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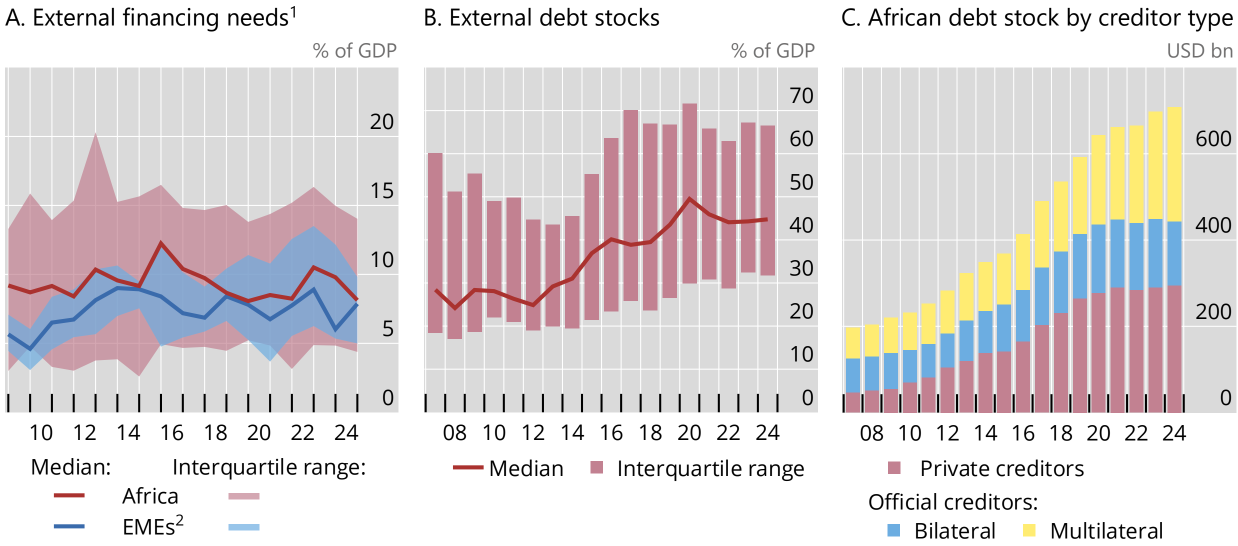
Online annex for BIS Bulletin no 132: Africa's public debt amid global headwinds: balancing resilience and vulnerabilities

Evolution of African external debt

Africa has historically relied more on external financing than other regions. This reliance stems from several factors. First, narrow tax bases and large informal economies have limited governments' ability to generate sufficient domestic revenues, pushing them to seek external borrowing to finance public spending and investment. Second, underdeveloped domestic financial markets have constrained governments' capacity to mobilise financing locally. Third, in many low-income countries, a heavy reliance on imports of food and manufactured goods has led to persistent trade deficits. These factors have collectively generated substantial external financing needs (Graph A.1.A) and contributed to the significant build-up of external debt in the region.

Africa's external debt | Graph A.1



[1] External financing needs are measured by the sum of the current account deficit, short-term external debt and debt service payments for long-term external debt, expressed as a percentage of GDP. [2] Emerging market economies (EMEs) include Argentina, Brazil, China, Colombia, India, Indonesia, Mexico, Peru, Philippines, Thailand and Türkiye.

Source: World Bank, *International Debt Statistics*.

Africa's external debt has risen sharply since the early 2010s, driven by increased borrowing to finance infrastructure projects, development needs and fiscal deficits. The median external debt-to-GDP ratio increased from around 25% in 2010 to 50% in 2020 (Graph A.1.B). However, in recent years the pace of debt accumulation has moderated, reflecting efforts to improve debt management, post-pandemic fiscal consolidation efforts and, in some cases, progress in debt restructuring.

Meanwhile, the growing role of private creditors has also increased debt vulnerabilities. During the past decade, while borrowing from bilateral and multilateral creditors expanded only gradually, financing from private creditors, including through eurobond issuance, grew rapidly. By 2024, debt owed to private creditors accounted for nearly 40% of total external debt stocks (Graph A.1.C). Because private financing is often provided with fewer concessional terms and at shorter maturities and higher interest rates, it can increase refinancing risks and debt servicing costs. Importantly, high levels of external debt expose African countries to currency risks, as most external loans are denominated in foreign currencies. This reflects the "original sin" problem, whereby many African economies have limited ability to borrow externally in their own currency.[1] This risk became particularly evident during the post-pandemic tightening of global financial conditions, when capital outflows and the retrenchment of international investors contributed to sharp depreciations in several African currencies. As a result, the domestic currency cost of servicing external debt increased substantially, inflation intensified and, in some cases, countries experienced debt distress or defaulted on their debt obligations. Recent debt restructuring episodes have also highlighted the challenges of coordinating an increasingly diverse creditor base, particularly where private creditors play a larger role.

Overall, external borrowing has played an important role in financing development across Africa. It has provided access to financing on a scale often unavailable in domestic markets. However, it has also increased exposure to exchange rate fluctuations, global financial conditions and shifts in investor sentiment. While external debt can provide access to larger funding sources than domestic markets, recent episodes of financial stress have highlighted the vulnerabilities associated with foreign currency borrowing.

References

Carstens, A and H S Shin (2019): "Emerging markets aren't out of the woods yet", *Foreign Affairs*, 15 March.

Eichengreen, B, R Hausmann and U Panizza (2005): "The pain of original sin", in B Eichengreen, R Hausmann and U Panizza (eds), *Other people's money: debt denomination and financial instability in emerging market economies*, University of Chicago Press.

[1] See Eichengreen et al (2005). However, even when emerging market and developing economies are able to borrow externally in their own currencies, they may remain exposed to fluctuations in global financial conditions. In such cases, the currency mismatch is transferred from borrowers' balance sheets to those of international investors, giving rise to the concept of "original sin redux" (see Carstens and Shin (2019)).