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POLICY BRIEF

EXTERNAL DEBT SUSTAINABILITY AND THE RECOVERY OF SOVEREIGNTY*

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Key Takeaways

This policy brief pursues a twofold objective. First, it surveys the key recent findings in the academic literature on debt sustainability in developing economies, focusing on the factors that have contributed to its marked deterioration in Sub-Saharan Africa. It then identifies the mechanisms that could place sovereign debt back on a sustainable trajectory and restore the fiscal space necessary for autonomous, long-term development strategies, free from austerity-driven constraints.

The Debt Burden and the Failure of Fiscal Austerity

Contrary to widespread belief, public debt in African economies had already entered an unsustainable trajectory with the COVID-19 pandemic. The 2010s had already revealed a marked acceleration in debt ratios. The 2020 shock, however, triggered a sharp further rise in financing needs, driven by the combined effects of revenue shortfalls, emergency health and social expenditures, and—subsequently—rising food and energy prices alongside higher international interest rates. According to the African Development Bank, the median debt-to-GDP ratio rose from 54.5% in 2019 to 64% in 2020, then stabilized around 63.5% between 2021 and 2023, before accelerating again starting in 2025 (65%)[1].

This trend is particularly pronounced for external debt. The median external debt service ratio for 49 countries thus rose from 6.8% of government revenue over the 2015–2019 period to 10.6% over the 2020–2022 period. In 2024, African countries had to allocate approximately $74 billion to debt service, compared to $17 billion in 2010, of which $40 billion was owed to private creditors. The structure of the debt exacerbates these vulnerabilities. Commercial debt now accounts for more than 40% of total outstanding external debt, approximately 70% of which is denominated in US dollars, exposing governments to interest rate hikes, currency depreciation, and costly refinancing. Domestic debt has also risen, from 32% of total public debt in 2010 to 39% in 2023.

Faced with these pressures, many countries have implemented fiscal consolidation policies. These policies take two main forms: increasing government revenue and, more commonly, cutting expenditures—the latter typically receiving priority[2]. In the most vulnerable countries, fiscal consolidation is often linked to debt restructuring. Ghana, whose public debt reached nearly 90% of GDP by the end of 2022, restructured its domestic debt and reached an agreement with its official creditors in January 2024. Zambia, whose public debt had peaked at 150% of GDP in 2020, concluded a $3 billion restructuring agreement with external bondholders in March 2024. Ethiopia, for its part, secured a moratorium on official bilateral debt service due between January 2023 and December 2024.

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[1] African Development Bank. (2025). African Economic Outlook 2025. Abidjan, AfDB.

[2] Angola has thus undertaken a reform of fuel subsidies, a reduction in the VAT threshold, a corporate tax reform, the introduction of a property tax, and the streamlining of tax incentives. Egypt has reduced untargeted fuel subsidies, eliminated 19 out of 58 VAT exemptions, and adopted a carbon tax. Ethiopia has streamlined tax exemptions, revised excise duties, strengthened vehicle taxation, and developed digital tools for tax administration.

* The views expressed here are those of the author(s) and do not necessarily reflect the views of IDAN.

These fiscal consolidation policies, however, present two fundamental problems. At best, they only partially restore debt sustainability; more critically, they significantly erode the policy space needed to pursue ambitious development agendas. The contradiction is therefore strong. On the one hand, governments must consolidate their public finances to avoid over-indebtedness, restore their credibility, and regain access to financing. On the other hand, this consolidation limits the necessary investments in infrastructure, education, health, the ecological transition, and structural transformation[3].

High debt levels and financing costs thus compel African governments to cut certain essential expenditures and redirect resources originally earmarked for development toward debt service. The risk, therefore, is a vicious cycle: debt necessitates austerity, austerity curtails public investment, reduced investment constrains future growth, and weaker growth makes debt stabilization increasingly difficult. Under these conditions, fiscal consolidation alone cannot constitute a strategy for development and structural transformation. Especially since the underlying problem is not so much the level of debt itself, but rather its use and long-term sustainability.

