



BANK OF ENGLAND

Special Topic: When sovereigns default, how big a share of government debt is involved?

David Beers¹, Elliot Jones² and John Walsh³

June 2020

Governments do not generally default on the totality of their obligations. More commonly, sovereigns “selectively default” on portions of the debt, and the shares evidently vary over time and across countries. Using historical central government data for most of the 147 sovereigns in the database, this section examines shares of the total stock of government debt in default on a country-by-country basis, outlines how we compile the data, and presents our preliminary findings.

Chart 1 shows the distribution of shares of government debt in default for 141 sovereigns, covering the period 1960 to 2018, a sample of 3,469 observations. For the vast majority, we use data on central government debt drawn from the IMF Global Debt Database (Mbaye, Badia and Chae 2018). In a few cases where those data are unavailable—including Cambodia, Georgia and Mauritius—we use *general government* debt as a proxy because borrowing is largely under the control of the national government. There are also three instances where we use *external* debt as a proxy for central government debt—the Cook Islands, Somalia and Yugoslavia. Almost all the external debt of the Cook Islands and Somalia consists of government borrowings, largely from official bilateral and multilateral creditors. As a centrally planned economy, Yugoslavia’s external indebtedness was closely tied to state control of the foreign trade and banking sectors, mainly reflecting external financing lent by domestic banks to “socialized” or publicly owned enterprises (Fleming and Sertic 1962).⁴

As the chart highlights, the distribution of the shares of sovereign debt in default is skewed towards lower values, with about 72 percent of observations equal to or below 10 percent of government debt.

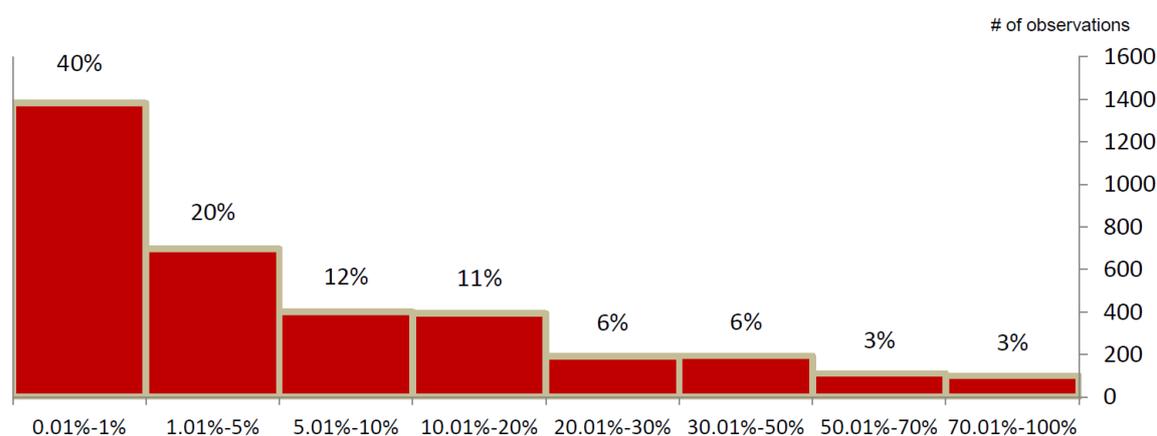
¹ Bank of England. Email: david.beers@bankofengland.co.uk

² Bank of England. Email: elliot.jones@bankofengland.co.uk

³ Bank of Canada. Email: jwalsh@bank-banque-canada.ca

⁴ Adjustments to the data were made to both the debt data numerators and denominators to ensure consistent treatment. For example, IMF loans in arrears for most countries are subtracted from the total sovereign default values since they are made to the central bank, not the government. However, they are included in the default values of monetary union countries where the IMF lends directly to governments. Interest arrears due to private and official creditors (excluding the IMF) are also added to the government debt data when national authorities do not include them.

Chart 1: Distribution of shares of sovereign defaults in government debt, 1960–2018



Percentages shown above the histogram bars refer to shares in the total number of observations.
Source: BoC–BoE database

Last observation: 2018

This confirms the tendency of sovereigns to engage in selective default. Only 48 sovereigns, 6 percent of observations, defaulted on shares of government debt ranging between 50 and 100 percent of the totals.⁵ The largest shares, above 70 percent, have occurred during periods of economic distress (e.g., Mexico, Puerto Rico and Russia) and political conflict (e.g. Angola, Iraq and Sudan).

Shares of government debt in default also appear to be linked to the length of time of defaults. In particular, small amounts in default tend to persist. The average time frame when sovereigns default on 10 percent or less of government debt is about 17 years. This reflects a mix of cases involving “holdout” official and private creditors, as well as new arrears. In contrast, defaults involving 50 percent or more of total debt persist only for about 18 months on average before they decline. Exceptions are countries with extended periods of conflict and countries subject to international sanctions (e.g., Cambodia, Iraq, Somalia, Sudan and Zimbabwe).

In seeking to explain such “selective defaults,” one focus in the literature is on differing governing laws and/or currency denominations of subsets of public debt (Erce and Mallucci 2018). Another is on the treatment of sovereign debt owed to official and private creditors, which often varies (Schlegl, Trebesch and Wright 2019). In cases of defaults involving different types of creditors, the length of time the sovereign takes to resolve defaults can indicate the relative priority given to creditors in each category, and our data do highlight the preferred treatment generally given to multilateral lenders like the IMF and the IBRD. By drilling down further into this new data in future updates of the technical report, we should gain additional insights about these differences in sovereign default dynamics.

⁵ Ten observations in the sample (involving Barbados, Bulgaria, Cambodia, Ecuador, Nicaragua, Somalia, Zambia), representing 0.3 percent of the total 3,469, have values ranging from 100.01 percent to 110 percent, which we treat as equivalent to 100 percent. The reasons for this anomaly include confiscatory currency reform cases, where by convention national statisticians do not count central bank currency as part of government debt, and cases where interest arrears are not counted as part of government debt.

References

Erce, A. and E. Mallucci. 2018. "Selective Sovereign Defaults." Board of Governors of the Federal Reserve System. November. Available at <https://www.federalreserve.gov/econres/ifdp/files/ifdp1239.pdf>.

Fleming, J. M. and V. R. Sertic. 1962. "The Yugoslav Economic System." *Staff Papers (International Monetary Fund)* 9 (2): 202–225.

Mbaye, S., M. M. Badia and K. Chae. 2018. "Global Debt Database: Methodology and Sources." IMF Working Paper WP/18/111. May. Available at <https://www.imf.org/en/Publications/WP/Issues/2018/05/14/Global-Debt-Database-Methodology-and-Sources-45838>.

Schlegl, M., C. Trebesch and M. Wright. 2019. "The Seniority Structure of Sovereign Debt." National Bureau of Economic Research. Working Paper 25793. May. Available at <https://www.nber.org/papers/w25793>.