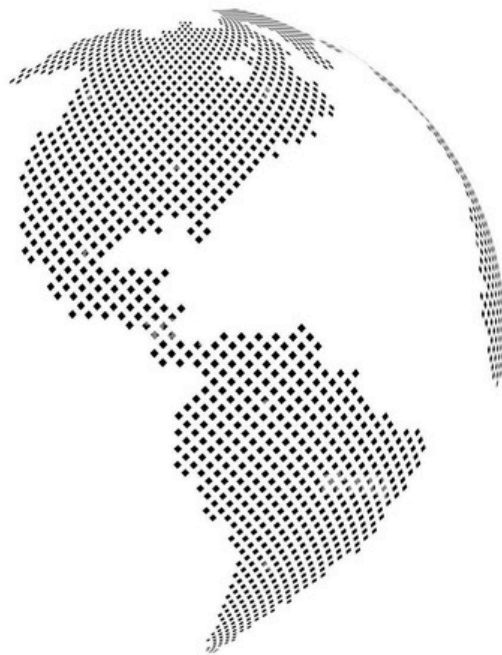
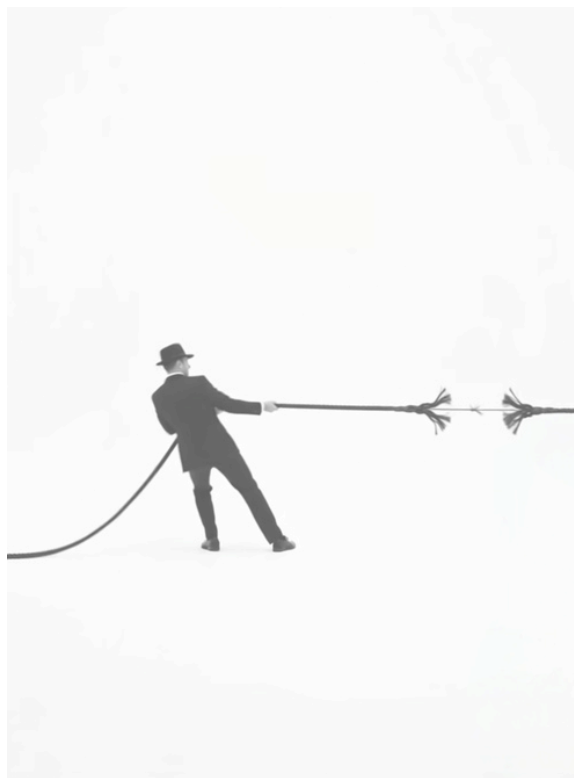




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PULLING AT THE SEAMS

How the Energy Crisis, Soaring Borrowing Costs and Debt Burdens, and El-Niño are Affecting Developing Economies.

Raymond B. Kaniu

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GLOBAL BUSINESS

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Abstract

Soaring borrowing costs, an escalating energy crisis driven by conflict in the Middle East, and a severe El Niño weather pattern are compounding a triple shock to developing economies. The 2026 Middle East conflict triggered by the US-Israel-Iran war and the subsequent blockade of the Strait of Hormuz has been described as the worst energy crisis in modern history. Developing nations face a massive external debt burden estimated in the near \$400 billion mark, with the median developing country spending roughly 9.5% of government revenue purely on interest payments, which is about three times the share of high-income nations. Collectively, they have paid nearly \$1 trillion in net interest on public debt in 2025, an amount nearly thrice what was paid in 2010, stalling vital investments in healthcare and education. Global public debt reached \$111 trillion in 2025, while debt-to-GDP ratios across major economies stand at their highest level since World War II and are heading toward 100%. The average welfare and economic losses in low-income countries from global warming are estimated to be roughly five times higher than those in developed nations. Estimated annual adaptation costs for developing nations range from \$310 billion to \$365 billion per year, yet international adaptation finance flows remain a fraction of that need. Growth in emerging and developing economies is projected to moderate around 3.8% to 4.0%, weighed down by heavy debt loads and tight external financial conditions. The sustenance of that projected growth will require a major overhaul in both public and private capital mobilization to close infrastructure and human capital deficit. Such is the weight of the triple shock, so we shouldn't be surprised when it all starts pulling at the seams.