Understanding the Sustainability of Sovereign Debt

Academic research does not universally conclude that austerity policies are necessary for growth—far from it. Empirical evidence and historical experience demonstrate that sovereign debt sustainability depends on considerably more complex mechanisms.

First, we must reject the idea of universal debt ceilings beyond which a crisis would be inevitable. The highly influential study by Reinhart and Rogoff, which proposed a critical threshold of approximately 60% of GDP for emerging economies (90% for OECD countries), has largely been invoked to justify austerity policies. It documented a correlation between high debt and slower growth, attributing this relationship primarily to crowding-out effects, rising risk premiums, and heightened vulnerability to crises. These findings, however, have been sharply contested on methodological and causal grounds. The literature now converges on the view that no universal threshold exists. Sovereign defaults in the 2020s (Argentina, Belize, Ecuador, Suriname, Zambia, Ghana, Ethiopia, Mozambique, Lebanon, Sri Lanka) occurred at highly varied debt-to-GDP ratios, ranging from 30% to 160%! The outlier cases of Japan (230%) and Singapore (176% in 2025), both of which face no major refinancing difficulties, further undermine the notion of mechanical thresholds.

Other determinants of debt sustainability therefore warrant examination. The so-called "golden rule," defined by the spread (r – g), holds that when the real interest rate on debt (r) falls below the GDP growth rate (g), the debt-to-GDP ratio tends to stabilize or even decline, even in the presence of a moderate primary deficit. When growth exceeds the cost of borrowing, it effectively "dilutes" the debt burden mechanically. Conversely, when r > g, stabilizing the debt-to-GDP ratio requires achieving higher primary budget surpluses, which makes debt sustainability more fragile and increases the constraints on fiscal policy.

[3] Jamaica's experience is often cited as one of the few examples of successful fiscal consolidation, with an exceptional reduction in public debt, which fell from 144% of GDP in 2012 to 72% in 2023, with a target of less than 60%. This strategy relied primarily on maintaining high primary budget surpluses (around 7% of GDP) over a long period. However, this experience has largely demonstrated its limitations, as the IMF itself acknowledges. It was accompanied by very weak growth (less than 0.75% per year), as well as restrictive fiscal trade-offs, severely limiting the room for maneuver for development. Furthermore, it relied on institutional and political conditions that are difficult to replicate elsewhere (Arslanalp, S., Eichengreen, B., & Peter, B. A. 2024. Debt reduction: The Jamaica exception. Brookings Papers on Economic Activity, spring).

The fiscal multiplier captures the idea that increases in public spending generate additional demand, which in turn raises income for firms and households. These agents reinvest a portion of this income into spending, creating a new wave of demand and then another, successively, until the effect is exhausted. The multiplier then measures the ratio between the final increase in GDP and the initial amount of public spending. For instance, a large public works program—spanning infrastructure, energy, and healthcare—generates income for firms, workers, and subcontractors, who in turn spend it, amplifying the effect on aggregate output. Conversely, fiscal austerity compresses aggregate demand and amplifies both the severity of the crisis and the debt burden. Empirical studies show that the multiplier is larger during economic slowdowns or recessions and is particularly strong for infrastructure spending. However, if the economy is already close to full employment or if demand is being diverted to imports, the income chain mechanism weakens and the multiplier becomes smaller.

Research building on Eggertsson[4], further emphasizes the need for close coordination between fiscal and monetary policy to achieve an optimal "policy mix." To strengthen debt sustainability, the government and the central bank must act in concert, pursuing coherent objectives—a condition that is not easily satisfied within a monetary union. From this perspective, the institutional framework of the WAEMU is highly restrictive, as the BCEAO (like the European Central Bank in the eurozone) must conduct a common monetary policy, which is expected to accommodatet all WAEMU member states, even though their macroeconomic situations, constraints, and priorities may differ significantly. Sharing monetary authority thus appears to be a delicate exercise, one that does not necessarily lead to an optimal policy mix, much less to an expansionary fiscal policy.

