



AFRICA'S INCONVENIENT TRUTH

**Debt Distress and Climate-Resilient
Development in Sub-Saharan Africa**



**DEBT RELIEF FOR A GREEN &
INCLUSIVE RECOVERY**

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Debt Distress and Climate-Resilient Development in Sub-Saharan Africa

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ABOUT

As the world grapples with the COVID-19 pandemic, a debt crisis is emerging in the Global South at the precise moment when substantial investment is needed to meet shared climate and development goals. Yet, the G20 Common Framework has been unable to engage all creditor classes or link debt relief to climate and development.

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The Debt Relief for Green and Inclusive Recovery (DRGR) Project, a collaboration between the Boston University Global Development Policy Center, Heinrich-Böll- and the Centre for Sustainable Finance, SOAS, University of London, argues it is time for comprehensive debt reform. Utilizing rigorous research, DRGR seeks to develop systemic approaches to both resolve the debt crisis and advance a just transition to a sustainable, low-carbon economy in partnership with policymakers, thought leaders and civil society from around the world.

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EXECUTIVE SUMMARY

Due to multiple external shocks since the outbreak of COVID-19, sub-Saharan Africa (SSA) is facing acute debt distress and new highs in the cost of foreign capital at exactly the time it needs to mobilize a stepwise level of financing to invest in human, physical and natural capital to meet the region's development and climate goals for the 21st century. This paper outlines the levels of sovereign external debt and service payments between 2023-2030 for SSA countries. We calculate the fiscal space level left to meet climate and development financing needs during the same period. The SSA region cannot meet those pressing needs without new forms of liquidity, concessional and grant finance to complement and bend down the cost of capital, as well as comprehensive debt relief.

Main findings:

- External public and publicly guaranteed (PPG) debt in SSA has more than tripled since 2008, with the region experiencing the largest increase in debt and the largest increase in debt-to fiscal revenue in the Global South—as capital costs have hit new highs.
- Multilateral development banks (MDBs) and private bondholders represent 60 percent of the region's external debt, with roughly equal shares of 30 percent. China and the Paris Club are owed 12 percent and 5 percent, respectively.
- SSA's external PPG debt service is the equivalent of 93 percent of the average country's climate financing needs, and only ten countries in the region have the borrowing space to finance those needs.
- The SSA region urgently needs new forms of liquidity, concessional and grant-based development finance that catalyzes low-cost private finance; and for those countries in debt distress, significant debt relief across all creditor classes that is aligned with the Paris Agreement and UN 2030 Sustainable Development Goals.
- MDBs need to participate in SSA debt restructuring and by our calculations will need to provide between \$13.4 billion to \$34.5 billion in debt relief, of which the World Bank International Development Association (IDA) would contribute \$2.4 billion to \$11 billion in a manner that does not harm their preferred creditor status and credit ratings.

SSA's debt distress is in large part a function of external shocks of which the region has had no control—such as the COVID-19 pandemic, Russia's war in Ukraine, climate shocks, the globalization of inflation from advanced economies and advanced economy interest rate hikes. Moreover, the region is responsible for roughly 0.5 percent of cumulative carbon dioxide emissions

but bears the highest level of the costs of climate change itself (Moss, 2020; IMF, 2017). African countries need significantly more voice and representation in the international economic architecture in general, and debt restructuring in particular. Further inaction will not only inflict material damage globally in the form of climate change and lost market opportunities, but also further erode the legitimacy of the architecture itself.

INTRODUCTION: EXTERNAL SHOCKS AND FINANCE NEEDS FOR SUB-SAHARAN AFRICA

Since the outbreak of the COVID-19 pandemic, sub-Saharan African (SSA) countries have been susceptible to multiple external shocks over which they have had limited control. The virus rapidly spread across the region, with governments left to manage infections without access to comprehensive treatments. Lockdowns in China and advanced economies disrupted supply chains and choked African trade. Climate shocks, the globalization of inflation from the advanced economies and subsequent interest rate hikes have exacerbated the situation. Moreover, SSA countries have remarkably little voice and representation in the international institutions established to prevent and mitigate external shocks such as these.

In the wake of the 2008 global financial crisis, the United States and other advanced economies engaged in historically unprecedented expansionary monetary policy that led to a 'surge' in foreign capital at low interest rates into emerging market and developing countries. This capital was welcome, particularly by many SSA countries that had historically faced limited access to private capital markets. The capital inflow had a profound impact, fueling aggregate demand and economic growth and leading to an appreciation of exchange rates across the region. Foreign capital largely came in the form of private bondholder debt, in addition to China's development and commercial banks, alongside traditional forms of external debt from multilateral institutions and the Paris Club (IDS, 2022).

Currency swaps and massive monetary and fiscal expansion in advanced economies led to significant capital outflows to the 'safety' of these protected markets, depreciating exchange rates and increasing external debt (see Hoek et al, 2021; Bhattari et al, 2021).

To cope with this shock, many SSA countries turned to private capital markets, even though the average bond spread rose to 9.4 percent, in contrast to the 5.6 percent observed between 2014-2019 for countries in the region (S&P Global, 2022). To a lesser extent, countries went to China at roughly

5 percent, and to the International Monetary Fund's (IMF) non-conditional flexible programs at less than 2 percent.

But COVID-19 was only the first wave of the 'polycrisis,' as the Russian invasion of Ukraine served another shock to many SSA countries. In recent years, the Federal Reserve Bank of the United States has been raising interest rates, leading to more capital outflows, currency depreciation, external debt and new highs in the cost of capital. The unwinding of the overly expansionary monetary policy in the United States and other advanced economies has only added to the plight of many in the region.

These shocks have put SSA countries in a bind. At exactly the time when the region needs to be mobilizing major increases in foreign and domestic capital, they are increasingly locked out of international capital markets and face weak domestic resource mobilization due to slow growth forecasts.

Climate change and climate shocks have also continued to take a toll on SSA. Many countries of the region have long been susceptible to drought and extreme weather events that became accentuated over the past few years. Indeed, the United Nations Economic Commission for Africa (UNECA) estimates that the economic costs of climate change cost the region 5 percent of gross domestic product (GDP) annually (UNECA 2014). Moving forward, 0.7° rise in average temperature in the region could lead to an additional two percentage points of losses in GDP (Asafu-Adjaye, J., Ndung'u, N., and Shimeles, A. 2022a,b). The past few years have seen extreme weather events, such as flooding in Nigeria and South Africa and extreme drought which has stressed agricultural production. Ninety-five percent of rain fed agriculture globally is located in SSA, from which upwards of 55 percent to 62 percent of people derive their livelihoods (Trisos et al. 2022). Climate change significantly impacts the ability of SSA governments to mobilize resources in two ways: through lost fiscal strength and space (i.e., lost revenue growth, negative impacts on productive debt, lower exports, etc.) due to the macroeconomic and sectoral effects of climate; and through increases in planned and unplanned expenditure to address climate-related disasters and chronic climate change effects (Were 2023).

Increasing temperatures and subsequent changes in rainfall are affecting SSA economies more than elsewhere (IMF 2020). The African Development Bank (AfDB) estimates that loss and damage costs due to climate change in the region are between \$289.2 billion to \$440.5 billion (AFDB 2022). Decreasing agricultural productivity from flooding and drought, as well as drop-offs in hydropower use, translate into lower revenue generation

possibilities from a crucial sector for African livelihoods and balance of payments (Were 2023).

