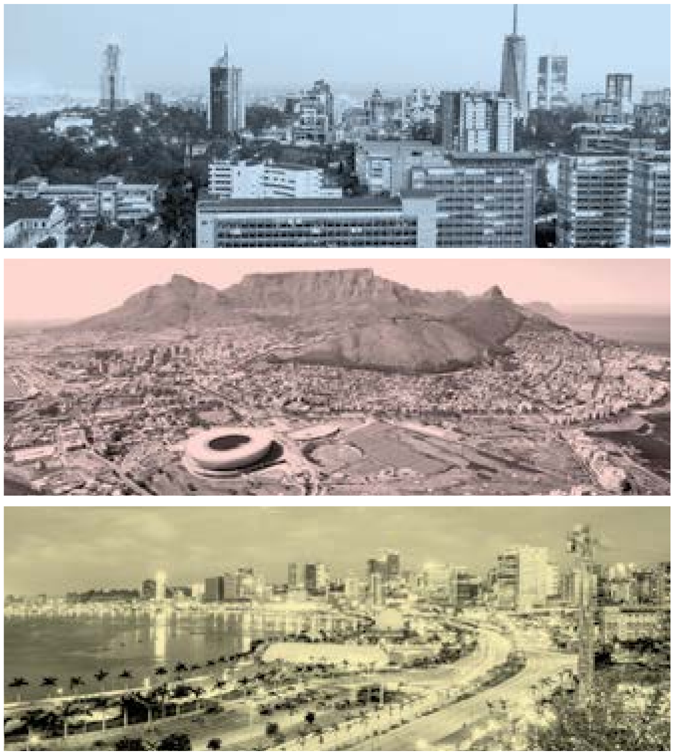
# Sovereign Debt Column: Is This Time Different for Sub-Saharan Africa?

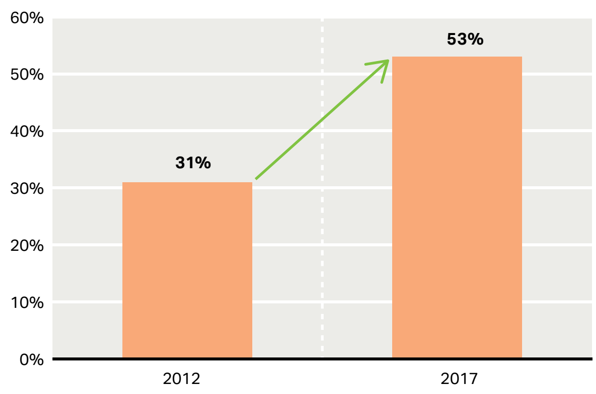
*By* **SUI-JIM HO**

On the face of it, sub-Saharan Africa's sovereigns appear once again to be drowning in systemic debt and heading toward a crisis. After a series of relief programmes in the 1990s that culminated in the Multilateral Debt Relief Initiative in 2005, which provided for outright forgiveness of debt owed by a group of 36 low-income countries (with the majority of these countries being African),[1] debt levels have since started to spiral. Today, as many as 16 sub-Saharan African nations are classified by the International Monetary Fund (IMF) as being at high risk of, or already in, debt distress – that's one-third of the countries in sub-Saharan Africa.

There are many reasons why the issues surrounding sub-Saharan African sovereign debt are different this time around. Since 2013, the region's debt has been on the rise, with the median debt ratio as a percentage of GDP increasing from 31% in 2012 to 53% in 2017.[2]

**Africa's Median Debt Ratio as a Percentage of GDP**




But before assuming that another crisis is around the corner, it is worth looking at both the reasons for the debt increase and the profile of the debt.

## Different debt drivers

Africa's debt levels have increased in part as a result of a policy response to the 2008 global financial crisis and the 2014 terms-of-trade shock. Given the low interest rate environment and significant infrastructure requirements in the region, many African countries have been driven to issue debt to meet their funding needs as government revenues have fallen.[4] On the supply side, international investors searching for yields have made such debt more freely available to the borrowers.

These drivers of government debt should be seen in the context of general global rises in sovereign borrowing across the board. It would be unfair to admonish sub-Saharan African nations for borrowing increasing amounts of debt when, in fact, we have seen bigger jumps in debt levels in developed economies.

