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A Comparative Analysis of External Debt in the East African Community Countries

Benson A. Ateng', Senior Lecturer*
Department of Economics and Resource Management
The Technical University of Kenya, P.O. Box 79803 – 00200, Nairobi, Kenya
Tel: +254-707-344154 E-mail: bensonateng@gmail.com

Abstract
Borrowing to finance public infrastructure has pushed debt levels to record highs within the East African Community (EAC) countries. Total external debt stock grew by 333.38 percent between 1970 and 2020. The rise in external debt exceeded growth in GDP and exports in all the countries except for the Democratic Republic of Congo between 2010 and 2020. The situation could have been worse had it not been for a massive external debt cancellation by the international community under the Heavily Indebted Poor Countries (HIPC) and Multilateral Debt Relief Initiative (MDRI) programmes that benefitted all the EAC countries except Kenya. Virtually all the countries are increasingly borrowing more long-term than short-term external loans. Multilateral and official bilateral creditors continue to be the major financiers in all the countries even though these countries are gradually diversifying their sources of borrowing. All the EAC countries except Burundi had publicly guaranteed private sector external debt from commercial banks between 2010 and 2020. Three of the countries, Kenya, Tanzania and Rwanda, had nonguaranteed private sector external debt during the period. Two countries, Kenya and Rwanda, have joined a fast growing number of African countries that are issuing international sovereign bonds. The EAC countries are in a vulnerable position, with public external debt already at elevated levels. Trends in some of the external debt ratios including debt-to GDP, debt-to-exports, and debt service-to-exports ratios suggest that these countries could face challenges in servicing their external debts and meeting other foreign exchange obligations. High levels of external debt seem to have led to a vicious cycle of debt. Even after benefitting from the HIPC and MDRI debt relief programmes, the countries are once again facing high debt ratios. In light of the above findings, governments of the EAC countries should: look for improved terms on new loans; restructure external commercial loans that have heavy maturities and high interest rates; continue to diversify sources of external financing to reduce high dependency on expensive loans; make concerted efforts to increase concessional public external debt; explore non-debt creating financing options for public investments such as Public Private Partnerships; and look into refinancing expensive debt with debt on more favourable terms.
Keywords: External debt, multilateral and bilateral debt, publicly guaranteed debt, external debt indicators, vicious cycle of debt
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1. Introduction
1.1 Background
The East African Community (EAC) is a regional intergovernmental organization of seven partner states: The Republic of Burundi, the Democratic Republic of the Congo, the Republic of Kenya, the Republic of Rwanda, the Republic of South Sudan, the Republic of Uganda, and the United Republic of Tanzania. Its headquarters is in Arusha, Tanzania.

A treaty that guides the work of the Community established the EAC. It was signed on 30 November 1999 and became effective on 7 July 2000 following its ratification by the original three partner states - Kenya, Tanzania and Uganda. Rwanda and Burundi became full members of the Community with effect from 1 July 2007, while South Sudan became a full member on 15 August 2016. The newest member, the Democratic Republic of the Congo (DRC), became a full member on 11 July 2022.

The EAC is home to an estimated 283.7 million people, of whom over 30 percent live in urban areas. It has a land area of 4.8 million square kilometres and a combined Gross Domestic Product (GDP) of US$ 262.36 billion[1] as at the end of 2020. Kenya has the largest economy in the Community. In 2020 Kenya's GDP was US$100.7 billion, followed by Tanzania (US$ 62.41billion), Democratic Republic of Congo (US$ 48.72 billion), Uganda (US$ 37.60 billion), Rwanda (US$ 10.18 billion), and Burundi (US$ 2.78 billion).[2]

The need to undertake this study emerged from a number of observations. Public debt is currently a topical issue, especially in the developing countries. There is a lot of debate going on concerning the magnitude and

[1] Excluding South Sudan
[2] World Bank (2021). *International debt statistics 2022*. World Bank Publications.

sustainability of public debt. Researchers have carried out a number of studies on public debt in the countries comprising the EAC. However, most of them focused largely on effects of public debt on economic growth, the relationship between public debt and economic growth, optimization of public debt and its impact on growth, and debt sustainability. For example, Achwoga (2016) examined the effects of public debt on economic growth in Kenya and concluded that economic growth is negatively and significantly related to external debt. Lotto and Mmari (2018) found that there is an inverse relationship between domestic debt and the economic growth of Tanzania. Similarly, Mbire and Atingi (1997) established a link between debt and economic growth in Uganda. In their study, Ryan and Maana (2014) examined debt sustainability and trade-offs of holding external or domestic public debt in Kenya and concluded that the public debt was sustainable at the time of the study. Rutayisire (2021) assessed whether in the case of Rwanda, there exists a threshold level or a turning point above which the impact of public debt on economic growth shifts from positive to negative. The empirical results of this study strongly suggested the presence of a concave nonlinear or an inverted U-shape relationship between public debt and economic growth in the country. International Monetary Fund (2015, 2016, 2021, 2022) has conducted debt sustainability analysis in all the EAC countries and concluded that while external debt distress for most of these countries remain, the margins have generally narrowed.

A gap exists in the area of comparative analysis of public debt in the EAC countries. This study set out to fill that knowledge gap. In order to keep the study manageable, it focuses only on one major component of public and publicly guaranteed debt, that is, external debt. Total external debt stock in the Community grew by 333.4 percent from US$1.191 billion in 1970 to US$95.892 billion in 2020. Total external debt in EAC varied strongly among countries. As a percent of GDP, it stood at 22.5 for Burundi, 12.6 for DRC, 37.9 for Kenya, 80.5 for Rwanda, 40.9 for Tanzania and 45.8 for Uganda.[1]

1.2 Definition

This study applies a commonly used definition of external or foreign debt.[2] It is the portion of a country's debt from foreign lenders, including international financial institutions, governments, and commercial banks. Thus, total external debt is the sum of public, publicly guaranteed, and private nonguaranteed long-term debt, and short-term debt. Short-term debt includes all debt having an original maturity of one year or less and interest in arrears on long-term debt.

External debt comprises multilateral, bilateral and commercial loans. Multilateral loans are debts issued by international institutions such as the World Bank and the International Monetary Fund (IMF) to member countries to promote socio-economic development whereas bilateral loans are loan agreements between individual nations. Multilateral and bilateral loans are classified as concessional loans due to the favourable terms offered in terms of either below-market interest rates, long grace periods or a blend of both. Commercial loans, on the other hand, are loans agreed between a country and an external commercial bank or an external financial debt channel. Commercial loans usually have higher interest rates and shorter grace periods.

1.3 Need to Borrow Externally

To attain their overall objective of sustainable socio-economic development, developing countries require substantial quantities of capital that may not be raised wholly from domestic sources. Due to lack of sufficient capital arising from low savings, majority of developing countries seek to borrow from an outside source to bridge the resource gap. Borrowing externally may facilitate investment and socio-economic development to the extent that it provides the country with more affordable financing and that the borrowed funds are channeled to productive sectors. Developing countries rely on international borrowing to finance special projects, infrastructure and to compensate for needed revenue which they cannot obtain through taxation.

1.4 Objectives of the Study

The study set out to achieve three main objectives:

(i) Compare trends and levels in external borrowing in the EAC countries;
(ii) Examine and compare the structure and composition of external debt in the EAC countries; and
(iii) Work out and compare trends in selected external debt ratios/indicators in the EAC countries.

1.5 Research Questions

The study set out to answer the following research questions in order to achieve the objectives:

(i) What explains differences, if any, in the structure and composition of external debt in the EAC countries?
(ii) What explains differences in values of and trends in selected external debt ratios/indicators in these

[1] Author's computation using data from World Bank (2021). *International debt statistics 2022*. World Bank Publications.
[2] Debt owed to nonresidents of the country payable in currency, goods or services.

countries?
(iii) Are the EAC countries borrowing from same external sources? If not, why not?