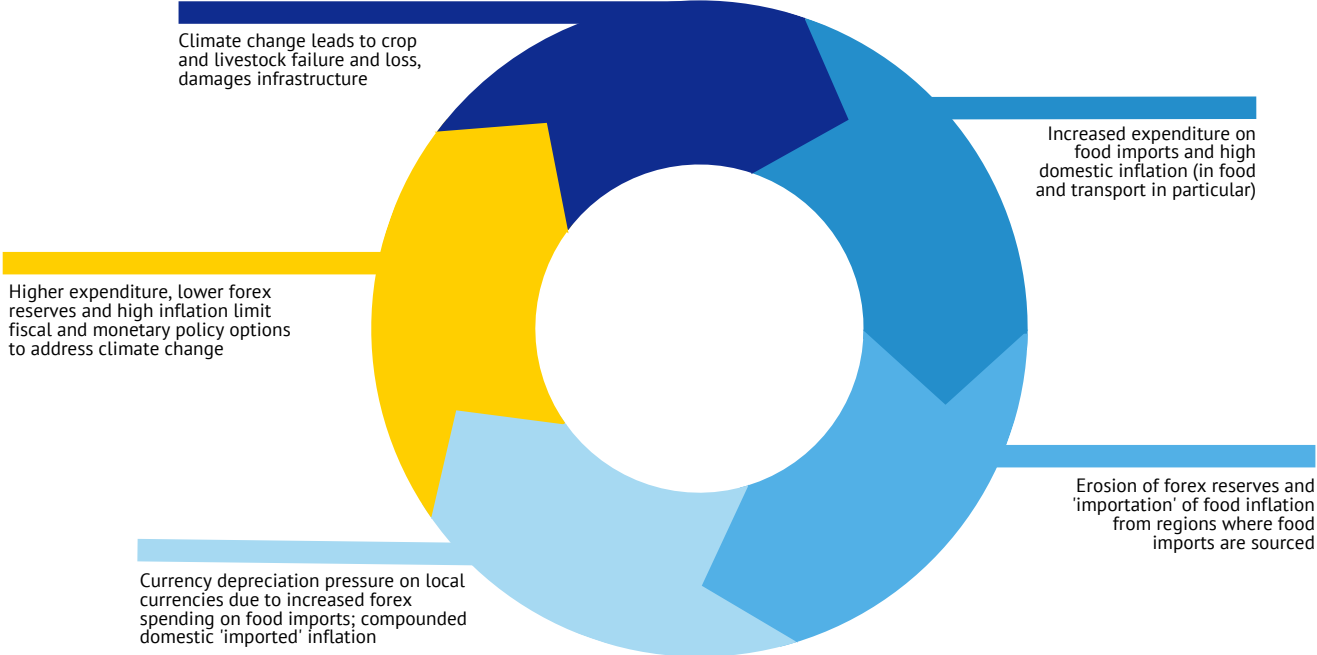
Climate change pushes large portions of Africa's population into poverty and destitution as livelihoods are lost to drought and floods. For African governments, this means lost current and future economic growth and fiscal health as the current effects of climate change impact Africa's future labor force as children and young people experience malnourishment and hunger. As the IMF points out, the human capital loss from deaths, malnutrition or lower school enrollment after a climate-related disaster is unrecoverable. Yet, under current climate projections, Africa will lose up to 16 percent of GDP due to malnutrition alone by 2050 (IMF 2020).

Songwe and Adam (2022) estimated that African countries are spending between 2 percent to 9 percent of fiscal budgets to respond to extreme weather events. More seriously, climate change increases the likelihood of conflict; a 1°C higher temperature is associated with a greater probability of conflict in the region of approximately 11 percent (AfDB 2022). Climate-induced conflict, according to the UN Intergovernmental Panel on Climate Change (IPCC), leads to increased expenditure to manage related insecurity and finance the relocation and resettlement of people displaced by the climate-related conflict in addition to those displaced by extreme weather events (Trisos et al. 2022).

The IPCC points out the effect of climate change on increasing inequality in temperate regions in the Northern Hemisphere and Africa. This translates into increased costs to pay for food relief and expanded social protection, while making it more difficult and expensive to finance economic transformation strategies aimed at addressing poverty and creating wealth. According to Were (2023), African governments are essentially stuck in a vicious cycle of the fiscal and monetary policy effects of climate change, as depicted in Figure 1.

This cycle translates to persistent vulnerability to climate change and the related economic and fiscal shocks that prevent governments from making their economies more climate resilient. It is grim and unfair to expect Africans to continue to shoulder the effects of a crisis they did little to create. It is unjust that African governments are losing current and future economic, fiscal and monetary policy space to combat climate change at a time when these fiscal and monetary policy options are sorely needed. To be sure, remaining vigilant to the persistent challenge of fiscal mismanagement and

Figure 1: The Fiscal and Monetary Policy Impacts of Climate Change



Source: Were 2023.

ensuring fiscal accountability are key, but it is important to reckon with the systemic fiscal and monetary policy vulnerabilities introduced by climate change (Were 2023).

Climate shocks further trigger capital flight and currency depreciation and raise the cost of capital for countries when a surge in private and public capital mobilization is needed to address climate change and other challenges. Table 1 summarizes the financing needs for SSA to meet the UN 2030 Sustainable Development Goals (SDGs) and Paris Commitments.

It is imperative that African countries mobilize the necessary resources to achieve the structural transformation necessary to meet the needs of roughly 2.5 billion people by 2050. Yet, African countries spend more on servicing debt than on health and education — Nigeria spends over 90 percent of tax revenue on debt service, Kenya, 65 percent (UN, 2023). Not only are debt levels and servicing at alarming highs, but the cost of capital for rollovers and new financing is out of reach for responsible fiscal policymaking in the region. Such a path is of global consequence, as it will drag global growth, accentuate social conflict and heighten the global cost of climate change.

Table 1: Financing Needs for SSA to Meet SDGs and Paris Commitments

	Gross spending 2019, US\$	Gross spending 2019, % GDP	Finance needs 2030, US\$ bn	Finance needs 2030, % GDP	Gap (2030-2019) US\$ bn	Gap (2030-2019), % GDP
Investment needs in energy to meet SDG7 targets (ECA)	n/a	n/a	500	12%	n/a	n/a
Investment needs for climate adaptation (Tufts/UNECA)	24	1%	438	10%	414	9%
Investment needs in mitigation and adaptation based on NDCs (CPI, 2022)	306	1%	280	7%	250	6%
Infrastructure and climate investment (AfDB, 2021)	n/a	n/a	75 - 150	2 - 4%	n/a	n/a
Of which:						
Mitigation			70 - 114	1.7 - 2.7%		
Adaptation			4-36	0.1 -0.9%		

Source: Songwe-Stern 2022.

