

Global Sovereign Debt Roundtable

Liability Management Operations: A Practitioner's Manual

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Introduction

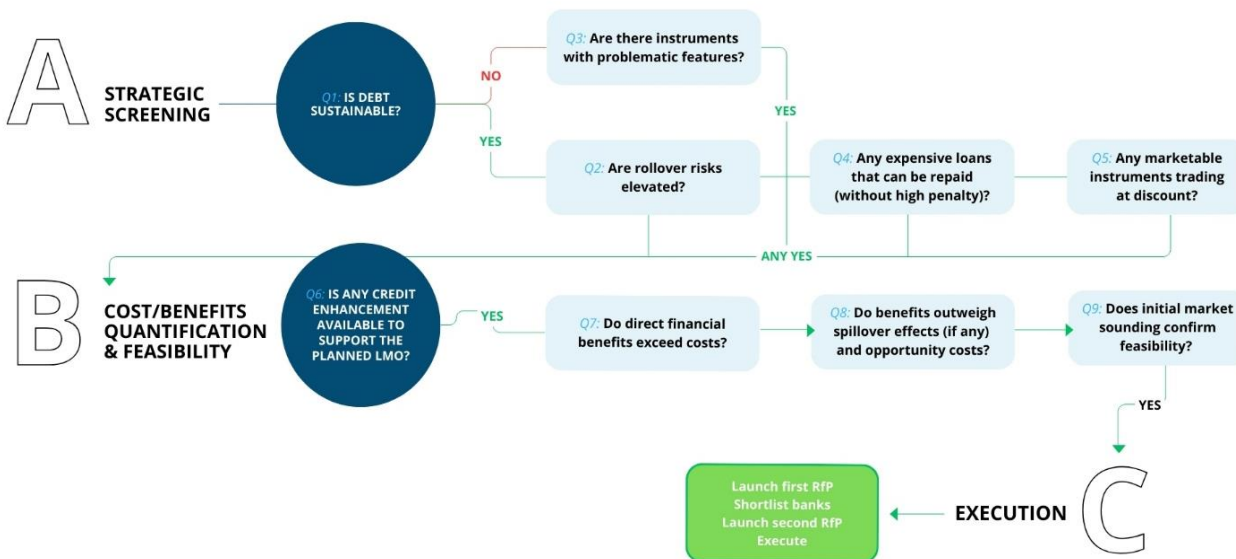
This document provides practical guidance for policymakers and debt managers on assessing the feasibility and implementing liability management operations (LMOs) supported by credit enhancements (CEs).¹ It serves as a step-by-step practical manual, drawing on lessons from recent LMOs and the results of a survey on CE availability conducted among major multilateral providers.

The guidance is intended to support decision-making but should be applied with due consideration to country-specific circumstances, constraints, and policy objectives.² The document, published as a GSDR Coauthors document, is non-binding and will be updated periodically to incorporate new insights and evolving practices that further facilitate the effective use of LMOs.

Practical Steps

Credit enhancements can significantly increase the effectiveness of LMOs by compressing borrowing costs, extending maturities, and broadening or strengthening investor demand. However, their impact can vary significantly based on the characteristics of the debt repurchased and the type of CE applied, and their implementation is neither automatic nor without costs and risks. Therefore, authorities should first perform a thorough analysis. Figure 1 summarizes the key decision and implementation steps:

Figure 1 – LMO with CEs: Decision and Implementation Framework



¹ LMOs are market-based transactions used to improve the cost-risk profile of public debt, through exchanges, buybacks and similar operations. Credit enhancements (CEs) are third-party instruments, usually provided by MDBs or bilateral creditors - such as guarantees or insurance - aimed at improving the terms of new debt instruments.

² For additional background on LMOs (with or without credit enhancement) see: IMF (2007) "A Primer on Sovereign Debt Buybacks and Swaps". IMF (2018) "A Primer on Managing Sovereign Debt-Portfolio Risks."

Stage A – Strategic screening

Strategic screening stage combines an assessment of debt sustainability and macroeconomic adequacy with a review of the debt portfolio. It determines whether an LMO is warranted, not appropriate at this stage, or requires further analysis, and provides an initial indication of potential objectives (e.g., cost reduction, risk management, liquidity relief) as well as the possible scope and instruments.

