Key Facts: Credit Ratings Agencies, Fiscal space and Fragility in Africa

The "Africa Premium"or the double standard by Credit Rating Agencies: $ billions lost for development

To achieve by 2030 the United Nations Sustainable Development Goals, the Brookings Institution estimates the financing gap in Sub-Saharan Africa alone at $256 billion per annum[1].

At the same time, the continent has to stop the leakage coming out of the tab of the Illicit Financial Flows (IFFs) costing yearly an estimated $88.6 billion, mainly to tax evasion and Profit Shifting [2].

Africa's debt is the lowest compared to the rest of the World but records the fastest debt accumulation with an average debt-to-GDP (Gross Domestic Product) ratio rising from 40% in 2009 to 71% in 2020.Africa's debt structure is another source of concern.

The composition of debt is a cause of concern as the share of commercial borrowing, mainly through Eurobonds, which is subject to currency risk, has been doubling over the last decade, from 27% in 2011 to 52% in 2020.

"Africa premium" on global debt markets: Estimated at 2.9 percentage points higher and resulted in a net additional loss of $2.2 billion to African governments between 2006 and 2014.

In response to the COVID-19 pandemic, African countries were left with almost no alternative than the issuance of Eurobonds to quickly mobilize resources for emergency spending and stimulus measures.

African countries launching financial stimulus packages and participating in international debt relief initiatives received either rating downgrades or threats thereof. In comparison with other regions, Africa's downgrades (62%) are disproportionally higher that the global average of 31%.

Since the start of the pandemic, most African rated countries (93%) are now either at junk, high or very high credit risk status.

A moral imperative: changing the risk perception to better reflect Africa's fundamentals

The lack of transparency in the CRA's methodology continues to undermine confidence in the quality and accuracy of their ratings leading to adverse consequences in Africa.
There is a moral imperative for the international community and African Countries alike to engage in a global dialogue on reforming the CRAs, questioning its credibility and modus operandi.

The African Union recommends the creation of a centralized debt management office, equipped with the required expertise and tools, able to conduct the necessary simulations and effectively communicate with the markets, enabling countries to challenge controversial rating decisions. This is a critical step towards debt sustainability and affordability as it would ensure better rating for the sovereign credit.

The way forward

Domestic resource mobilization is the key to Africa's sustainable development. The focus needs to be broader than managing the "so-called" debt burden alone.

Good governance to ensure secure property rights, data-informed and transparent decision making and quality of investments matter at least as much.

Access with fair and equitable terms to international capital market should continue to be priority for African countries. African countries should lead the dialogue with the CRAs within and outside the UN system on reforming the CRAs business models for achieving the SDGs.

African Countries would also benefit from long-term ratings that could boost long-term productive investments in the SDGs and enhance long-term debt management of countries.

As per the African Union recommendations, it is critical to deepen domestic and sub-regional capital markets to ensure sustainable sources of financing and build resilience to crises, including by tapping into pension, insurance and sovereign wealth funds markets.

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[1] Brookings Institute, 2020, "Foresight Africa: Top priorities for the continent 2020-2030", Africa Growth Initiative.

[2] United Nations Conference on Trade and development (UNCTAD), 2020,"Economic Development Report in Africa 2020: Tackling Illicit Financial Flows in Africa for Sustainable Development".