2. Methodology

The study utilized descriptive statistics obtained from in-depth desk review approach of data and reports on historical external debt of each of the six EAC countries included in the study,[1] covering the period 1970 to 2020. This covered various phases of external debt in the region. In addition, a comparative analysis of key external debt ratios was carried out to highlight similarities and differences among the countries. A number of debt ratios (external debt stocks-to-exports, external debt stocks-to-gross domestic product, debt service-to-exports, short-term debt-to-external debt stocks, multilateral-to-external debt stocks, and foreign reserves-to-external debt stocks) were analysed and compared among the countries. In addition, the study analysed the major sources of foreign loans. That review provided the following information:

(i) Problems and challenges that were being addressed at each stage by each country;
(ii) The recommendations and policies that were put in place to address the problems/challenges; and
(iii) The extent to which the recommendations were implemented and the results.

3. Analysis and Findings

3.1 Evolution of External Debt Stocks

Figure 1 gives a historical perspective of the movement of external debt stocks in the EAC countries from 1970 to 2020. Borrowing to finance public infrastructure pushed debt levels to record highs. Total external debt stock grew by 333.38 percent from US$1.191 billion in 1970 to US$95.892 billion in 2020. In 1970, Kenya had the highest external debt stock followed by DRC, Tanzania, Uganda, Burundi, and Rwanda, respectively. Country positions changed from year to year. By 2000, DRC had the highest external debt stock followed by Tanzania, Kenya, Uganda, Rwanda, and Burundi, in that order. Tanzania, with external debt stock of US$8.94 billion, took over the top position in 2010, followed closely by Kenya (US$8.86 billion). Kenya overtook Tanzania in 2014 and remained in that position to date. DRC's external debt stocks dropped sharply from US$13.09 billion in 2009 to US$4.96 billion in 2018 before rising to US$6.14 billion in 2020. All the six countries with the exception of DRC and Burundi have registered sustained increases in external debt stocks in recent years.

Total external debt stock rose steadily up to around 2004/05 and then decreased during 2006 - 2010 as several countries in the EAC benefitted from Heavily Indebted Poor Countries (HIPC) and Multilateral Debt Relief Initiative (MDRI) debt relief programmes.[2]

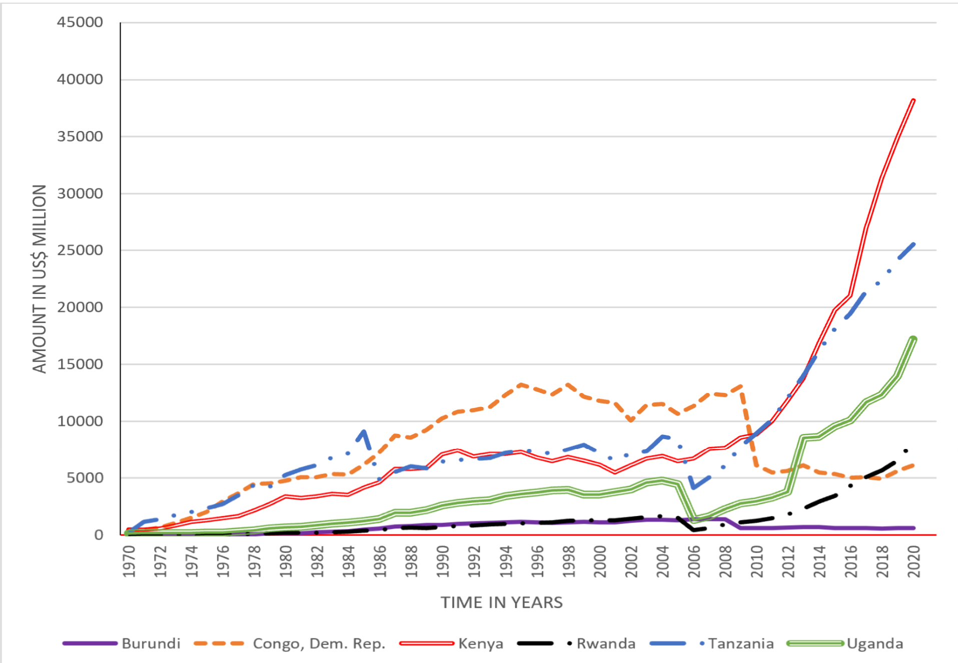

Figure 1: Total External Debt Stocks by Country (US$ Million)
Source: Computed from World Bank (2021). *International debt statistics 2022*. World Bank Publications.

[1] This study excludes the Republic of South Sudan due to no availability of comparable data.
[2] Wealthy countries and international financial institutions took action to relieve debt burdens in many of the world's poorest countries – primarily through the 'Heavily Indebted Poor Country' (HIPC) scheme and the 'Multilateral Debt Relief Initiative' (MDRI) – but debt burdens are still a problem. All the EAC countries, except Kenya, benefited from debt relief under the HIPC scheme.

Burundi's external debt stock remained relatively low and increased steadily up to 2008 when it dropped from US$1,390 million to US$607 million in 2009, a decrease of 56.33 percent. It averaged US$626 million from 2009 to 2020, reaching an overall high of US$690 million in 2014 and a record low of US$585 million in 2018. The drop in external debt stocks in 2009 was due to the benefit from HIPC initiative and additional debt relief under the MDRI.

The DRC's external debt has remained low following a substantial debt relief in 2010 when the country benefitted from HIPC and MDRI.[1] As a result, the ratio of public and publicly guaranteed external debt-to-GDP dropped from 75 percent at end of 2009 to 22 percent in 2010 and fell further to 13 percent in 2014. Private external debt increased marginally from 2.0 percent of GDP in 2012 to 3.8 percent in 2014.[2] The country's external debt for 2020 was US$6,137 million, a 9.25 percent increase from 2019. The external debt for 2019 was US$5,618, a 13.36 percent increase from 2018. These were relatively high increases compared to decrease of 2.52 percent between 2017 and 2018 and an increase of 1.24 percent between 2016 and 2017. The country's debt-carrying capacity is weak, with limited space to absorb shocks. The country shows vulnerability in debt repayment capacity due to weak revenue mobilization. As of December 2021, the country had accumulated external arrears amounting to $287 million.[3]

Kenya sustained a substantial increase in its external debt stocks between 2010 and 2020. The debt increased from US$8,862 million to US$38,194 million during the same period. In light of its Vision 2030 aiming at achieving and maintaining a sustainable and inclusive annual growth of 10 per cent, Kenya government embarked on expansionary fiscal policy, which involved investing in growth enabler projects such as revamping existing infrastructure systems and establishing new ones. However, most of these projects required large funding beyond the country's domestic revenue capacity and led to a widening of budget deficit, financed through public debt. This explains the substantial increase in external debt stocks.

Tanzania's total external debt declined from US$7.7 billion, or 57.3 percent of GDP at end-June 2006, to US$4.5 billion, or 24.8 percent of GDP. The country benefited from extensive debt relief under the HIPC and MDRI. As of end-June 2008, its public external debt stood at US$3.7 billion (20.9 percent of GDP), compared with US$7.2 billion (53.4 percent of GDP) at end-June 2006, before MDRI went into effect.[4] The country's external debt stock has been rising since 2010. It increased from US$8,937 million in 2010 to US$25,538 million in 2020. Non-concessional borrowing has increased in recent years to finance the country's public infrastructure agenda.