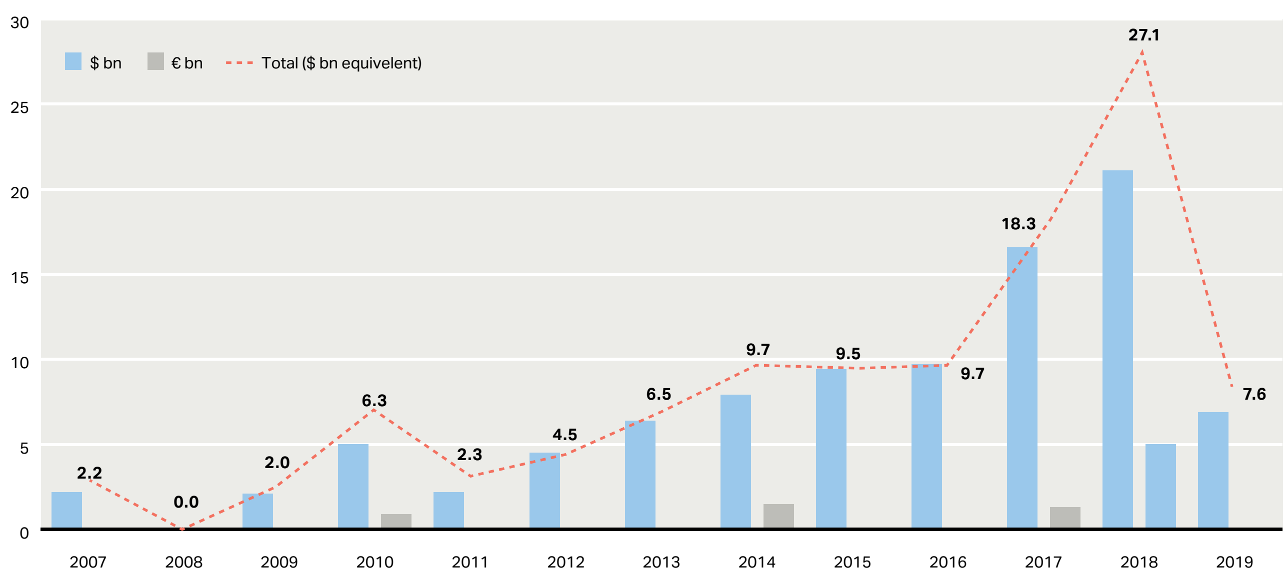
Responsible sovereign borrowing is an important tool for economic development and progress. But too much debt incurred too quickly can create distress, especially against the backdrop of a challenging economic context, the trade war between the US and China, the dependency of some sub-Saharan economies on the export of natural resources, and the likelihood of adverse movements of interest rates.

## A new debt profile

There are key differences in the structure of sub-Saharan Africa's debt profile today, most notably as a result of a fall in concessional loans over the past decade and a move towards accessing market-based, non-concessional financing. This debt is more expensive to service, and exposes countries to greater market volatility and factors outside the control of policymakers – including debt rollover risk, interest rate exposure and foreign exchange risk.

Countries are also accessing different types of non-concessional lending: while commercial loans were historically the main source of financing among sub-Saharan African sovereigns, we have seen a shift towards Eurobonds over the last 10 years, with some issuers tapping the market on an annual basis. Africa's Eurobond debt passed the US$100 billion milestone in March 2019 when Ghana issued US$2.7 billion, following a record US$27.1 billion of issuances in 2018 alone.[4] In 2010, just 10 African countries had issued Eurobonds; today, that figure has more than doubled.

**Increase in Africa Eurobond Issuances, 2007–2019[5]**



The shift to Eurobonds brings creditor base diversification as well as refinancing risk, as we also see more complex debt structures coming into the region. These range from commodity prepayment transactions secured on natural resources, to securitised instruments supported by guarantees from international financial institutions. Such financing is designed to reduce the interest burden on the issuer, but could prove more difficult to restructure in the event of financial difficulties.

