

MEASURING AFRICA'S WEALTH AND MONEY



Chapter from Africa 2025: Prospects and Challenges
Handbook by the HSE University Center for African Studies
Edited by Andrey Maslov

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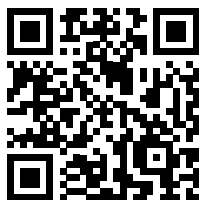
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The chapter **Measuring Africa's wealth and money** examines the financial framework of African countries, whose main attributes - high debt burden and deep trade imbalances - are seen as interdependent phenomena. The chapter uses both well-known and author's indicators to categorise African states by debt sustainability. It discusses currency regimes in detail, opening a discussion on the reserves of African countries, where they are held, under what conditions, and whether their management policies align with real economic development needs. The chapter serves as an integral part of the handbook *Africa 2025: Prospects and Challenges* prepared by the HSE University Center for African Studies.

Africa 2025: Prospects and Challenges is to serve as a handbook on Africa's development, challenges and prospects. Its target audience is government officials, businessmen, scholars and experts. The handbook aims to provide alternative positive vision on some issues that Africa faces, among them being the fight for food and energy sovereignty, debt crisis, digital transformation, rapid urbanisation and population growth.

The book was prepared by the team of experts and scholars coordinated by HSE University Center for African Studies (Moscow, Russia).

Digital version
of the Handbook
is available here:



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Measuring Africa's wealth and money

What is the real value of African money?

One of the main factors holding back Africa's development is a lack of data and information, and thus of knowledge relevant for decision-making. The unknown leads to overestimation of risk, and overestimation of risk leads to an inflated cost of capital. As a result, the cost of financing a business in Africa can be several times higher than in a developing country outside the continent - not to mention rates in the US or Europe. There is also 'cheap' money in Africa - international funds, banks and several countries offer low-cost financing to certain projects and sectors, providing them an additional, non-market competitive advantage driven by non-African interests and external agenda.

Africa is not a single capital market. Almost every country suffers from the capital drain, at the same time the most of them rely on external funding for balancing their budgets. Nevertheless, the individual capital markets in Africa share many common features, and investors often regard Africa or its sub-regions as destinations which are best looked at together. So, there are funds focused on investments in the continent. In addition, the role of Pan-African institutions is steadily growing, with AfDB, Afreximbank, the African Union and UNECA among them.

One of such common features on the continent is the dependence of budgets and economies on external borrowing and trade. Taxes on domestic transactions have played a lesser role. However, the banking sector is growing dynamically, and in many countries, banks play a key role in development acting as intermediaries for external capital markets. Below we examine these and a number of other

phenomena that shape the financial dimension of risks and prospects for projects in Africa.

Income from the foreign trade and borrowings both are highly volatile and tend to dry up during crises due to the undiversified resource-based export structures and predominance of an external debt over domestic. Better comprehension of existing vulnerabilities could help governments, businesses to implement workable strategies and policies, and navigate among country-specific risks.

Our study examines the evolution of African debt throughout the 21st century and its distribution across the continent. The debt is reviewed in conjunction with issues regarding trade: trade balances, export diversification and national currencies. The research quantifies the existing debt burden and sheds light on the problem of credit rating agencies, finally offering directions for future research to enable an unbiased country classification.

African debt: what has changed?

As horrific as it may sound, the rest of developing countries experienced 2.5 times faster debt expansion during the same period.

Since the beginning of the 21st century African public debt has quadrupled and reached USD 1.8 trillion in 2022¹

After a series of defaults in the 1980s and 1990s, African countries embarked on a path of debt deceleration, reducing the debt-to-GDP ratio from 65% in 2000 to 39.3% in 2008.² This trend was mainly supported by full-scale debt relief programmes of multilateral financial institutions. In 1996, the IMF

1 UNCTAD. A world of debt report 2024. URL: <https://unctad.org/publication/world-of-debt>

2 Afreximbank. State of Play of Debt Burden in Africa in 2024. URL: <https://www.afreximbank.com/reports/state-of-play-of-debt-burden-in-africa-2024-debt-dynamics-and-mounting-vulnerability/>

launched the Heavily Indebted Poor Countries initiative (HIPC) which was targeted at low-income countries with unmanageable levels of debt. Since then, 31 African countries have graduated from HIPC and received full debt forgiveness, reaching USD 70 billion. In 2005, HIPC was supplemented by the **Multilateral Debt Relief Initiative** (MDRI), which guaranteed debt relief on the claims of the IMF, World Bank and African Development Bank for 29 African states at the cost of more than USD 30 billion.

Though HIPC and MDRI were effective in nominal terms, their impact on the long-term debt sustainability may be contradictory. To enter both programmes, a state needed to commit itself to structural reforms (more political than economic), thereby delegating decision-making to G8 (now G7) countries. Also, since the IMF offered a bailout, more and more countries started to account for the future prospect of similar debt relief, applying riskier debt management practices.

Then came the global financial crisis of 2008 when the modern history of African debt began. In response to weakening economic activity, the Fed and the ECB lowered interest rates which resulted in yield decrease on developed markets and triggered a search for higher returns elsewhere. Being less involved in global finance and thus less affected by the crisis, Africa had demonstrated an average annual GDP growth rate of 5.3% during 2000-2008 and offered a substantial risk premium, which was not perceived as that risky anymore after the collapse of what seemed to be solid western banks.

Since 2008, the African debt-to-GDP ratio has sharply increased, reaching 69% in 2023; yet the expansion was asymmetrical in regard to external and internal obligations. In the early 2010s, most sovereigns did not have capacity or credibility to

accommodate capital in their own bond markets. Little has changed since then.

In 2023, two-thirds of the total African debt or USD 1.2 trillion was external

By 2022 the domestic debt has reached a notable level in five countries: **Egypt** (USD 258 billion), **South Africa** (USD 116 billion), **Nigeria** (USD 83 billion), **Algeria** (USD 95 billion), and **Morocco** (USD 30 billion).

Unlike internal debt which depends mostly on the national economy's performance and can be 'printed' during times of hardship, external debt relies heavily on global macroeconomic conditions and has to be paid back in hard currency. The large share of external debt along with the overexposure of many African countries to commodity prices and a limited capacity to deal with disasters and crises are a volatile combination as was seen during the 2014 commodity price plunge, global pandemic in 2020 and crisis of 2022.

However, the African debt-to-GDP ratio has soared not only due to the rise of the debt itself. It can be attributed also to a slowdown in economic growth (3.2% on average in 2010-2022) and currency depreciation (35% devaluation relative to USD since 2014 for emerging economies³) as the debt is mostly external.

While comparison to GDP exposes the increase of the debt level as the main trend, it fails to reveal the magnitude of the change. Debt is very heterogeneous as it comes on different terms from different sources: other governments, multinational financial institutions or private banks.

The private sector has become the main source of African debt, shifting from 25% in 2000 to 54% in 2023, leaving 27% to multilateral creditors such as the IMF or World Bank and less than 19% to bilateral loans from other countries⁴

3 Federal Reserve Bank. Nominal Emerging Market Economies U.S. Dollar Index. URL: <https://fred.stlouisfed.org/series/DTWEXEMEGS>

4 Afreximbank. State of Play of Debt Burden in Africa in 2024. URL: <https://www.afreximbank.com/reports/state-of-play-of-debt-burden-in-africa-2024-debt-dynamics-and-mounting-vulnerability/>

Among the top lenders are private bondholders (i.e. eurobond market participants from all over the world), Chinese (USD 24 billion) and British (USD 14 billion) investors. Although this is indicative of improved investment attractiveness, it poses a number of challenges for African countries.

Firstly, private debt is more expensive than bilateral or multilateral, meaning higher interest rates, lower grace periods and less space for restructuring. The UNCTAD report entitled A World of Debt 2024 shows that in 2020-2024 the borrowing costs of African countries were ten times higher than in developed economies, 44% higher than in the LATAM region and 85% higher than in Asia and Oceania, even though the share of private debt in Africa is lower than average for developing countries.⁵

Secondly, flows of private debt are more volatile and tend to reverse in times of crisis as foreign investors' main concern is short to middle-term profit but not long-term and also not the abstract financial stability of a certain country. In 2022, developing countries experienced a net outflow of USD 49 billion on external public debt, among them were 21 African countries – five more than in 2021 and 11 more than in 2019.⁶

Thirdly, in case of default on private debt it may take longer to restructure it with a greater number of counterparties, who are not always willing to cooperate. At least 15 African countries have become targets of 'vulture funds' that specialise in purchasing distressed debt on the secondary market at a substantial discount and trying to recover the premium, usually through litigation and delays of the overall restructuring process.⁷ For example, in 2007 a vulture fund received USD 15.5 million from Zambia after buying a debt of USD 3.2 million, meaning that the fund's return was 484%.⁸

After a series of legal patches the activity of vulture funds in Africa has diminished; however, a new wave of defaults may attract more sophisticated parties seeking to profit from distressed debt.

It should also be considered that a large proportion of lenders labelled 'private' are in fact government affiliated. This is particularly true of lending from the Middle East and China.

Africa's external debt

The debt landscape is not homogenous across Africa. Two-thirds of the external debt is concentrated in ten countries: **South Africa** (USD 172 billion), **Egypt** (USD 163 billion), **Nigeria**, **Morocco**, **Mozambique**, **Angola**, **Kenya**, **Tunisia**, **Côte d'Ivoire**, and **Ghana**. Almost all these countries are within the Top 10 in terms of GDP, with only Tunisia and Mozambique standing out. As local financial markets grow and become more interconnected, debt distress in one of these heavyweights may trigger a wave of defaults across the continent.

An issue with African external obligations is the 'wall of debt' – portions of eurobonds that were actively issued last decade and mature mainly in 2024-26

Eurobonds are issued in foreign currency outside the country of origin and have several benefits: they do not entail any policy changes; they are liquid relative to other types of debt, and they can be repurchased or bought back on the secondary market. However, issuing countries rely heavily on the global interest rates and their own credit rating as most eurobonds are paid off by issuing new portions of debt. Nowadays, both global and African interest rates remain high due to the tight monetary policy adopted by developed countries in the post-Covid era, currency depreciation and climate shocks. The frequency and magnitude of these shocks for Africa

5 UNCTAD. A world of debt report 2024. URL: <https://unctad.org/publication/world-of-debt>

6 Ibid.

7 African Development Bank Group. Vulture Funds in the Sovereign Debt Context. URL: <https://www.afdb.org/en/topics-and-sectors/initiatives-partnerships/african-legal-support-facility/vulture-funds-in-the-sovereign-debt-context>

8 BBC. Zambia pays 'vulture fund' \$15m. URL: <http://news.bbc.co.uk/2/hi/business/6589287.stm>

is increasing faster than anywhere else on Earth, and many countries are trying to address the problem by issuing climate-related catastrophe bonds.

In 2024, there are USD 10.3 billion in eurobonds maturing, a sharp increase from USD 3 billion in 2023. Some countries have already re-entered the eurobond market in 2024 to refinance maturing obligations: **Côte d'Ivoire** issued USD 2.6 billion in January and **Kenya** raised USD 1.5 billion in February. Large portion of maturing debt is still held by **Egypt** (USD 3.3 billion), **South Africa** (USD 1.5 billion), **Morocco** (USD 1 billion) and **Ethiopia** (USD 1 billion). **South Africa** and **Morocco** are not likely to face challenges paying off their debt, but Egypt may need new lines of credit including one with the IMF, while Ethiopia might end up in default by the end of 2024.⁹

In 2025 African countries will face USD 10.2 billion in maturing eurobonds, with USD 3 billion being held by **Egypt**, USD 2 billion by **South Africa**, USD 1 billion by **Tunisia**, USD 864 million by **Angola**, USD 750 million by **Namibia**, USD 700 million by **Gabon** and USD 500 million by **Nigeria**.

Luckily, as inflationary expectations are decreasing worldwide, the Fed and ECB are starting to cut interest rates gradually which will lead to cheaper debt. However, defaults in countries with the most vulnerable debt level are very likely to occur in the next two-three years.

Market sentiment is useful to define the probability of default on a debt. Ghana's bonds maturing in 2026 had an even greater yield — 54.4%, an increase by 8.2 percentage points from 2022. Ethiopia and Ghana is the main candidate to default in 2026, adding a new portion of arrears to the existing debt in default and further limiting their ability to borrow on the international market. At the same time, country can find ways to limit the scale of the debt crisis through political leverage.

China remains a major bilateral lender to Africa with over USD 90 billion in active debt commitments (fourfold increase from 2012), constituting 11% of the total external debt.¹⁰ Chinese loans to Africa started to grow from USD 100 million in 2000 and reached its peak in 2016 (USD 28.8 billion). Since then, the trend has reversed – lending dropped to just USD 1 billion in 2022.¹¹

From a cumulative USD 180 billion, 80% was attributed to infrastructure projects such as power plants, roads and railroads, port facilities and cell networks implemented by the supply of goods and services from China. Technically the money often doesn't leave China, only the financial liabilities being recorded for the African states.

