Global Debt Challenges: Canada's Role in a Complex Landscape

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Issue

The ongoing global debt crisis alongside global macroeconomic turbulence has provided Canada with an opportunity to take a leadership role in debt governance efforts, to advance trade diversification and strengthen diplomatic ties with strategic partners.

Background

The sudden fluctuations in the global economy such as trade disruptions, higher financing costs and shifting foreign policy priorities, particularly under the Trump administration, have resulted in rising debt vulnerabilities. The impacts are felt the most by low-income and emerging economies, whose debt grew increasingly unsustainable, narrowing the fiscal space to invest in basic sectors such as health, education and infrastructure. These constraints are severely stressing political, economic and social institutions. The World Bank (2024a) also adds that the percentage of export earnings used to service interest by 35 developing countries has risen over twice as much since 2015, now equivalent to approximately six percent of total exports, a foreboding indicator of growing debt servicing. While Canada does not necessarily have an interest in most sovereign debt transactions themselves, it does take issue with the implications.

Interconnected economic interdependence means that economic instability in the Global South has real spillover effects for Canada, resonating in trade and supply chains, rendering it difficult to stabilize financial markets, and undermining advances in multilateral climate and development partnerships. Collapse of highly indebted countries' investments in resilience, green transitions and shared prosperity also represents systemic risk to achieving global objectives, to which Canada has high-level ambitions and commitments, for example, the Paris Agreement on Climate Change (Paris Club) and the UN Sustainable Development Goals. The declining trend in US foreign assistance over the longer term has also put pressure on the international development system.

Even though it was never a panacea, USAID had alleviated budget deficits in nations that were already facing shortages and high debt servicing costs. This shift has prompted governments to use borrowing on deteriorating or less-transparent terms, usually with other financiers, adding further to their vulnerability. Although Canada has stepped forward to fill the space with targeted bilateral and multilateral support, the larger international response has not yet discovered the way to bring debtor countries' perspectives and agendas into the broader policy discussion. The result is one in which debt distress is being compounded by geopolitical tensions, fragility and halted progress in development, something requiring a realistic, connected and sensitive response.

Adding to this complexity is the growing involvement of non-traditional creditors. China, now the world's largest bilateral creditor (Chen 2023), is a vital stakeholder in debt governance. Meanwhile, private bondholders and asset managers increasingly hold sovereign debt but are often out of reach of coordinated debt restructuring efforts. As of 2024, private creditors hold US$13 billion more debt than they did in 2022, and many are resistant to engaging in debt relief efforts (United Nations Conference on Trade and Development [UNCTAD] 2024a). In the meantime, 40 percent of low-income countries remain without transparent and comprehensive debt reporting mechanisms, and needs cannot be gauged nor can relief mechanisms be fitted to suit them (ONE Campaign 2024; UNCTAD 2024b).

Domestic Challenges as Foundation for Global Action

Canada has both economic and strategic interests in contributing to this worldwide debt crisis. Unsustainable debt reduces the level of commerce, disrupts supply chains and destabilizes regions vital to Canadian trade priorities and foreign policy. The Caribbean, for example, is not only an economic partner of significant worth, but a critical climate ally. Natural disasters in the Caribbean, such as hurricanes and floods, displace millions of people and deepen environmental challenges. Canada allocated CDN$1.2 million in 2024 for Hurricane Beryl relief, reflecting its role in addressing regional humanitarian needs resulting from climate vulnerabilities (Government of Canada 2024). Besides, a default by one of Canada's trading partners in Latin America, the Caribbean or Africa could adversely affect Canadian exports, Canadian investments and Canadian-based multinational enterprise operations.

Canada's domestic fiscal situation must also be managed carefully. A study by the Department of Finance Canada indicates that the country's federal debt has reached CDN$1.4 trillion as of 2024. Canada faces limitations in expanding emergency grants and concessional loans for poverty reduction development finance because of its own federal debt burden. The humanitarian aid and development finance systems work separately from commercial export credits under Organisation for Economic Co-operation and Development (OECD) rules. Under OECD market-rate terms, the export credits from Export Development Canada (EDC) reach developing nations with CDN$12 billion worth of cleantech-focused credit support (EDC 2023).