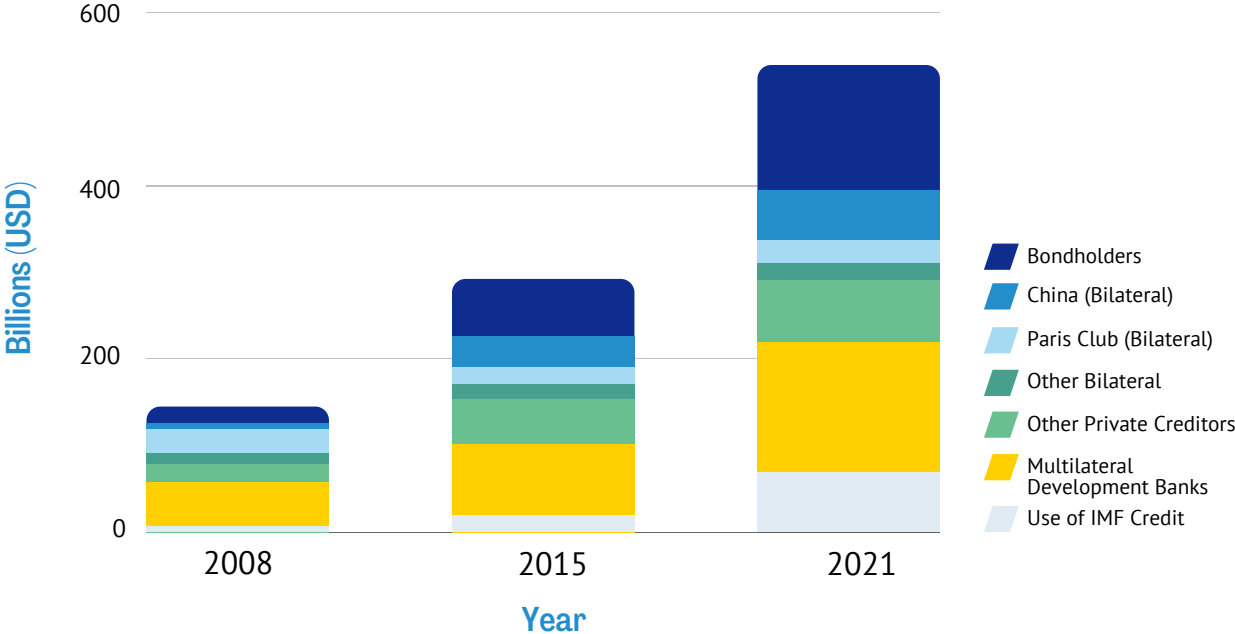
Following this contextual introduction, this paper has three sections. Section 2 outlines and analyzes the rise in SSA external debt, its impact on public spending and the new highs in the cost of capital for the region. Section 3 examines how these debt dynamics impact the ability of SSA countries to meet their climate finance needs. Section 4 outlines key components of concerted action necessary for SSA countries to finance sustainable growth trajectories for the 21st century.

EXTERNAL DEBT IN SUB-SAHARAN AFRICA

External public and publicly guaranteed debt (PPG) stocks and service payments have reached alarming levels in many countries in the SSA region. Distinct from earlier eras of debt distress, external debt is owed to a wider array of foreign creditors and serves as a growing portion of government revenue, all as the cost of external capital reaches new highs.

Figure 2 exhibits a significant surge in external debts, which have more than tripled since 2008, reaching a substantial \$539 billion in nominal terms by 2021. The largest increase in financing sources has been through private capital markets. In 2010, only five countries in the region had accessed private capital markets; this number jumped to 17 by 2020. While accessing

Figure 2: External PPG Debt on the Rise in SSA

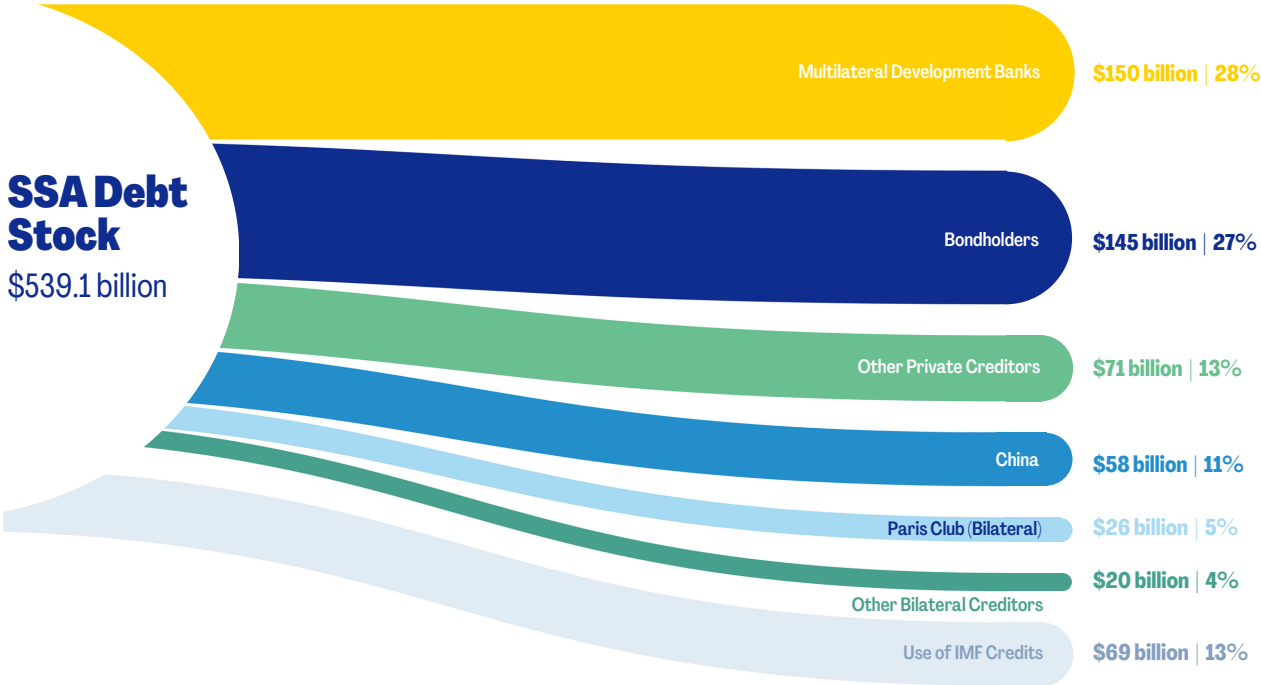


Source: World Bank, IDS 2022.

private capital markets has been an institutional achievement for many countries in the region, providing diverse funding sources and more agency for SSA governments, the cost of that capital after 2020 has been very high.

Figure 3 shows the scale and composition of SSA external PPG debt stock for 2021 (in nominal terms), with the most available data. Multilateral development banks (MDBs) remains the region’s largest creditor at 30 percent of the total stock, but private bondholders follow closely at 29 percent. An emerging trend is the rise of loans from China, which now account for 12 percent of the overall debt. Conversely, Paris Club financing, previously a significant external funding source for African nations, has diminished significantly to 5 percent of the total debt stock.

Figure 3: Scale and Composition of SSA Debt Stocks, 2021



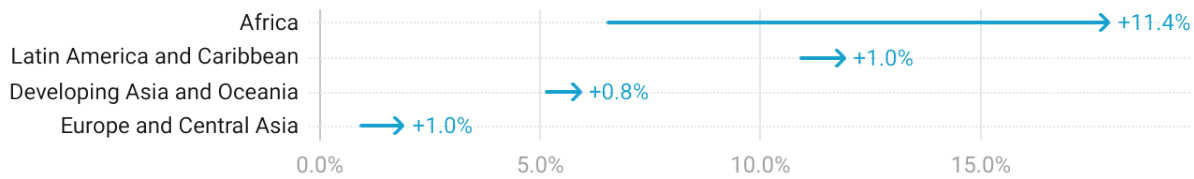
Source: World Bank, IDS 2022.

Figure 4 shows just how dire SSA's debt predicament has become relative to other regions. First, public debt interest payments as a share of government revenue increased by more than 10 percentage points from 2010-2021, and was at 17.9 percent of government revenues in 2021. External PPG debt as a share as a GDP stood at 24.4 percent in 2021, increasing by 12.6 percentage points since 2010.

