Global Debt is Becoming the Next Constraint on Economic Policy

Key Takeaways:

- Global public debt is no longer only a balance-sheet issue. It is increasingly becoming a direct constraint on how governments respond to future shocks.
- The IMF estimates that global government debt rose to nearly 94% of GDP in 2025 and could approach 100% by 2029, a level previously seen mainly after World War II.
- Interest payments have risen from around 2% to nearly 3% of global GDP in just four years, reducing room for public investment, welfare, infrastructure, defense, and climate adaptation.
- Geopolitical tensions are increasingly transmitting into fiscal pressure through higher oil, LNG, and food prices, weaker economic activity, tighter financial conditions, and rising subsidy burdens.
- The next phase of fiscal policy is likely to depend less on broad stimulus and more on targeted support, credible medium-term planning, and market confidence.

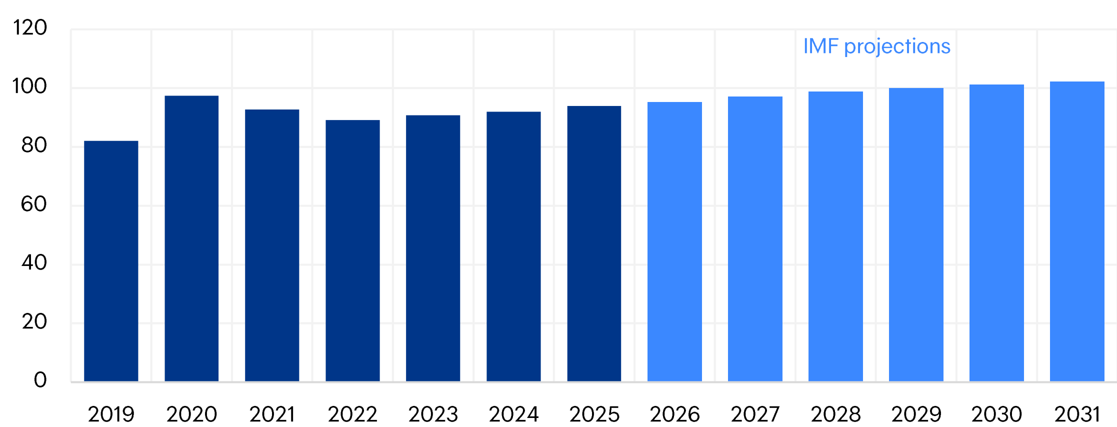
High Debt Leaves Governments with Less Room to Move

The global economy is not facing a shortage of spending needs. It is facing an increasing shortage of fiscal flexibility.

The IMF's April 2026 Fiscal Monitor shows that global public finances remain under pressure even after the pandemic and earlier energy shocks have faded. Global gross government debt climbed to 93.9% of GDP in 2025, while the global fiscal deficit remained broadly unchanged at around 5% of GDP. Under current trajectories, public debt is projected to approach 100% of GDP by 2029, a threshold previously reached mainly in the aftermath of World War II.

The challenge is not simply that debt levels are high. Public debt is still rising while governments face a growing list of structural spending pressures. Aging populations, defense commitments, climate investment, energy security, industrial policy, and rising healthcare costs are all pushing expenditures higher. At the same time, many of the fiscal buffers built before earlier crises have already been depleted.

General Government Debt (Percentage of GDP)



Source: IMF, *Fiscal Monitor*, April 2026.

This is steadily changing the role of fiscal policy itself. In previous crises, governments were often able to deploy large-scale support packages first and address fiscal consolidation later. That approach is becoming increasingly difficult to repeat. The next major shock may arrive before many countries have rebuilt sufficient policy capacity to respond aggressively.

Interest Costs Turn Debt into a Budget Constraint

The most important pressure is no longer the debt stock alone. It is the cost of carrying it.

According to the IMF, global interest payments have increased from around 2% to nearly 3% of global GDP in only four years, as governments refinance maturing debt at higher interest rates. This is increasingly transforming debt from a balance-sheet issue into a direct budget constraint.

Unlike productive public investment, rising interest payments do not directly improve infrastructure, strengthen productivity, enhance education systems, or raise long-term growth potential. They largely reflect the growing cost of financing past borrowing. As financing costs rise, governments have less room to support future growth-enhancing policies.

For advanced economies, this increasingly complicates decisions surrounding defense spending, pensions, healthcare, and climate-transition policies. For emerging markets, higher debt-servicing costs may crowd out infrastructure investment and social spending. For many low-income countries, where debt service already absorbs a significant share of fiscal revenue, the trade-offs are becoming even more severe.