China has often used resource-backed lending in countries such as Angola, Democratic Republic of Congo, Guinea and Ghana, pursuing also the goal of securitisation its strategic imports from these countries.

In 2024, the top debtors to China were Angola (USD 21 billion), Ethiopia (USD 7 billion), Kenya (USD 7 billion), Zambia (USD 6 billion) and Egypt (USD 5 billion), some of them in default or being on the edge of debt distress. Yet, it remains unclear whether Chinese loans have deteriorated the debt profiles of African countries or China was just more willing to accept greater risks.

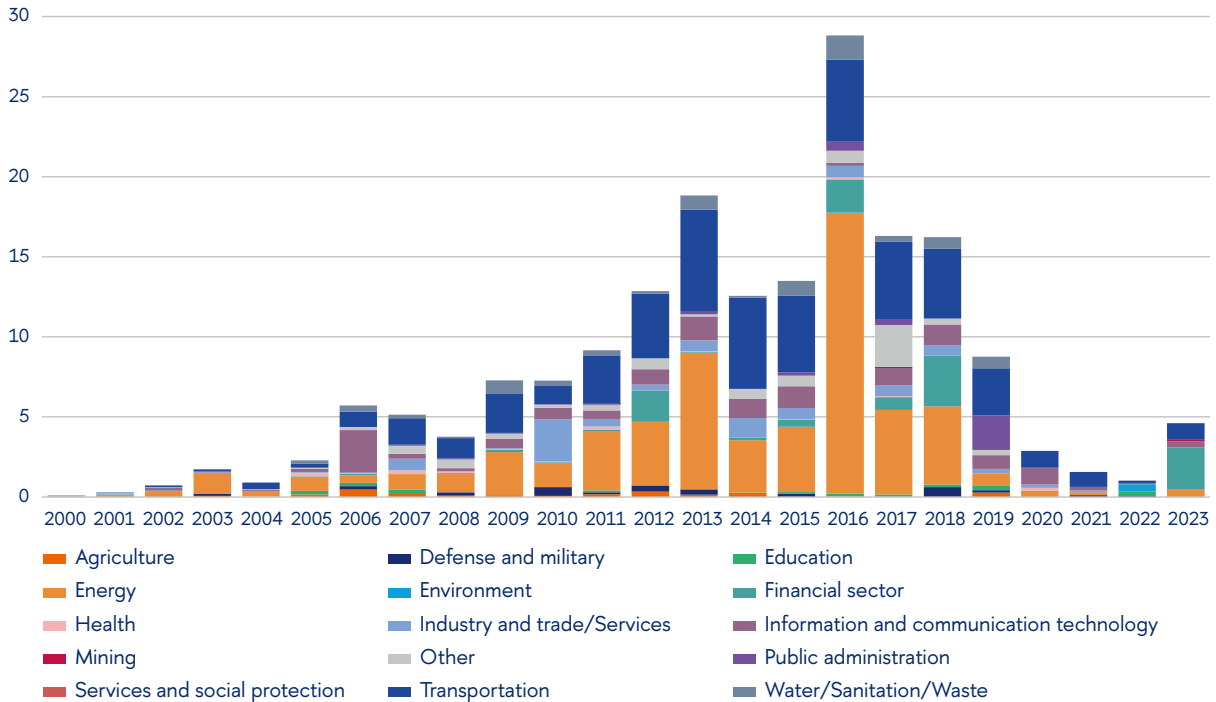
However, in 2023 China demonstrated renewed interest in Africa with USD 4.5 billion in loans, mainly in finance and infrastructure. USD 1.3 billion was provided to Egypt as a line of credit, with the same amount being spent on facilitating trade with Africa. Nigeria received USD 1 billion to construct the Kaduna-Kano section of the Lagos-Kano railway, more than USD 250 million was offered to Madagascar, Uganda and Angola on energy and telecommunication projects. What seemed to be a Chinese retreat from Africa could be strategic realignment before reevaluating risks and entering new markets.

9 Gregory Smith. Africa's eurobond wall revisited. URL: <https://www.linkedin.com/pulse/africas-eurobond-wall-revisited-gregory-smith/>

10 World bank. International Debt Report 2023. URL: <https://openknowledge.worldbank.org/entities/publication/02225002-395f-464a-8e13-2acfa05e8f0>

11 Boston University. Chinese Loans to Africa Database. URL: <https://www.bu.edu/gdp/chinese-loans-to-africa-database/>

New Chinese loans to Africa, 2000-2022, USD billion



Source: prepared by the HSE University Center for African Studies based on Boston University Global Development Policy Center data.

Main defaulters

In 2023, African debt in default totalled USD 130 billion, 13% lower than in 2022 but still 30% more than 2020. Four countries account for 90% of the defaulted debt: **Ghana** (USD 44 billion), **Sudan** (USD 43 billion), **Zimbabwe** (USD 16 billion) and **Zambia** (USD 14 billion)¹². Significant stocks of debt in arrears are also held by **Mozambique**, **Libya**, **Tanzania**, and **Ethiopia**.

Sudan owes most of its debt to Paris Club countries (23%), Saudi Arabia (13%), Kuwait (7%), China (6%) and the IMF (8%). In 2021, Sudan entered the HIPC initiative and was planning to restructure 90% of its USD 55 billion in debt. However, in 2022 IMF suspended the programme after the military coup and removal of the transitional government.¹³

Ghana's 60% of debt in arrears is attributed to eurobonds which complicates the restructuring as it involves many private lenders and non-Paris Club countries. After defaulting on a debt of USD 30 billion in 2022, Ghana entered the G20 Common Framework in January 2023, which helped to facilitate the restructuring process with China and India. In June 2024, Ghana stated that it had reached an agreement on USD 13 billion of eurobonds with private lenders; yet the remaining debt remains high. With the current yield on eurobonds maturing in 2026, Ghana will not be able to roll over the debt and default is most likely to occur without massive support from the external lenders.

Zimbabwe's debt in default is mostly owed to bilateral creditors (67%), in particular to China. Chinese lending is opaque relative to other bilateral creditors to the level that the fact of technical default may not

¹² Afreximbank. State of Play of Debt Burden in Africa in 2024. URL: <https://www.afreximbank.com/reports/state-of-play-of-debt-burden-in-africa-2024-debt-dynamics-and-mounting-vulnerability/>

¹³ Al-Monitor. Western creditors suspend debt relief to Sudan over coup as country's economy sinks. URL: <https://www.al-monitor.com/originals/2022/06/western-creditors-suspend-debt-relief-sudan-over-coup-countrys-economy-sinks>

be disclosed. Little visible progress has been made to restructure Zimbabwe’s debt: in January 2023, the US left the restructuring programme¹⁴ “due to lack of progress on democratic reforms, alleged voter fraud and political violence targeted at opposition parties”¹⁵.

In 2023, **Zambia** reached an agreement with creditors including China to restructure USD 6.3 billion of debt and is planning to complete its restructuring programme in 2025.

Quantifying the debt burden

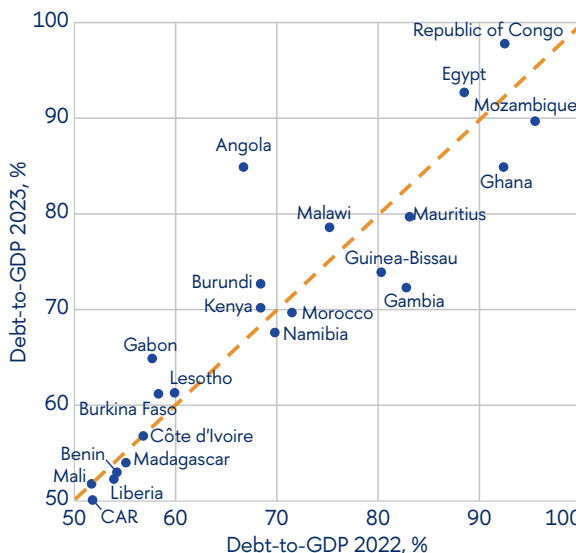
Debt-to-GDP ratios above 100% are common among developed economies with well-capitalised markets, diversified sources of credit and hard domestic currency. Usually, for developing countries debt greater than GDP is a crisis that has already occurred.

In 2023, only three states had public debt level above GDP: Cabo Verde (113%), Sudan (256%) and Zambia (110%) with Sudan and Zambia being among top defaulters. 11 countries fell in range between 75 and 100% and 22 sovereigns resulted in 50-75% debt-to-GDP bracket.¹⁶ Overall, 19 out of 51 countries with available data demonstrated debt-to-GDP ratios above 70%.¹⁷ However, in 2023, only 22 countries experienced debt-to-GDP ratio increase.

In theory, external debt had to be paid in foreign currency earned mainly through trade. Thus, another dimension of debt sustainability can be obtained by comparing external debt with exports and primary income (profits from investments in other countries and residents’ remittances from abroad). In 2022, 15 countries surpassed the 240% debt-to-exports threshold, and 9 more sovereigns breached the ‘medium’ target of 180%.

In the long term, greater importance for debt sustainability of developing export-oriented African economies attached to **export diversification**,

Public debt to GDP in 2022–2023



Source: prepared by the HSE University Center for African Studies and Intexpertise based on World Bank data.

since fluctuation of individual commodity prices are common and may question economic growth for years, which is the case with, for example, oil-rich Angola. The diversification of the exports is a target recognised by many governments, yet there is a lack of measurable indicators to follow the achievements.

If the export is grouped by main categories, the sectoral Hirschmann index may be used to measure the distribution of a country’s exports across different sectors of the economy.¹⁸ The index was calculated by for 54 African countries for the year 2022 based on the data taken from the two-digit level of the Harmonised System and grouped by categories by expert assessments.

The index ranges from 0 to 1, with higher values indicating that exports are more concentrated in fewer sectors. Conventionally, we can assume that values between 0 and 0.25 represent a ‘very high’ level of export diversification, values between 0.25 and 0.5 represent a ‘high’ level, values between 0.5 and 0.75

14 The US does not have a great presence in Zimbabwe’s bilateral debt, however, their influence on the overall restructuring progress should not be underestimated since a large share of banks and credit rating agencies are located in the US.

15 VOA Zimbabwe. United States Suspends Role in Zimbabwe’s Debt Restructuring Program Citing Electoral Fraud. URL: <https://www.voazimbabwe.com/a/united-states-suspends-role-in-zimbabwe-s-debt-restructuring-program-citing-electoral-fraud/7463023.html>

16 Afreximbank. State of Play of Debt Burden in Africa in 2024. URL: <https://www.afreximbank.com/reports/state-of-play-of-debt-burden-in-africa-2024-debt-dynamics-and-mounting-vulnerability/>

17 International Monetary Fund. The Debt Sustainability Framework for Low-Income Countries. URL: <https://www.imf.org/external/pubs/ft/dsa/lic.htm>

18 Calculated by the authors on the basis of World Bank and ITC Trade Map data using the formula: $\sqrt{\sum_i \left[\frac{X_{i,c}}{X_c} \right]^2}$, where s is the country of interest, d – other countries, i – sector of interest, x – the commodity export flow, X – the total export flow of country s .

represent a 'low' level, and values between 0.75 and 1 represent a 'very low' level of export diversification.