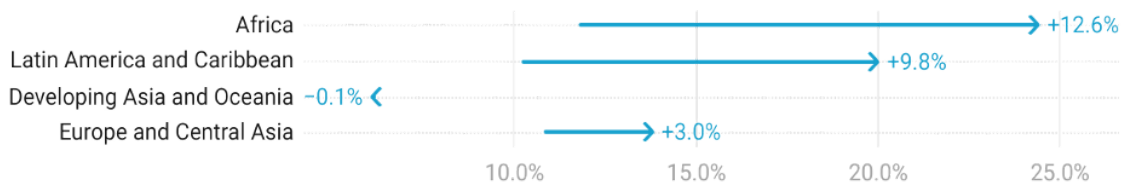
External and PPG debt service payments are significantly high ahead of the 2030, the year the SDGs are due to be achieved, with 2024 and 2025 the peak years. Figure 5 exhibits how \$356 billion is due over this period, while Figure 6 depicts the scale and composition of SSA debt service across creditor classes with private bondholders (26 percent), China (26 percent), MDBs (23 percent) and Paris Club (16 percent) owed over 90 percent of the debt service over the next few years.

Figure 4: Comparing Debt Dynamics in Africa with Other Regions, 2010 vs. 2021

Public debt interest payment, as a share of government revenues, 2010 vs. 2021

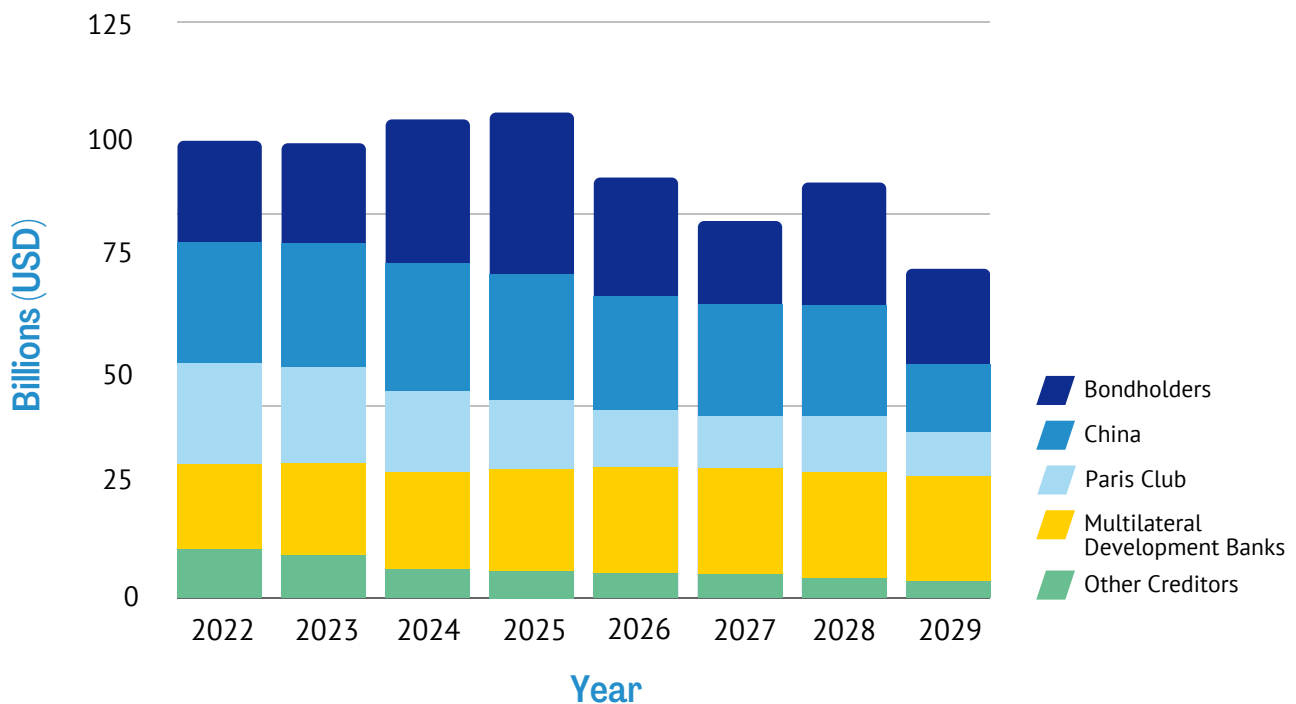


External public and publicly guaranteed (PPG) debt as share of GDP, 2010 vs. 2021



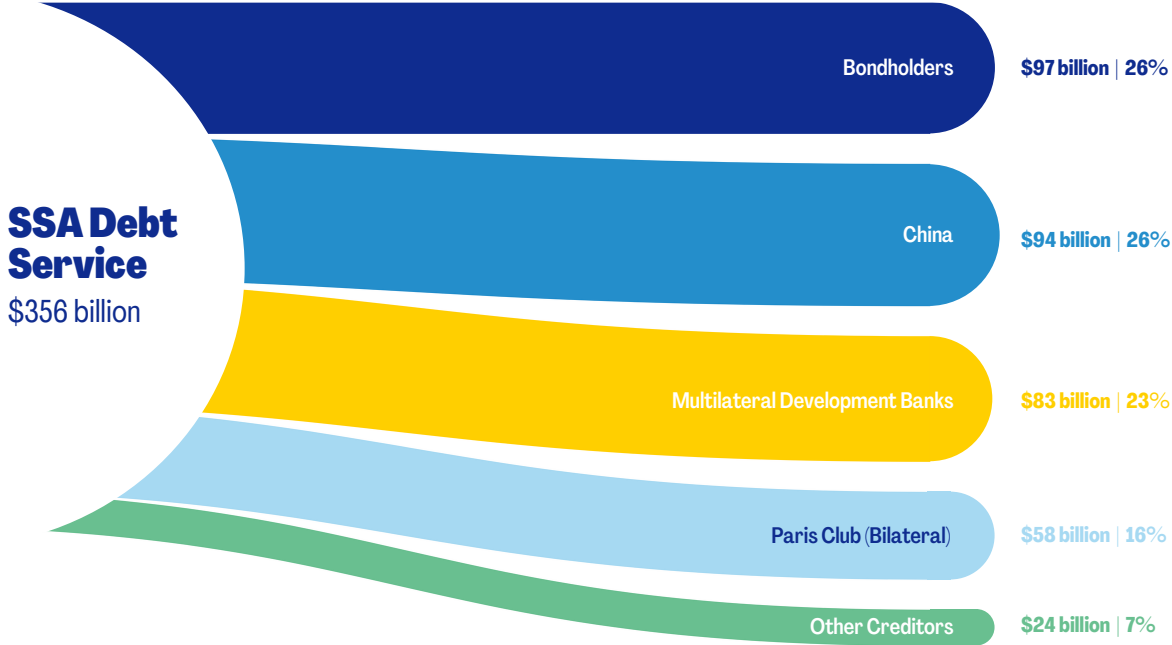
Source: IMF, 2023; World Bank IDS, 2022.

Figure 5: Debt Service for SSA Countries, 2022-2029



Source: World Bank, IDS 2022.

Figure 6: Scale and Composition of Debt Service in SSA



Source: World Bank, IDS 2022.

Debt service will take a significant share of government spending in SSA, with the average SSA country spending 12 percent of government revenue on external debt service. Table 2 shows the countries who will need to devote more than 12 percent to external debt service, with Angola, Zambia, Benin and Ghana all spending 25 percent or more of government revenue to service external debts.