Multilateral and official bilateral creditors continue to be Tanzania's major financiers, accounting for about 70 percent of the stock of public and publicly guaranteed debt in FY2019/20. However, in recent years, commercial borrowing as a share of new disbursement has increased to about 50 percent, and in FY 2020/2021, it reached about 68 percent, as authorities borrowed US$1.3 billion through commercial loans to finance the Standard Gauge Railway project.[5]

Rwanda's external debt declined from 85 percent of GDP in 2000–04 to about 15 percent of GDP since 2006, thanks to substantial debt relief.[6] The country benefitted from massive external debt cancellation by the international community under HIPC and MDRI. The country's external debt for 2020 was US$8,193 million, a 25.76 percent increase from 2019. The external debt for 2019 was US$6,515 milli0n, a 14.68 percent increase from 2018.

Uganda's external debt followed an increasing trend from 1970 to around 2005/206. The HIPC initiative contributed to the reduction of the external debt stocks by 70.84 percent from the previous year.[7] The gradual upward trend continued again up to 2013 when the debt increased by 126.68 percent from the previous year[8]. The country's external debt for 2020 was US$17,207 million, a 23.16 percent increase from 2019. The country's external debt for 2019 was US$13,971 million, a 13.45 percent increase from 2018. Analysts project the external debt stock to continue increasing in the short to medium term given the robust Second and Third National Plan's core projects and priorities, which are likely to continue attracting more borrowing.

All the EAC countries except Burundi had publicly guaranteed private sector external debt from commercial banks between 2010 and 2020. Kenya's debt in this category increased from US$289 million in

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[1] Africa Development Bank Group (April 2011). DRC Completion Point Document under the Enhanced HIPC Initiative.

[2] International Monetary Fund (August 17, 2015). Democratic Republic of Congo, Staff Report for the 2015 Article IV Consultation – Debt Sustainability Analysis, Washington, DC, p. 2

[3] International Monetary Fund (December 2021). Democratic Republic of the Congo: First Review Under the Extended Credit Facility Arrangement, Request for Modification of Performance Criteria, and Financing Assurances Review—Debt Sustainability Analysis

[4] World Bank/International Monetary Fund (May 15, 2009). UNITED REPUBLIC OF TANZANIA Joint World Bank/IMF Debt Sustainability Analysis, Washington, DC, p. 2

[5] IMF (December 2021). United Republic of Tanzania: Requests for Disbursement Under the Rapid Credit Facility and Purchase Under the Rapid Financing Instrument—debt Sustainability Analysis

[6] Rwanda reached the HIPC Completion Point in April 2005 and benefited from MDRI relief in January 2006.

[7] Uganda generously received 100 percent debt forgiveness/cancelation, which consequently reduced its debt to US$1.6 billion.

[8] High Uganda Shilling interest rates attracted foreign exchange inflows and skewed domestic lending toward foreign currency.

2010 to US$7,406 million in 2020 compared to Uganda's case that increased from US$1 million in 2016 to US$519 million in 2020. Three of the EAC countries, Kenya, Tanzania and Rwanda, had nonguaranteed private sector external debt during the period. Kenya and Rwanda were the only countries in the Community that had private sector external debt from bondholders between 2010 and 2020.[1]

Table 1 summarises the movement of external debt stocks in the EAC countries from 1970 to 2020. The countries are in a vulnerable position, with public external debt already at elevated levels relative to their respective GDP and export earnings.

Table 1: EAC Total external debt by country (US$ billions)

COUNTRY	1970	2000	2010	2020
BURUNDI	0.02	1.13	0.62	0.63
DRC	0.35	11.80	6.14	6.14
KENYA	0.48	6.15	8.86	38.19
RWANDA	0.01	1.29	1.23	8.19
TANZANIA	0.20	7.20	8.94	25.54
UGANDA	0.15	3.54	2.97	17.21
TOTAL	1.19	31.10	28.76	95.89

Source: Computed from World Bank (2021). *International debt statistics 2022*. World Bank Publications.

Figure 2 presents the share of the external debt stock among the EAC countries in selected years between 2010 1nd 2020. Kenya has sustained an increasing and largest share over the period followed by Tanzania. The shares of Kenya, Tanzania, Uganda and Rwanda increased while those of DRC and Burundi declined.

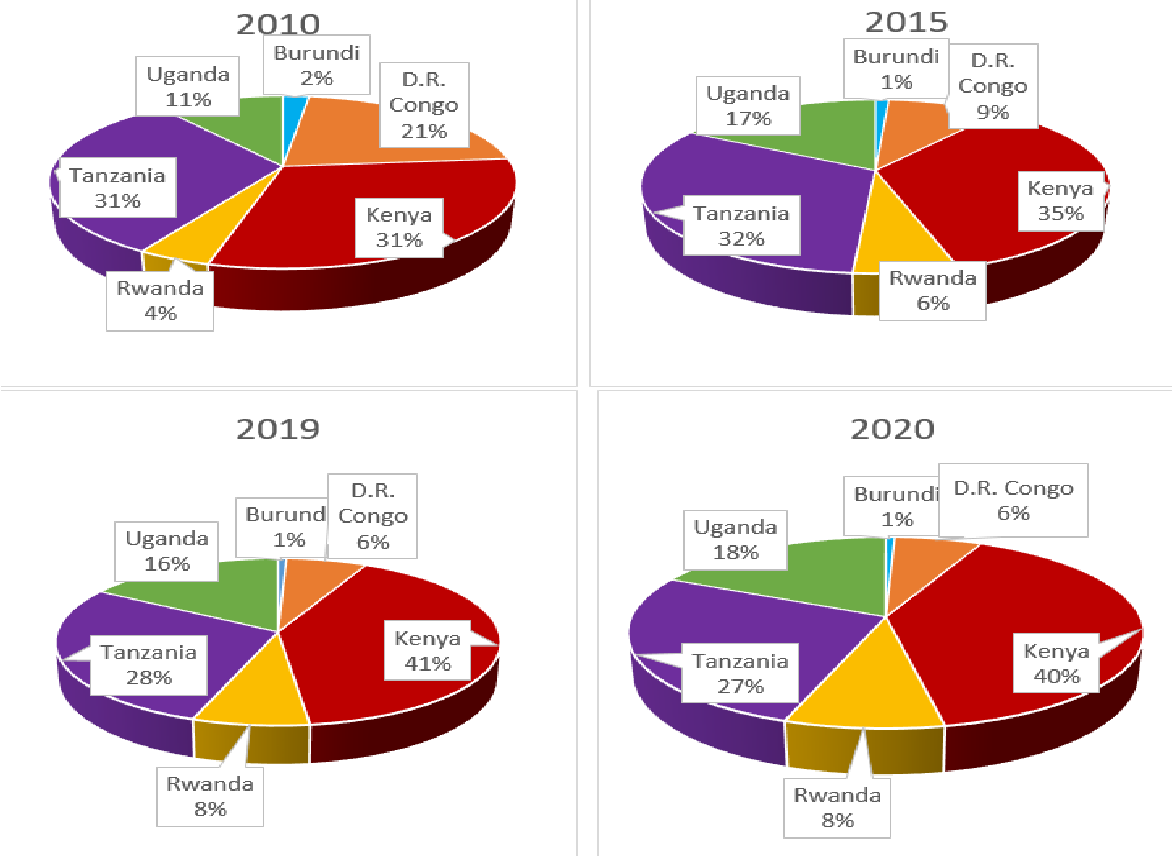

Figure 2: Total EAC External Debt by Country

Source: Computed from World Bank. (2021). *International debt statistics 2022*. World Bank Publications.

