AFRICAN FORUM AND NETWORK ON DEBT AND DEVELOPMENT

Terms of Reference

Domestic Debt Conundrum in Africa – Implications on National Agenda and Fiscal Consolidation (Case of Senegal, Kenya, and Ethiopia)

The African Forum and Network on Debt and Development (AFRODAD) is a Pan-African civil society organisation established in 1996 to advocate for debt cancellation and addressing debt related issues in Africa. Over the past 25 years, AFRODAD has built expertise on public debt management issues and its intersectionality with domestic resource mobilisation, and international public and private finance in Sub-Saharan Africa and continues to be concerned that African economies do not become highly indebted and in debt distress as in the 1980s. We work with Government Officials across Africa, Members of Parliament, Media and Journalists, Civil Society Organisations, and representatives from the global financial architecture at continental and global levels. We advocate for accountable and transparent public debt and financial management; strengthening of legal and policy frameworks to curtail leakages through illicit financial flows and profit shifting; prioritising revenue generating opportunities through all forms of finance in Africa. Our work focuses on influencing African governments and institutions to adopt accountable and transparent public debt management policies and practices for sustainable development and eradication of poverty. Since our establishment, we have been contributing to finding sustainable solutions to Africa's challenges in debt and resources mobilisation, including financial development. Our main focus areas are Sovereign Debt Management, Democratisation of the Debt Discourse, Collective Action on Debt and Development and Institutional Development & Sustainability.

A. Introduction

Africa's indebtedness is at its highest level in over a decade with the total debt-to-GDP ratio expanding by 39.3 percentage points between 2008 and 2020, reaching 68.6% in 2023(cite). The continent's share of total external debt owed to its bilateral, multilateral private (excluding china) and private(China) creditors stands at USD 685.47 billion, which is an estimated 24.5% of countries' GDP, according to the World Banks's International Debt Statistics of 2024[1]. This upward trend has been a cause for concern, especially as foreign debt now represents nearly 60% of the region's total public debt stock. A 2024 IMF Debt Sustainability assessment found that 32 SSA countries were at moderate or high risk of debt distress, while 9 were rated as being in debt distress.[2] Conversely, the share of Africa's domestic debt in its overall public debt composition has been on an upward trend since during COVID-19, rising from 35% in 2019 to approximately 42 percent in 2021, mirroring a similar trend observed after the 2008 financial crisis. At the time, this was because of a tightening global financial landscape which limited African countries' access to the international capital markets and the need to finance widening fiscal deficits and mitigate the effects of the financial crisis. Domestic bond issuance observed a sharp increase estimated at $307 billion at 13% of GDP in 2010 and 2015, declining slightly to 11% of GDP in 2021. African countries tend to resort to domestic financing whenever external financing opportunities shrink. Domestic borrowing has its advantages, including avoiding the risk of exchange/currency volatilities and conditionalities attached to

[1] World Bank International Debt Statistics(IDS)database: https://www.worldbank.org/en/programs/debt-statistics/ids

[2] https://www.imf.org/external/pubs/ft/dsa/dsalist.pdf

external debt or the risk of sudden capital reversal or short-term lending, which can have a potentially destabilising effect on the economy. While domestic debt is considered a safer alternative to foreign debt due to lower exposure to currency risk, its rapid growth has added substantial pressure on national budgets. This is especially true in the context of deteriorating macro-financial conditions, such as falling economic growth rates, depreciating domestic currencies, and rising interest rates, which exacerbate the challenges associated with managing domestic debt.

The rapid rise in domestic debt, coupled with the vulnerability of these economies to global and local economic shifts, poses a serious challenge to their long-term fiscal health. Despite the optimistic projections that suggest a stabilization of debt levels in the near future(cite), the domestic debt outlook remains fraught with risks. The continued reliance on domestic markets for financing could constrain governments' ability to respond to future economic shocks, and the increased debt burden could crowd out investment in other critical sectors such as health and education. Furthermore, as domestic debt levels increase, governments may find themselves with fewer resources to invest in poverty reduction programs or promote inclusive growth, potentially stalling progress toward achieving development goals.