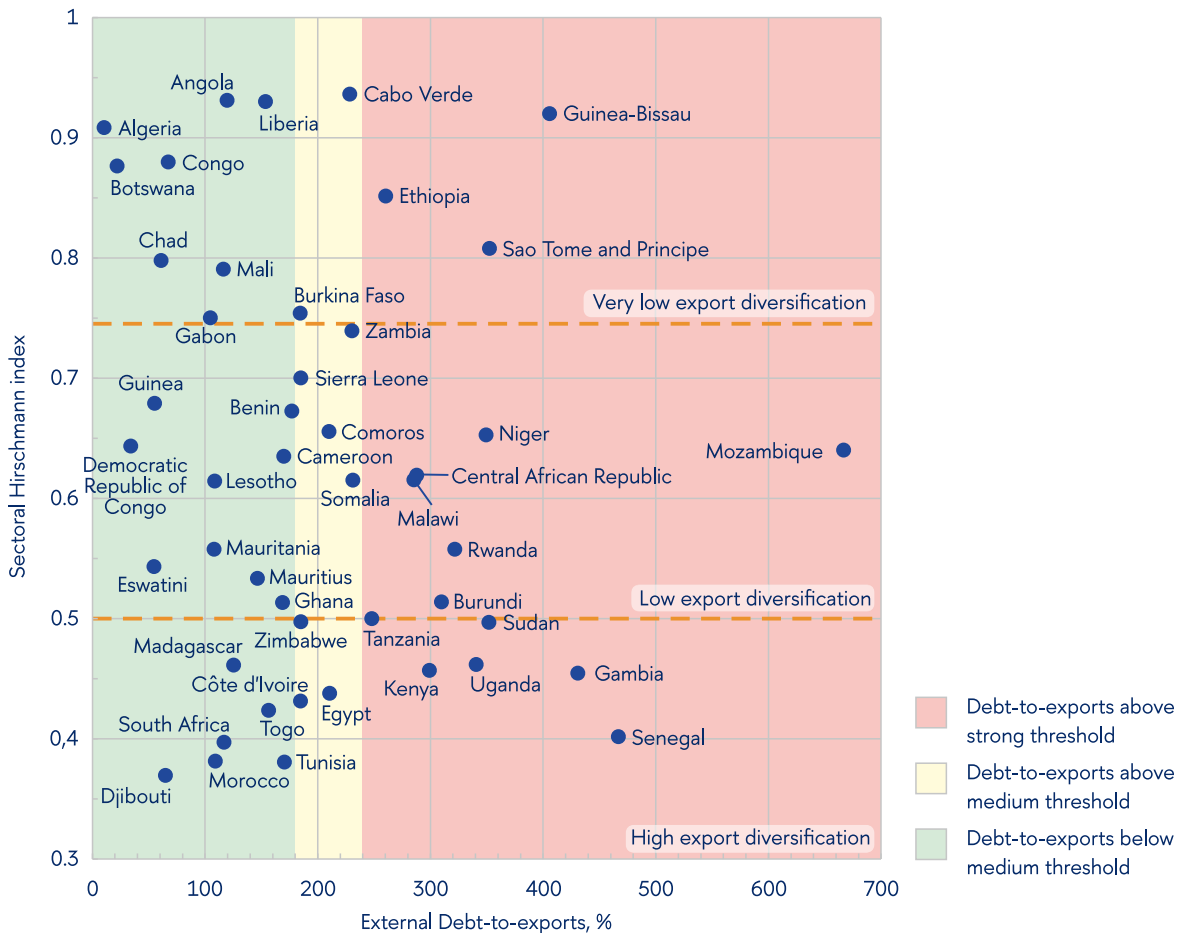
In this regard, the most vulnerable countries are those with high debt-to-exports ratio and very low export diversification, namely Guinea Bissau, Sao Tome and Principe, and Ethiopia

The cost of servicing debts also matters in this regard, although it is more difficult to account due to lack of data. Nevertheless, what is more important in the long run, that debt can stimulate the development of new industries and export diversification (which is needed almost everywhere in Africa). If this does not happen, and debt accumulates without diversification effects, the economy is likely to approach a crisis.

Very low export diversification and above medium threshold debt-to-exports ratio are observed for Cabo Verde, in turn above strong threshold debt-to-exports and low export diversification can be seen for Mozambique, Niger, Central African Republic, Rwanda, Malawi and Burundi.

In case commodity prices plummet or international trade stops, which was the case during pandemic, currency inflow dries up and governments appeal to central banks for currency reserves to finance external debt. From now on, time is ticking as reserves are getting thin (15-20% decrease of reserves in month-of-imports ratio from 2019 and 50% from 2007) and more investors are betting on

External debt and trade diversification



Source: prepared by the HSE University Center for African Studies and Intexpertise based on World Bank data.

national currency depreciation (10% since 2019 for developing countries). In 2022, precariously low levels of reserves relative to external debt had Zimbabwe (4.3%), Mozambique (4.5%), Chad (5.9%), Ethiopia (10%), Zambia (10.3%) and Ghana (11.6%).¹⁹

Abstract debt level directly affects the social sphere. In theory, countries invest borrowed money in lucrative projects and use their proceeds to pay off debts while both national income and standard of living improve.

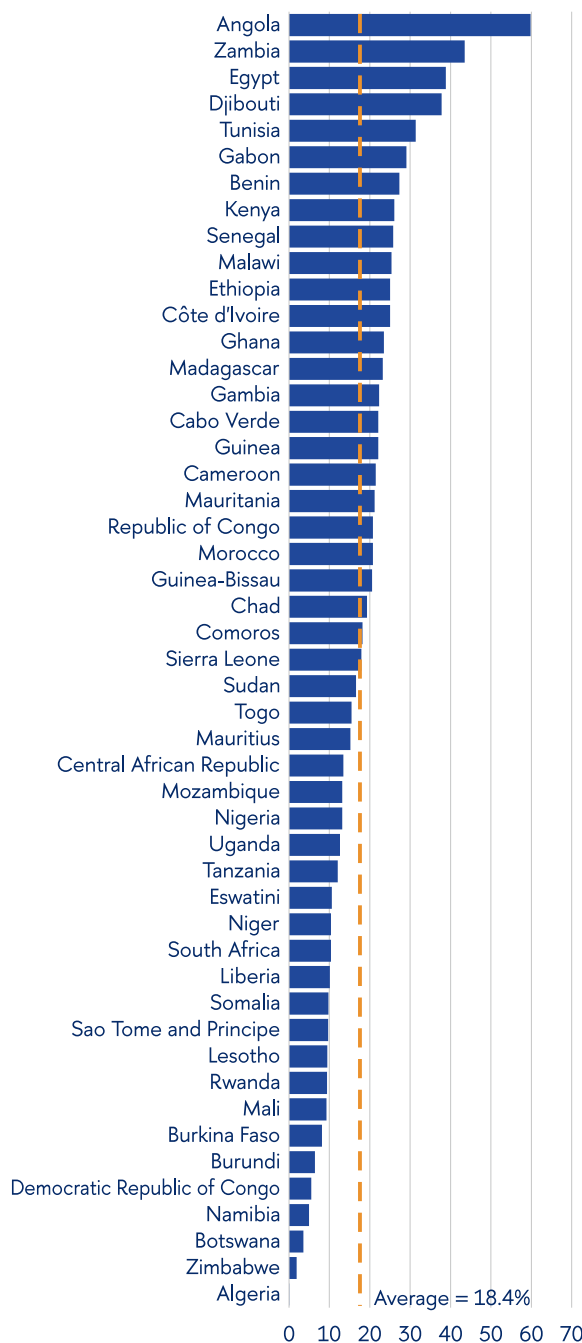
In Africa, however, debt service accounts for 16% more expenditures per capita than education and 79% more than health, which often leads to the opposite of an improved standard of living²⁰

In 2024, payments on external debt are expected to take more than 23% of government revenues in 14 countries.²¹ A particularly dramatic share of revenues is spent on debt service in Angola (60%), Zambia (43.5%), Egypt (39%) and Djibouti (38%).

Internal lending between African countries is conducted mainly through the African Development Bank. Borrowing from government to government is vastly underdeveloped and is carried out in foreign currency, mainly US dollars. Private lending via establishing branches of national banks abroad is untraceable and often depends on the policy of foreign investors since they represent a significant share of ownership of African banks.

The exceptions prove the rule, with some politically driven deals: Libya has offered loans to Chad (USD 277 million), Angola to Sao Tome and Principe (USD 18 million), Guinea (USD 15 million), Guinea Bissau (USD 5 million); Côte d'Ivoire to Burkina Faso (USD 100 million).

Debt service to government revenues, %



Source: prepared by the HSE University Center for African Studies and Intexpertise based on World Bank data.

19 World Bank

20 A world of debt 2024: A growing burden to global prosperity

21 Debt data portal. URL: <https://data.debtjustice.org.uk/>

Rating agencies and African premium

International credit rating agencies (CRA) still play a vital role in accessing credit risk. Major rating agencies like S&P, Moody's and Fitch have limited coverage with only 30 African countries included. However, rating agencies are not only observers: in fact, they determine the cost of borrowing, and it is their decision which may exacerbate the debt burden. Recent studies question credibility of the CRA towards Africa: according to the UNDP.

African countries have lost USD 74.5 billion because of biased credit ratings²²

Researchers from UNDP have found that African countries have lower credit ratings on average than non-African states with the same level of GDP per capita. For instance, Tunisia has a 2.5 times lower rating than Philippines, Egypt has a 1.8x lower rating than Indonesia, Mauritius has a 30% lower rating than Chile. Advocates of CRA associate the disparity with underdevelopment of political institutions in African states, which sometimes may be difficult to capture statistically. In turn, their opponents remind about the country of origin of all widely accepted ratings (the US) and the resulting overuse of western-centric financial power.²³ In 2022 Moody's purchased a controlling stake in leading African CRA Global Credit Rating, further consolidating its leadership on the continent.²⁴

Another important problem lying in the same dimension is risk perception of Africa among foreign investors. The existence of an "African premium" – i.e. higher borrowing cost solely because of the geographical affiliation with Africa – is a highly controversial issue. While according to traditional models it may seem irrational, the lack of transparency and structural challenges as was

mentioned previously could explain elevated yields.²⁵ From a behavioural perspective, there are several interpretations: ambiguity aversion based on the lack of relevant information about most of the African states and their economies, the presence of foreign bias as a result of the greater distance between Africa and its main investors' countries of origin or, finally, simple overestimation of probabilities of shocking events such as wars and natural disasters.

Taking into account the role that CRA played in the global financial crisis of 2008, their opinion may be far from objective as their main incentive remains their own profit. Several initiatives among African countries were announced as alternatives in the field of credit ranking like **Sovereign Africa Ratings** (SAR) or **African Credit Rating Agency**. However, SAR has published reports only for Ghana, South Africa and Kenya. Until 2019, the Chinese **Dagong Global Credit Rating**²⁶ published ratings of 16 African countries. They were significantly different from western agencies' estimations and favoured borrowers and trade partners of China. In 2019 Dagong was nationalised after a series of corruption stories and stopped updating African ratings. In any event, the insightful supervision and suitable methodology matter more for debt sustainability than the final rating.

External debt country classification

Any linear rating of countries takes into account many heterogeneous factors with different weights. If it claims to be unbiased, it is likely to be manipulated. A linear rating can only be correct in relation to the interests of a single actor who orders this rating - for their own decision-making or for

22 UNDP. Reducing the cost of finance in Africa. <https://www.undp.org/sites/g/files/zskgke326/files/2023-04/Full%20report%20-%20Reducing%20Cost%20Finance%20Africa%20Report%20-%20April%202023.pdf>

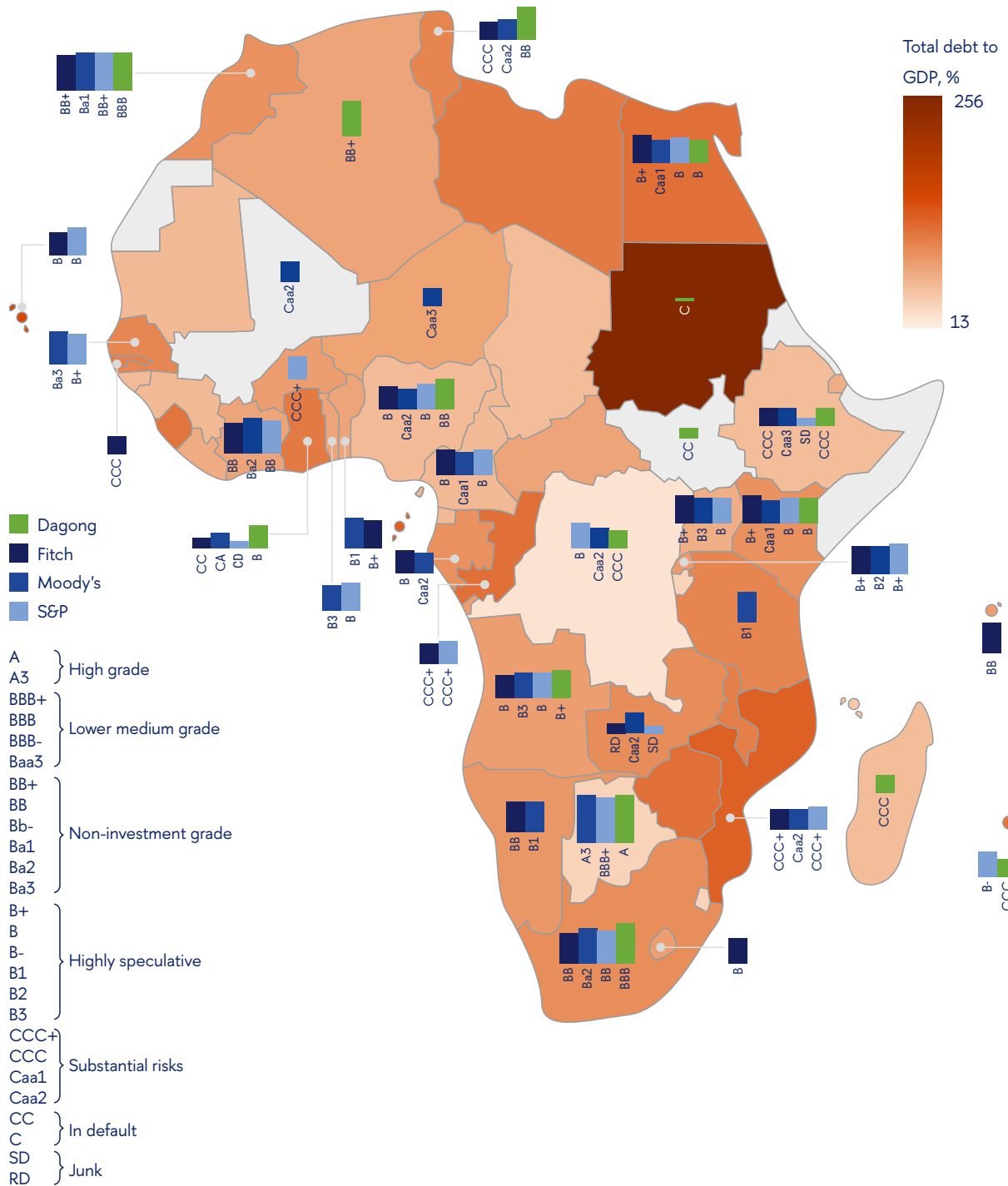
23 Reuters. How Africa's 'ticket' to prosperity fueled a debt bomb. URL: <https://www.reuters.com/investigations/how-africas-ticket-prosperity-fueled-debt-bomb-2024-08-01/>