## Greater variety of lenders

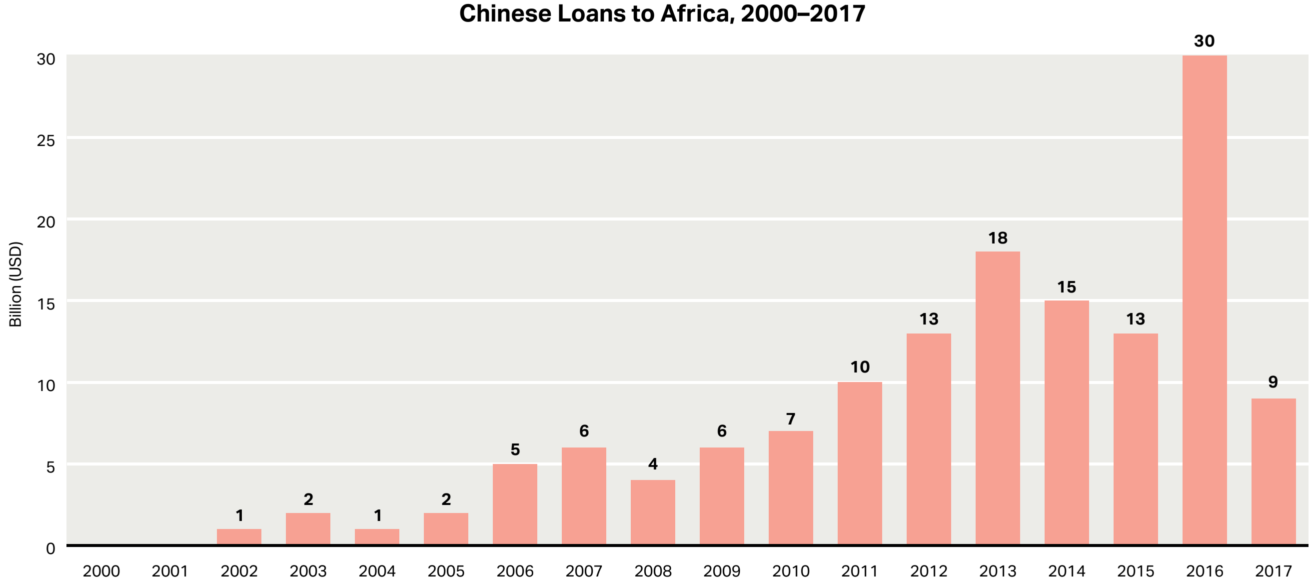
Africa has attracted an increasingly diverse set of lenders as a result of its natural resources. Chad, for example, signed a deal with the Anglo-Swiss trading giant Glencore in 2014.[6] Glencore lent Chad's oil company around US$1.45 billion in exchange for access to oil. The loan was restructured in 2015 but, by the end of 2016, Glencore held 98% of Chad's external commercial debt. In February 2018, the loan was restructured again as the country struggled to meet repayments.

Angola, sub-Saharan Africa's third largest economy, has also run up significant foreign and domestic debt despite being the second largest oil-producing country in Africa. It has become heavily indebted to China, its biggest trading partner, which has emerged as an increasingly popular lender to sub-Saharan Africa's sovereigns.

A growing proportion of official sector debt in the region is now coming from emerging market lenders from outside the Paris Club of major creditor countries, with China being the largest single creditor nation in sub-Saharan Africa today. This is largely a result of its funding of infrastructure projects as part of the Belt and Road Initiative.

The rise of China has prompted some concerns over the opaque nature of loans and their terms, and how China would react in the event of non-payments. Concerns were heightened at the end of 2017 when China took control of a port in Sri Lanka because the Sri Lankan government had failed to keep up with repayments on Chinese debt. There have also been recent reports in the press that Kenya is at the risk of losing its lucrative Mombasa port to China over unpaid loans.[7] The Sri Lanka experience appears to be a one-off incident and notwithstanding reports such as the potential seizure of the Mombasa port, China continues to fill the gap and provide much-needed infrastructure financing to the region with multilaterals and Paris Club lenders retreating from lending to sub-Saharan Africa.