Problem Analysis

Domestic debt in Africa has become a significant source of concern, particularly as it has risen sharply in recent years, placing strain on national development agendas and fiscal consolidation efforts. This problem arises from a complex interplay of economic, political, institutional, and fiscal factors. Governments in many African countries, including Senegal, Ethiopia, and Kenya, have increasingly turned to domestic borrowing to finance budget deficits and address critical infrastructure and social needs, often due to constrained access to concessional external funding, unpredictable international markets, and the necessity to finance public services. In 2024, Kenya's domestic debt stood at Shs. 5.41 trillion(($42Billion) out of Shs.10.6 trillion($73billion) of its total public debt stock accounting for 68% of its debt servicing obligations. Kenya's domestic debt has been on an upward trend in the last decade from Shs. 1.023 trillion ($79.6 Billion) in 2013 despite introduction of new tax measures that have generally led to higher taxes meant to reduce its persistent fiscal deficit. Ethiopia's domestic debt stood at $40 billion, making up 59% of its total public debt of $68.9 billion by June 2024. This represents a 14% increase in domestic debt over the past year.[3] Regarding Senegal, a court of auditors revealed that the country's previous administration had misreported the actual public debt figures, indicating a precarious situation. This misreporting of debt levels has raised concerns about the country's fiscal health, with the IMF certain to move its status from moderate to high risk of debt distress, with increased potential risks associated with its domestic debt management.[4]

Macroeconomic factors such as budget deficits are central to the rise in domestic debt. In many African countries, limited revenue generation capacities and narrow tax bases have forced governments to borrow domestically to fund public investment and meet social obligations. The high reliance on volatile revenue sources, such as oil exports in a section of African countries, has made them particularly susceptible to external shocks, further driving them toward domestic borrowing as a means of financing deficits for

[3] https://addisstandard.com/ethiopias-total-public-debt-soars-by-a-quarter-in-five-years-reaches-68-9-billion-by-end-of-2024/
[4] https://www.voanews.com/a/audit-shows-senegal-s-previous-government-misreported-debt-other-key-data-/7972823.html

example, Nigeria. While domestic borrowing can play a role in funding vital infrastructure and public services, it also comes with significant costs, particularly in the form of rising debt servicing obligations. Additionally, political pressures to meet the growing demand for public goods and social welfare have contributed to the expansionary fiscal policies that often result in unsustainable borrowing. As domestic debt servicing costs increase, governments are forced to divert resources away from other critical areas, such as education, healthcare, and poverty alleviation programs.

Furthermore, the average maturity period for African domestic debt is around eight years which is much shorter than the official external debt, which averages 30 years, ideally, inadequate to finance many African countries' long-term development needs, more so infrastructure. This means that governments must roll back their domestic debt more frequently, putting more pressure on their budgets. This growing reliance on domestic debt has, in many cases, worsened debt dynamics on the continent. Research suggests that a unit increase in domestic borrowing reduces economic growth by 0.06 percent and raises inflation by 0.14 percent, while the same increase in foreign borrowing reduces economic growth by 0.01 percent and increases inflation by 0.05 percent, holding other factors constant. This implies that domestic borrowing has a relatively larger impact on macroeconomic variables compared to foreign borrowing[5]. Additionally, the heavy borrowing in local currency increases the risk of crowding out private sector credit, as governments absorb a large portion of available domestic savings. Additionally, the need to service high-interest rates on domestic debt adds strain to fiscal budgets, particularly as economies face slower growth and reduced revenues. The debt servicing burden can quickly become unsustainable, undermining the very infrastructure projects and development programs that the borrowing was meant to finance. For instance, during COVID-19, in efforts to mobilise additional financial resources, countries like Malawi, Ghana and Egypt issued government bonds at high interest and with very short maturity (less than six years), resulting in high debt servicing costs, refinancing pressures, and domestic debt defaults. Ghana defaulted on its sovereign debt obligations in 2022.

As governments borrow more domestically, they create upward pressure on interest rates, which in turn crowds out private sector investment. High borrowing costs make credit less accessible to small and medium-sized enterprises, limiting their ability to expand and contribute to economic growth. This phenomenon is particularly evident in Kenya, where high levels of government borrowing have reduced the availability of credit to businesses, undermining private sector development. According to a World Bank report, domestic borrowing is a significant factor behind reduced credit to the private sector, dampening investment and economic growth in Kenya. In countries like Ethiopia, the domestic debt has increased an average of 36% per year from approximately USD 5 billion in 2018/19 to USD 35 billion as of 2022, comprising Treasury bills, government bonds, treasury notes, and long-term loans for state-owned enterprises (SOE). Ethiopia's domestic debt composition is unique, as the stock of SOE borrowings accounts for the majority of total domestic debt. In such situations, state-led financial systems tend to restrict private access to credit, creating an environment where public borrowing becomes the primary source of funding for national development.