24 The conversation. Moody's has bought a leading African rating agency: why it's bad news. URL: <https://theconversation.com/moodys-has-bought-a-leading-african-rating-agency-why-its-bad-news-176827>

25 William Gbohoui, Rasmané Ouedraogo, Yirbehogre Modeste Some. Sub-Saharan Africa's Risk Perception Premium: In the Search of Missing Factors. URL: <https://www.imf.org/en/Publications/WP/Issues/2023/06/23/Sub-Saharan-Africas-Risk-Perception-Premium-In-the-Search-of-Missing-Factors-534885>

26 Note that Dagong Global Credit Rating is a Chinese state-owned credit rating agency with headquarters in Beijing, while Global Credit Rating also known as GCR Ratings has become affiliate of Moody's with offices in Mauritius, South Africa, Nigeria, Kenya and Senegal.

African countries investment grade



Source: prepared by the HSE University Center for African Studies and Intexpertise based on Dagong, Fitch, Moody's, S&P and World Bank data.

influencing markets through publications. But some components are unbiased and worth considering, so that everyone can make their own rating weighing these components their own way.

Indicators reviewed in this chapter (sectoral Hirschmann index, debt-to-GDP, debt-to-export, reserves-to-debt, debt-to-service and service-to-revenues ratios) might be summarised and adjusted to reflect heterogeneity caused by restructuring practices as well as country's debt repayment discipline.

Four countries are considered **solvent under most scenarios**, namely **Algeria, Botswana, Mauritius and Morocco**. Their strong debt indicators and impeccable repayment history guarantee future performance on the external debt. 19 more countries are solvent under normal conditions – i.e. if no abrupt hikes in global interest rates or highly unexpected domestic shocks like civil war appear.

15 countries are sensitive to adverse trade shocks equivalent to pandemic or severe currency depreciation as their debt greatly exceeds their export revenues which are often poorly diversified and backed by small amounts of foreign currency reserves.

Ten countries have significant risk of debt distress even under current conditions. Either their expansionary debt dynamic causes concern, future debt repayments, poor fiscal performance or political uncertainty.

Finally, 4 countries are in default on most of their external debt. They participate in restructuring programmes and are mainly excluded from the international capital market.

This external debt classification requires further research, adjustment and validation, including the use of tools based on artificial intelligence. Such research is highly recommended as this preliminary assessment reveals that there are significant discrepancies between unbiased calculations and publicly available ratings.

With some exceptions, fast-growing Eastern African economies demonstrate less sustainable debt levels in comparison with slower-developing Western African countries. Three explanations can be drawn to attention:

Monetary. Western African countries use the CFA franc, which is pegged to the euro, thus alleviating currency and inflationary risks and resulting in a sustainable debt profile. However, the usage of national currencies in Eastern Africa may have a positive impact on overall growth since countries are free to conduct independent monetary policy.

Geopolitical. Eastern Africa gravitates towards market-oriented China and cultivates corresponding values such as competition and pursuit of revenue, while Western Africa is more attached to the Paris Club countries, promoting transparency but giving the best offers to the most loyal governments with a lot of loans being politically driven.

Reciprocal. Key trading partners of Eastern African countries are rapidly developing Asian economies willing to allocate capital to cover future demand. Overall positive expectations backed by strong demographics and economic indicators fuel the debt expansion process.

The domestic debt of Africa

Most African countries have traditionally relied on external debt in the form of long-term, concessional financing from multilateral and bilateral lenders or non-concessional private financing. In an effort to diversify their financing sources and reduce the risk of external debt vulnerability, they have turned to domestic debt markets in recent decades. Although, the amount of external financing continues to exceed that of domestic funding.

Domestic debt refers to the portion of a country's total debt that is owed to creditors within its own borders. Domestic debt can therefore be described as debt which is issued in the sovereign's local currency, or debt which is governed by the domestic sovereign laws. It can also be defined as debt which is held by residents of the issuing sovereign.

Significant share of the domestic debt is held by the entities borrowing themselves from abroad. Most of the domestic debt issued by low-incomes sub-Saharan African countries is held by commercial banks which, in turn, often have foreign shareholders. In 2022, the size of domestic debt in **Egypt** was estimated at 72% of GDP, while in **Zambia** it was 40% of GDP and in **Zimbabwe** it was 12% of GDP.

The structure of domestic debt also differs. In Benin, government bonds account for 91% of the domestic debt, in Senegal it is 67% and in Zimbabwe it is 30%. Government bonds and eurobonds account for a significant portion of Egypt's domestic debt. In Rwanda, they make up 50% of the total, in Mauritania 68%, and in Nigeria 79%. In Mali, they account for an even larger percentage – 92%.

The detailed structure of the holders of domestic debt is rarely disclosed. For example, in Kenya, 43% of the debt is owed to commercial banks, 33% - to pension funds, while 7% to insurance companies, and 4% is held by the Central Bank²⁷. The main buyers of Tanzanian government bonds are pension funds, commercial banks and the Bank of Tanzania. Together, these three financial institutions account for almost 80% of the total volume of loans on the financial market. Approximately 29% of this volume is accounted for by commercial banks and pension funds, with the Bank of Tanzania accounting for 22%²⁸.

Domestic debt has several advantages, especially for African countries. First of all, most of the domestic debt in Africa is denominated in local currencies, which means that it is shielded from exchange rate fluctuations and currency mismatches. In addition, issuing debt in domestic currency gives central banks and governments the

flexibility to use monetary policy tools for domestic debt management. For decades, businesses and households have preferred to invest money abroad, and capital flight remains a critical issue for most African economies, co-existing with extensive external borrowing. Investing in domestic debt is a good alternative, especially if intermediated by strong local banks.

Domestic debt defaults are less common than external debt defaults

The reason is that authorities have more options for dealing with domestic debt, such as inflating it away, rather than resorting to outright default. In the event of a debt default, domestic debt is usually easier to restructure, as it is subject to domestic court jurisdiction. A case study conducted by the IMF on debt restructurings between 1988 and 2020 concluded that domestic debt restructuring took considerably less time to complete compared to external debt restructuring, largely due to a greater sovereign control of the terms and laws governing domestic debt²⁹. Moreover, by restructuring domestic debt, countries can avoid the potential reputational costs associated with external debt restructurings and, in some cases, maintain access to international financing.

Well-developed domestic public debt markets offer local investors opportunities to invest in government securities, providing a two-fold advantage. First and foremost, domestic investors have the opportunity to participate in the economy and receive a reasonable return on their investments, given the relatively low risk associated with government securities.

Levels of development in local capital markets differ³⁰ – from more than 100% of GDP in Egypt, Morocco, Mauritius and South Africa to below 40% in Cameroon, DR Congo, Ethiopia, Madagascar

27 REPUBLIC OF KENYA THE NATIONAL TREASURY AND PLANNING. Annual Public Debt Management Report For Financial Year 2022/2023. URL: <https://www.treasury.go.ke/wp-content/uploads/2024/01/Annual-Public-Debt-Report-2022-2023-Sept-2023.pdf>

28 World Bank. 20th Tanzania Economic Update. URL: <https://documents.worldbank.org/en/publication/documents-reports/documentdetail/099031124044543127/p1796101f356d10fa1b47215b969e1205b2>

29 UN. World Economic Situation and Prospects: April 2024 Briefing, No. 180. URL: <https://www.un.org/development/desa/dpad/publication/world-economic-situation-and-prospects-april-2024-briefing-no-180/>

30 The size of the financial system can be determined by various indicators, such as the total assets of the banking sector, market capitalisation of banks, credit facilities, insurance, and investments. Other indicators include the financial transactions of capital markets, the ratio of private credit to GDP, and the percentage of adults who have formal bank accounts. Additionally, the stability of financial institutions is also a factor in determining the size of the system.

and Uganda³¹: in the more developed economies, governments have more opportunities to raise funds domestically.

Secondly, by attracting financing from the domestic market, governments provide residents an alternative for capital outflows. Some countries combine borrowings with the measures to reduce capital outflow exposure. For example, Zambia, which has a relatively higher level of non-residents participating in the domestic debt market (above 20%), has enacted measures to limit non-residents' participation in the government bonds primary market to 5%.

Nevertheless, domestic debt can have several long-term implications that can negatively impact the economy of a country. One of the main disadvantages of domestic debt is that it can lead to significant crowding out effects for the domestic private sector. This is because when the government is a major borrower, the credit available to the private sector from banking and non-banking financial institutions can decrease.

Another challenge is the maturity structure of domestic debt instruments, as many governments are unable to issue long-term instruments at reasonable interest rates. In 2022, in Zambia and Kenya short- and medium-term securities comprised 78.5% and 78% of the domestic debt portfolio respectively. The proportion was even higher in Ghana, where short- and medium-term securities accounted for approximately 90%. This short-term debt structure increases the risk of rollover, where governments continuously borrow to pay off maturing debts.

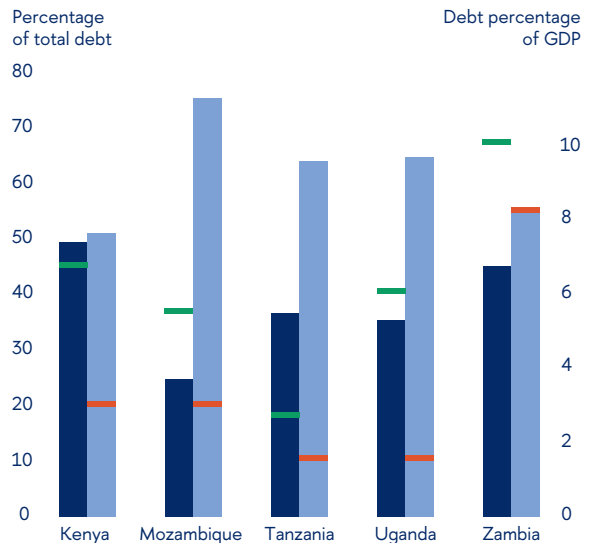
In leading economies like Egypt, Ethiopia, and Nigeria the financial sector is partly publicly owned. Consequently, the authorities may attempt to maintain the debt at a manageable level through various financial measures. However, the side effects can include crowding out lending to the private sector with long-term detrimental effects on economic performance and competitiveness.

In some countries, the high burdens of domestic debt service place a heavy strain on government finances, leading to further reductions in spending that could be allocated to investments in crucial sectors. For example, in **Kenya, Mozambique, Tanzania, Uganda** or **Zambia** domestic debt service cost was higher than external debt service, despite domestic debt stock being lower than external debt stock. In 2023, the cost of servicing domestic debt in Uganda was 2.8% of GDP, while external debt was only 0.9%.

Since 2020, two African countries (Ghana and Mozambique) have defaulted on domestic obligations, while five (Angola, Ethiopia, Kenya, Uganda, and Nigeria) have engaged in non-commercial debt exchanges.

Debt service payments in selected economies in Africa, 2022

- Domestic debt stock as a percentage of total debt (LHS)
- External debt as a percentage of total debt (LHS)
- Domestic debt service as a percentage of GDP (RHS)
- External debt service as a percentage of GDP (RHS)



Source: prepared by the HSE University Center for African Studies and Intexpertise based on IMF and UN DESA data.

31 S&P Global. African Domestic Debt: Reassessing Vulnerabilities Amid Higher-For-Longer Interest Rates. URL: <https://www.spglobal.com/research/articles/231101-african-domestic-debt-reassessing-vulnerabilities-amid-higher-for-longer-interest-rates-12900489>

Ghana's debt default (external and domestic) and the subsequent restructuring has put the spotlight on domestic debt in Africa. Domestic debt grew from 22% of GDP in 2015 to approximately 40% of GDP in 2021 mainly because of government borrowing to finance the energy sector and to bail out the finance sector following the 2018–2019 financial crisis.