Table 2: External and PPG Debt Service and SSA Government Spending

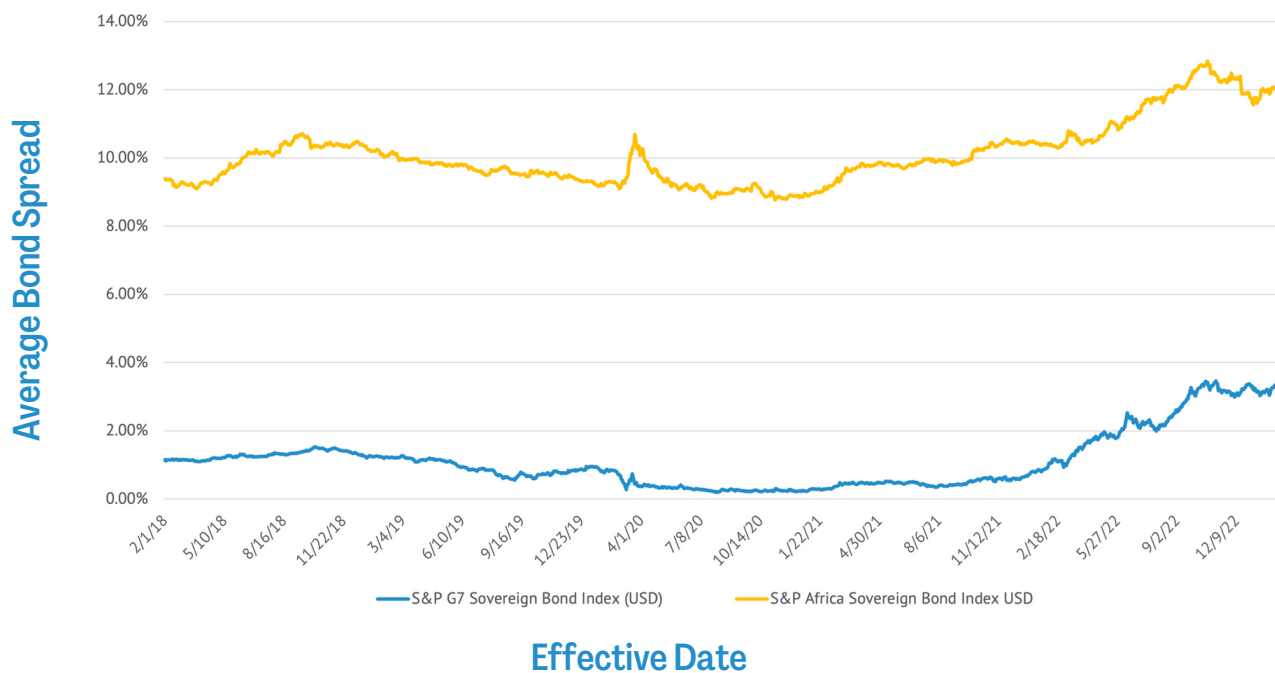
Country Name	Average Debt Service/ Government Revenue (2023-2027)
Angola	28%
Zambia	26%
Benin	25%
Ghana	25%
Mauritania	24%
Cabo Verde	22%
Senegal	21%
Cote d'Ivoire	20%
Guinea-Bissau	19%
Cameroon	18%
Gambia, The	17%

Country Name	Average Debt Service/ Government Revenue (2023-2027)
Ethiopia	17%
Guinea	15%
Mozambique	15%
Congo, Rep.	15%
Kenya	15%
Chad	12%
Average	12%

Source: IDS and IMF 2022.

The convergence of the polycrisis and domestic factors has led to an unprecedented surge in the cost of capital for SSA. From 2014-2022, the average spread reached 560 basis points. However, as of the beginning of 2023, the average spread escalated significantly to 944 basis points, as shown in Figure 7. In April 2023, 28 countries worldwide had bond spreads exceeding 700 basis points, with 15 of them Africa. This shows the severity of the economic challenges faced by the region during that period.

Figure 7: Rising Spread in Sovereign Public African Bond Yields



Source: S&P Global 2023.

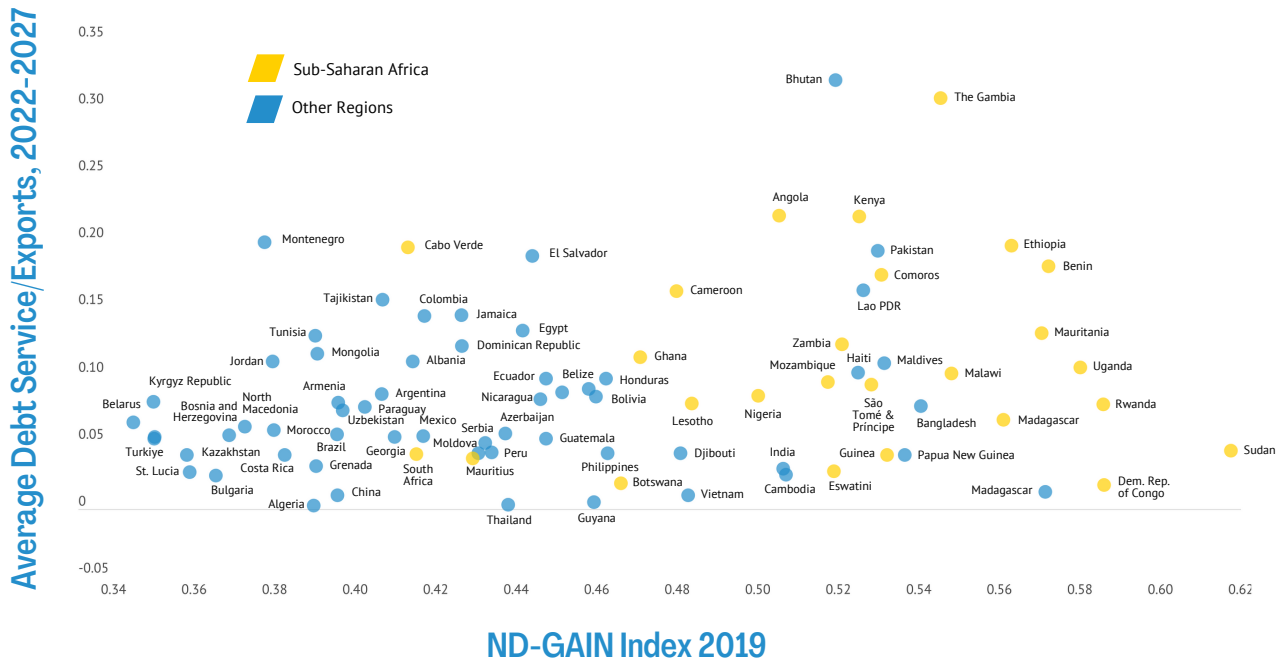
This section has demonstrated the scale and composition of the rise in external debt in the region, and how it is taking a significant bite out of the ability of SSA governments to finance expenditure. Increasing external financing to recover from multiple shocks and put countries on a sustainable growth path is swiftly becoming more and more prohibitively expensive.

DEBT DISTRESS AND CLIMATE CHANGE IN SSA

In this section, we calculate debt distress versus climate financing needs for SSA countries. As indicated by the framework outlined in Figure 1, we find that SSA countries in debt distress are also among the more climate vulnerable in the world economy; and debt distress and the rising cost of capital is making it increasingly difficult for SSA countries to mobilize resources for climate transformations.