The first step is taking stock of the country’s debt sustainability and the adequacy of its macroeconomic policy framework (Q1). LMOs are generally not appropriate when a country’s debt situation is such that a comprehensive debt restructuring is required to restore sustainability. Moreover, CEs are often restricted to countries that meet certain credit or debt sustainability analysis (DSA) criteria, and where the macroeconomic policy framework is deemed credible. Finally, LMO conducted in distressed scenarios may also trigger rating action (see Annex 1). An exception may arise when the LMO is used to prepay specific instruments that might delay or complicate future restructurings (Q3).³

In a country where liquidity - rather than solvency – is the main concern, a LMO supported by a CE can be effective in several scenarios. A standard case is when a country faces significant roll-over risk or debt service spikes (Q2) and may benefit from the LMO to bridge the funding gap at lower cost or smooth the debt profile. For countries that have market access and sufficient resources to meet upcoming debt service obligations, LMOs can also be leveraged for opportunistic reasons—for example, to remove instruments with problematic legal or financial features from the portfolio (Q3)⁴ or – more commonly – to take advantage of the favorable conditions granted by the CE compared to existing loans (Q4) or bonds (Q5). In those cases, an instrument-by-instrument analysis of the existing debt portfolio is a crucial step. WB or financial advisors can offer technical assistance to help identify the instruments that offer the greatest potential for cost-savings and debt sustainability improvements, complementing the broader debt management capacity development support available from IFIs.

The above rationales are distinct yet may reinforce one another. For example, a country experiencing liquidity risk is likely to see its marketable debt pricing impacted. The existence of at least one strong rationale may justify advancing to Stage B.

³ Though care must be taken when replacing it with more senior debt (Q8).

⁴ For example: collateralized debt, long-standing arrears, bonds without CAC or illiquid. Authorities should be cognizant that CE-backed instruments used to replace problematic debt may carry de facto seniority — see Q8.

Stage B – Cost/Benefit Quantification and Feasibility

The cost/benefits and feasibility stage assesses the availability of credit enhancements and quantifies the financial and operational implications of a potential LMO. It evaluates whether expected benefits outweigh costs and risks, considers spillovers and opportunity costs, and tests feasibility through initial market sounding, providing a basis for deciding whether to proceed to execution.

Authorities should first assess the existing CEs available (Q6) which are typically provided by official sector creditors. Many of the major Multilateral Development Banks (MDB) offer credit enhancement products with varying conditions (see Annex 2 for survey results), as well as several bilateral creditors.⁵ MDBs typically impose regional, risk or income-based eligibility criteria. Additionally, many CE providers place restrictions on how proceeds can be used, such as whether they may support LMOs, refinancing or debt-for-development (D4D) swaps.⁶ They might also set guidelines regarding currency selection and instrument types, so these conditions should be addressed early in the process.

A fundamental prerequisite is that the LMO generates direct savings, both in nominal terms and net present value (NPV) terms (Q7). Practical steps involve calculating the cash flows—including principal, interest, and fees/commissions—for both the existing⁷ and new (guaranteed) debt in a consistent currency. The difference in total debt service yields the nominal savings, which should be assessed within a limited time horizon (such as 3 or 5 years) to mitigate the impact of the different time distribution of the cash flows.⁸ A second key metric is NPV savings, calculated by discounting each set of cash flows using the sovereign yield curve relevant to each instrument's duration. In situations where reliable market benchmarks are unavailable, a single discount rate (e.g., the marginal cost of borrowing) may be applied to both streams.⁹

Some costs and benefits of an LMO with CE are not fully captured in the direct saving calculation. Estimating indirect cost and benefits (Q8) is a crucial step in determining whether to move forward with the transaction. The key ones are the following:

- (1) *Alignment with debt management strategy.* The LMO should support, not undermine, the medium-term debt strategy and market development objectives (e.g., share of domestic vs. external debt or development of a liquid domestic market).

⁵ E.g.: Bpifrance Assurance (France), DFC (US).

⁶ Specific guidance on debt-for-development swaps can be found in the [WB/IMF 2024 framework](#).

⁷ Should the operation facilitate a roll-over without buying back existing debt, a counterfactual scenario can be designed based on borrower's unguaranteed cost of borrowing.

⁸ Note that the duration of the two cash flow streams may differ—typically, the new instruments have a longer maturity; therefore, additional interest payments corresponding to the counterfactual scenario of a standard roll-over should be incorporated into the original cash flows for accurate comparison.

⁹ NPV savings should reflect the value of the CE and measured against the total direct and indirect benefits of the operation. Any LMOs must be at least NPV neutral.