Table 2 shows GDP, exports and external debt growth in the EAC countries between 2010 and 2020. The rise in external debt exceeded growth in GDP and exports by very large amounts in all the countries except for DRC. For example, while Kenya's GDP and exports increased by 121.71 and 6.20 percent, respectively, the country's external debt grew by 330.99 percent over the same period. Rwanda's GDP and exports grew by 66.37

[1] World Bank (2021). *International debt statistics 2022*. World Bank Publications.

and 198.84 percent, respectively, while its external debt rose by 564.48 percent during the period. Exports grew in Burundi up to 2014, then declined steadily up to 2020, and then rose slightly in 2021.

Table 2: GDP, exports and external debt growth between 2010 and 2020 (percentage)

COUNTRY	GDP	EXPORTS	EXTERNAL DEBT
BURUNDI	36.83	-38.84	0.82
DRC	125.90	57.18	0.00
KENYA	121.71	6.20	330.99
RWANDA	66.37	198.84	564.48
TANZANIA	94.94	42.13	185.76
UGANDA	40.97	57.18	478.39

Source: Computed from World Bank (2021). *International debt statistics 2022*; and *World Bank national accounts data, and OECD National Accounts data files*. World Bank Publications.

3.2 Structure of External Debt

External debt is broadly divided into long-term and short-term debt. Long-term debt accounts for most of the external debt stock in all the EAC countries. Virtually all the countries are increasingly borrowing more long-term than short-term external loans as shown in Table 3. In 2010 long-term loans accounted for 61.49 percent of Burundi's total external debt stocks compared to DRC (74.82 percent), Tanzania (77.45 percent), Kenya (79.03 percent), Rwanda (88.05 percent), and Uganda (89.85 percent). All the six countries registered increased share of long-term debt-to-total external debt stocks between 2010 and 2015. However, three countries -- DRC, Rwanda and Uganda -- registered small decreases in the share of long-term external debt between 2015 and 2020.

Table 3: Long-term-to-total external debt stock (percentage)

COUNTRY	2010	2015	2020
BURUNDI	61.5	67.8	78.8
DRC	74.8	76.0	73.3
KENYA	79.0	84.6	90.4
RWANDA	88.1	90.0	89.0
TANZANIA	77.5	84.6	86.6
UGANDA	89.9	92.7	88.6

Source: Computed from World Bank. (2021). *International debt statistics 2022*. World Bank Publications.

Figure 3 shows trends in long-term external debt stocks by country between 2010 and 2020 while Figure 4 shows trends in short-term external debt during the same period. Kenya, Tanzania and Uganda registered increase in value of long-term debt in each year over the period.

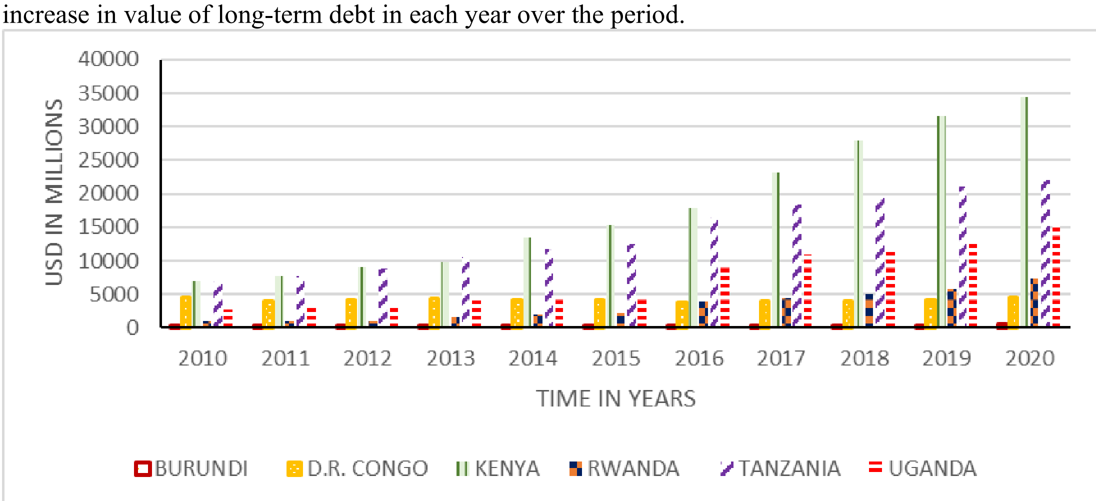

Figure 3: EAC Long-term External Debt Stocks

Source: Computed from World Bank. (2021). *International debt statistics 2022*. World Bank Publications.

In terms of volume, Tanzania leads in short-term external debt followed by Kenya and Uganda, in that order. The amount for Burundi and Rwanda are relatively very small. Burundi's short-term external debt stock remained at US$0.3 million per year between 2016 and 2020, having decreased from US$15.7 million in 2010.

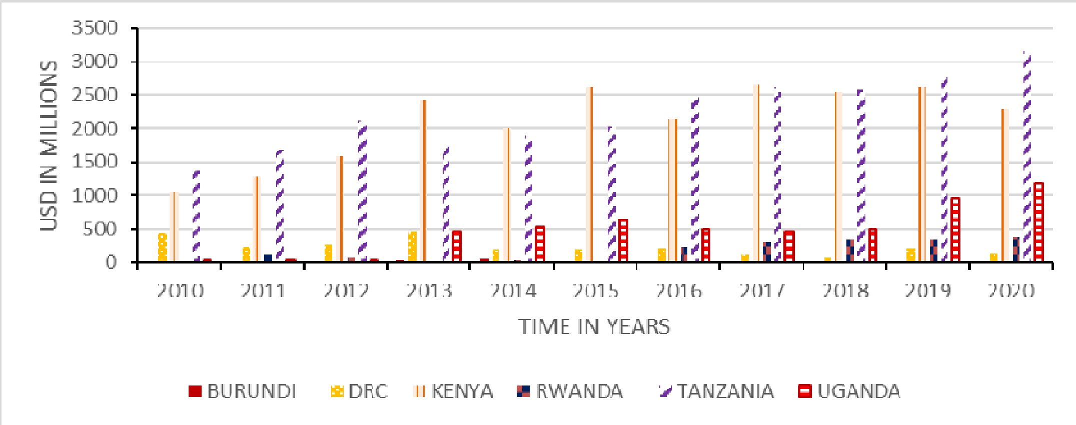

Figure 4: EAC Short-term External Debt
Source: Computed from World Bank. (2021). *International debt statistics 2022*. World Bank Publications.

3.3 Long-term External Debt Mix (Multilateral, Bilateral and Commercial Banks)

Multilateral and official bilateral creditors are the major financiers in all the EAC countries. They accounted for 100 percent of the stock of public and publicly guaranteed external debt in Burundi, Rwanda and Uganda and over 95 percent in DRC, Kenya and Tanzania in 2010. Details are in Table 4. In recent years, commercial/private sector borrowing (bondholders, commercial banks and others) has increased in all the countries with the exception of Burundi. For example, the contribution of private sector financiers to Kenya's external debt increased from 4.13 percent in 2010 to 21.98 percent in 2020 while that of Rwanda went up from zero to 14.55 percent and the one of Tanzania rose from 2.37 percent to 13.20 percent over the same period. Kenya and Rwanda have joined a fast growing number of African countries that are issuing international sovereign bonds.[1] Tanzania's commercial borrowing as a share of external debt has increased as the authorities borrowed US$1.3 billion through commercial loans to finance a Standard Gauge Railway project.[2]

Table 4: Long Term Debt Mix by Country (percentage)

	2010			2020		
	Multilateral	Bilateral	Private	Multilateral	Bilateral	Private
BURUNDI	85.15	14.85	-	71.60	28.40	-
DRC	56.31	42.02	1.68	50.93	46.06	3.00
KENYA	58.67	37.20	4.13	44.99	33.03	21.98
RWANDA	84.19	15.81	-	72.96	12.50	14.55
TANZANIA	77.42	20.21	2.37	63.43	23.37	13.20
UGANDA	90.39	9.61	-	63.65	31.77	4.58

Source: Computed from World Bank. (2021). *International debt statistics 2022*. World Bank Publications.