Breaking free from dependence on external debt

The debt sustainability of developing economies also depends on the pronounced asymmetry of the international monetary system, which curtails their sovereignty relative to that of core countries. Developing economies have less sovereignty, particularly due to the structure of their external debt. The "original sin" hypothesis holds that a significant share of external debt is denominated in hard currencies, while income, tax revenues, and non-export receipts are generated primarily in domestic currency. This asymmetry is rooted in the architecture of the current international monetary system: so-called "advanced" economies, such as the United States and France, are exempt from "original sin" because they can issue sovereign bonds in their own currency. The sustainability of public debt in developing economies is therefore not solely linked to the isolated vulnerability of debtor countries; it also stems from the international monetary hierarchy[5].

This constraint on foreign-currency debt significantly reduces the room for maneuver of developing economies. When the exchange rate depreciates, the real burden of foreign-currency debt rises sharply, even as the nominal amount remains unchanged, thereby substantially elevating the risk of default. The inability to borrow in their own currency creates a dependence on foreign exchange markets, interest rates in the reference currency (often the US dollar or the euro), and confidence shocks, making their debt trajectory much more fragile than that of countries that can finance themselves in domestic currency.

[4] Eggertsson, G.B. (2011). What Fiscal Policy Is Effective at Zero Interest Rates? NBER Macroeconomics 2011-25: 59-112.

[5] Fritz, B., de Paula, L. F., & Prates, D. M. (2018). Global currency hierarchy and national policy space: A framework for peripheral countries. European Journal of Economics and Economic Policies: Intervention, 15(2), 208–218.

To service their foreign-currency debt, developing countries must mobilize foreign exchange, prompting them to boost exports, restrict imports, or draw down their reserves. This constraint places a lasting burden on development strategies by imposing a constant need to generate foreign exchange. This steers economies toward export-led growth models, at the expense of domestic demand and national priorities, and tends to lock them into extractivist trajectories when their productive specialization centers on raw material extraction. Ultimately, the "original sin" constraint not only undermines debt sustainability but also reinforces the exploitation of labor—since wage costs must remain low to maintain export price competitiveness—and drives environmental degradation.

Another challenge stems from the fact that issuing securities in local currency on international markets remains a complex operation. During the 2010s, countries such as Brazil, Colombia, and Russia broke new ground by attempting to escape the "original sin" constraint. However, these initiatives were quickly curtailed, or even abandoned, due to the reluctance of international creditors and the fact that these local-currency issuances ultimately proved more costly than foreign-currency borrowing[6]. The first quarter of 2024 was marked by an attempt by several African countries, notably Benin, Kenya, and Côte d'Ivoire, to return to the Eurobond market after several years of hiatus. This return, however, came at higher borrowing costs and was denominated predominantly in foreign currencies.

In this context, a frequently proposed solution is to enhance regional financing capacity, particularly through the WAEMU public debt market, by mobilizing CFA franc-denominated resources. In March 2025, Côte d'Ivoire issued a CFA franc-denominated bond on an international market accessible to global investors (220 billion CFA francs at a rate of 6.875% over a three-year maturity). While this type of operation constitutes an attempt to circumvent the "original sin," the current architecture of the WAEMU does not, however, allow for a complete break from it[7].