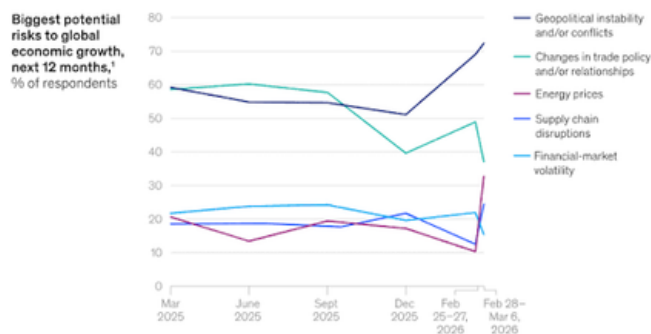
Introduction: A Compounding Triple Shock

Developing nations face a compounding "triple shock" of soaring borrowing costs, an escalating energy crisis driven by conflict in the Middle East, and a severe El Niño weather pattern. A developing economy is a country with a lower industrial base, a modest per capita income, and a lower Human Development Index (HDI) relative to industrialized nations. If this description fits your nation, you most likely have a heavy reliance on agriculture, raw materials, or primary commodities rather than advanced manufacturing, commerce, and technology. Your income and living standards indicate a strong inclination towards lower gross domestic product (GDP) per capita and widespread poverty or income inequality. Your infrastructure is most likely features limited or developing transportation, energy grids, digital connectivity, and healthcare systems; while your demographic is brimming with higher birth rates and a youthful population with strong challenges in education and capital.

The Energy Crisis

The energy crisis, wrought by lofty oil prices and subsidy strains as a direct result of the Strait of Hormuz blockade has adversely affected developing nations, especially those without reserves to offset the imbalance. Brent crude oil prices have surged past \$100 per barrel following the resumption of hostilities involving Iran earlier in the year. To shield citizens from high prices, many developing governments initially deployed emergency fuel subsidies, tax cuts, and price controls. These fiscal cushions are now wearing thin or running out entirely, forcing governments to pass high global prices directly onto struggling populations. The energy shock is impacting an estimated 100 countries.

Geopolitical instability is the primary perceived disruption to global economic growth, while focus on energy prices has also increased.



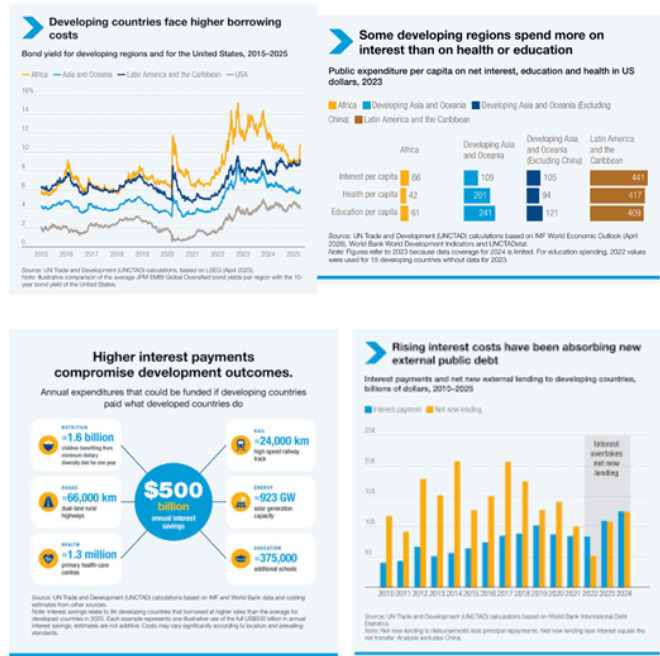
The 5 topics shown are the most commonly cited out of 16 topics offered as answer choices. Feb 25-Mar 7, 2025, n = 988; May 29-June 6, 2025, n = 898; Aug 27-Sept 5, 2025, n = 799; Nov 24-Dec 5, 2025, n = 1,011; Feb 25-27, 2026, n = 313; Feb 28-Mar 6, 2026, n = 607. Source: McKinsey Global Surveys on economic conditions, 2025-26