The fiscal debate is gradually shifting from “Can governments still borrow?” toward “What will governments have to sacrifice in order to keep borrowing?”

Energy Shocks Are Now Fiscal Shocks

The conflict in the Middle East has added another layer of fiscal pressure to the global economy. Higher oil, LNG, and food prices can weaken household purchasing power, raise business costs, and intensify political pressure for government intervention.

For energy-importing economies, the transmission mechanism is relatively direct. Governments often respond through energy subsidies, tax reductions, price controls, or direct transfers to households and businesses. However, these measures effectively transfer part of the global commodity shock onto public balance sheets.

Energy shocks are therefore no longer only inflation problems. They are increasingly fiscal problems as well. A geopolitical conflict does not need to occur inside a country to affect its public finances. It only needs to disrupt commodity prices, tighten financial conditions, weaken currencies, or increase borrowing costs.

Over time, these pressures can widen fiscal deficits, increase sovereign borrowing needs, and reduce policy flexibility precisely when governments need it most. In many economies, rising energy-security spending and subsidy burdens are becoming an increasingly important component of fiscal risk.

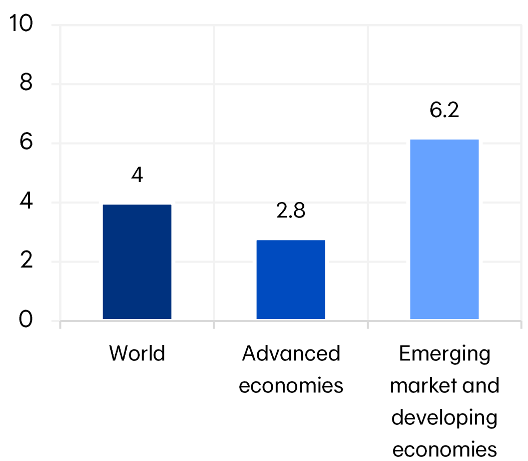
Governments Face a Harder Policy Trade-Off

Fiscal policy is entering a significantly more difficult phase. During the pandemic, the policy choice was relatively clear: governments needed to spend aggressively to prevent economic collapse. Today, however, the balance has become far more complicated.

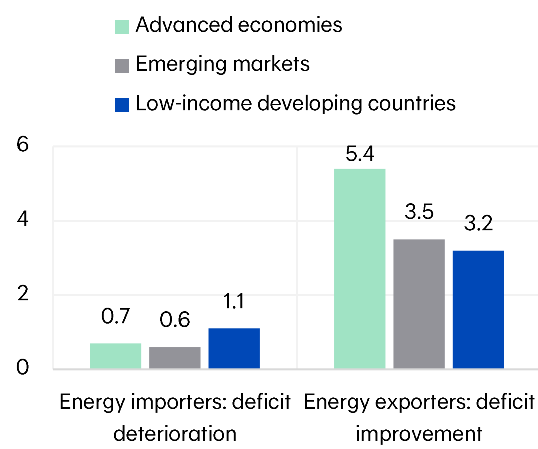
Excessive fiscal support can widen deficits, lift debt burdens, and prolong inflationary pressure. Excessive tightening, meanwhile, can weaken growth, reduce employment, and intensify social pressure. The IMF has warned that fiscal responses extending beyond automatic stabilizers and targeted relief measures could contribute to persistently higher inflation and interest rates.

The challenge is therefore not simply about cutting spending. The larger challenge is restoring fiscal credibility without undermining economic growth. That requires clearer spending priorities, better policy sequencing, and a sharper distinction between temporary relief measures and permanent spending commitments.

Debt-at-Risk Impact from Middle East Conflict
(Percentage of GDP)



Fiscal Effects of Energy Price Booms in 1991-2025
(Median deficit change Percentage point of GDP)



Source: IMF, *Fiscal Monitor*, April 2026.

Fiscal Space Becomes the New Stability Anchor

Countries with credible fiscal frameworks, targeted support mechanisms, and clear medium-term policy plans will likely retain greater flexibility when future shocks emerge. Countries that delay adjustment may still retain access to borrowing, but often at a higher financial cost and with less policy flexibility.

This is why global debt is increasingly becoming one of the world's most important policy constraints. The central issue is no longer only whether public debt remains technically sustainable. The deeper question is whether governments will still be able to mobilize fiscal policy effectively when the next major shock arrives.

In a world shaped by higher interest rates, geopolitical fragmentation, aging societies, and persistent spending pressures, fiscal space itself is becoming a strategic asset.

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