**Chinese Loans to Africa, 2000–2017**

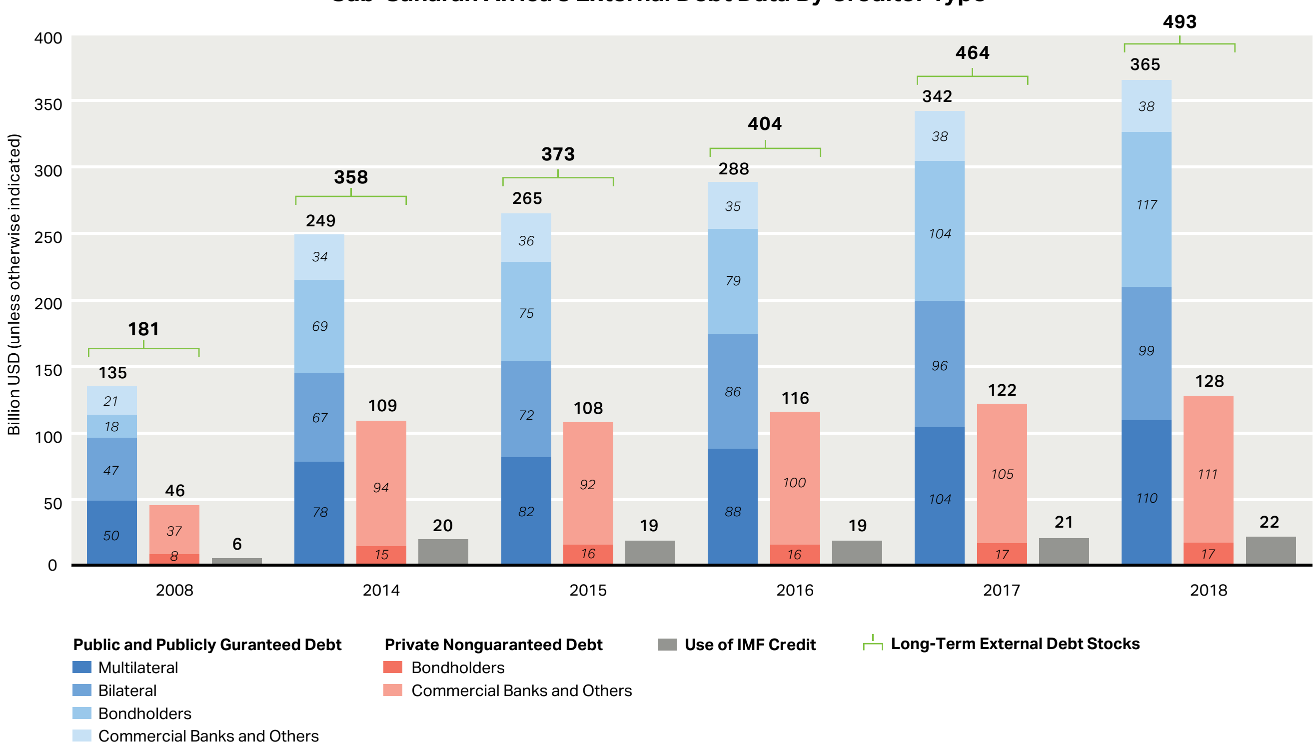



Source: SAIS China Africa Research Initiative

## Advances in sovereign debt technology

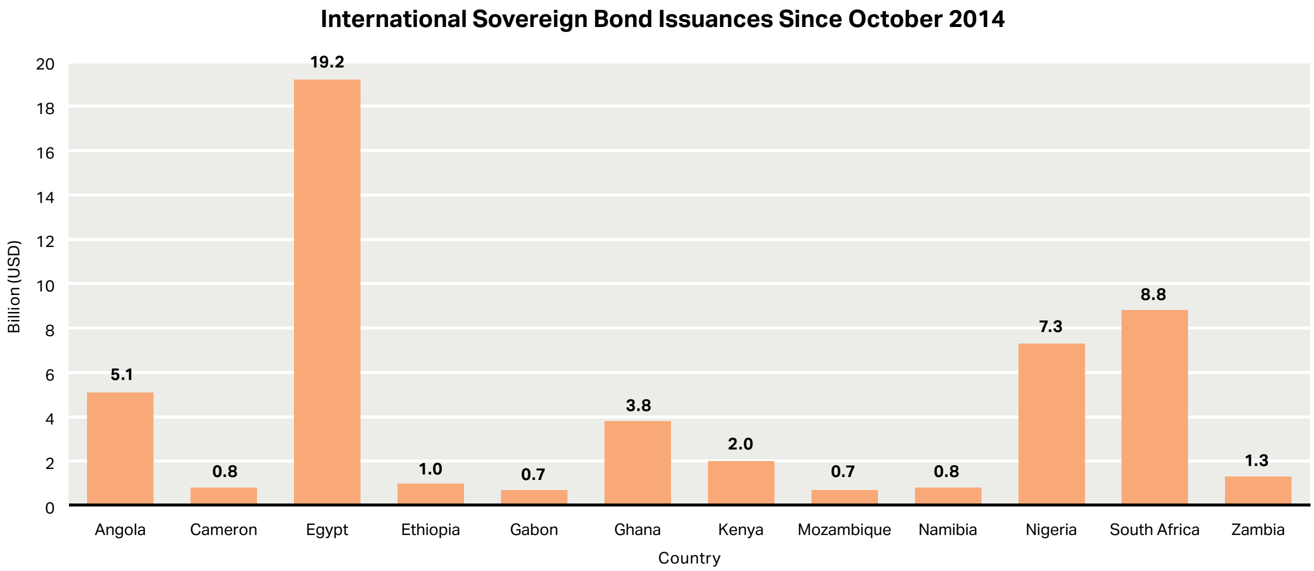
A new debt profile and an increasingly diverse set of lenders will make any future debt restructuring more complex, considering that many developments – such as the rise of Chinese lending – remain relatively untested in a restructuring context. In the event of financial difficulties, some recent developments in sovereign debt technology will mitigate the impact of these new complexities.