- (2) *Risk of rating action.* The LMO can reduce refinancing risk and borrowing costs, hence possibly improving ratings, but it may be also viewed negatively, if perceived as distressed by CRAs or signaling refinancing difficulties. Early communication with credit rating agencies is therefore important. See Annex 1 for more details.
- (3) *CEs' opportunity cost.* Where the CE draws on an MDB's capped country allocations, its use entails an opportunity cost. Authorities should therefore assess which alternative operations (e.g., policy lending or investment projects) would be displaced and compare their value against the expected benefits of the LMO. Leveraged operation (such as the WB's PBG that accounts up to 1:4 on the country allocation) can reduce but not eliminate the opportunity cost.
- (4) *DSA impact.* A saving-generating LMO - in principle - is expected to improve the DSA. Yet, authorities should simulate the transaction's impact on the DSA by comparing projected cash flows of the old and new debt over the relevant horizon, with particular emphasis on whether the operation reduces breaches of liquidity thresholds. This analysis informs both the potential benefits of the LMO and the tailoring of the redemption profile of the new debt. The DSA simulation is particularly critical when swapping domestic debt with external one, and where tradeoffs related to improving solvency vs liquidity indicators are present.
- (5) *Change in seniority.* Authorities should also consider the implications on credit seniority if the CE is called, including the possible reduction of the restructurable perimeter, as the guaranteed portion may effectively displace debt that would otherwise be available for restructuring.

It is essential to confirm funding assumptions—both pricing and volumes—through an initial market sounding. Engaging with potential investors early via market soundings (Q9) helps minimize execution risks and provides the flexibility to postpone or even cancel the transaction if conditions are unfavorable. Market soundings also offer an opportunity to gauge market timing and identify the optimal group of investors to target, which streamlines the subsequent execution phase. The CE provider or the DMO's financial advisor are typically best positioned to connect with final investors.

Advisory services can optimize the cost and risk profile of the operation. Financial advisors can strengthen the LMO value proposition by leveraging their relationships with investors, CE providers and other stakeholders¹⁰. Legal advisors offer critical guidance, particularly when authorities' legal counsellors lack expertise in LMOs' contracts. It is important that any ad-hoc mandate with advisors is established according to transparent criteria aligned with the requirements of the LMO.

¹⁰ Including, for instance, private foundations or philanthropies that may be interested in funding D4Ds.

Stage C – Execution

The execution stage implements the LMO, including transaction design, engagement with advisors and creditors, and the launch and completion of the operation. It translates the identified objectives and structure into a market transaction, along with effective coordination, communication, and risk management throughout the process.

The first step of the LMO execution is the launching of a Request for Proposals (RfP) among multiple potential investors for the new financing¹¹. A competitive process – usually managed by the DMO or its financial advisor - is a very effective mechanism for achieving optimal pricing and terms. Regular engagements with market participants, including through non-deal roadshows - are effective ways to identify potential investors. Before the RFP is launched, the borrower must develop a clear narrative to be presented to investors/lenders. This involves articulating how the transaction fits within the debt strategy, and how it strengthens the issuer’s credit profile.

Clear and precise transaction parameters are essential to obtaining the best possible terms. The key terms – summarized in Term Sheet - typically include the following: size of the financing, tenor, base rate (fixed or floating) currencies, CE’s coverage level, pricing, and any legal/regulatory constraints. While it might be strategic to maintain flexibility on certain terms (for example on currency or base rate options) to optimize final terms, leaving too many variables open can be detrimental. If the RFP is too vague, investors/lenders may struggle to provide firm underwriting¹², and the borrower might be unable to compare the offers. The borrower should, therefore, clearly define the core financial parameters while allowing for some flexibility on the less critical ones. The CE’s legal structure should be clearly specified upfront, as any ambiguity will ultimately be reflected in pricing offers, resulting in higher costs.

Appropriate information sharing mechanisms should be ensured throughout the RfP process. It is important for the DMO or its financial advisor to design a Q&A and an investor relation strategy that provides investors with all possible clarifications in a timely manner, as they work on structuring their offers and obtaining relevant approvals. This helps prevent misunderstandings of key transaction terms that could later delay or derail execution.

A structured selection process should allow the issuer to refine terms while ensuring competition. In most cases, it is helpful to have a two-step process, where the top 2-3 bidders are shortlisted into a second round. This allows the issuer to clarify terms, harmonize the specific requests of the different investors, and ensure the best possible outcome. It is, however, important not to drag the process for too long, given that pricing and other terms in the offers have a certain validity period (usually 90 days). A well-managed RfP process can generally be completed within approximately four weeks, end to end.

¹¹ In the range of 10/12, typically large international commercial banks or institutional investors/asset managers.