Kenya and Rwanda have issued international sovereign bonds (Eurobonds[3]). This development is positive in many ways, including creditors such as China offering quicker deals and fewer conditions. However, it also brings new risks. The bonds are denominated in foreign currencies such as the US dollar, which can significantly increase the repayment costs for governments if their national currency weakens against the dollar. This risk becomes even more critical if the prices of exports upon which these borrowing countries are dependent start to fall. A further development is that the private sector has an increasingly large role, mostly during the economic recession affecting many developed countries, leading speculators to look for better returns further afield. This has resulted in higher average interest rates for borrowing countries and led to fragmentation of creditors, which makes it very difficult to coordinate action to prevent debt crises.

Kenya is reviewing its external borrowing options after its Eurobond yields hit double digits, indicating the high finance cost the country faces if it were to sell a new international bond. The Government has agreed with the IMF to stick to concessional finance to reduce debt vulnerabilities that have seen the country turn away from

[1] For example, in 2014 alone, Zambia, Kenya, Côte d'Ivoire, South Africa, Senegal and Ghana issued bonds raising a total of almost US$7 billion.
[2] IMF (September 2021). United Republic of Tanzania: Requests for Disbursement Under the Rapid Credit Facility and Purchase Under the Rapid Financing Instrument—debt Sustainability Analysis
[3] A Eurobond is a fixed-income debt instrument (security) denominated in a different currency than the local one of the country where the bond is issued. Hence, it is a unique type of bond. Eurobonds allow corporations to raise funds by issuing bonds in a foreign currency.

syndicated loans and only focus on multilateral loans and Eurobonds.[1] In real terms, the more expensive commercial debt has worsened the external debt burden due to the persistent fall in the value of the Kenya shilling and the economic slump that followed the COVID-19 restrictions.[2]

Rwanda had issued two bonds by August 2021. In 2021, the country raised US$ 620 million through a 10-year Eurobond whose proceeds will: retire the country's existing Eurobond, fund priority projects that will support recovery from the economic downturn caused by the COVID-19 pandemic, and finance strategic investments in health and agriculture.[3]

3.4 External Debt Indicators

3.4.1 External debt stocks-to-exports (percentage)

External debt stocks-to-exports is the ratio of total outstanding external debt at the end of the year to the country's exports of goods and services for any one year. It is useful as trend indicator closely linked to the repayment capacity of a country. The ratio can be used as a measure of debt sustainability because an increasing debt-to-exports ratio over time, for a given interest rate, implies that total debt is growing faster than the economy's basic source of foreign exchange, signaling that the country may have problems meeting its debt obligations in the future. Significant amounts of the export earnings are spent on servicing external debts.

External debt stocks as a percentage of exports are summarised in Table 5 for the period 2010 to 2020. In 2010, Burundi had the highest external debt stocks-to-exports ratio (341.4 percent) followed by Rwanda (172.0 percent), Tanzania ((137.0 percent), Kenya (97.0 percent), Uganda (84.0 percent), and DRC (69 percent). However, while Burundi's ratio remained high, it was on a declining trend starting from 2015 and had dropped to 193.8 percent by 2018. DRC's ratio had dropped to 43.0 percent by 2020. Kenya's external debt stocks-to-exports ratio followed an upward trend, starting from 97 percent in 2010 to 380 percent in 2020. By 2020, Rwanda's ratio was the highest (422.0 percent), followed by Kenya (380.0 percent), Uganda (304.0 percent), Tanzania (295.0 percent), and DRC (40.0 percent).

Table 5: External debt stocks-to-exports (percentage)

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
BURUNDI	341.4	248.6	283.3	290.9	313.7	325.3	289.1	213.6	193.8	--	--
DRC	69.0	53.1	62.1	51.2	43.3	51.9	42.0	44.0	31.0	37.0	43.0
KENYA	97.0	100.3	106.1	125.3	147.8	177.5	210.0	254.0	267.0	298.0	380.0
RWANDA	172.0	130.3	123.0	130.4	160.9	158.5	283.0	264.0	276.0	288.0	422.0
TANZANIA	137.0	132.1	131.6	153.0	162.4	157.3	227.0	267.0	259.0	245.0	295.0
UGANDA	84.0	75.6	75.5	90.4	105.0	118.1	208.0	227.0	217.0	226.0	304.0

Source: Computed from World Bank. (2021). *International debt statistics 2022*. World Bank Publications.

Figure 5 presents a visual comparison of the trend in the external debt stocks-to-exports ratio in the EAC countries from 2010 to 2020. Except for Burundi, the ratio has been upward in all the countries in recent years.

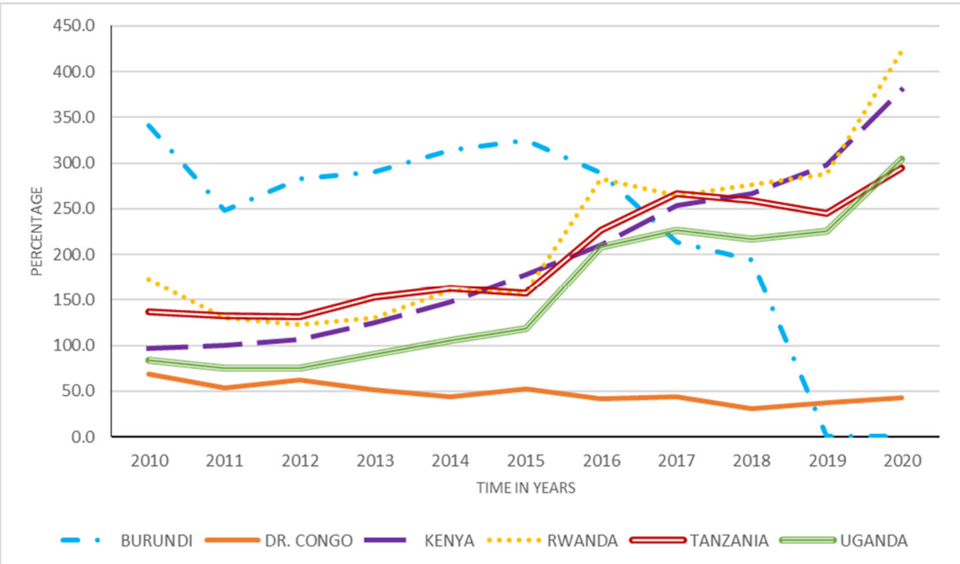

Figure 5: External Debt Stocks-to-Exports (percentage)

Source: Computed from World Bank. (2021). *International debt statistics 2022*. World Bank Publications.

[1] Central Bank of Kenya
[2] Central Bank of Kenya
[3] Government of Rwanda, Ministry of Finance and Economic Planning (2 August 2021).

External debt-to-export ratio has been and remains elevated in all the countries except DRC. It has increased by 283 percent in Kenya, 250 percent in Rwanda, 220 percent in Uganda, and 158 percent in Tanzania between 2010 and 2020. This signals that a shock in export earnings can easily lead to default in debt service. It also underscores the importance of enhancing revenue mobilisation and looking for concessional loans where possible.