The Notre Dame-Global Adaptation Country Index (ND-GAIN) is a periodical index that assesses a country's susceptibility to climate hazards, considering a country's exposure, sensitivity and adaptive capacity across six vital sectors: food, water, health, ecosystem services, human habitat and infrastructure (Chen et al. 2015). Figure 8 shows that SSA countries have higher debt service as a percent of exports and ND Gain average than other countries and regions, with SSA countries represented by 'yellow dots' that occupy the vast majority of countries in the upper right-hand quadrant with

Figure 8: External Debt Service/Exports vs Climate Vulnerability



Source: IDS 2022; ND-Gain 2023.

deteriorated indicator of debt sustainability (as per External Debt Service/ Exports ratio) and higher climate vulnerability.

Debt service is crowding out climate finance needs in much of SSA. We find that between 2022-2028, SSA countries will face debt servicing costs in dollars that amount to an average of 93 percent of their climate finance needs on an annual basis. Table 3 breaks down the countries with the largest gaps between debt service payments and climate finance needs.

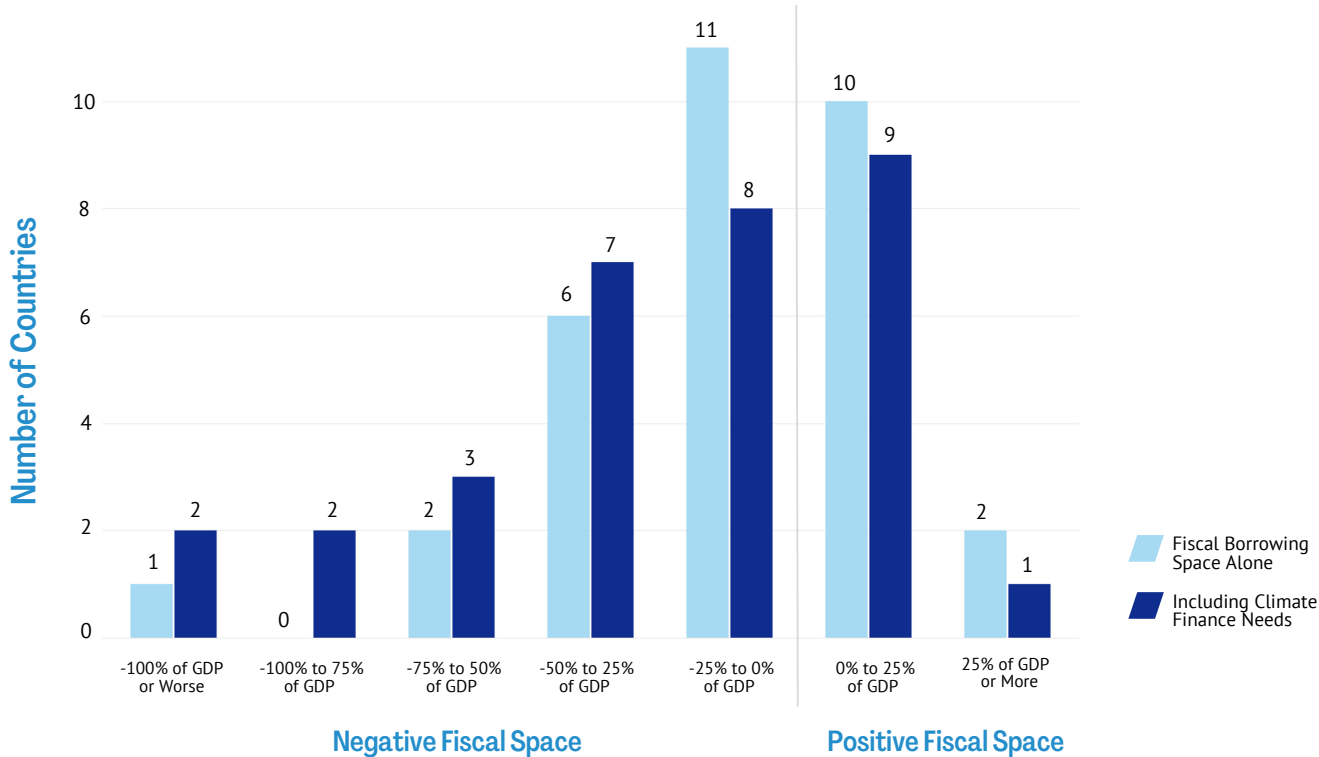
Table 3: Debt Service and Climate Finance Needs

Country	Avg. Amount Debt service (in \$ million)	Need average per year	Debt service/ Climate Needs
Cote d'Ivoire	2,563	200	1281%
Burkina Faso	383	100	383%
Gambia	91	38	238%
Lesotho	90	38	237%
Senegal	1,577	800	197%
Ghana	2,956	1,600	185%
Benin	799	500	160%
Uganda	927	700	132%
Congo, Rep	641	700	92%
Angola	7,285	9,200	79%
Cabo Verde	140	200	70%
São Tome and Principe	10	15	68%
Guinea-Bissau	65	100	65%
Kenya	3,441	5,400	64%
Niger	380	700	54%

Source: IDS and CPI 2022.

Figure 9 juxtaposes sovereign borrowing space for African countries versus their climate financing needs. Borrowing space is defined by the IMF as the difference between the country’s present value of debt as a percentage of GDP in 2021 and its specific high risk of debt distress threshold, according to the IMF-World Bank Debt Sustainability Framework for Low-Income Countries (Chamon et al, 2022). It illustrates the investment requirements for climate finance in a select group of African nations with their borrowing capacity. Most of these countries already have a negative borrowing capacity, meaning their current debt levels exceed the IMF’s thresholds for sustainable debt. Including the investment needs for climate finance further highlights the limited fiscal capacity. Countries on the left-hand side

Figure 9: Sovereign Borrowing Space vs. Climate Finance Needs



Source: CPI, 2022 and Chamon et al, 2022.

of the figure have negative borrowing capacity, while those on the right have positive borrowing capacity. However, when accounting for climate finance needs (indicated by the dark blue bars), more countries shift to the left. Three nations require investment needs (i.e., negative fiscal borrowing space) of over 100 percent of their GDP. Chamon et al. (2022) found that only seven of the 29 low-income countries examined had the fiscal capacity to undertake the climate investments outlined in their national plans.

THE NEED FOR AMBITIOUS ACTION: DEBT RELIEF FOR A GREEN AND INCLUSIVE RECOVERY

Sub-Saharan Africa stands at a crossroads. Breaking free from the vicious cycle discussed requires new forms of liquidity, development finance and private finance at favorable financial terms and, for certain countries, comprehensive debt relief. We turn now to a proposal for debt relief for a green and inclusive recovery.

Debt relief is not a panacea and needs to be part of a multi-pronged effort that includes new forms of liquidity and development finance. New liquidity could come from further issuances of IMF Special Drawing Rights (SDRs)

and from fulfilling the pledge by advanced economies to ‘re-channel’ SDRs to developing countries through the Resilience and Sustainability Trust, the Poverty Relief and Growth Trust (both at the IMF) and the AfDB (Vasic-Lalovic 2022; Truman 2023). Moreover, IMF liquidity programs must be reformed to deliver economic growth and financial stability. IMF programs emphasize fiscal consolidation, which drags economic activities and increases debt distress (IMF 2023). Modeling by the Brookings Institution shows that re-channeled IMF funds towards stimulus packages aligned with the recommended spending levels proposed in the Songwe-Stern (2022) report would have positive impacts, such as improved growth trajectories, enhanced creditworthiness and a transformative journey towards a green and inclusive recovery (Kharas and Rivard 2022).