¹² Investors can choose to underwrite 100% of the amount of the loan or bond, i.e., providing the full amount of loan at the indicated terms, irrespective of whether the investor intends to keep the full loan amount on its books (hold), or to subsequently syndicate it (selling part of the loan to other investors).

Selection should depend on an “all-in” cost analysis to provide an accurate comparison of the offers. Investors often have different ways of presenting their offers, and often have different fee types and structures, which should be evaluated on an “all-in cost” basis. The spread compression - relative to the unguaranteed yield - is a useful metric to consider. However, non-price considerations - such as execution capability, track record with similar types of transactions or in similar jurisdictions – should be factored in.

A smooth execution requires scrutiny of clauses that may result in less favorable terms once an investor is selected and mandated. While pricing remains the most critical element, investors need to be able to stand by it. Accordingly, the issuer must carefully review and negotiate any language that allows investors/lenders to change the price or terms if market conditions change.¹³ Moreover, the issuer must clarify the banks’ underwriting strategy, for example what percentage would be underwritten, hold levels, expected syndication strategy, and whether the indicative pricing is “subject to syndication” or is on “best efforts” basis.

Once secured, the new funds are used to ensure repayment of maturities falling due or implement LMOs targeting bonds or loans. Loan prepayment is operationally more straightforward since contractual clauses typically offer prepayment options, and the borrower is required only to notify the creditor. The amount consists of the loan outstanding balance, and any prepayment fees or accrued interest. Required budget provisions and proper debt recording should be planned to ensure transparency and compliance with domestic and international accounting and reporting standards. Any indemnity agreement signed as part of the CE should be reported publicly.

For bond buybacks or switches, reverse auctions or tender offers are the most common methods. A reverse auction is an operation in which the sovereign announces its intention to buy existing instruments and investors bid at their preferred prices. The government sets the target (amount, eligible bonds, price caps, single vs multiple price auction), and market participants compete to sell. However, to limit placement risk, both types of LMOs can also be conducted through a standing offer to purchase (or exchange) the bond at prices either fixed or defined through a bookbuilding process. These transactions can be conducted through the fiscal agent or through a market intermediary acting on behalf of the issuer. It is important to note that markets may move unfavorably for the issuer following the announcement of such a transaction. The final buyback price of the bonds- at a premium relative to prevailing secondary market levels - will depend on the size of the targeted amount, reflecting the marginal premium required by investors.

Credit-enhanced LMOs are a powerful tool to support the WB-IMF three-pillar approach. When well designed and anchored in a credible macroeconomic and debt management framework, they can strengthen a sovereign’s debt profile. However, they are not suitable in all cases and should be used selectively, transparently, and based on rigorous analysis to ensure durable gains aligned with long-term sustainability.

¹³ For example, “market flex” clauses allowing investors to change price post-selection, if the original price does not clear.

ANNEX 1 - Information sharing and dialogue with credit rating agencies (CRAs)

LMOs, with or without CE, increase debt managers’ toolkit and can help support CRAs’ ratings if conducted transparently and in line with a credible strategy as part of active debt management. Despite some methodological differences (see table below), CRAs typically deem an LMO or exchange “distressed” when it signals the sovereign cannot or would not meet its original obligations and when creditors receive reduced value compared to original terms.

Across all three agencies, a proactive engagement can help clarify considerations and circumstances around avoiding respective distressed exchange classifications. An early, transparent engagement with CRAs, clear articulation of the policy rationale, evidence of continued market access or alternative financing, and transaction design that avoids coercive features, is considered useful information by CRAs. Providing CRAs with timely cost-risk analysis, DSA implications, and investor-feedback may help reinforce the non-emergency nature of the operation. Treating CRAs as key stakeholders - through regular updates, and prompt responses to data requests - reduces the risk of unexpected outcomes.