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[5] Sumba, Jerry Ogutu, Rogers Ochenge, Paul Mugambi, and Collins Muimi Musafiri. 2024. "Public Debt and Macroeconomic Stability among Sub-Saharan African Countries: A System GMM Test Approach." Cogent Economics & Finance 12 (1). doi:10.1080/23322039.2024.2326451.

At the institutional level, weak fiscal management and inadequate debt management frameworks have exacerbated the domestic debt problem. Many African countries struggle with poor enforcement of fiscal frameworks and insufficient debt transparency, which undermines sustainable debt management. This has resulted in inconsistent policy responses, which further strain public finances and hinder efforts to bring debt levels under control. The legislative guidelines on domestic debt procurement are generally found in Public Debt or Finance Management laws and fiscal frameworks making requirements for domestic debt contraction less stringent than the requirements for external debt contraction. For instance, in Ethiopia approval of the House of People's Representatives is not required for domestic debt that involves treasury bills through the National Bank of Ethiopia or through direct advances or agreements. However, for external debt, such approval is mandatory.

The case of Senegal, Ethiopia, and Kenya highlights both unique and common challenges related to domestic debt accumulation. In Senegal, the pressure to achieve fiscal consolidation and reduce deficits from 11% to 3% by 2027 is compounded by external vulnerabilities and rising debt servicing expenses, which limit social spending. Ethiopia's reliance on domestic borrowing is further strained by internal conflict and a state-led financial system that limits private sector access to credit, driving inflationary pressures. In Kenya, political cycles often result in spikes in borrowing, exacerbating the debt problem and reducing fiscal transparency. Despite these differences, all three countries share common issues, such as low domestic revenue mobilization, which forces them to borrow to finance national priorities, and the growing burden of debt service costs, which erode fiscal space for development spending. Additionally, the increase in domestic debt across these nations has led to reduced private sector investment, further hindering economic growth.

It can be noted that, the rapid rise in domestic debt in these countries demonstrates the delicate balance between fiscal consolidation and national development. The reliance on domestic borrowing, while necessary in the short term to finance deficits and development projects, has long-term implications for fiscal sustainability, economic growth, and the ability of governments to respond to external shocks. The challenge of managing domestic debt requires effective fiscal frameworks, enhanced revenue mobilization, and improved debt management practices to ensure that borrowing does not undermine future economic stability. Fiscal consolidation measures, also known as fiscal reaction functions, are used to assess the actions taken by governments to stabilize or reduce public debt. These measures are akin to an inbuilt mechanism used by governments to ensure that debt is stabilized. Despite existing studies, there is a need to assess the degree of fiscal consolidation by African countries to contain increases in public debt. This study aims to estimate fiscal response functions for SSA countries, with a focus on those with high risks of debt distress. A deeper understanding of public debt dynamics and how governments respond to restore fiscal sustainability is critical for assessing risks to sovereign debt. It is against such a background that, this study aims to examine the factors contributing to domestic debt accumulation in Africa, with a focus on Senegal, Kenya and Ethiopia, and to assess the implications for fiscal sustainability, economic growth, and poverty reduction.[6]

B. Objectives of the study

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https://aercafrica.org/wp-content/uploads/20220/04/Research-paper-385.pdf

(i) To examine the political economy factors contributing to the accumulation of domestic debt in Africa, with a focus on Senegal, Kenya, and Ethiopia, including:

a. Regional trends and patterns in domestic debt accumulation
b. Common drivers of domestic debt growth in Africa, such as fiscal policy decisions, economic shocks, and institutional factors
c. Country-specific factors contributing to domestic debt accumulation in Senegal, Kenya, and Ethiopia

(II)To assess the impact of domestic debt on the realization of the country case Senegal, Kenya, and Ethiopia in realising their national agenda and fiscal consolidations and long-term implications including:

a. Effects on domestic resource mobilization and revenue generation
b. Implications for public service delivery and social spending and allocation of resources for key sectors such as education, health, and infrastructure
c. Investigate the role of domestic debt in shaping fiscal policy decisions, including national budgeting, prioritization of government expenditures, and revenue generation.
d. Analyse the sustainability of domestic debt in relation to economic growth and the fiscal capacity of African countries.
e. Impact on the overall attainment of SDGs and Agenda 2063 goals, particularly in relation to poverty reduction, inequality, and economic transformation

(III) To identify policy options and recommendations for managing domestic debt and promoting fiscal consolidation in Africa, drawing lessons from the experiences of Senegal, Kenya, and Ethiopia, and considering the regional and global context.