Track Record of Innovative Debt Solutions

Canada is in a position to contribute positively to debt management globally. Among Group of Seven (G7) countries, Canada is in the middle-tier position of deficit reduction, providing a sound policy foundation to support sustainable debt reforms. While the federal government aims to reduce its debt-to-GDP ratio from 42.4 percent to 37.9 percent by 2028 (Department of Finance Canada 2024), this excludes provincial liabilities. The consolidated debt-to-GDP ratio of Canada's federal and provincial sectors stands at 107.5 percent. Structural problems persist due to decreasing real GDP per capita from 2022 along with immigration growth that hides unchanging productivity rates (IMF 2024a) while provincial health care and educational expenses have increased provincial debt levels.

Canada's record of international contributions to debt relief and climate finance remains noteworthy. Through the Heavily Indebted Poor Countries (HIPC) Initiative, Canada cancelled over CDN$1 billion in debt and assisted in creating more stable economies. Its support for climate-sensitive development finance has also been broadened. Notably, Canada has committed CDN$5.3 billion for 2021 through 2026 from its climate fund to cover initiatives such as Ghana's green energy upgrade and Indonesia's rehabilitation of mangrove forests (Government of Canada 2024).

Presently, Canada uses lending financial tools such as Climate Resilient Debt Clauses (CRDCs) in loan packages to Moldova and Guyana. These measures allow countries to delay debt repayment during climate crises (Department of Finance Canada 2025). EDC has raised CDN$4.2 billion in green bond sales since 2014 to fund 47 renewable energy projects, which indicates Canada's commitment to linking debt financing with climate action (EDC 2023).

Structural Barriers in Debt Governance

Multiple structural challenges affect the current debt governance architecture, including fragmented creditor coordination, lack of binding frameworks for private sector participation and inadequate information-sharing mechanisms. The majority of non-Paris Club creditors have not implemented debt relief promises. Just 51 percent of committed assistance has been activated by 2025, a rate slowing down and delaying restructuring for countries like Zambia and Sri Lanka (IMF 2025). Furthermore, there are no legally binding frameworks to compel private creditors to follow a coordinated relief process. Without global guidelines or incentives, the rate continues to lag and become uneven.

Previous international debt initiatives have frequently fallen short of their objectives. The HIPC and Multilateral Debt Relief Initiatives, while providing over US$100 billion in debt relief to 37 countries (World Bank 2024b), failed to prevent renewed debt accumulation in many cases. Post-relief analyses reveal that 11 out of 13 HIPC countries experienced deteriorating debt-to-export ratios due to structural economic challenges and new borrowing (IMF 2025). The Debt Service Suspension Initiative, introduced during the COVID-19 pandemic, exacerbated inequities by excluding 18 small island developing states and 48 upper-middle-income countries from eligibility, despite their acute vulnerability to climate and economic shocks (European Network on Debt and Development 2020).

Similarly, the Group of Twenty's (G20's) Common Framework for Debt Treatments has been criticized for slow implementation, with many countries hesitant to apply due to concerns about credit rating impacts and creditor treatment. These historical precedents suggest the need for measured expectations about what new initiatives might achieve (UNCTAD 2024b).

Opportunities for Systemic Reforms

This is where Canada's future presidency in 2025 presents a meaningful opportunity for leadership. As host, Canada can lead a continued and enhanced agenda on transparency, equity, and climate resilience in sovereign debt markets. This could include advocating for the universal adoption of CRDCs as a component of all bilateral and multilateral loan agreements, encouraging the adoption of transparent debt reporting frameworks, recognizing the sovereignty concerns and capacity constraints that may affect implementation, and leveraging its pension reserves of CDN$1.4 trillion to use climate-debt swaps via the contemplated global debt-climate facility (World Bank 2024a).