CRA	Core Criteria - Distressed Exchange	Key Indicators Used	Implications
S&P	<ul style="list-style-type: none"> - An exchange is distressed when , in the absence of such an exchange, the issuer is likely to default in a conventional manner. and - When investors receive less value than originally promised, including if coupons appear lower or maturities longer. 	<ul style="list-style-type: none"> - Evidence of financing pressure or lack of market access. - Exchange appears forced or motivated by upcoming maturities the sovereign cannot meet. - Economic loss to creditors. - Unclear alignment with market pricing. 	<ul style="list-style-type: none"> - Classified as a Selective Default (SD) until future payments normalize. - Local or Foreign Currency CY or FCY ratings may be temporarily set to SD.
Moody’s	<ul style="list-style-type: none"> - An exchange is distressed when it results in diminished value relative to the debt obligation’s original promise for creditors; and - has the effect of allowing the issuer to avoid a likely eventual default, for instance amid liquidity or solvency stress. 	<ul style="list-style-type: none"> -Sovereign faces heightened liquidity or solvency pressures, typically indicated by elevated yield levels or a low rating level. - Market access is limited or has deteriorated; high rollover risk. - Exchange part of a broader restructuring or undertaken near payment deadlines. 	<ul style="list-style-type: none"> - Typically classified as an event of default under Moody’s definitions once exchange is completed.
Fitch	<ul style="list-style-type: none"> - There is a material reduction in terms¹⁴; and 	<ul style="list-style-type: none"> - Material reduction in terms: principal, interest, maturity, currency, payment 	<ul style="list-style-type: none"> -Leads to a Restricted Default (RD) rating. A

¹⁴ Unless it can be clearly shown that creditors would likely be indifferent between the old and new terms.

	<ul style="list-style-type: none"> - The exchange is designed to avoid a traditional payment default. 	<ul style="list-style-type: none"> form, or coercive indenture amendments - Whether non-participating creditors continue to be serviced on original terms - Maturity profile, volume, and price of debt exchanged - Whether the sovereign could have met original obligations without the exchange 	<ul style="list-style-type: none"> forward-looking rating based on credit fundamentals is applied once the exchange is concluded. .
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Source: CRAs' websites

ANNEX 2 – Mapping of existing CEs by MDBs

TO BE FURTHER COMPLETED BASED ON ADDITIONAL SURVEY RESULTS

Dimension	What Should Country Authorities Check?	ADB - Credit Enhancement Products	AfDB – Partial Credit Guarantee	AIIB – Partial Debt Guarantee	IDB – Policy Based Guarantee (PBG)	WB – Policy-Based Guarantee (PBG)
1. Eligibility & Macroeconomic Conditions	<ul style="list-style-type: none"> • Does my country meet general eligibility requirements? • Does my country meet risk requirements? 	Developing member country (DMC) of ADB Debt sustainability assessed during processing	All regional member countries depending on DSA rating	All AIIB members are eligible.	All borrowing IDB member countries are eligible,	Available to eligible IBRD/IDA borrowers. Requires moderate risk rating under DSA
2. Opportunity Cost & Leverage	<ul style="list-style-type: none"> • Does the guarantee use country allocation or other scarce capacity? • Can allocation be leveraged (e.g., 1:4)? 		Uses country allocation. \$1 of allocation can support up to \$4 of guarantee for ADF.		Uses country allocation. \$1 of allocation can support \$1 of guarantee.	Uses country allocation. \$1 of allocation can support up to \$4 of guarantee.
3. Indemnity & Fiscal Implications	<ul style="list-style-type: none"> • Is a sovereign counter-guarantee or indemnity agreement required? 	Optional sovereign indemnity agreement.	Requires sovereign indemnity agreement.	Requires sovereign indemnity agreement.	Requires sovereign indemnity agreement.	Requires sovereign indemnity agreement.

4. Risk Coverage & Structure	<ul style="list-style-type: none"> • What risk is covered? • Is coverage partial or full? 	Non-payment risk and political risks Up to 100% coverage.	Non-payment risk. Partial coverage (no min or max).	Non-payment risk. Up to 100% coverage.	Covers non-payment risk. Partial coverage (no min or max).	Non-payment risk. Partial coverage (40 - 60%).
5. Eligible Instruments & Currency	<ul style="list-style-type: none"> • Can the guarantee apply to FX bonds, loans, or local currency instruments? 	Either local currency or FX-denominated loans or bonds.	Either local currency or FX-denominated loans or bonds.	Either local currency or FX-denominated loans or bonds.	Either local currency or FX-denominated loans or bonds.	Typically FX-denominated instruments.
6. Pricing & Timeline	<ul style="list-style-type: none"> • How are fees determined (rating, tenor, size)? • What is the expected approval timeline? 	With counter-indemnity: policy-based pricing. No counter-indemnity: based on credit risk. Timeline varies.	Guarantee Fee = Lending Margin for AfDB and Service Charge for ADF Typically ~9 months.	- With sovereign indemnity: AIB pricing policy and decision. Typically ~6 months.	Flat fee. On average, a range between 9-24 months (timelines vary widely)	Fees based on IDA/IBRD pricing framework. Typically ~6 months.

Source: Credit enhancement survey carried out among IFIs and bilateral creditors in February-March 2026.