3.4.2 External debt stocks-to-GDP (percentage)

The debt-to-GDP ratio is the ratio of a country's public debt to its gross domestic product. The ratio is handy because it relates debt to resource base. It is an indicator of a country's solvency. Interpreted differently, the ratio represents the number of years it would take to pay back debt if GDP was used for repayment. The higher the debt-to-GDP ratio, the less likely the country will pay back its debt and the higher its risk of default. According to the findings of a World Bank study, countries whose debt-to-GDP ratios exceed 77 percent for prolonged periods experience significant slowdowns in their economic growth.[1]

Table 6 shows trends in the external debt stocks-to-GDP ratio in each of the six countries between 2010 and 2020. Except for Burundi and DRC, the ratio was on an upward trend, with Rwanda recording the highest increase of 60.4 percent. In 2010 Burundi had the highest external debt-to-GDP ratio (30.6 percent) followed by DRC (28.5 percent), Tanzania (27.9 percent), Rwanda (20.1 percent), Kenya (19.5 percent), and Uganda (11.2 percent). However, by 2020 the relative positions had changed largely. Rwanda now topped the list (80.5 percent) followed by Uganda (45.8 percent), Tanzania ((40.9 percent), Kenya (37.9 percent), and DRC (12.6 percent).

Figure 6: External debt stocks-to-gdp (percentage)

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
BURUNDI	30.6	27.0	28.6	27.9	25.5	20.2	22.8	22.4	22.0	23.0	22.5
DRC	28.5	21.2	19.2	18.8	15.3	14.1	13.5	13.4	10.4	10.9	12.6
KENYA	19.5	21.4	20.9	22.3	24.7	28.2	28.1	32.8	34.1	34.8	37.9
RWANDA	20.1	21.2	23.7	29.6	35.3	40.4	49.7	54.9	58.9	62.9	80.5
TANZANIA	27.9	29.3	30.4	30.6	32.5	38.3	39.0	40.2	39.2	39.5	40.9
UGANDA	11.2	11.7	13.8	29.6	26.5	29.6	34.5	38.0	37.4	39.5	45.8

Source: Computed from World Bank. (2021). *International debt statistics 2022*. World Bank Publications.

With the HIPC debt relief, the ratio decreased significantly in Burundi, Tanzania, Rwanda and Uganda during the period up to 2010. The recent upward trend is associated with these countries' increased access to international financial markets. With increased fiscal space, the countries embarked on an infrastructural upgrade programme that resulted in increased debt-to-GDP ratios. The ratios for Burundi and DRC declined between 2010 and 2020 while those for Kenya, Rwanda, Tanzania, and Uganda increased. Kenya's external debt-to-GDP ratio declined from 21.4 percent in 2011 to 20.9 percent in 2012, but increased thereafter driven largely by spending on infrastructure and more recently, COVID-19 related spending. Rwanda's ratio increased by 60.4 percentage points of GDP between 2010 and 2020, driven by borrowing to meet the development needs envisaged in the National Strategy for Transformation.

Figure 6 gives a visual representation of the trends in external debt stocks-to-GDP in the six countries from 2010 t0 2020. The trend was generally upward.

[1] Grennes, T. et al. (2010). Finding the Tipping Point – When Sovereign Debt Turns Bad. World Bank Policy Research Working Papers, Washington, DC

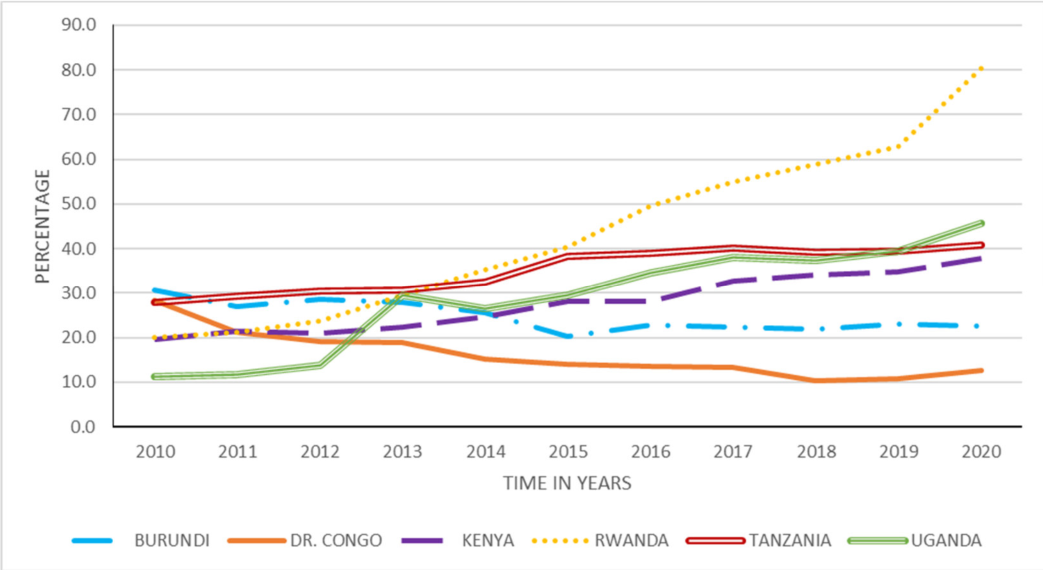

Figure 6: External Debt Stocks-to-GDP (percentage)
Source: Computed from World Bank. (2021). *International debt statistics 2022*. World Bank Publications.

3.4.3 External debt service-to-exports (percentage)
Debt service-to-exports ratio is the ratio of debt service payments from a country to that country's export earnings. It is a proxy for a country's liquidity position. Table 7 and Figure 7 represent the ratios for the EAC countries for the period 2010 to 2020. All the countries, with a few exceptions in a limited number of years, had low single digit ratios between 2010 and 2015. The ratios have since been in double digits in Kenya, Rwanda, and Tanzania, with Kenya reaching a high of 38 percent in 2019. Kenya's high ratio in 2019 was mainly because of a one-off US$750 million Eurobond repayment. The ratio declined to 28 percent the following year due to an improvement of the terms on new external loans.[1] The high debt service-to-export ratios suggest that over the medium-term some of these countries have limited space to absorb shocks. DRC is the only country that maintained a low debt service-to-exports ratio throughout the period.

Table7: Debt service-to-export (percentage)

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
BURUNDI	2.4	4.2	8.9	13.8	13.3	13.5	16.0	9.6	9.9	0.0	0.0
DRC	3.0	2.5	3.1	3.3	3.2	3.7	4.0	3.0	2.0	7.0	2.0
KENYA	4.0	4.3	5.3	5.9	10.9	6.8	11.0	15.0	24.0	38.0	28.0
RWANDA	7.0	2.1	2.2	3.2	4.5	7.7	15.0	13.0	13.0	14.0	15.0
TANZANIA	3.0	1.9	1.8	1.8	2.7	3.6	9.0	10.0	12.0	13.0	15.0
UGANDA	2.0	1.5	1.4	1.5	2.1	1.8	17.0	4.0	9.0	5.0	12.0

Source: Computed from World Bank. (2021). *International debt statistics 2022*. World Bank Publications.

[1] Central Bank of Kenya

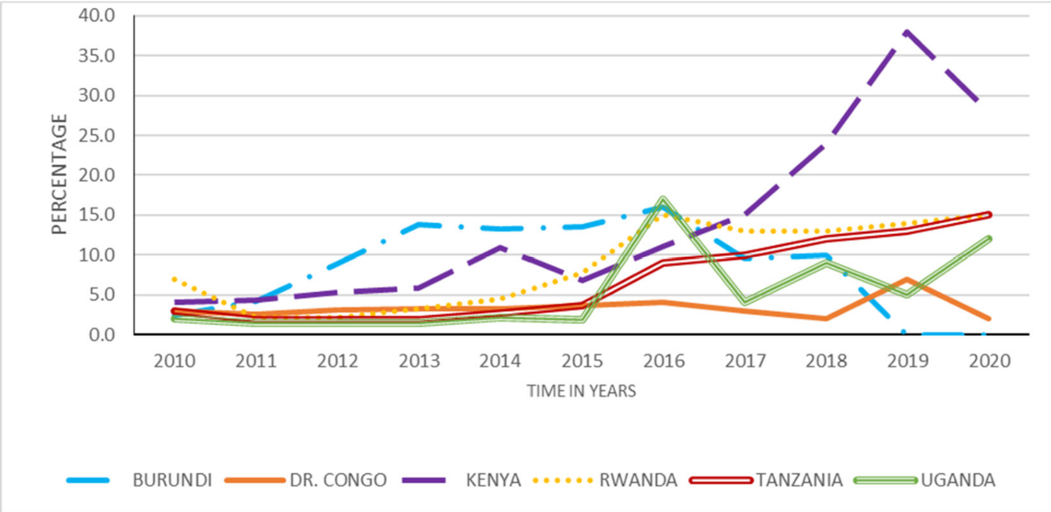

Figure 7: Debt Service-to-Exports (percentage)
Source: Computed from World Bank. (2021). *International debt statistics 2022*. World Bank Publications.