C. The scope of the assignment

i. Examine the intersection of domestic debt, fiscal policy, and development outcomes in Africa, with a focus on Senegal, Ethiopia, and Kenya.

ii. Assess the opportunities, challenges, and risks associated with domestic debt accumulation in Africa, including the impact on fiscal sustainability, economic growth, and poverty reduction.

iii. Analyze the salient issues arising from domestic debt accumulation, including the impact on public service delivery, social spending, and human development, based on current affairs, borrowing thresh holds, texts of laws, and treaties and where available, texts of debt contracts.

iv. Develop a framework for a domestic debt management approach that prioritizes human development, poverty reduction, and fiscal sustainability, and analyze the elements of such an approach

v. Develop a framework for restructuring domestic debt that can guide African governments in the event of default

D .Key Outputs

- Assessment Paper (25 pages excluding references, cover page and annexes). Formatting requirements include Times New Roman, Font 11, Spacing 1.15.

D. Analysis Approach

The assessment paper should have and/or follow the structure proposed below which enables flow of arguments and the tying down of cutting-edge policy propositions

- **Introductory or background section**

- Presents an overview of the subject.
- Expresses a clear research problem with related research questions.
- Includes aim and objectives of the study with a justification of why study is needed.
- Summarises and justifies the methods used in the study.

- **Literature Review**

- Presents clear conceptual clarifications.
- Looks at related literature and identifies gaps.
- Looks at issues related to the problem and questions raised.

- **Findings and Discussions**

- Tackles the questions raised.
- Determines whether the main problem is being solved.

- **Conclusions and Policy Recommendations**

- Determines whether the research aims and objectives were met.
- Engages in policy discussions and advances recommendations.

The paper should:

- Be well written with references and acknowledgement of sources of materials that are referred to in the text, end notes and bibliography at the end of the report.
- Have a table of contents and list of tables, glossary and list of acronyms if any.
- Contain an executive summary, and a section on key findings, conclusions and recommendations.
- Contain recommendations for Parliament, Governments, private sector, civil society and the international community.
- Outputs should be tailored to specific events and audiences during the dissemination of findings.

E. Timing

The Research Study should be completed within 30 working days from the time the contract is signed between the selected consultant and AFRODAD.

	Wk1	Wk2	Wk3	Wk4	Wk5	Wk6
Inception meeting with consultant	xxxx					
First draft and review	xxxx	xxxx				
Second Draft and Validation			xxxx	xxxx		
Final Draft and design				xxxx	xxxx	
Approval and Webinar launch						xxxx

F. Reporting

The consultant will report to both the Policy and Advocacy Manager and the Sovereign Debt Management (SDM) Policy Officer theo@afrodad.org and catherine@afrodad.org

I. Competencies

The Consultant should have skills and experience in the following areas:

- Policy aptitude and experience on development economics with a focus on Macroeconomics and fiscal Policy, sovereign debt, and international economics in
- A strong understanding of Political Economy and African Development, contract law, sovereign debt contracts and treaties relevant to debt management and restructuring
- Postgraduate degree in Economics, or Political Science specialising in Public Policy analysis, Political Economy, African Politics and Undergraduate degree in Economics with experience on macroeconomics, public finance, and development economics.
- A minimum of 3 years of professional experience in undertaking similar or related tasks; familiarity with sovereign debt and debt instruments, sovereign debt management, political economy of debt in Africa

Expressions of interest should be sent to recruiment@afrodad.org, copying theo@afrodad.org and catherine@afrodad.org with the subject line **"EOI: Domestic Debt Conundrum in Africa –**

Implications on National Agenda and Fiscal Consolidation". Expressions of interest should be submitted by **12th May 2025 at 11.59 p.m.** (GMT).