At the time of default in December 2022, domestic debt stood at 46% of GDP. Some of the factors contributing to the default included an inflated import bill due to effects of the Ukrainian crisis, drastic depreciation of the Ghanaian cedi and increased cost of debt service. At the same time, external shocks triggered significant capital outflows, which diminished access to international financial markets. Moreover, foreign exchange reserves dwindled to 2.7 months of import cover at end-December 2022, down from 4.3 months at end-December 2021.

In December 2022, the Ghanaian government initiated a domestic debt exchange programme, aimed at restoring sound public finance management and debt sustainability. Domestic bondholders were offered an option to exchange their holdings with a fresh issuance of bonds with longer average maturities and lower coupon rates. New bonds were issued at a coupon rate between 0% and 10%. Before the exchange, interest rates for two-six years notes ranged between 21.5% and 29.85%. Although the programme managed to lower interest rates on government securities and lengthen their maturities, analysis by the country's financial sector regulators showed that it adversely affected the solvency of some banks and insurance companies. The government formed the Ghana Financial Stability Fund to minimise impacts of the restructuring process to the financial sector and to avoid risks of a potential financial crisis. The restructuring also took a relatively short time, with the domestic debt exchange programme concluded in 2023. Inflation declined from 54% in December 2022 to 23% in February 2024. The economy also grew at an average of 3% in 2023.

Africa's trade: a terrible scarcity or a huge opportunity

Africa relies heavily on international trade, and this reliance has increased over the past decades. Trade serves as a source of foreign exchange, which is needed to import the capital goods required by local producers. Additionally, it has the potential to enhance productivity and to contribute to job creation and economic growth. In 2000, Africa's total trade was around USD 500 billion. By 2023, it had grown to over USD 1.3 trillion.

The trade dependence index³² has increased significantly in all regions of the world, including Africa, over the past three decades. The trade dependence index demonstrates the importance of trade for a particular country and also characterises the degree of openness of the economy, which involves both,

risks and opportunities. Africa's average trade ratio has increased from 45% in 1991–2000 to 59% between 2020 and 2023. However, there is a wide variation in index ratios among economies, ranging from 8% in **Sudan** to **Djibouti** and **Lesotho** with their ratios of 264% and 125%, respectively, in 2023.

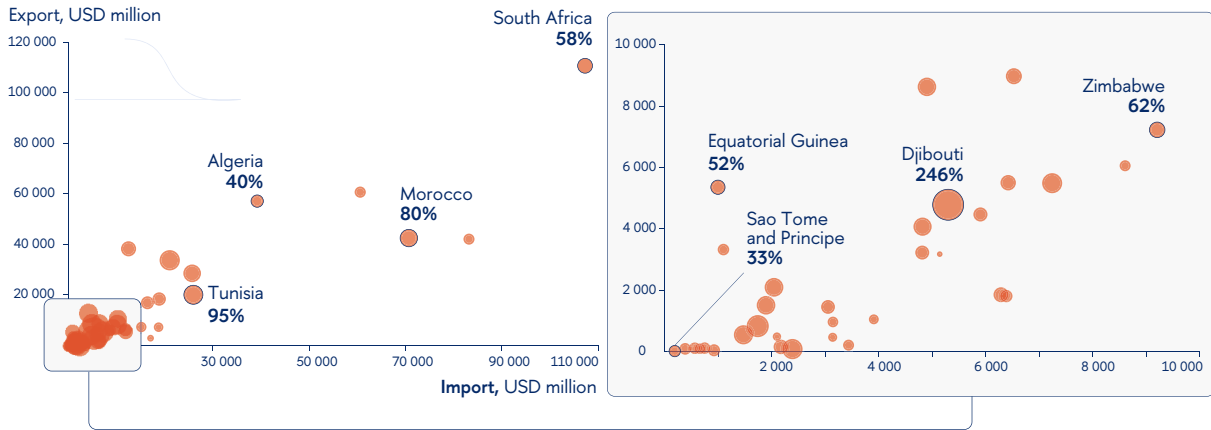
For 25 countries the trade dependence index is still below 50% level, for 22 it ranges from 50% to 100%. In Djibouti, Lesotho, Libya, The Gambia and Namibia the index exceeded 100% in 2023. While Djibouti, Lesotho and the Gambia are re-exporting extensively to the neighbouring countries, Namibia and Libya are both the exporters of natural resources with relatively small populations.

However, the increased role of international trade in African economies was accompanied by growing **trade deficits** in many countries on the continent.

³² Calculated by the authors on the basis of World Bank and ITC Trade Map data using the formula: $\frac{\sum_s X_{ds} + \sum_s M_{sd}}{GDP_d} \times 100$, where d – country under study, s – is the set of all other countries, X – total bilateral exports of country d , M – total bilateral imports of country d , GDP – gross domestic product of country d .

Trade dependence index for African countries, 2023

Trade Dependence Index, % 10% ○ ○ ○ ○ 250%



Source: prepared by the HSE University Center for African Studies and Intexpertise based on ITC Trade Map data.

The increasing trade deficits pose challenges for job creation and poverty reduction efforts especially when the deficits are caused by rising imports of consumer goods that can be produced by domestic industries. The trade deficit often co-exists with the current account deficit, which in turn may increase debt burden. Growing current account deficits often presage disruptive economic trends such as sudden stops in capital flows, severe decreases in credit and spending and sharp economic slowdowns, which generate high unemployment and poverty.

A trade deficit is sustainable as long as there are sufficient funds to finance it. In last decades African countries had probably better access to international finance than ever. However, with growing interest rates and slowing growth, the continent faces risks of much more complicated access to finance which will make financing of the deficits increasingly challenging.

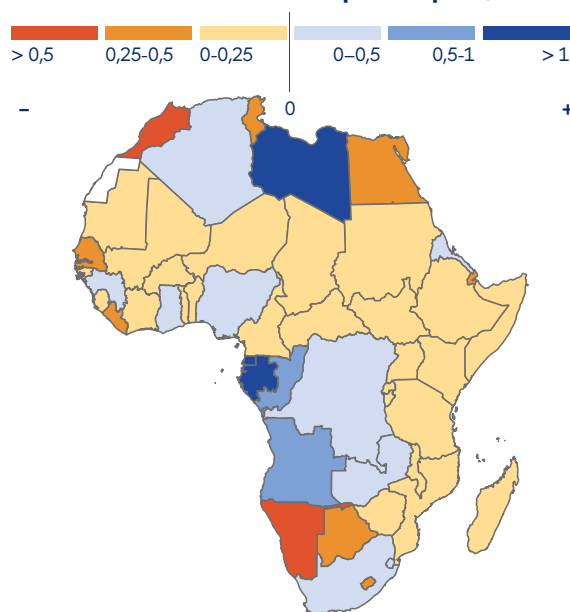
In 2023, the overall external trade deficit of Africa amounted to USD 84.8 billion. Although some countries experience a high surplus in their trade balance, the large deficit recorded by most negates these surpluses, resulting in a deficit trade balance for the continent. In 2023, the sum of the trade deficits was USD 169.5 billion.

Only 15 out of 54 countries on the continent recorded a trade surplus, their total was 84.9 billion. The top five countries with the largest trade surpluses in 2023 were **Angola** (USD 25.8 billion), **Algeria** (USD 17.9 billion), **Libya** (USD 12.7 billion), Gabon (USD 8.5 billion) and **Equatorial Guinea** (USD 4.4 billion). All these countries are oil and natural gas exporters.

On the other hand, the five largest countries in terms of trade deficit were **Egypt**, **Morocco**, **Ethiopia**, **Kenya** and **Tanzania**. Collectively, these five countries recorded the total trade deficit of USD 102.8 billion. Among the deficit countries, there has been a deterioration in the trade deficits over the time. Between 2013 and 2023, the trade deficit in Morocco increased by 26%, in **Ethiopia** by 21%, in **Senegal** by 75% in **Uganda** by 44% and in **Niger** by 124%.

In per capita terms, three countries had significant surpluses: **Gabon** (USD 3,469 per person), **Equatorial Guinea** (USD 3,469 per person) and **Libya** (USD 3,469 per person). In 2023, **Nigeria's** per capita trade surplus was USD 0.3. The island countries had the highest trade deficit per capita, with Seychelles, Mauritius and Cabo Verde topping the list.

Africa's trade balance per capita, 2023



Source: prepared by the HSE University Center for African Studies and Intexpertise based on ITC Trade Map data.

Exports and imports of most countries are highly volatile as they depend on commodities. So, the **accumulated trade balances** of the individual countries would provide a clearer picture of their role in international trade.

Africa's cumulative trade deficit over the period from 2014 to 2023 amounts to USD 839 billion

Over this ten-year period, **Angola** has been a significant leader with a trade surplus of USD 234.3 billion. By a wide margin, **Libya** (USD 83 billion), **Nigeria** (USD 81 billion), **South Africa** (USD 62 billion), **Equatorial Guinea** (USD 50 billion), **Djibouti** (USD 48 billion), and **Gabon** (USD 46 billion) were the next on the list of African countries with a trade surplus. Most of the countries that have a trade surplus are resource-rich (Angola, Libya, Equatorial Guinea, Gabon, Nigeria, etc.) or serve as the logistics hubs for neighbouring countries (Djibouti, Ghana). In total, only **16 countries** on the continent were identified with a long-term positive trade balance.

However, the number of countries with persistent trade deficits is considerably higher. **Egypt** accounts for almost half of Africa's total trade imbalance, which amounts to USD 455 billion. **Morocco** (USD 217 billion), **Ethiopia** (USD 127 billion), **Kenya** (USD 112 billion), **Tunisia** (USD 64 billion), **Tanzania** (USD 55 billion), **Sudan** (USD 44 billion), **Senegal** (USD 42 billion) and **Uganda** (USD 41 billion) have also become leaders in the cumulative trade deficit.

A number of African countries have recorded relatively low trade deficits, up to USD 5 billion: **Guinea-Bissau** (USD 0.8 billion), **Democratic Republic of the Congo** (USD 1.1 billion), **Sao Tome and Principe** (USD 1.5 billion), **Comoros** (USD 2.3 billion), **Central African Republic** (USD 4 billion) and Botswana (USD 4.7 billion). But if USD 1.1 billion in 10 years seems to be close to nothing for DRC, USD 1.5 billion for São Tomé is huge.

The most balanced trade³³ over a ten-year period is recorded for **Nigeria** (0.08), **Côte d'Ivoire** (0.05), **Zambia**, **South Africa**, **Eswatini** and **Ghana** (with 0.3 for each country), as well as **Algeria** (-0.02), **Botswana** (-0.03), and **DRC** (-0.04). Guinea, Angola, and Chad have a tendency towards a large surplus in their accumulated trade balance.

In contrast, Gambia, Cabo Verde, Sao Tome and Principe, Liberia, Somalia and the Comoros tend toward a deficit in their trade balances.

Persistent and increasing trade deficits are explained differently from country to country. Chronic trade deficits can be evidence that domestic producers cannot compete with imports and/or their competitors in the global markets.

Trade deficit in some cases results from a country investing in physical capital (through imports of intermediate goods) and productive capacity, which has the potential of boosting employment and reducing poverty, provided the investments are effective and allocated to job-creating activities³⁴.

³³ The index is compiled by the authors. It is calculated according to the formula: $\text{export} + \text{import} / (\text{export} - \text{import})$ for a 10-year period.

³⁴ UNCTAD. Trade and Current Account Balance in Sub-Saharan Africa: Stylised Facts and Implications for Poverty. URL: https://unctad.org/system/files/official-document/webaldc2016d2_en.pdf

The top ten importers of capital goods in Africa in 2023 were: South Africa, Egypt, Morocco, Nigeria, Algeria, the DRC, Angola, Tunisia, Ethiopia and Tanzania. Of these countries, one half experienced a trade deficit in 2023.

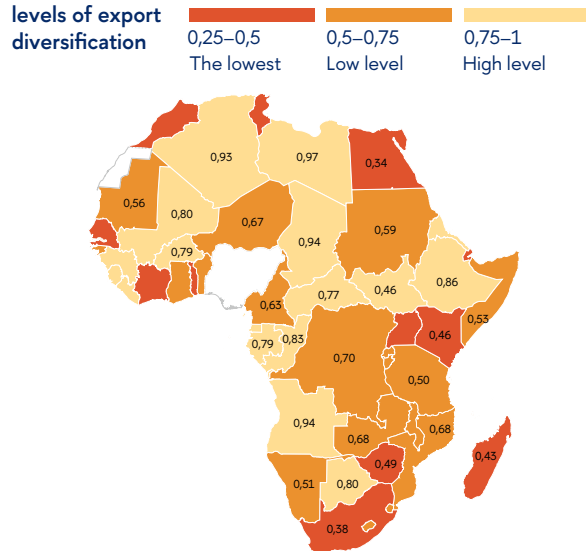
Although Africa's share of manufacturing value added to GDP is expanding, Africa's market share in manufacturing exports lags far behind the global average, accounting for roughly 1.3% of world exports. This gap in exports is largely responsible for the widening trade deficit. While the end of the commodity super cycle in 2014-2016 highlighted the cost of external imbalances, the lockdowns triggered by Covid-19 underscored the risk of depending excessively on imports for manufactured products. The above mentioned sectoral Hirschmann index fits well to measure the level of diversity in African exports.