Regaining fiscal space also requires renegotiating external debt. This requires conducting a thorough audit of external debt—an essential prerequisite for restoring credibility and rebalancing the power relationship with international creditors. However, a sustainable restructuring cannot be conceived solely from the creditors' perspective: it must take into account macroeconomic constraints and the debtor's actual repayment capacity. In this regard, the argument of the debt Laffer curve, popularized by Paul Krugman[8], can be invoked. By analogy with the adage "too much tax kills tax," it emphasizes that "too much debt kills debt"—illustrating a nonlinear relationship between the level of debt and the capacity to service it. Beyond a certain threshold, excessive debt creates a debt overhang: economic agents anticipate that future revenues will be primarily earmarked for debt service, which discourages investment and slows economic activity. This yields a slowdown in growth, an erosion of the tax base, and, ultimately, a decline in effective debt-servicing capacity.

[6] Faudot, A. & Ponsot, J.F. (2016). "The Dollar Dominance: Recent Episode of Trade Invoicing and Debt Issuance." Journal of Economic Integration, 31.1: 41-64.

[7] Because the BCEAO is obliged to accumulate sufficient foreign exchange reserves (Pigeaud, F. & Sylla N.S. 2021. Africa's Last Colonial Currency. The CFA Franc Story, Paris, La Découverte., Paris, La Découverte). In the WAEMU zone, where trade deficits are chronic, these reserves come mainly from external debt. In this context, the ability to borrow in CFA francs on the regional market therefore depends on the prior ability to take on foreign currency debt, which does not eliminate the "original sin."

[8] Krugman, P. (1988). "Financing vs Forgiving a Debt Overhang," Journal of Development Economics, 29 (3), 253-268.

A reduction in the debt stock, through restructuring or partial write-down, can therefore enhance overall sustainability by stimulating investment and growth. In this case, it is not only in the debtor's interest but also, paradoxically, in that of the creditors, by maximizing the amounts actually recoverable in the medium term. While discussions on restructuring focus primarily on external debt, the domestic debt of African economies should not be overlooked. The cases of Ghana and Zambia illustrate this issue. Domestic restructurings can indeed have severe effects on resident creditors (banks, pension funds, and savers), particularly in shallow financial systems.

A more radical, yet potentially effective, option would be to consider a unilateral suspension of part of the external debt, should an audit establish that it is "illegitimate." The Ecuadorian experience of 2008–2009 is instructive in this regard. Following a debt audit, the government suspended payments on certain external bonds maturing in 2012 and 2030, which subsequently experienced a sharp decline in market value. Ecuador then repurchased a large share of these bonds for approximately USD 900 million, despite their face value being around USD 3.2 billion.[9] The effectiveness of such a strategy, however, depended on a strong domestic political consensus and is primarily relevant to external debt.

Domestic Financing and Sovereignty

The connection between debt and sovereignty extends beyond the issue of foreign currency debt[10]. Chief among these considerations is the identity of debt holders. The sustainability of high debt levels in Japan and Singapore, stems primarily from the predominance of domestic creditors (over 90%). Conversely, the higher a country's share of foreign-currency debt or degree of dollarization, the more fragile its debt position becomes[11].

Since the late 2000s, several emerging and developing economies have sought to diversify their external creditors in order to reduce their dependence on traditional lenders—whether bilateral (the United States in Latin America, France in Sub-Saharan Africa) or multilateral (such as the World Bank), as well as the associated conditionalities. This realignment, driven by economic and geopolitical considerations alike, has manifested in China's rapid rise as a preferred trade and financial partner. The intensification of Sino-African trade, which rose from approximately $10 billion in 2000 to $282 billion in 2023, has not, however, altered the structure of trade, as Africa remains primarily an exporter of primary products and an importer of manufactured goods. On the financial front, Africa's external debt has shifted significantly toward China, which is now the leading bilateral creditor (accounting for 42% of financing in 2022, far ahead of France at 10% and Saudi Arabia at 7.9%).