3.4.4 Short-term debt-to-external debt stocks (percentage)

Short-term debt includes all debt having an original maturity of one year or less and interest in arrears on long-term debt. The countries are increasingly borrowing less short-term vis-à-vis long-term loans as illustrated in Table 8 and Figure 8. While Tanzania's short-term-to-external debt stocks remained in double digits between 2010 and 2020, the trend was downward.

Table 8: Short-term debt-to-external debt stocks (percentage)

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
BURUNDI	2.5	0.1	1.1	4.6	7.0	0.0	0.0	0.0	0.0	0.0	0.0
DRC	7.0	4.1	4.7	7.2	3.4	3.4	4.0	2.0	2.0	4.0	2.0
KENYA	12.0	12.7	13.3	17.6	12.0	13.7	10.0	10.0	8.0	7.0	6.0
RWANDA	1.0	9.2	6.8	0.7	1.2	0.5	5.0	6.0	6.0	5.0	5.0
TANZANIA	15.0	16.8	18.3	13.4	13.2	13.5	13.0	12.0	12.0	12.0	12.0
UGANDA	1.0	0.8	0.7	9.8	10.7	11.2	5.0	4.0	4.0	7.0	7.0

Source: Computed from World Bank. (2021). *International debt statistics 2022*. World Bank Publications.

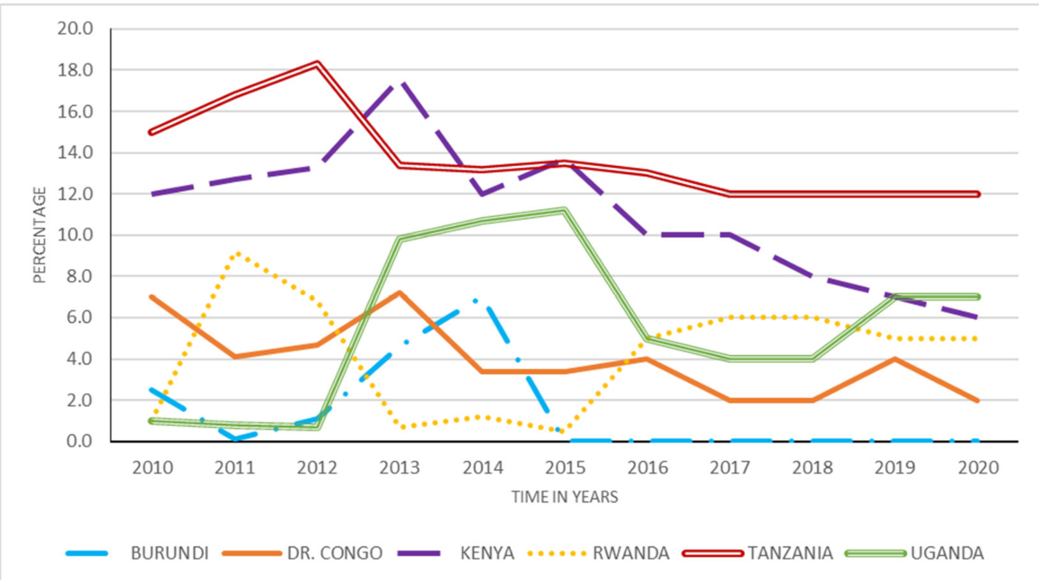

Figure 8: Short-term Debt-to-External Debt Stocks (percentage)
Source: Computed from World Bank. (2021). *International debt statistics 2022*. World Bank Publications.

3.4.5 Multilateral-to-external debt stocks (percentage)

The ratio of multilateral-to-external debt stocks declined in all the countries except Burundi between 2010 and 2020 because of increase in the number of bilateral and commercial lenders (Table 9 and Figure 9).

Table 9: Multilateral-to-external debt stocks (percentage)

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
BURUNDI	52.4	51.1	50.4	47.2	45.5	49.1	51.5	52.6	53.6	57.6	56.4
DRC	42.0	43.5	41.7	36.7	35.8	35.4	34.0	39.0	41.0	38.0	37.0
KENYA	46.0	45.4	43.0	42.4	37.3	35.2	33.0	33.0	32.0	36.0	40.0
RWANDA	52.0	67.4	69.4	55.2	54.5	60.9	38.0	41.0	43.0	46.0	46.0
TANZANIA	49.0	47.6	47.0	48.5	47.5	48.9	40.0	41.0	42.0	42.0	44.0
UGANDA	81.0	83.0	80.5	74.2	73.0	67.5	40.0	42.0	41.0	40.0	42.0

Source: Computed from World Bank. (2021). *International debt statistics 2022*. World Bank Publications.

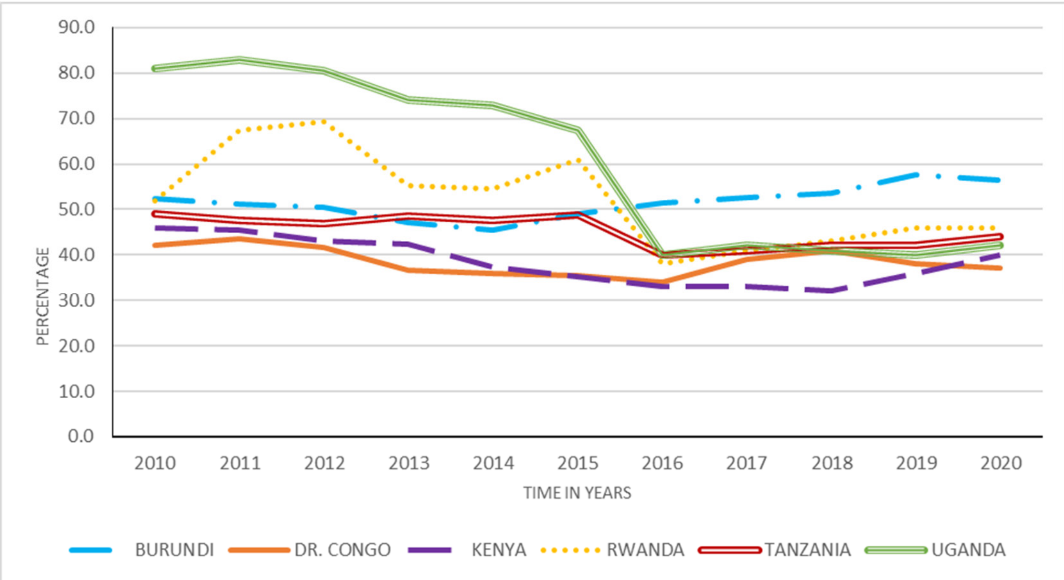

Figure 9: Multilateral-to-External Debt Stocks (percentage)

Source: Computed from World Bank. (2021). *International debt statistics 2022*. World Bank Publications.

