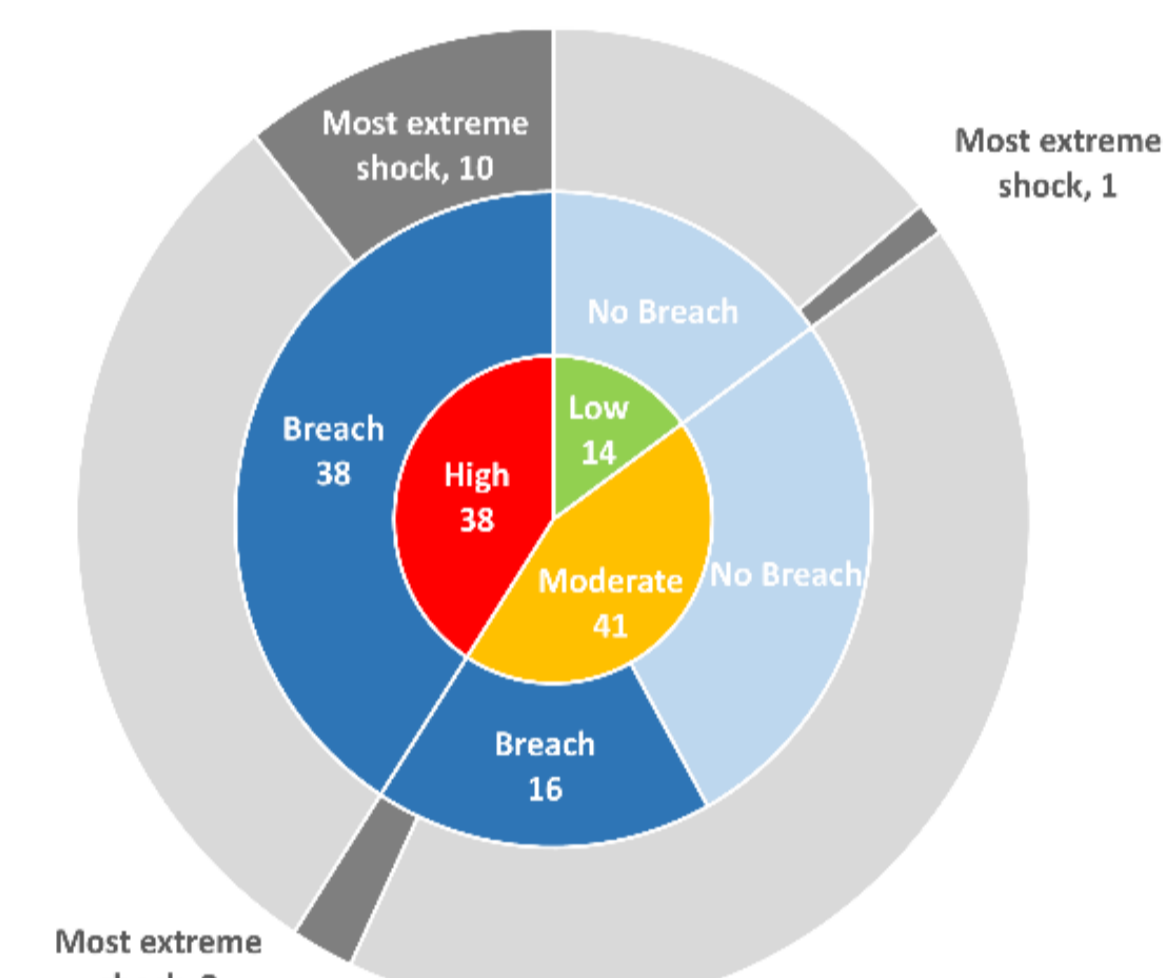
Figure 1: Indicators of Public and Publicly Guaranteed External Debt under Alternatives Scenarios, 2024-2034



3. Main Channels to Capture Climate-Related Debt Risks in DSAs

- The natural disaster stress test is the main channel for capturing climate-related debt risks in the DSA. It is mandatory for the most vulnerable countries and has been used in 40% of DSAs since 2018.
- The second channel extends the time horizon of the risk assessment from the standard 10 to 20 years, allowing more time for chronic climate risks to manifest as late debt threshold breaches, used in 5% of the cases.

Figure 2. LIC-DSAs: Frequency and Mechanical Signal from Tailored Natural Disaster Stress Test by Final Risk Rating, 2018-23 (Number of DSAs)



Source: Staff analysis of joint IMF-WB LIC-DSF country analyses.
 Notes: The 3-level pie chart illustrates the frequency of use of the tailored natural disaster stress test by final risk rating, and within each group whether it resulted in threshold breaches, and if so whether these breaches made the stress test the most extreme among those used in the analysis.

4. DSAs Country Examples

Baseline scenario + extended horizon:

- [Tuvalu](#) – July 2023. Threshold breaches after year 11 of projections.

Alternative Scenarios:

- [Niger](#) – December 2023. Based on Sahel G5 CCDR scenarios.

Customized Natural Disaster Stress test:

- [Benin](#) – March 2024. Incorporates World Bank's CAT-DDO.

[Supplementary Guidance Note](#)

5. Key lessons learned

- Given the challenges in long-term macroeconomic projections, a module for climate change is needed to aid the risk assessment and ensure cross-country consistency.
- The ongoing framework review will also enhance coverage in DSAs of Climate Change risks, adaptation and mitigation investments and policies, as well as new financing instruments.



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