[9] FToussaint, E. (2024). Ecuador's poisoned loans from the World Bank and the IMF, CADTM. https://www.cadtm.org/Ecuador-s-poisoned-loans-from-the-World-Bank-and-the-IMF

[10] For approaches highlighting the role of debt in monetary sovereignty and financial autonomy, see: Aglietta, M., Ould Ahmed, P., & Ponsot, J.F. (2016). La monnaie, entre dettes et souveraineté, Odile Jacob, Paris. Alami, I., Alves, C., Bonizzi, B., Kaltenbrunner, A., Koddenbrock, K., Kvangraven, I., & Powell, J. (2023). International financial subordination: A critical research agenda. Review of International Political Economy, 30(4), 1360–1386.
Murau, S., & van 't Klooster, J. (2023). Rethinking monetary sovereignty: The global credit money system and the state. Perspectives on Politics, 21(4), 1319–1336.

[11] For an assessment of the macroeconomic constraints and loss of sovereignty in dollarized economies, see Ponsot, J.-F. (2019). Économie politique de la dollarisation. Mondes en développement, 188.

Rather than promoting more sustainable development financing, this shift in capital flows and the new terms of financial assistance and debt restructuring have given rise to new forms of financial dependence, often marked by a lack of transparency regarding both amounts and conditions. "Chinese debt" has thus contributed, in several cases (Ecuador and Venezuela in Latin America, Zambia, Ethiopia, and Angola in Sub-Saharan Africa), to a significant deterioration in debt trajectories, reinforcing external vulnerabilities rather than financial autonomy and SDG financing.

Finally, let us not forget the controversial debate surrounding the appropriateness of monetary financing of the budget deficit. Should the central bank be called upon to ease the financial constraints on governments? This question has been widely debated since the widespread adoption of the principle of central bank independence. From a theoretical standpoint, forgoing the central bank's financing capacity effectively means relinquishing sovereignty[12] and amounts to imposing an unnecessary financial constraint, as governments do not necessarily issue bonds primarily to obtain the funds needed for their expenditures, but rather to influence private credit conditions via interest rates[13]. In practice, monetary financing is the rule rather than the exception wherever monetary sovereignty is exercised, whether in so-called "advanced" economies or in emerging and developing economies[14]. More broadly, the possibility of reducing or canceling Senegal's sovereign debt held by the central bank—if it is unsustainable—should be considered. The architecture of the WAEMU and the prerogatives of the BCEAO therefore do not, in their current configurations, allow for the implementation of fully sovereign policies, whether fiscal or monetary[15]. They should therefore be thoroughly reformed.

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[12] See Tymoigne, E. (2020). Monetary sovereignty: Nature, implementation, and implications. Public Budgeting & Finance, 40(3). And Tcherneva, P. R. (2016). Money, power, and monetary regimes (Working Paper No. 86). Levy Economics Institute of Bard College.

[13] Wray, R. (2024). "Sovereign currency and non-sovereign budgets: the Modern Money Theory approach to provincial, state, and local government budgets," in: Yeva Nersisyan & L. R. Wray (eds.), The Elgar Companion to Modern Money Theory, pp. 378-385, Edward Elgar Publishing.

[14] See Berkeley, A., Ryan-Collins, J., Tye, R., Voldsgaard, A., & Wilson, N. (2025). The Self-Financing State: An Institutional Analysis of Government Expenditure, Revenue Collection and Debt Issuance Operations in the United Kingdom. Journal of Economic Issues, 59(3), 852–880. Felipe, J. & Fullwiler, S. (2022). "How 'Monetization' Really Works. Examples from Three Asian Nations' Responses to Covid-19." Review of Political Economy 34 (3): 397–419.

[15] See: Gadha, M. B., Kaboub, F., Koddenbrock, K., Mahmoud, I., & Sylla, N. S. (Eds.). (2022). Economic and Monetary Sovereignty in 21st Century Africa. London: Pluto Press. Nubukpo, K., Ze Belinga, M., Tinel, B., & Dembele, D.M. (eds.)(2016). Sortir l'Afrique de la servitude monétaire. À qui profite le franc CFA ?, Paris, La Dispute.