McKinsey & Company

For a sharp shock, it has to be put bluntly. The 2026 Middle East conflict triggered by the US-Israel-Iran war and the subsequent blockade of the Strait of Hormuz has been characterized by the International Energy Agency (IEA) and regional leaders like QatarEnergy as the worst energy crisis in modern history. The conflict choked maritime traffic through the Strait of Hormuz, cutting off roughly 20% of global liquefied natural gas (LNG) and 25% of seaborne oil supplies. Global oil production losses reached 11 million barrels per day alongside 140 billion cubic meters of gas, compounded by lingering effects from Russia's war in Ukraine. At least 40 regional energy assets and key pipelines like the Saudi East-West pipeline have suffered severe damage. The IEA orchestrated a record release of 400 million barrels of oil from strategic reserves. Plunging global inventories, including the US reserves, are hitting lows not seen since 1983. It has driven spikes in gasoline, jet fuel, and agricultural fertilizer costs. The severe fossil fuel crunch has accelerated renewable energy deployment and policy reforms across Europe, Asia, and other regions. Brent crude has repeatedly climbed past \$100–\$116 a barrel, dramatically raising the cost of imported fuel, diesel, and transport. Developing nations face a massive external debt burden estimated in the near \$400 billion mark, with the median developing country spending roughly 9.5% of government revenue purely on interest payments, which is about three times the share of high-income nations. Governments can no longer afford to subsidize consumer fuel and food prices, forcing them to abandon domestic price-cushioning. Higher energy and fertilizer prices have spiked the cost of producing and shipping food, threatening millions with acute deprivation and driving up regional inflation.

Borrowing Costs & Debt Burdens

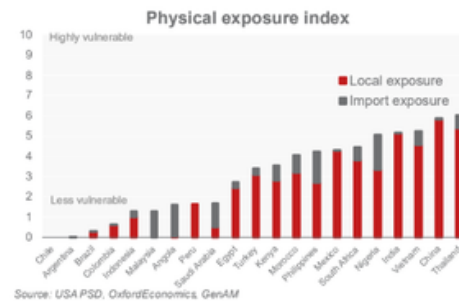
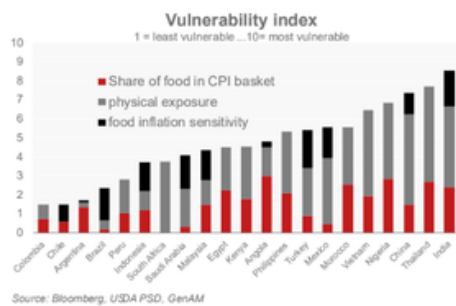
As if that's not enough, soaring borrowing costs & debt burdens are hitting developing nations where it hurts. Global government borrowing costs have hit their highest levels in decades, exacerbated by capital outflows seeking higher interest rates in major economies like the United States. Public debt levels are near historic highs, surpassing levels last seen around World War II. The combination is sapping national growth and forcing developing states to borrow more just to finance existing emergency measures.



The United Nations Development Program (UNDP) warns of a potential "domino effect" pushing vulnerable nations toward distress levels similar to the COVID-19 pandemic, when emergency debt relief was required. Rising borrowing costs and debt burdens divert critical public funds away from health, education, and social services. Developing countries paid nearly \$1 trillion in net interest on public debt in 2025, an amount nearly thrice what was paid in 2010, stalling vital investments in healthcare and education. Global public debt reached \$111 trillion in 2025, while debt-to-GDP ratios across major economies stand at their highest level since World War II and are heading toward 100%. Developing nations pay an average public debt interest rate of 5.2%, compared to just 2.2% in developed economies. The middle value of money spent on servicing debt when a set of entities, institutions, or data points is arranged in numerical order, also referred to as 'median interest spending,' has reached 9.5 percent of government revenue, a 25-year high and triple the share of wealthy nations. In 51 developing countries housing over 3.7 billion people, interest payments outpace healthcare or education spending. External debt repayments exceeded new financing by \$741 billion from 2022 to 2024. This is in addition to the cost disparity and yields which pile an extra \$500 billion in debt service costs compared to developed peers, with African and weaker-credit bond yields ranging from 9% to over 11.6%. Closing the borrowing-cost gap between developed and developing economies could save low- and middle-income countries roughly \$500 billion per year. On a global scale, total developing nation public debt stands at \$31 trillion, with low income debt growing twice as fast as in rich economies. According to the International Monetary Fund (IMF), there are nine low-income countries in debt distress, 23 at high risk, and 27 at moderate risk.

Changing Climate Patterns and El-Nino

Thirdly, changing climate patterns and El-Nino are gradually adding to the soufflé. Changing weather patterns heavily disrupt developing economies by damaging core livelihoods, straining public budgets, and widening global economic inequality. Rising temperatures and unpredictable monsoons or rainfall cut staple crop production by an estimated 15% to 20% in vulnerable regions. More than half of the population in many developing countries works in agriculture, making rural communities immediately susceptible to droughts, desertification, and soil salinization. The Food and Agriculture Organization notes that climate shocks drive over 75% of acute food crises worldwide. Rising temperatures and extreme heat reduce outdoor labor output across agriculture, construction, and manufacturing, leading to massive lost work hours and wages. Warmer weather expands the habitats of disease-carrying vectors, threatening millions with malaria, dengue, and Zika, which strain fragile local healthcare systems.