In 2023, a group of 13 countries on the continent recorded a relatively **high** level of export diversification. This includes both major players in trade, such as Egypt (0.34), Morocco and South Africa (0.38 each), Tunisia (0.39) and Senegal (0.41), as well as transit hubs like Djibouti (0.36), Mauritius and Togo (0.43 each) alongside Uganda, Kenya (0.46 each) and Zimbabwe (0.49) having shown impressive performance in implementing their export diversification strategies.

In 2023, a total of 21 African countries recorded a low level of export diversification. The index in this group ranged from 0.50 in Tanzania, 0.55 in Ghana and Rwanda, and to 0.7 in the DRC to 0.73 in Guinea-Bissau. In 2023, 19 countries recorded the lowest levels of export diversification. This group included countries such as Central African Republic (0.77), Burkina Faso (0.79), Botswana and Mali (0.8 each), Republic of Congo (0.83), Ethiopia (0.86), Algeria (0.93), Angola (0.94), Libya and Eritrea (0.97 each).

The exports of these countries mainly consist of minerals such as oil, gas and gold, as well as agricultural crops like coffee. Among primary commodities, exports are concentrated in products

Sectoral Hirschmann index of African countries, 2023



Source: prepared by the HSE University Center for African Studies and Intexpertise based on ITC Trade Map data.

with relatively low levels of value-added or processing, which further limits the low potential for employment typical of commodity outputs. Consequently, the fluctuations in global commodity prices can severely impact their trade balance.

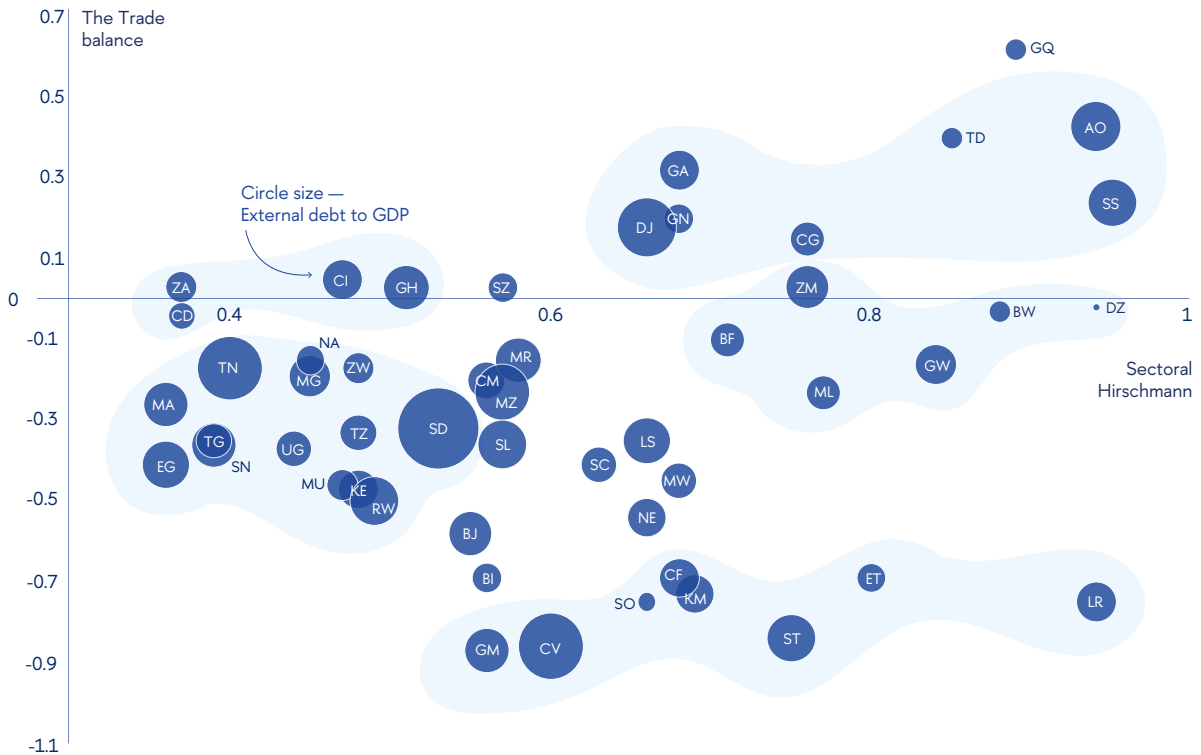
If we take the average value of the sectoral Hirschmann index over ten years and the trade balance index, we will get the following picture.

Firstly, a group of oil and gas exporting countries with a low level of export concentration and a high trade surplus can be clearly distinguished. A relative trade surplus above 1.05 (Côte d'Ivoire level) can only be found in countries with an export concentration of 0.7 or higher. The high level of export concentration also leads to a significant capital outflow, as there are less export-oriented promising industries to invest in. This group includes, inter alia, Angola, Libya and Equatorial Guinea.

The second group includes Ghana, South Africa, DRC and Côte d'Ivoire. These are exporting countries with relatively well-developed industries and a high degree of diversification, as well as a trade surplus.

Trade balance index and sectoral Hirschmann index of African countries

The trade balance index and the sectoral Hirschmann index value over a ten-year period from 2014 to 2023 are used. The index ranges from 0 to 1, with higher values indicating that exports are more concentrated in fewer sectors.



Source: prepared by the HSE University Center for African Studies and Intexpertise based on ITC Trade Map data.

However, Ghana was in default due to economic policy distortions and government waste.

The third group includes small economies, such as Liberia, Central African Republic, the Comoros and Somalia. These countries are vulnerable due to high trade deficits and lack of export diversification. As a result, they are at risk and need to either reduce their trade deficits or diversify their exports in order to ensure their economic stability.

The fourth group also includes countries that are almost exclusively dependent on exports of raw materials. Botswana, Algeria, Mali and Burkina Faso spend a significant amount of money on imports. Therefore, their governments may need to carefully monitor their imports, as they should focus on investments aimed at import substitution or the development of new export industries.

The larger economies like Egypt, Kenya, Tanzania and Morocco have relatively diverse exports and experience a relative trade deficit.

It is also worth considering how African countries cover their trade deficits.

Unilateral transfers (both current and capital) have been the main source of external finance in Africa for decades. Their weight increased during the 2000s from 2.6% of GDP in the 1990s to 4.4% in 2013 – driven by the strong rise of workers’ remittances and capital transfers that more than compensated for the decline in current transfers in the form of aid, donations and official assistance.

In 2022, remittances accounted for an average of 7.6% of GDP in Western Africa, 6.8% in Eastern Africa, 4.4% in Northern Africa, 3.7% in Southern Africa

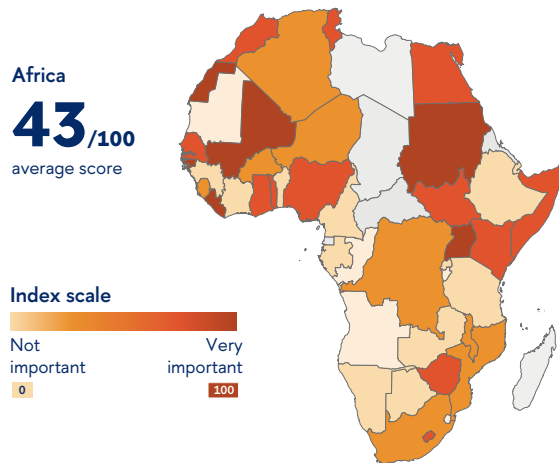
and 1.4% in Central Africa³⁵. In 2022, the World Bank remittance inflow data reported that **Egypt** is the largest recipient market (USD 32 billion), followed by **Nigeria** (USD 21 billion) and **Morocco** (USD 11 billion). These three markets account for 65% of all remittances to African countries. Most in the top 12 in terms of remittances in 2022 have chronic trade deficits, with the exception of Nigeria and Ghana.

In 2023, the total amount of remittances sent by migrants to and within Africa was almost USD 95 billion³⁶

The high reliance of most African countries on unilateral transfers reflects their increasing dependence on external sources. It is clear that for some countries remittances are vitally important to their economies. This particularly applies to **Gambia** (27% of GDP in 2022), **Somalia** (23%), **Comoros** (22%), Lesotho (20%), **Cabo Verde** (16%) and **Guinea-Bissau** (11%). Although these transfers represent a substantial source of external finance that can be an important tool for poverty alleviation, they also entail significant costs. The strong reliance on income generated from external sources increases the economic vulnerability of recipient countries and exposes them to the economic cycle of the source countries.

Beside unilateral transfers, **Foreign Direct Investment** (FDI) is also one of the main sources of external finance for Sub-Saharan Africa. FDI is often seen as the preferred and safer alternative source of private foreign capital for developing countries because of its 'non-debt' character. In addition, as FDI inflows do not involve the direct payment of principal and interest charges, they are a preferred method of financing deficits, especially in developing countries, where these deficits can be large and sustained³⁷.

The importance of remittances index



Source: prepared by the HSE University Center for African Studies and Intexpertise based on ITC Trade Map data.

Since 2000, FDI flows replaced “other investments” (mainly foreign loans) as the main source of external finance other than unilateral transfers. Net FDI flows more than doubled their share to GDP from 0.9% in the 1990s to 2% in 2013, while net flows of foreign loans registered a drastic fall, reaching high negative values as a consequence of the debt relief initiatives.

In 2021, there was an all-time high inflow of FDI into Africa, reaching USD 82 billion, but this decreased to USD 53 billion by 2023³⁸

In 2023, almost 50% of all foreign direct investment flows to Africa were directed towards Northern and Western Africa. Investments in the East accounted for 21.3% of the overall volume, with the South receiving 17.3%, and the Central receiving 11.2%.

In 2023, the accumulated amount of foreign direct investment into Africa reached USD 1.04 trillion. The **leaders are** Egypt, South Africa, Nigeria and Morocco.

35 RemitSCOPE. Africa. URL: https://gfid.org/wp-content/uploads/2023/06/RemitSCOPE_Africa_preliminary_release.pdf

36 IFAD. Improving the management of remittances and their use for development impact in Africa. URL: <https://www.ifad.org/en/prime-africa#:~:text=Remittances%20sent%20by%20migrant%20workers,quarter%20is%20invested%20or%20saved>

37 Demekas et. al., 2005, p. 209.

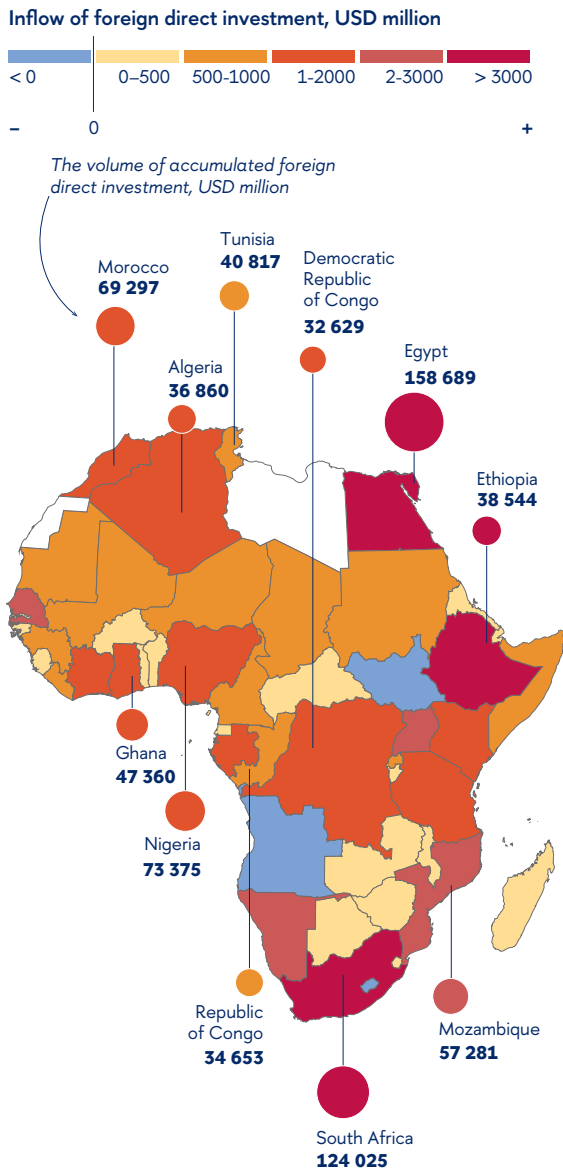
38 UN. 2024 World investment report. URL: https://unctad.org/system/files/official-document/wir2024_en.pdf

Although it is true that FDI does not involve the direct repayment of capital and interest, foreign direct investors do not invest without the expectation of profit and the eventual repatriation or relocation of the investment. Actually, the return on FDI is the highest compared to that of

other external sources of financing as the rates of profit of foreign firms largely exceed the rate of interest on foreign loans or the rate of profit related to portfolio investments.