MDBs also need a stepwise capital increase to expand their balance sheets and work to bend down the cost of capital. Songwe-Stern (2022) estimates that MDBs will need to triple their lending, while Kharas and Bhattacharya (2022) calculate that the World Bank will need a loan book of \$1 trillion by 2030. Capital increases must align with the Group of 20 (G20) Capital Adequacy Framework (CAF) recommendations, ensuring the preservation of MDBs’ AAA credit rating status. CAF adjustments like lowering the equity-to-loan ratio and hybrid capital experiments are important, however, they will not expand the lending amount necessary nor make more concessional and grant financing available. Much of this financing must be blended with private sector financing, which is increasingly out of reach for the region (see Figure 7). Zucker-Marques and Gallagher (2023) propose that MDBs issue ‘Sustainable Future Bonds’, purchased by central banks and rolled over indefinitely as equity to leverage and expand balance sheets. Development finance institutions must expand their balance sheets not only for non-concessional finance but also to accommodate concessional finance and significantly increase grants to the region.

Even with ambitious new forms of liquidity and development finance, some countries in the region will need debt relief. In anticipation of this, the G20, to its credit, established the Common Framework for debt relief. Unfortunately, it has three key limitations. First, only low-income countries are eligible. Second, there are no mechanisms to entice the diversity of creditors to come to the table and significantly reduce debt. Finally, the goal of the Common Framework is to get countries back to the level of sub-optimal spending and investment they undertook before 2020, which will not be enough to achieve the SDGs and Paris Agreement commitments. Figure 10 outlines the three pillars of a proposal put forth by the Debt Relief for a Green and Inclusive Recovery Project, which has been endorsed and expanded upon by

Figure 10: Debt Relief for Green and Inclusive Recovery in Africa



Source: Debt Relief for a Green and Inclusive Recovery Project 2023.

the Vulnerable Twenty (V20) Group of Ministers of Finance of the Climate Vulnerable Forum, a group of 58 climate vulnerable finance ministers, with Ghana serving as the current President.

Pillar 1: Public & Multilateral Creditors

Under Pillar 1, public creditors would take haircuts commensurate to what an enhanced DSA deemed to be necessary for those entities, adjusting to the relative level of concessionality in the original loans and debt instruments, as shown in Table 4.

Two main approaches are considered for intercreditor burden sharing¹: the “economic” and the “legalist” approaches (Lazard 2022). The former uniformly reduces each creditor’s present value claims by the same percentage, neglecting that private creditors price default risks on their lending operation, while official lending is often concessional (Zucker-Marques, Volz, Gallagher 2023, forthcoming). Hence, in the “economic” approach, private lenders end

¹ While there is a third approach called market-based, we have excluded it from our analysis due to its unrealistic application and potential to create uncollaborative behavior among creditors towards the debtor (Lazard 2022)

Table 4: New Common Framework Countries, SSA (33 countries), Intercreditor Burden Sharing
According to Distinct Comparability of Treatment Rules and Haircut Levels

	Nominal Value (Outstanding Debt as of 2021) (a)	Grant Element (b)	Present Value (a*(1-b))	39% Haircut					64% Haircut				
				Flat Rate CoT		Fair CoT			Flat Rate CoT		Fair CoT		
				Rate	USD bn	Rate	USD bn	Diff. CoT Rules	Rate	USD bn	Rate	USD bn	Diff. CoT Rules
Private	107.6	-4%	111.5	39%	43.5	52%	58.2	14.7	64%	71.4	72%	80.1	8.7
China	43.4	18%	35.4	39%	13.8	39%	13.9	0.1	64%	22.6	64%	22.7	0.1
Other bilateral	16.8	27%	12.3	39%	4.8	32%	4.0	-0.8	64%	7.9	60%	7.4	-0.5
Multilaterals (excl. IDA)	61.6	33%	41.5	39%	16.2	27%	11.0	-5.2	64%	26.6	57%	23.5	-3.1
Paris Club	19.3	37%	12.2	39%	4.8	22%	2.7	-2.1	64%	7.8	54%	6.6	-1.2
IDA	42.5	45%	23.5	39%	9.1	10%	2.4	-6.7	64%	15	47%	11.0	-4.0
TOTAL/AVERAGE	291.2	19%	236.5	39%	92.2	39%	92.2	-	64%	151.3	64%	151.3	-

Source: Authors calculations, based on Zucker-Marques et al. 2023.

up being subsidized by concessional lenders (Lazard 2022). The “legalist” approach translates the cost of borrowing to burden sharing by considering that every dollar of debt that has financed the government’s budget should equally contribute to restoring the debt sustainability going forward. For this reason, the “legalist” approach computes the debt relief efforts of each creditor not in terms of present value of individual creditors, but in terms of nominal value of the old debt (Lazard 2022).

Following Zucker-Marques, Volz and Gallagher (2023 Forthcoming), we estimated a “fair” burden sharing among six creditor classes, as shown in Table 4. The “Fair” CoT is based on the method developed by Diwan et al. (2023), analogous to the “legalist” approach from Lazard (2022). We then compare the results with the “economic” approach (or flat rate CoT). We consider 33 SSA countries in our sample.² These countries belong to the so-called New Common Framework countries (identified as having acute debt vulnerabilities by the DRGR Project; see Ramos et al. 2023). We assumed two scenarios of debt reduction (as per global present value), one with 39 percent and other 64 percent, following historical tendencies and the results of the Highly Indebted Poor Countries (HIPC) Initiative (Meyer et al. 2022).

With a 39 percent haircut, we estimate this group of countries requires a debt reduction of \$92.2 billion. Under the “flat rate” CoT, private lenders would bear \$43.5 billion, but the “fair” CoT suggests they should bear \$58.2 billion given their higher cost of lending. China’s concessionalism is slightly below the average for this sample, resulting in an increased contribution of approximately \$0.1 billion under the “fair” CoT. On the other hand, other official creditors would see a reduction in their burden sharing under the “fair” CoT. For example, WB International Development Association (IDA), the creditor with the highest grant element, would have a reduction of its contribution by \$6.7 billion and would have a haircut of 10 percent instead of 39 percent. The right side of Table 4 summarizes the result for a HIPC-scale debt reduction of 64 percent. The pattern follows the previous case.

Pillars 2 and 3: Private & Commercial Creditors and Credit Enhancement

To entice private and commercial creditors to the table, the second pillar involves the creation of a Brady-bond like guarantee facility where newly restructured bonds are partially guaranteed (Qian 2021). The new bonds

² Angola, Benin, Burkina Faso, Burundi, Cabo Verde, Cameroon, Central African Republic, Chat Comoros, Congo, Eritrea, Eswatini, Ethiopia, Gabon, Gambia, Ghana, Guinea-Bissau, Kenya, Liberia, Madagascar, Malawi, Mali, Mauritania, Mozambique, Niger, Nigeria, Sao Tome and Principe, Sierra Leone, Somalia, South Sudan, Sudan, Zambia, Zimbabwe.

and debt relief would be linked to country-designed plans, such as Nationally Determined Contributions, SDG Plans or Climate Prosperity Plans to ensure they are linked to sustainability and recovery. According to Figure 8, all but 13 African countries would need debt relief. The thirteen countries that still have access to capital markets and the borrowing space for capital mobilization will need to bend down the cost of capital significantly. Under pillar three, MDBs work with private capital markets to lower the cost of capital with credit enhancements (Ramos et al. 2023).