These changes also contribute to infrastructure and urban risks. Major commercial hubs and ports in Mumbai, Guangzhou, Rio de Janeiro, and Dar es Salaam face rising sea levels, storm surges, and permanent inundation of vital trade infrastructure. Frequent floods and landslides wipe out public investments in roads, power grids, and housing, forcing governments to divert development funds toward emergency relief. The soil isn't the only thing being eroded by these patterns, macroeconomic growth is eroded too, further contributing to poverty. The World Bank projects that climate impacts could push roughly 100 million more people into poverty by 2030. Annual GDP losses from extreme weather and lower productivity risk erasing years of economic convergence, widening the income gap between wealthy nations and developing economies.

Developing nations face severe, compounding challenges from global climate shocks that threaten their economic stability, food supplies, and public health. Climate disasters drive massive internal displacement, contributing to tens of millions of displaced individuals and projected figures reaching over 140 million internal migrants by 2050 across Sub-Saharan Africa, South Asia, and Latin America. Over 70% of the population in Least Developed Countries (LDCs) relies on rural agriculture. Droughts, land degradation, and changing rainfall patterns slash crop yields and expose up to 76% of crisis populations to acute food insecurity. Rising temperatures and shifting water cycles expand the reach of infectious and vector-borne diseases putting over 1 billion people at risk. Climate-vulnerable countries often spend up to 25 times more on debt servicing than on climate action. Extreme weather events like hurricanes or severe droughts destroy critical infrastructure, shrink national revenues, and push governments deeper into debt distress. Low- and middle-income nations are squeezed simultaneously by soaring borrowing costs, volatile energy/fuel price shocks, and extreme weather events like El Niño. The average welfare and economic losses in low-income countries from global warming are estimated to be roughly five times higher than those in developed nations. Estimated annual adaptation costs for developing nations range from \$310 billion to \$365 billion per year, yet international adaptation finance flows remain a fraction of that need.

Policy Direction

A combination of fiscal reforms with coordinated international financial support can help developing economies survive the triple shock. These economies can replace costly, untargeted fossil fuel and food subsidies with direct cash transfers to vulnerable households. They can prioritize expenditure and exercise spending restraint by redirecting scarce state revenues away from non-essential spending, given the fact that median developing nations currently spend over 9.5% to 10% of government revenue purely on interest payments. Moreover, they can accelerate investments in domestic renewable energy to reduce exposure to volatile global oil prices driven by geopolitical conflicts. Agriculture is the proverbial bread basket of many developing nations so the sector should be strengthened by scaling up early warning systems, climate-resilient crops, and grain reserves ahead of extreme El Niño-induced droughts and floods.

However, domestic action alone would not be sufficient to deal with the shocks. Strategic international and multilateral support will be key. Developing nations will have to call on multilateral lenders, donors, and the International Monetary Fund to expand low-cost financing and concessional loans to sustain social safety nets. Liquidity backstops will have to be implemented to make use of central bank liquidity tools like international currency swap lines modeled after those used by the U.S. Federal Reserve to stabilize local markets and prevent credit freezes. Nations will have to push for structured international debt relief frameworks or temporary payment reprieves similar to G20 initiatives used during the most recent global economic shocks.

Developing economies are shaping their future by pivoting toward regional trade, digital leapfrogging, clean energy transitions, and homegrown policy reforms to navigate slowing global growth and high public debt. The core drivers of that transformation will have to come from less reliance on traditional Western partners by expanding regional trade networks like the South-South commerce that is growing to over \$5.6 trillion by recent estimates by the UN trade and development arm. These economies would have to bypass legacy systems to adopt mobile finance, digital services, and targeted artificial intelligence tools, though deep broadband gaps remain with many more still offline. They would have to tap into global clean energy shifts by drawing record green investments and driving regional manufacturing hubs like electric vehicle battery production in Indonesia and Morocco. This should be strongly augmented by structural and governance reforms in a scenario where international financial institutions place stronger emphasis on business regulations, improving public governance, and mobilizing private capital are vital to spark investment accelerations. Growth in emerging and developing economies is projected to moderate around 3.8% to 4.0%, weighed down by heavy debt loads and tight external financial conditions. The sustenance of that projected growth will require a major overhaul in both public and private capital mobilization to close infrastructure and human capital deficit. Such is the weight of the triple shock, so we shouldn't be surprised when it all starts pulling at the seams.

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