However, for many projects with foreign investment, there are also shareholder loans and transfer pricing to avoid taxes. The actual price of raw materials is underestimated, and a country's budget does not receive the taxes that should be paid. Investors earn on access to cheaper, unmarketable raw materials so formal returns on investment are no longer as important to them. In addition, investors lend to their companies at commercial rates, as debt repayment is easier than income from capital. It is difficult to assess the impact of transfer pricing and undervaluation of exports on the balance of payments in African countries, but this can reach tens of billions of dollars per year.

Foreign direct investment in Africa, 2023



The diversity of Africa is in its currencies

The currency and exchange rate play an important role in assessing the economic stability of developing countries.

- The Moroccan dirham is classified as having a **pegged exchange rate** within horizontal bands, which since 2020 has been pegged to the euro and the US dollar in a ratio of 60% and 40%, respectively (basket of currencies).
- The Botswana pula is classified as having **crawling pegs** (in terms of a soft peg) with a bucket of the special drawing rights (SDR) and the South African rand.
- The **soft pegged** exchange rates of five countries (Malawi, Mozambique, Nigeria, Sudan and Tanzania) are categorised as peg stabilised arrangements.
- The **crawl-like** arrangements category includes 12 African countries (Algeria, Kenya, Mauritius, Tunisia, Rwanda, etc.).

Source: prepared by the HSE University Center for African Studies and Intexpertise based on UNCTAD data.

- The **conventional peg** is the largest category, including 21 countries. Of these, 17 have currencies pegged to the **euro**: the Central African CFA franc and the West African CFA franc. Three countries are pegged to the South African **rand**, including Lesotho, Namibia and Eswatini. One country's currency, Nakfa (Eritrea), is pegged to the **US dollar**.

The **floating** exchange rate is used by seven countries: Angola, Egypt, Zambia, Madagascar, Seychelles, the Republic of South Africa and Uganda. The Somali shilling's exchange rate is **free floating**.

The exchange rates of four countries (South Sudan, Zimbabwe, Liberia, and Sierra Leone) are categorised as **"other managed arrangements"**.

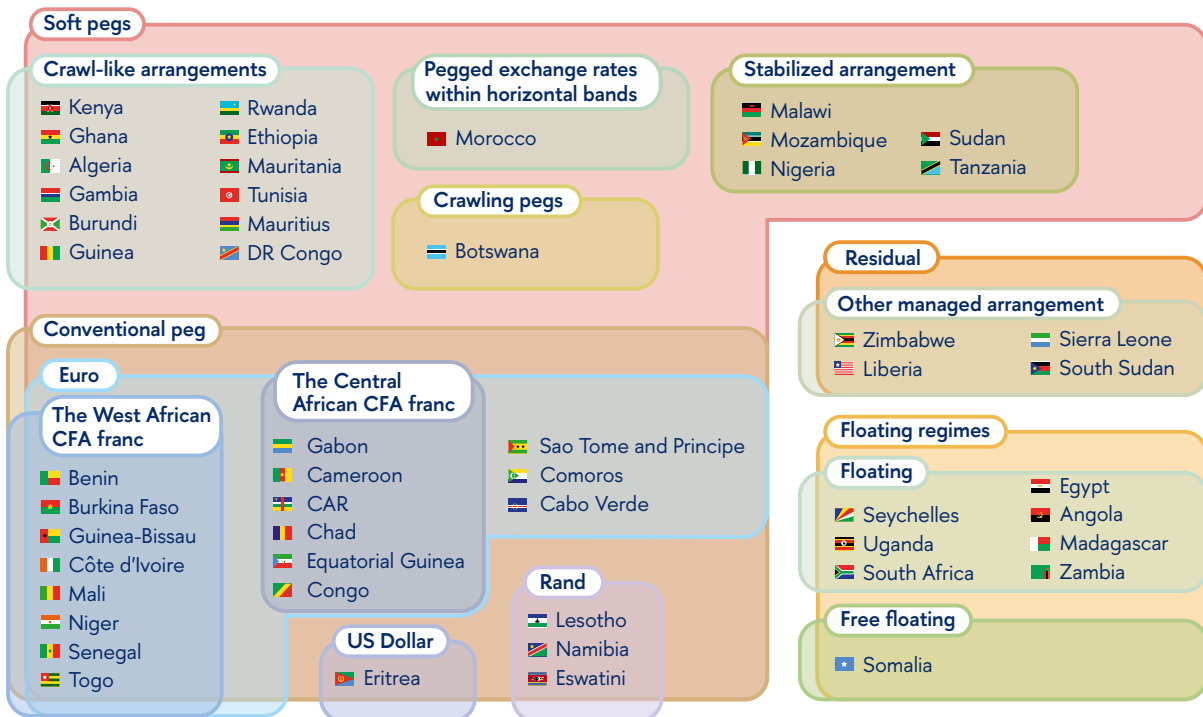
Also, based on IMF data, African countries can be classified according to the main principles of their monetary policies. There are four of them: exchange rate anchor, monetary aggregate target, inflation-targeting framework, and other.

Exchange rate anchor means that the monetary authority buys or sells foreign exchange to maintain the exchange rate at its predetermined level or within a range. The exchange rate thus serves as the nominal anchor or intermediate target of monetary policy. This type includes the WAEMU and CEMAC countries, along with Lesotho, Eswatini, Namibia and Botswana.

Monetary aggregate target is the measure when the monetary authority uses its instruments to achieve a target growth rate for a monetary aggregate, such as reserve money, M1, or M2, and the targeted aggregate becomes the nominal anchor or intermediate target of monetary policy. This monetary policy framework is implemented by 13 countries, including Nigeria, Algeria, Zimbabwe, Angola, Ethiopia, Rwanda, etc.

Inflation-targeting framework involves the public announcement of numerical targets for inflation, with an institutional commitment by the monetary authority to achieve these targets, typically over a medium-term horizon. Additional key features

Exchange rate regimes of African countries



Source: prepared by the HSE University Center for African Studies and Intexpertise based on IMF data.

normally include increased communication with the public and the markets about the plans and objectives of monetary policymakers and increased accountability of the central bank for achieving its inflation objectives. This type includes Kenya, Seychelles, Ghana, Uganda and South Africa.

The **other monetary policy framework** category means that the country has no explicitly stated nominal anchor, but rather monitors various indicators in conducting monetary policy. This category is also used when no relevant information on the country is available. This group includes Malawi, Mozambique, Sudan, Tunisia, etc.

Many African countries have substantial external debt, often denominated in foreign currencies like the US dollar or the euro

This can make debt servicing more vulnerable to exchange rate fluctuations. Fluctuations in the exchange rate can significantly impact the debt servicing costs. For example, if the local currency depreciates against the currency in which the debt is denominated, the cost of servicing and repaying that debt increases in local currency terms. This can strain the country's financial resources and balance of payments. However, countries with a fixed exchange rate regime or a currency peg might face challenges if they have high levels of external debt. Maintaining the peg can be costly, especially if the country faces a balance of payments crisis or needs to defend its currency.

Since 2022, a number of African currencies have recorded significant depreciation against the US dollar. Currency depreciation leads to an increase in foreign currency-denominated external debt. For example, **Nigeria's** external debt in 2023 increased by 100.1% over a year because of the depreciation of the national currency — the exchange rate of the Nigerian naira fell by 70% against the dollar³⁹. In **Kenya** for instance, as of December 2023, external debt – 67% of which was dollar denominated – increased by USD 1.3 billion

owing in part to depreciation of the Kenyan shilling. Also, approximately 98% of Ghana's external debt stock growth in 2023 was a result of the Ghanaian cedi's depreciation against the dollar.

The CFA franc is pegged to the euro, which has two consequences for the respective national debt. Given that external debt and international trade are both denominated in the US dollar, a depreciation of the euro relative to the dollar leads to an automatic increase in the value of the external debt of the countries that use the franc. On the other hand, an appreciation of the euro also leads to a decrease in external debt, but this can have harmful effects, such as a loss of competitiveness and market share for products being exported from these countries. In addition, this stability attributed to the franc does not necessarily reflect the reality of the economies that use it.

Thus, we see that the pegging to the euro has apparently saved the countries in the CFA franc zone from high levels of debt (as in East Africa). However, these countries are experiencing slower economic growth.

Nowadays, an increasing number of African countries are turning to gold to hedge against global political risks and protect themselves against currency losses. Several countries are trying to increase their foreign currency reserves. For instance, **Nigeria** has launched a plan to buy gold domestically to boost its reserves. **Tanzania** has announced a plan to spend USD 400 million on six tonnes of gold. The central bank of **Uganda** has announced a programme to buy gold directly from local artisanal miners.

However, in some countries, there is a discussion about tying the national currency to gold. For example, the Vice President of **Ghana**, Mahamudu Bawumia, has said that if he is elected president in the upcoming December election, he plans to introduce a new exchange rate system that will link the Ghanaian cedi to gold.

³⁹ Bloomberg. Understanding Nigeria's Currency Slump, and What Happens Next. URL: <https://www.bloomberg.com/news/articles/2024-07-30/why-nigeria-s-naira-currency-ngn-usd-slumped-and-why-it-matters>

However, for gold-backed currencies to function effectively, African countries need to have sufficient reserves in order to maintain the stability and longevity of these currencies. In addition, linking a country's currency to gold can make its economy vulnerable to fluctuations in the price of the precious metal.

Africa's digital currency

The digitalisation of financial services in Africa and their transfer to mobile platforms is a natural step towards expanding public access to financial services. This is particularly important in a region

where less than half of the population over the age of 15 has a bank account.

African countries account for 66% of the global volume of money transfers through the electronic mobile payment systems. In 2022, more than 50% of new accounts worldwide were opened by users from Sub-Saharan Africa⁴⁰. In 2023, there were 835 million registered mobile money accounts in Sub-Saharan Africa and USD 912 billion in transactions made.

The adoption of mobile communication and wireless internet has opened up a plethora of opportunities for the development of payment services, money

In 2024, the Reserve Bank of Zimbabwe launched ZiG – a new currency backed by gold, as it seeks to tackle high inflation and stabilise the country's long-floundering economy. The Zimbabwean dollar lost almost 100% of its value against the US dollar in 2023.

ZiG (literally Zimbabwean Gold) started trading on 8 April 2024, at an exchange rate of 13.56 ZiG to the dollar. All Zimbabwean dollar account holders had their balances converted to ZiG. The change also affected stock prices on the Zimbabwe Stock Exchange, as it rebased 56 of its listed securities. In order to comply with international standards, the Reserve Bank of Zimbabwe began the process of changing the currency code from ZWL to ZWG (also Zimbabwe Gold).

The Reserve Bank of Zimbabwe claimed that the new currency would be fully backed by USD 100 million in cash and 2,522 kilograms of gold worth USD 185 million. Meanwhile, the central bank added that it would also adopt a tight monetary policy, linking money supply growth to growth in gold and foreign exchange reserves.

On 30 April, new banknotes were released, and the Reserve Bank of Zimbabwe launched a publicity campaign to raise awareness about the new currency. In order to stimulate demand, Zimbabwe made it compulsory for companies to pay at least half of their quarterly taxes using the new currency. Certain taxes can only be paid in ZiG.

However, in practice, ZiG is still a rare occurrence, as public confidence in the new currency has not yet been fully established. Zimbabweans continue to prefer using US dollars for transactions, and most consumer goods are still priced in dollars. Although there are no major obstacles to paying for goods with the new currency or receiving change in ZiG at the Central Bank's official exchange rate. The authorities say that dollar-denominated transactions have declined to around 70% from 85% when it was introduced⁴¹.

40 Bloomberg. All About ZiG, Zimbabwe's Latest Shot at a Stable Currency. URL: <https://www.bloomberg.com/news/articles/2024-08-08/zimbabwe-s-new-zig-currency-how-does-it-work-and-can-it-last>

41 GSMA. The Mobile Economy Sub-Saharan Africa. URL: <https://www.gsma.com/solutions-and-impact/connectivity-for-good/mobile-economy/wp-content/uploads/2023/10/20231017-GSMA-Mobile-Economy-Sub-Saharan-Africa-report.pdf>

M-Pesa

One of the most successful examples of introducing e-finance technologies in Africa is the **M-Pesa**. This mobile phone-based money transfer and payment service was launched in **Kenya** in 2007 by Vodafone and Safaricom. After 14 months since the launch of the service, its user base had grown to 2.7 million. Two years later, it reached seven million, which is about 40% of the adult population. In 2014, it had grown to 19 million users.

