Eighty Fourth Sovereign Debt News Update: Kenya unlikely to receive Debt Restructuring despite Credit Downgrade

By:

The African Sovereign Debt Justice Network

29 May, 2023

Kenya is hard-pressed for finances amid debt maturity pressure and highly ballooned debt-servicing costs in recent years. Data from the Central Bank of Kenya (CBK) shows that public debt was estimated at KSh9.145 trillion ($73 billion) in December 2022, with KSh4.673 trillion ($37 billion) in external debt and debt repayments consuming almost 58 percent of the total revenues. As a result, Kenya has been pressing for debt forgiveness due to significant short-term debt obligations and predicted income collection that is expected to increase by 34% in 2023–2024. On the eve of the Spring Meetings, Kenya's members of the Parliamentary Public Debt and Privatization Committee and their counterparts from Finance and Planning met with representatives from the World Bank and the International Monetary Fund (IMF) to start discussions about the debt forgiveness. Kuria Kimani, the chairman of the parliamentary finance and national planning committee, acknowledged the need for immediate assistance as the nation is in debt difficulty. Mr. Kimani noted that: "*It is not a secret that we are in debt distress. We appreciate some of the fiscal discipline measures initiated by the IMF and World Bank. However, those are long term. We need urgent intervention to prevent a default*."

However, according to the head of IMF's Africa Department, Kenya is not expected to seek a restructuring of its debt despite current strains and a looming $2 billion Eurobond maturing in June 2024. At interest rates of 6.78% and 5.87%, respectively, the nation borrowed $2.75 billion in two tranches that included a 10-year paper and a five-year issuance ($750 million). The revenues of another $2.1 billion Eurobond issued in May 2019 were used in part to repay the five-year paper.

Despite being denied the opportunity to restructure its debt, the country is experiencing severe financial hardship brought on by both domestic and external factors. On the one hand, Kenya has received a series of grants from the Africa Export and Import Bank (Afrexim Bank). For example, on 2 May 2023, the Kenyan Government received $3 billion (Ksh408 billion) economic support loan from Afrexim Bank. The three-year Afrexim Bank country programme is set to support viable trade and trade-related investments in Kenya in both the private and public sectors. According to the Afrexim Bank, the financing package will be implemented using "*several instruments, including loans, guarantee facilities, trade services, investment banking and advisory services*". According to one source, the loan is also intended to encourage the importation of essential commodities in order to lower the high cost of living, aid in the development of the nation's post-Covid infrastructure projects, and promote industrialization.

Importantly, Kenya will be the first country to access Afrexim bank's recently introduced Climate Change Adaptation Facility to be implemented as a component of the country programme, with an US$800 million Kenya Climate Change Adaptation Facility (KCCAF). This will be used to create 200 irrigation projects via a public-private partnership framework and sovereign debt and budget-neutral arrangements. In addition, Afrexim Bank has pledged to promote the ongoing development and growth of the Kenyan banking sector by increasing the lines of credit and other products it makes available to Kenyan banks, giving them the resources, they need to support the national economy. In addition, Kenya is set to receive a Sh128.9 billion ($1.0 billion) budget support loan under the Development Policy Operation (DPO) facility from the World Bank Group expected by June 30, 2023.

The IMF Managing Director Kristalina Georgieva who was recently in Kenya where she met top government officials including President William Ruto, gave an enthusiastic endorsement of Kenya's economic management and expressed confidence that the cash-strapped nation would keep servicing its debts. Ms Georgieva noted that the IMF has a very strong programme with Kenya, and intends to expand by deploying a new long-term concession of financing instrument to create resilience and sustainability. Furthermore, the discussions also focused on the pressures resulting from the country's exchange rate. The IMF recommended that Kenya allows the exchange rate to move because protecting it means depletion of much-needed forex reserves. This recommendation is problematic. Kenya's external debt is mostly dollar-denominated, therefore, for every depreciation of the Kenya Shilling against the US dollar there is a corresponding increase in the country's debt payable. Overall, Ms Georgieva noted that in the IMF's assessment, Kenya's debt is sustainable and the administration of President William Ruto is moving swiftly to improve its fiscal position.