Such initiatives would not only be a source of critical support for nations facing debt distress but also be in Canada's long-term interests. Stable, economically vibrant partner states are a more viable market for Canadian goods and services and key allies in addressing shared global challenges. They are a more effective force to work with on common problems such as reducing climate change, resettling refugees and peacekeeping in their area.

While these opportunities exist, it is important to recognize the complexity of debt governance reform. The reality is that transforming debt governance requires navigating a complex web of competing interests, including those of private creditors who may resist coordinated restructuring efforts.

Overall, although the international debt crisis presents complex challenges for the global community, it also presents an opportunity for Canada to advance a principled and pragmatic leadership agenda. Canada can contribute constructively to evolving debt governance reform. The present moment calls for a forward-looking policy approach that supports sustainable debt management while safeguarding Canada's economic and geopolitical interests.

Recommendations

Leveraging debt support mechanisms to diversify trade. Ongoing diplomatic and economic tensions with the United States have placed a strain on the Canadian economy, particularly given the United States' status as Canada's primary trading partner. Geographical proximity and global trade patterns have traditionally necessitated close economic integration between the two nations, complicating efforts to diversify Canada's trade portfolio. Concurrently, the United States is scaling back its foreign and humanitarian aid commitments and reassessing its international trade engagements. This global shift presents an opportunity for Canada to assert leadership by expanding its economic relationships, particularly with countries experiencing debt distress. By aligning trade diversification with debt support initiatives, Canada can cultivate new markets for its goods and services, notably in sectors less reliant on physical goods, such as financial services, e-commerce and digital technologies. Redirecting debt support mechanisms to align with Canadian economic interests can position Canada as a dependable development partner and promote the "Made in Canada" brand. This approach not only supports Canadian economic resilience but also upholds Canada's commitment to international development. Collaborating with initiatives such as the Bridgetown Initiative, which advocates for sustainable and equitable debt governance, could enhance Canada's global leadership in debt-related development assistance.

Enhancing Canada-Europe relations through collaborative debt relief initiatives. Considering the recent unpredictability in US foreign policy, it is increasingly critical for Canada to reinforce its alliances with other strategic partners, particularly European nations. Effective global debt governance depends on robust international collaboration, especially within multilateral lending frameworks. The G20's Common Framework for Debt Treatments provides a platform for coordinated debt restructuring by engaging all relevant creditors and debtors. This initiative draws heavily from the principles of the Paris Club, of which both Canada and several European countries are permanent members. By deepening its cooperation with European partners in these debt-restructuring and relief mechanisms, Canada can simultaneously strengthen transatlantic ties and contribute to more effective global debt solutions. Joint investments in data infrastructure and transparency initiatives related to sovereign debt are one example of a practical steps towards more efficient and equitable debt governance.

Rebuilding bilateral relations with China through joint debt relief mechanisms. Canada's diplomatic relationship with China has been strained in recent years due to a series of geopolitical tensions. However, as the United States increasingly undermines established global governance norms, it is imperative for Canada to recalibrate its relationships with other major powers. China has emerged as the world's largest bilateral creditor and is, therefore, a pivotal actor in any future framework for global debt sustainability. Notably, China's preference for extending new loans contrasts with the debt relief strategies employed by Canada, the European Union and other Western creditors, which often involve partial debt forgiveness (Chen 2023). These divergent approaches have hindered consensus on comprehensive debt relief strategies. Nevertheless, innovative mechanisms such as debt-for-nature swaps and investments in sustainable development may offer common ground, especially given China's growing engagement in global climate governance (Lewis 2024). Canada should play a leading role in advancing pragmatic, inclusive debt governance solutions within the G20's Common Framework for Debt Treatments, which could also provide a constructive avenue for rebuilding mutual trust in Canada-China bilateral relations.

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