The app provides payment services for subscribers of mobile operators in Kenya, Tanzania, Democratic Republic of Congo, Egypt, Ethiopia, Ghana, Lesotho and Mozambique⁴². More than 60 million M-Pesa customers conduct transactions worth over USD 314 billion annually. Outside of Africa, M-Pesa has also been used in countries such as Afghanistan (until 2022) and Romania. In Afghanistan, the service has been used to pay the salaries of police officers and social workers.

In Kenya, the percentage of the population with access to financial services increased to 83% in 2019, while the percentage of people completely excluded from these services decreased from 41% to 11%⁴³. Out of the 26 million people in Kenya who own cell phones, 22 million use M-Pesa, which represents almost every adult Kenyan.

In 2021, Nigeria became the first African country to issue its own digital currency, **eNaira**. The exchange rate of the digital naira is linked to that of the regular naira and its circulation is controlled by the Central Bank. By 2023, the number of transactions increased by 63% and reached 22 billion naira (approximately USD 48 million) due to the currency crisis that occurred earlier this year.

However, eNaira faces several challenges that need to be addressed before it can be widely adopted in the country. Some of these challenges include the lack of necessary technological infrastructure, the need for additional training for financial institution employees who will manage the system, concerns about data privacy, the current electricity crisis and fears of potential financial crimes.

transfers, peer-to-peer lending and micro-insurance. Global payment giants such as Visa, Mastercard and American Express are planning to expand their presence into this niche market. African operators such as **MTN** (South Africa) are successfully competing with these global players.

In a country where traditional banking infrastructure remains limited, mobile money is reshaping how people interact with financial services. According to a World Bank survey, mobile money can improve Somalis' financial inclusion. About 63% of mobile money

users keep their savings on mobile phones and get remittances through their mobile accounts. Hormuud Telcom's mobile money service, EVCPLUS, is by far the most popular mobile money service in Somalia, with a 73% penetration rate and a 92% customer satisfaction score. EVC-PLUS is utilized for settling transactions, saving money, and banking the unbanked communities.

However, mobile payments do have some serious drawbacks. Reliability and security issues contribute to the challenges businesses face in Africa when converting to mobile banking.

42 M-PESA. URL: <https://www.m-pesa.africa>

43 FinAccess. 2019 FinAccess Household Survey. URL: https://www.centralbank.go.ke/uploads/financial_inclusion/2050404730_FinAccess%202019%20Household%20Survey-%20Jun.%202014%20Version.pdf

While many mobile payment platforms available in East Africa rely on SMS, it remains the least secure messaging option. While mobile technology is definitely more prevalent in Africa than it once was, it can still be a challenge for people in more rural areas to gain access to a mobile phone, thus enabling them to participate in mobile payments.

In the long term, the growth of mobile money settlements preserves the dependence of economies and budgets on foreign trade. Mobile money is deposited in the accounts of operators (mostly foreign). Transaction fees are taxed - but not the transactions themselves, which are usually treated as private transfers. As a result, governments are still unable to develop a sustainable tax base that could form the basis of their financial sovereignty. The ultimate beneficiaries of mobile money platforms are banks and telecom operators, both foreign, while governments remain dependent on foreign trade and credit.

Is there anything to know about Africa's foreign exchange reserves?

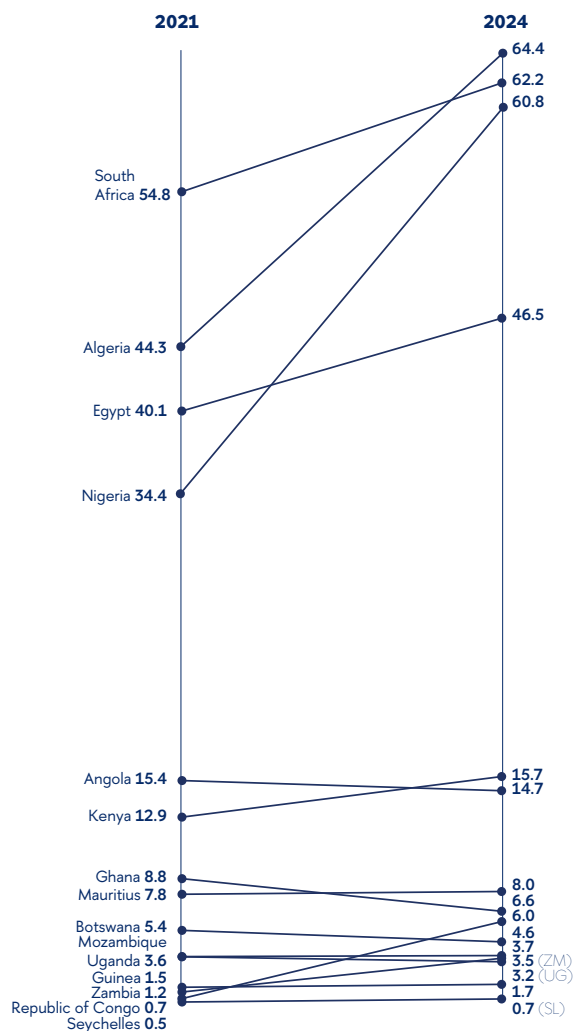
Foreign exchange reserves are an essential part of a country's policy toolkit regardless of the type of exchange rate and national currency, serving as a buffer against economic shocks and complementing monetary policy to maintain price and financial stability. In recent years, changes in foreign exchange reserves in African countries have been driven by policy responses to fluctuations in export revenues, transfers, and capital flows. For example, the decline in oil prices in 2014 led to a 33% reduction in the foreign exchange reserves of oil-exporting countries as authorities resisted pressure to devalue their currencies. Political instability is also a significant factor, especially in lower-income nations. This can lead to uncertainty and volatility in foreign exchange markets, impacting reserves.

As for 2021, **Libya** with USD 81 billion had the highest nominal foreign exchange reserves among African countries, followed by **South Africa** (USD

50 billion), **Algeria** (USD 46 billion), **Nigeria**, **Egypt**, **Morocco**, and **Angola**⁴⁴.

In a vast majority of African countries, the total amount of foreign exchange reserves has increased over the period from 2019 to 2024. In dollar terms, **Algeria's** foreign exchange reserves have increased to USD 64.4 billion at the beginning of 2024. According to the **Central Bank of Egypt**, the country's

Dynamics of foreign exchange reserves change in selected African countries



Source: prepared by the HSE University Center for African Studies and Intexpertise based on Trading Economics data.

44 Statista. Foreign exchange reserves in Africa as of 2021, by country. URL: <https://www.statista.com/statistics/1351876/foreign-exchange-reserves-in-africa-by-country/>

international reserves increased to USD 41.1 billion in April 2024. The growth of reserves was also noted in the Republic of Congo, Guinea, Kenya, the Seychelles, the Republic of South Africa, and Zambia.

However, in some countries, there has been a noticeable trend of a decrease in the nominal value of foreign exchange reserves. Foreign exchange reserves are now frequently being drawn down as central banks endeavour to fight currency depreciation while households withdraw reserves from the formal financial system. For example, in **Botswana**, reserves decreased from USD 5.4 billion in 2021 to USD 4.3 billion in 2024, in **Ghana** reserves decreased from USD 11 billion in 2021 to USD 6.6 billion in 2024. Countries with significant reductions in foreign exchange reserves also include **Angola** and **Uganda**.

In general, foreign exchange reserves form an integral part of a country's self-insurance, especially in low-income countries where the government often provides insurance against foreign currency shortages. These reserves provide several benefits, including a buffer to finance necessary imports or repay foreign exchange debt in case of unavailability or extreme expense of foreign exchange funding. Additionally, foreign exchange reserves allow for policy flexibility to maintain price and financial stability during large exchange rate fluctuations.

Having sufficient foreign exchange reserves to cover imports for several months is a top priority.

The largest number of reserves to cover imports for 14 months was recorded in Algeria

Comoros had reserves that could cover imports for about seven months, **Cabo Verde** for six months, **Morocco** and **South Africa** for five months. The shortest import coverage period was observed in **Zimbabwe** (0.7 months), followed by **Djibouti** (1.4 months), **Eswatini** (1.9), **Mozambique** (2.1) and **Sao Tome and Principe** (2.6 months).

The fall in the import cover ratio was widespread during 2022-2023 because of rising global food and energy prices and, as a result, rising inflationary pressures. Countries with the most significant decline during 2022 and early 2023 included Angola, Gambia, Mauritius, Mozambique, Kenya, Ghana and Nigeria⁴⁵. However, in 2024, there was a gradual recovery in the volume of foreign exchange reserves for these countries.

While foreign exchange reserves offer crucial benefits, holding them comes at a cost for the economy. From the perspective of the consolidated public sector balance sheet, accumulating reserves amounts to issuing debt to invest in foreign currency assets. From an accounting perspective, foreign exchange reserves are typically held on the central bank's balance sheet in African countries, so these costs are borne – above all – by the central bank. The financial cost of foreign exchange reserves depends on the difference between the return earned on reserve assets and the interest paid on the corresponding liabilities.

In simpler terms, to place the amount in advance in international reserves, countries need to withdraw this amount from their national economy and transfer it to the EU and the US for safekeeping. This accumulation of reserves has a downside, as countries may refuse to honour their loan obligations, as has happened with Libya. The Libyan Investment Authority (LIA), set up under Muammar Gaddafi in 2006 to manage the country's oil wealth, has been under a United Nations asset freeze since the 2011 riot that toppled Gaddafi. This means that in order for Africa's largest sovereign wealth fund to make new investments, or even move cash from negative interest rate accounts, the LIA needs UN Security Council sign-off. In 2020, the LIA said that the freeze had cost it some USD 4.1 billion in potential equity returns. Libyan assets are effectively confiscated and cannot be considered sovereign assets.

It is very rare for central banks in African countries to disclose information about which

45 S&P Global. Sub-Saharan African currencies will be more vulnerable to exchange rate pressures in 2023. URL: <https://www.spglobal.com/marketintelligence/en/mi/research-analysis/-sub-saharan-african-currencies-will-be-more-vulnerable-to-exch.html>

currencies their reserves are held in, where these reserves are located and in what share. Non-disclosure helps to prevent speculative attacks on national currencies as precariously low reserves may trigger further withdrawals. African reserves are typically held in major international currencies such as the US dollar, the euro and the British pound.

Some information about reserves is available from the **South African Reserve Bank**. According to the bank's report for January 2024, the Republic of South Africa's total reserves in dollar terms amount to USD 61 billion. This includes USD 46.7 billion in foreign exchange reserves, which consist of foreign currency deposits and other assets, USD 8.2 billion in gold reserves and USD 6.2 billion dollars in holdings with special drawing rights.

Against the backdrop of a general lack of transparency regarding the foreign exchange reserves of African countries, also the **Central Bank of Egypt** stands out. The regulator publishes annual financial reports on Egypt's external position, including detailed information on foreign exchange reserves. According to the bank's report for the end of 2023, Egypt's net international reserves amount to USD 35.2 billion. This includes USD 27 billion in foreign exchange reserves, USD 8.4 billion in gold reserves and USD 36 million in holdings with special drawing rights.

Overall, Africa's foreign exchange reserves are crucial for managing economic stability and growth, but their effectiveness can be impacted by global economic conditions and internal economic policies. Some African countries may use their reserves to service foreign debt or secure additional borrowing.

The Libyan example clearly shows that it is not the size of sovereign reserves that guarantees sovereignty. Much more important is where and in what form these reserves are held. One of the most reliable forms of reserves is gold - if stored in the country itself. An expensive but **worth considering alternative is to invest in reserves of exchange-traded commodities, on the import of which the country is critically dependent**. Of course, these

reserves cannot be considered as foreign exchange reserves, as their international liquidity will be limited. However, for the macroeconomic stability of many countries with foreign trade deficits, in terms of ensuring their financial sovereignty, as well as their food and energy sovereignty, the investments in such reserves should be recognised as a necessary and important measure.

African money – dynamic space for research

Thus, African debt has increased not only in absolute terms but also relative to GDP. Secondly, it remains mostly external and concentrated in ten countries, which are essentially the largest economies. External debt has become more private, which increases the cost of borrowing and may complicate future restructurings. In turn, the domestic debt market is underdeveloped, even though it is easier to pay off than external obligations. China, which had significantly decreased lending to Africa, is starting to return in the region; however, the pattern is unclear so far. The analysis of African trade reveals a prevalence of trade deficits and low export diversification for most countries, which generates additional pressure on public debt. Overall, 14 countries are already troubled with their debt levels and 15 more countries are prone to have debt problems if the global conditions worsen.

There are questions that require further investigation and research. Does Africa need its own credit rating agency, and what approach should be used to evaluate national creditworthiness of African states? What is the relation between trade imbalances, financial flows and economic growth? Is there any political backing of decisions on external debt? How do currency regimes affect debt sustainability and availability? Where are foreign exchange reserves of African countries stored and who benefits from them?

And, finally, can financial sustainability be achieved without financial sovereignty, and how can the latter be structured, measured, and achieved?



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