Underpinning this proposal, all countries that are deemed to have unsustainable debt after an enhanced Debt Sustainability Analysis (DSAs) would be eligible for treatment under the Common Framework. Enhanced DSAs would have to include SDG and Paris Agreement commitment spending needs, and model potential external climate and other shocks to give a more accurate picture of the resource mobilization needs up to 2030.

For African governments, the decision to pursue a debt restructuring arrangement is difficult and complicated, regardless of its necessity. The most alarming aspect is the potential impact on the country's credit rating, leading to a loss of access to private capital markets, which have been crucial for economic growth in the past decades. Credit ratings play an important role in today's financial markets, independently evaluating a country's creditworthiness and directly influencing the terms and conditions for government debt market access. Hence, maintaining a good sovereign rating is imperative to manage public debt efficiently and attract investors. Over the past decade, some countries have strengthened their market access in Africa, diversifying and increasing their external financing mix to fund their agendas. In that wave, engagement with credit ratings also increased. The number of African countries rated by the three major rating agencies increased from ten in 2003 to 31 in 2021. Meanwhile, the average annual credit ratings issued for African countries rose from seven between 1994-2007 to 37 between 2008-2020 (Chirikure et al. 2022).

Griffith-Jones and Kraemer (2021) examined credit rating institutions to assess whether their rating actions during the COVID-19 pandemic had a potential bias. At the onset of the COVID-19 pandemic, they found that advanced economies contracted by more than twice as emerging markets, at minus 4.7 percent against minus 2.2 percent in 2020. Advanced economies' average government debt ratio rose by 16 percent to 120 percent of GDP, while emerging markets saw a smaller rise of nine percent to 63 percent. Despite this, advanced economies only received five percent of all downgrades. Of the 154 rated sovereigns, 61 were downgraded by one of the big three credit rating agencies – Moody's, Fitch and S&P Global. Middle-income

countries accounted for most downgraded sovereigns at 60 percent. Simultaneously, 11 of 21 small island developing states and seven of the 19 least developed and other low-income countries were also downgraded.

Other authors show rating agencies may consider the business cycle when assigning credit ratings for African sovereigns (Pretorius and Botha 2017). Procyclicality was confirmed for Fitch and Moody's, as both business cycle indicators proved statistically significant for their models. This implies that African sovereigns are likely to be upgraded during boom phases and downgraded during recession phases by these two agencies. In that sense, these institutions can be difficult to navigate in African debt restructuring schemes.

African finance ministers are thus reluctant to ask their private creditors for restructuring, especially after it became clear that the credit rating agencies would treat such a request as a credit event. Rating agencies have become known for being bearers of bad news by making negative and reputationally damaging statements on the continent (African Peer Review Mechanism 2021). For example, the Government of Ethiopia's credit rating was downgraded after officially announcing that it would seek debt assistance under the G20 Common Framework for Debt Treatments beyond the Debt Service Suspension Initiative (DSSI). In February 2021, Fitch Ratings scored Ethiopia's Long-Term Foreign-Currency Issuer Default Rating a 'speculative grade', explicitly citing DSSI and signaling that the country is on the brink of defaulting on its foreign debt (African Peer Review Mechanism 2021; Landers and Lee 2022).

An analysis of recent sovereign credit ratings found that between 2019-2022, in a sample of 24 SSA countries, 16 had at least one score downgrade, as shown in Table 5.

Several countries have openly rejected the offer to participate in the debt moratorium. For example, Kenya's 2020 DSA suggested the country was susceptible to export and market financing shocks, and more prolonged and protracted shocks to the economy would also present downside risks to the debt outlook. Yet, the Kenyan government openly indicated its lack of interest in participating in the Common Framework, as they believed debt restructuring talks would have harmed Kenya's credit rating, making refinancing its commercial debt more expensive (Vines et al. 2022).

The empirical literature reveals mixed results regarding the economic consequences of credit ratings following a sovereign debt restructuring (Cheng et al. 2019). A debt restructuring typically leads to new payment promises involving a combination of lower principal, lower interest payments and longer maturities (Martinez et al. 2022). Empirical evidence shows that

Table 5: SSA Sovereign Credit Rating Actions, 2019–2022

Country	2019	2020	2021	2022
Angola	B	B-	B-	B-
Benin	B	B	B+	
Botswana		A	A-	
Burkina Faso	B	B	B	CCC+
Cabo Verde	B	B-	B-	
Cameroon	B	B		
Côte d'Ivoire	B+		BB-	
Democratic Republic of the Congo				B-
Ethiopia	B	B	CCC	CCC-
Gabon	B	CCC	B-	
Ghana	B	B		B-
Kenya	B+		B	B
Lesotho	B	B	B	B
Mauritius		BBB+	BBB	BBB-
Mozambique	CCC			CCC+
Namibia	BB	BB	BB	BB-
Nigeria	B+	B	B	B-
Republic of the Congo	CCC	CCC	CCC	CCC+
Rwanda	B+	B+	B+	B+
Senegal	BB-	BB-		BB-
Seychelles	BB	B+	B+	BB-
South Africa	BB+	BB		BB
Uganda	B+	B+	B+	B+
Zambia	CCC	CC	RD	RD

Source: Authors' elaboration based on Fitch Ratings.

Note: Yellow highlight indicates credit rating downgrade.

resolving a debt crisis by restructuring government debt can reduce the debtor country's economic costs and benefit their creditors (Krugman 1988; Asonuma et al. 2019). Restructuring can bolster confidence and reduce debt overhang by improving debt sustainability, supporting economic recovery and post-crisis expansion (Reinhart and Rogoff, 2010). In the long term, debtors and creditors could benefit from a restructuring that enables a shift from a crisis situation characterized by elevated yields and depressed bond prices to a state with low-risk spreads and renewed market access (Schumacher and Andritzky 2021). Marchesi et al. (2023), analyzed 130 final restructurings and found a heterogenous impact of debt restructurings,

confirming that official and private defaults may have different costs and induce selective defaults. Marchesi and Masi (2020) showed that countries involved in only private restructurings couldn't recover the contraction in their credit rating in the medium-long run.

Drawing on the experience of the Common Framework to date, entering debt renegotiations could lead to a credit downgrade. However, as stressed by the literature, it is unclear whether such a downgrade would lead to a prolonged restriction in accessing credit markets. Market access is likely to be restored more swiftly if a restructuring comes quickly and orderly. The longer governments hesitate, the deeper the haircuts will need to be and the longer the exclusion from the debt market will last. Calculations by Volz et al, 2020 illustrate that a pre-emptive and comprehensive restructuring of sovereign debt can soften the recession in the debtor country. Avoiding a deeper recession by restructuring early also leads to better outcomes for creditors. Delays and repetitive restructurings have led in the past to larger haircuts (Forni et al. 2016). Evidence from sovereign default episodes suggests that a deeper haircut in turn leads to a longer loss of market access. Following restructurings with haircuts below 30 percent, there was a 50 percent probability of overcoming market exclusion within one to two years. On the other hand, in cases where the haircut was over 60 percent, it has historically taken more than a decade to overcome market exclusion (Cruces and Trebesch 2013). Procrastination is a lose-lose proposition, as the ultimate financial loss for creditors will grow, while borrowing countries' recessions will be deeper and longer, and their loss of market access more prolonged (Volz et al. 2020).

Debt relief would give SSA a fresh start and a return to capital markets. But countries will still need support from other international institutions and improve domestic policy frameworks to ensure the effective use of these investments.

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