**Sub-Saharan Africa's External Debt Data By Creditor Type**[8]




For Eurobond debt, an example is the move towards aggregated collective action clauses (CACs). Aggregate CACs allow for multiple series of debt securities to be amended with the consent of a qualified majority of bondholders across all affected series in aggregate. They could make a big difference for those negotiating Eurobond restructurings, given that one of the perennial challenges in restructuring first generation Eurobond debt was that a separate threshold of consent was required for every affected series of bonds – meaning holdout creditors could block the passing of a resolution especially for the smaller issuances.

While some sovereigns have started to implement aggregated CACs in new issuances, this will not necessarily capture outstanding historic bonds that have series-by-series CACs. Zambia, for example, had external debt of around 40 per cent of GDP in 2018, approximately 30% of which was in US$3 billion of Eurobonds.[9] The country has issued three series of Eurobonds, but only the most recent series included an aggregated CAC. In effect, should it require a restructuring, Zambia will need to obtain consent on a series-by-series basis for these three bonds.




With many sub-Saharan African sovereigns still reliant on bank lending, the question now is how advances in bond contracts can be mirrored in commercial loan agreements, which still generally require unanimous lender consent for changes to money terms, including principal and interest amounts and maturity dates.

In any event, any future debt restructurings in the region will look wholly different to the debt relief initiatives that have gone before, but recent advances in contractual technologies will mitigate some of the complexities of the new era.

## Conclusion

Africa's potential for development and growth is vast, and debt is an essential feature to realise this potential. The need for increased sovereign debt is not unique to sub-Saharan African countries, but other factors such as currency depreciation and poor governance potentially make sovereign debt more risky in this region. Although a systemic sovereign debt crisis in African countries may not be imminent, governments and policy-makers need to ensure that they identify weaknesses in their debt policies and practices and should take steps to avoid the risks of a debt crisis. ■

1. https://www.imf.org/external/np/exr/facts/mdri.htm
2. https://www.brookings.edu/research/is-sub-saharan-africa-facing-another-systemic-sovereign-debt-crisis/ and https://www.brookings.edu/blog/africa-in-focus/2019/04/05/looming-debt-crisis-in-africa-myth-or-reality/
3. https://www.un.org/africarenewal/magazine/april-2015/how-healthy-africa%E2%80%99s-sovereign-bond-debt
4. https://qz.com/africa/1588751/the-size-of-africas-growing-debt-isnt-its-biggest-problem/
5. Extracted from https://www.africanbondmarkets.org/en/news-events/africa-financial-markets-news/article/african-eurobonds-an-evolving-and-now-100-billion-asset-class-158468/
6. https://www.independent.co.uk/voices/africa-oil-companies-g20-summit-fix-glencore-debt-chad-a8660606.html
7. https://www.hellenicshippingnews.com/china-to-take-over-kenyas-main-port-over-unpaid-huge-chinese-loan/
8. https://openknowledge.worldbank.org/bitstream/handle/10986/32382/9781464814617.pdf?sequence=7&isAllowed=y
9. https://www.imf.org/external/pubs/ft/dsa/pdf/2015/dsacr15152.pdf

▼ **Sui-Jim Ho** is a partner based in Cleary Gottlieb's London office. Jim's practice focuses on cross-border finance and restructuring. He advises on a broad range of financial products including loans, bonds and derivatives. He is particularly noted for his expertise in complex emerging markets and sovereign-related matters. He holds a law degree from the London School of Economics and Political Science where he graduated with First Class Honours.