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The Product Of All Fears: IMF's USD GDP Forecast Quality During EM Bond Restructurings

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Both in the academic literature and in private conversation with official sector representatives, one finds the notion that IMF tends to err on the side of optimism when making projections for its programs[1]. Thus, when creditors envision more growth, exports or FX appreciation than IMF does, they are charged with engaging in self-interested "wishcasting", which risks tipping the freshly-restructured obligor into a dreaded double-dip crisis. Meanwhile, IMF DSAs explicitly crafted to frame restructuring negotiations often include *sui generis* "buffers" meant to account for specific weaknesses of the patient in question. Creditors are left feeling like they are up against double jeopardy: cautious economic forecasts that are portrayed as generous; sandbagged DSAs handed down as unappealable fiat and not modified for multiple review cycles. Is it any surprise, then, that restructuring advisors have reached for a proliferating menagerie of contingent instruments, warrants and macro-linked bonds that no one is much pleased with?[2]

To make better decisions in the future and negotiate optimally, bondholders must examine the past first. To that end, I turn to the single most important variable for external creditors: the level of nominal, USD-denominated GDP 5 years ahead, i.e. at the LIC DSA forecast horizon. Multiplied by a coefficient set by the IMF, it determines the envelope of cashflows "available to service foreign debt". As the denominator in external-debt-to-GDP, it frames the optics of a restructuring as "generous to bondholders"[3], if the ratio seems high at the end of the forecast horizon due to pessimism about GDP.

How does the Fund do at forecasting it? To answer, I have looked at every restructuring event in the Asonuma and Trebesch default event database[4] for which there was an IMF report published just before or, if not available, just after the commercial debt exchange operation. I extracted the 5-years-ahead nominal, USD-denominated GDP forecast, and compared it to either the realization (for deals closed in 2018 and earlier) or latest available IMF forecast in the April 2024 World Economic Outlook database.

The results are shown in Table 1. The restructuring-time projections understated the USD GDP level by an average of **28%**. By count, 14 of the 18 forecasts (**78%**) were too pessimistic. The margin of error does shrink in the more recent era but remains very substantial and consistent in direction.

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[1] Aldenhoff, Frank-Oliver. "Are economic forecasts of the International Monetary Fund politically biased? A public choice analysis". The Review of International Organizations". 2007.
[2] Buchheit, Lee and Gregory Makoff. "A sweeter sovereign debt restructuring sweetener". Financial Times. 2024.
[3] Maret, Theo and Brad Setser. "Is the IMF setting Sri Lanka up for a second car crash?". Financial Times. 2023.
[4] Asonuma, Tamon and Christoph Trebesch. "Sovereign Debt Restructurings: Preemptive or Post-Default". Journal of European Economic Association. 2016. (Database updated by authors 2020.)

Table 1

country	document date	target year	original 5y forecast	realization / last forecast	error
			$ bil	*$ bil*	*%*
Argentina	2020-03-19	2025	570	559	-1.9%
Belize	2019-11-12	2024	2.4	3.3	38.9%
Ecuador	2020-04-29	2025	115	124	8.0%
Barbados	2019-11-27	2024	6.3	6.9	9.3%
Mozambique	2019-05-15	2024	24	23	-5.1%
Belize	2016-06-15	2021	2.2	2.5	14.5%
Mongolia	2017-04-23	2022	14.6	16.8	15.3%
Ukraine	2015-07-22	2020	138	157	13.7%
Grenada	2015-11-10	2020	1.2	1.0	-14.9%
Belize	2013-06-05	2018	2.0	2.3	14.9%
Ivory Coast	2012-04-26	2017	38	52	37.9%
Greece	2012-03-09	2017	294	200	-32.2%
Seychelles	2009-12-04	2014	1.2	1.4	17.1%
Grenada	2005-05-24	2010	0.7	0.8	18.5%
Argentina	2005-05-31	2010	247	425	71.7%
Uruguay	2003-06-27	2008	16.2	33.0	104.2%
Moldova	2002-06-26	2007	2.5	4.4	73.3%
Ukraine	2001-08-31	2006	48.9	107.8	120.3%
				average	28.0%

Forecasting under the “fog of war” of a crisis nadir is understandably challenging. A degree of caution is to be expected. With that conceded, the bias here is so clear and significant for creditors that, at a minimum, the official sector must accept that bondholders will insist on contingent mechanisms to improve recovery values if reality once again predictably exceeds the Fund projections. Considered more broadly, I do not think that such a tilt facilitates the good faith, transparent negotiations that must always occur to achieve mutually beneficial resolutions of default episodes.

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