Following this endorsement, on the 23rd of May 2023, the IMF staff and the Kenyan authorities reached staff-level agreement on economic policies and reforms to conclude the fifth reviews of Kenya's Extended Fund Facility (EFF) and Extended Credit Facility (ECF) arrangements; extension of the program and augmentation of access under those arrangements; and reforms for access under a 20-month Resilience and Sustainability Facility. According to the press release by the IMF, the IMF team and the Kenyan authorities additionally reached staff-level agreement on *an augmentation of access under the EFF/ECF totalling 75 percent of quota (SDR407.1 million, about US$544.3 million) given challenging global financing conditions; an extension of the duration of the EFF/ECF arrangements by 10 months to April 2025 to allow sufficient time for meeting the program objectives; and a new 20-month Resilience and Sustainability Facility (RSF) arrangement with access also of 75 percent of quota that will run in parallel with the EFF/ECF arrangements until April 2025*.

These developments come at a sensitive time for the East African nation with Moody's Investors downgrading the country's foreign currency issuer ratings from B2 to B3, citing an increase in government liquidity risks and deteriorated domestic funding conditions over the past two months with very low net domestic issuance contributing to financing shortfalls. This means that Kenya is now classified as "high credit risk" and just one level above "very high credit risk". The downgrade by Moody's comes a little under a month after the Treasury invited expressions of Interest from global banks to underwrite the country's next Eurobond it plans to issue in the 2023/24 financial year. Effectively, the downgrade means that Kenya's creditworthiness has lowered in the eyes of both domestic and international lenders at a time the country is shopping for the fifth Eurobond bond to retire the inaugural one taken in 2014. It is also expected to activate risk concerns amongst domestic borrowers who have already ditched long-term bonds or are quoting rates in the range of 15 per cent. The majority are opting for short-term bonds and Treasury bills whose yields are threatening to break the 10 per cent wall.

The two conflicting views from the IMF and Moody's on Kenya's sovereign debt situation raise a number of concerns. Foremost, how credible are these statements? On the one hand, the IMF boss observed that Kenya's debt is sustainable, and went ahead to give an enthusiastic endorsement of Kenya's economic management and expressed confidence that the cash-strapped nation would keep servicing its debts. On the other, although unsolicited, Moody's downgraded the country's foreign currency issuer ratings, effectively lowering Kenya's creditworthiness in the eyes of both domestic and international lenders. The impact this has on the country's outlook is that Kenya's bonds will continue being expensive as investors rely on credit agency ratings. Rating downgrades are watched closely by global investors and viewed as unfavourable signals of a country's position. At the moment, investors are asking for an average of 18% for Kenya's bond that is about to be issued, reflecting the market's concern over the East African country's ability to service its debts. This is way too much for the country to afford.

The conflict also exposes the glaring challenges of the concept of debt sustainability as per the IMF. According to EURODAD, the "examination of debt burdens should go far beyond a country's capacity to repay debts. Instead, debt sustainability assessments (DSA), including the World Bank-IMF DSAs, should integrate development priorities and independent human rights impact assessments to assess countries' ability to cover the needs of their populations". Simply, and as far as the IMF and World Bank Debt Sustainability Framework Review is concerned, whether debts are sustainable should be based on an assessment of whether the debt is preventing the meeting of basic needs rather than judging based on ability to pay.

Against this backdrop, Kenya's sovereign debt is not sustainable as the country is struggling to meet its human rights obligations. For instance, the Kenyan government was unable to pay civil servants, including Members of parliament, their March 2023 salaries because of financial challenges. Kenya's Deputy President said that the money collected by the Kenya Revenue Authority was meant to pay salaries, but was instead used to repay government loans that had matured. Failure to pay salaries has a corresponding effect on the ability of civil servants to afford healthcare, education, and other essential public services. The government has also significantly cut back its development projects.

It, therefore, means that for as long as Kenya is unable to meet its human rights objectives as a result of debt servicing then the country's debt is unsustainable. Furthermore, Kenya's continued "loan-harvesting" carries repercussions sending the country deeper into poverty and unemployment, and barring it from future credit to rebuild. Therefore, the African Sovereign Debt Justice Network (AfSDJN) calls upon African Governments to practice sustainable borrowing which speaks to their developmental needs and aspirations.

View online: Eighty Fourth Sovereign Debt News Update: Kenya unlikely to receive Debt Restructuring despite Credit Downgrade

Provided by Afronomicslaw