Reflections on the Current Reality of Africa's debt landscape

By:

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The Covid19 pandemic has thus far had an unprecedented and devastating social, economic and health impact globally. It has recast the spotlight on debt sustainability, default and sovereign debt restructuring. For African countries, a pertinent question today is—what will be the impact of the pandemic on debt repayment and what are the new debt service initiatives that may be required (including debt relief, restructuring and other measures)? While some short terms solutions, including the G20 Debt Service Suspension Initiative (DSSI), are providing some temporary breathing space for countries, the question needs to be explored from a more long-term perspective. In light of this question, this blog post opens the discussion by presenting some preliminary reflections on Africa's sovereign debt landscape.

A brief historical trajectory of Africa's post-colonial sovereign debt landscape

Numerous African countries became independent in the 1960s and inherited economies that were founded on a weak economic base and that were plagued by distortions, including ‘high export dependency; high concentration on a few commodities; low and declining terms of trade; high instability of exports earning due to these factors; and a chronic balance of payments crisis’. (Omotola & Slia, 2009). Resultantly, the 1970s to 1980s saw a progressive increase in developing country debt levels. Between the late 1970s to early 1980s, there was increased reliance on medium to long-term syndicated bank loans and more reliance on the London Club restructuring mechanism. (Eichengreen, 2003). The London Club is a ‘case-by-case restructuring routine developed between major Western banks and developing country governments in the late 1970s and early 1980s.’ It first met to restructure Zaire’s commercial bank debt in 1976, which was also the first indication that developing countries faced structural economic weaknesses and insolvency, rather than liquidity challenges. Nevertheless, this went relatively unnoticed until the crisis of the mid-1980s which posed a greater threat to global economic stability. The unsustainable debt levels culminated in the ‘1980s third world debt crisis’ that began with the Mexican crisis in August 1982. This was the first time that developing country debt became a focus, despite that the 1976 rescheduling was already an early warning sign of commercial bank debt vulnerabilities.

Africa’s debt profile from the 1970s to the 1990s, continued to evolve, firstly in terms of volumes, increasing from approximately USD11 billion in 1970, to roughly USD120 billion in the 1980s, and USD340 billion in 1995. Secondly, is the change in debt composition of African country debt in the mid-1990s now mostly comprising multilateral and official debt. In response to the unsustainable debt levels, in September 1996 the World Bank and IMF launched the Heavily Indebted Poor Country program (HIPC), a debt relief and poverty reduction program. The HIPC, and later, the Multilateral Debt Relief Initiative, (MDRI), attempted a broad-based approach aimed to ‘permanently end repeated rescheduling of debts for these countries’. (Isar, 2012) The HIPC was remodelled, and launched as the Enhanced HIPC (1999), to better link debt relief and country-specific poverty reduction policies and deliver deeper, broader and faster debt relief.

Reflections on Africa's Present-day Debt Landscape

- ***We have long been going deeper down the debt rabbit hole pre-COVID19***

Before the Covid19 pandemic, there was already a concern that African debtors could revert to their pre-HIPC levels. After the HIPC and MDRI, 8 countries were considered in high risk of debt distress, yet by March 2018 this number increased to 18 countries. Furthermore, in 2018, over 40% of Sub-Saharan African low-income countries with World Bank Debt Sustainability Analysis prepared were already at a high risk of debt distress, twice the number since 2013. Between 2008 and 2018, Sub-Saharan Africa's total debt levels rose from USD 236 billion to USD 583 billion. A major factor that contributed to this increase was an exchange rate depreciation resulting from falling commodity prices which affected the servicing of foreign currency-denominated debt. In 2020 at the brink of the first wave of the pandemic African countries again became in danger of debt distress, with Zambia being the first country to default on Eurobond interest payments.

- ***Africa's debt landscape is evolving and there is evidence of growing problems***

Africa's debt landscape is evolving in terms of composition, as countries explore alternative sources of financing. Notably, while the multilateral and Paris Club bilateral lenders are still significant creditors, new non-Paris Club lenders have now become essential lenders, particularly - China, India and Saudi Arabia, with China being the most important. It remains to be seen how the restructuring process of Non-Paris Club sovereign debts will be conducted. Of major concern has been the transparency of Africa's Chinese debt as the terms of the debt are generally not known. Another change has been the increased use of foreign currency bonds (Eurobonds). Seychelles was the first Sub-Saharan African country, other than South Africa, to issue Eurobonds in 2006 followed by a number of other countries. Africa's leading issuers are South Africa, Angola, Côte d'Ivoire, Ghana, Kenya, Nigeria, and Senegal. In addition to potential interest rate risk, Africa's Eurobonds are mostly USD denominated; as such, they carry foreign currency risk. Africa's bonds have mainly been issued subject to both UK and US law and disputes are to be resolved in these jurisdictions. The African history of debt renegotiation has been plagued with the challenge of predatory litigation in foreign jurisdictions by vulture funds. Claims against poorer countries (most of which are in Africa) are significant when compared to the GDP of these countries, and that targeting enforcement of non-traditional assets (such as payment streams) and in multiple jurisdictions around the world.

- ***This is not a 'jubilee moment, the next wave of restructurings is going to be different and difficult***

An African debt crisis is looming and a new mechanism for sovereign debt restructuring is needed. In an opinion piece on 30 November 2020, the South African President (Cyril Ramaphosa) referenced the previous debt relief initiatives and has called for a similar approach or a global debt relief response to Africa's payment difficulties resulting from Covid-19. This would be in the form of an extension of the IMF's special drawing rights, but now including the private sector (some sort of private debt service suspension initiative – PSSI?). This points straight to the main issue that was not previously present, a debt relief that includes private sector debt. Africa's debt profile has changed substantially since the HIPC/MDRI programs where African countries mostly owed to multilateral lenders, Paris Club bilateral lenders and London Club commercial lenders. As such, the rules around how to restructure the continent's debt have substantially changed and the approach to debt relief will have to be rethought.

Conclusion

What does this mean for policy makers in the planning process? From 17-23 March 2021, the UN Economic Commission for Africa will hold the fifty-third session of the Conference of African Ministers of Finance, Planning and Economic Development. While the theme of the session is 'Africa's sustainable industrialization and diversification in the digital era in the context of Covid-19', it is hoped that the subject of debt restructuring, or relief will not escape discussion. Now more than ever, the issue of sovereign debt should be among the top issues on the agenda. Of note, it is hoped that not only will Africa's finance ministers discuss the subject in the context of the immediate economic recovery, but that a broader discussion will be held on debt restructuring. It is becoming evident, now more than ever that the current reform of the 'non-system' of restructuring that is reactionary will not work for African countries in the long-term.

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