3.4.6 Reserves-to-external debt stocks (percentage)

Increasing foreign exchange reserves assist governments in meeting their foreign exchange requirements and external debt obligations. The higher the foreign exchange reserves-to-external debt stocks ratio, the better off a country is in terms of meeting its external debt obligations. Overall, the ratio decreased in all the countries between 2010 and 2020. (Table 10 and Figure 10). The decrease ranged from a high of 43 percent for Rwanda to a low of 9 percent for DRC. If the trend continues, the EAC countries could have challenges in meeting their external debt obligations and foreign exchange requirements.

Table 10: reserves-to-external debt stocks (percentage)

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
BURUNDI	53.3	48.6	46.0	48.0	45.8	21.6	15.6	15.8	11.4	18.5	14.1
DRC	21.0	23.0	29.0	27.2	28.2	22.4	14.0	14.0	13.0	21.0	12.0
KENYA	49.0	42.0	48.0	48.1	47.4	39.4	36.0	27.0	26.0	26.0	22.0
RWANDA	65.0	86.4	67.2	63.2	52.7	45.9	23.0	23.0	24.0	22.0	22.0
TANZANIA	44.0	37.2	35.0	35.6	30.6	27.1	22.0	27.0	23.0	--	--
UGANDA	91.0	80.2	83.9	69.5	66.4	50.5	31.0	32.0	27.0	--	--

Source: Computed from World Bank. (2021). *International debt statistics 2022*. World Bank Publications.

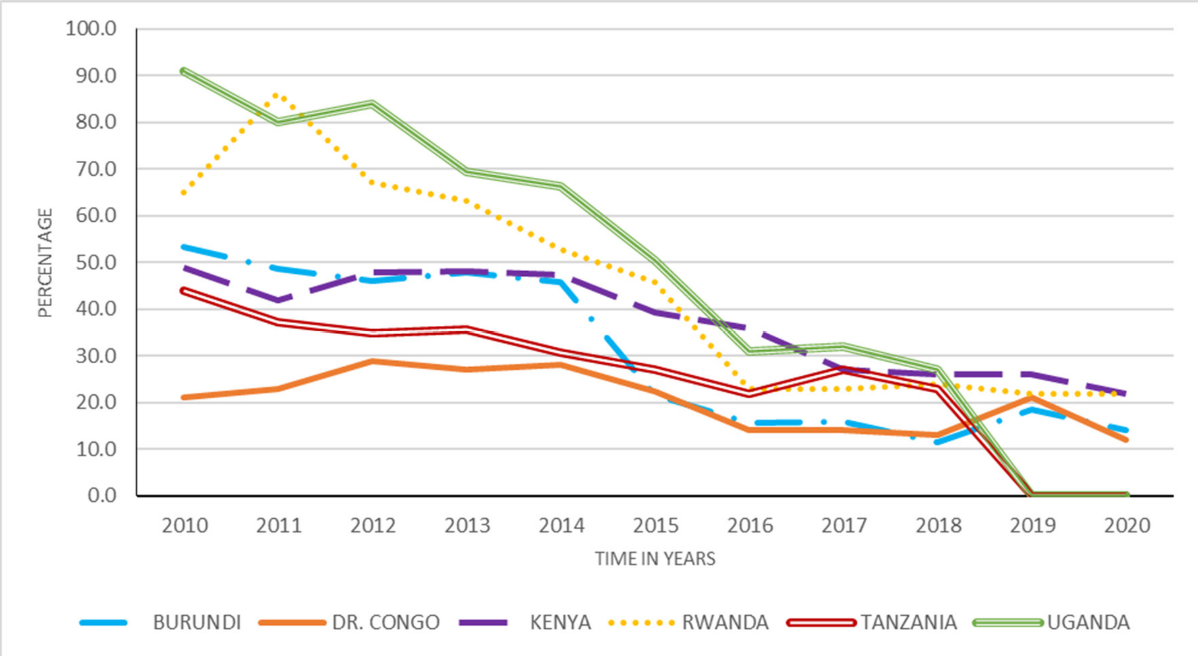

Figure 10: Reserves-to-External Debt Stocks (percentage)
Source: Computed from World Bank. (2021). *International debt statistics 2022*. World Bank Publications.

4. Conclusions

The EAC countries are in a vulnerable position, with public external debt already at elevated levels relative to their respective GDP and export earnings. Borrowing to finance public infrastructure has pushed debt levels to record highs in the Community. Total external debt stock grew by 333.38 percent between 1970 and 2020. The recent upward trend in external debt-to-GDP ratio is associated with the countries' increased access to international financial markets.

The rise in external debt exceeded growth in GDP and exports in all the countries except for DRC between 2010 and 2020. The situation could have been worse had it not been for a massive external debt cancellation by the international community under the HIPC and MDRI debt relief programmes that benefitted all the EAC countries except Kenya.

With the HIPC debt relief, external debt-to-GDP ratio decreased significantly in Burundi, Tanzania, Rwanda and Uganda during the period up to 2010. With increased fiscal space, the countries embarked on an infrastructural upgrade programme that resulted in increased debt-to-GDP ratios. Kenya did not qualify for the HIPC debt relief programme. The country's stock of external debt has been rising sharply since around 2010 because of the Government's expansionary fiscal policy that involved investing in growth enabler projects such as revamping existing infrastructure systems and establishing new ones. These big projects depended on foreign funding.

Almost all the countries are increasingly borrowing more long-term than short-term external loans. With the exception of DRC and Uganda, all the EAC countries registered increased share of long-term debt-to-total external debt stocks in 2020 compared to 2010.

Multilateral and official bilateral creditors continue to be the major financiers in all the countries even though these countries are gradually diversifying their sources of borrowing.

All the EAC countries except Burundi had publicly guaranteed private sector external debt from commercial banks between 2010 and 2020. Only Kenya, Tanzania, and Rwanda had nonguaranteed private sector external debt during the period. Two of the countries, Kenya and Rwanda, have joined a fast growing number of African countries that are issuing international sovereign bonds.

The rise in external debt in the EAC countries exceeded growth in GDP and exports by very large margins in all the countries except for DRC in the last decade. The rise in external debt exceeded growth in GDP and exports by very large amounts in all the countries except for DRC. For example, while Kenya's GDP and exports grew by 121.71 and 6.20 percent, respectively, between 2010 and 2020, the country's external debt grew by 330.99 percent over the same period.

Trends in some of the external debt ratios including debt-to-GDP, debt-to-exports, and debt service-to-exports suggest that these countries could face challenges in servicing their external debts and meeting other foreign exchange obligations. High external debt levels have economic consequences. Selected debt ratios show that the high debt levels have narrowed the fiscal space in these countries. The ability of the governments in the Community to service their debt obligations and still have resources left for development and recurrent expenditure has narrowed considerably. High external debt levels have also narrowed the fiscal buffers in the Community -- the countries cannot save budgetary resources and reduce external debt in good times.

Public debt that is too large may cause investors to raise interest rates in return for the increased risk of default. Thus, more resources are required to service the debt. It follows that excessive levels of foreign debt can hamper these countries' ability to invest in their economic future as their limited revenue goes to servicing their loans. This could impede long-term economic growth.

External debt often leads to a vicious cycle of debt for countries. Even after benefitting from the HIPC and MDRI debt relief programmes, the countries are once again facing high debt ratios. The debt relief created space that was followed by a cycle of continuous borrowing, accumulating payment burden, and eventual debt distress again.

5. Recommendations

In order to reduce external debt burden, the EAC countries should:

- Look for improved terms on new loans and make concerted efforts to increase concessional public external debt
- Restructure external commercial loans that have heavy maturities and high interest rates
- Diversify sources of external financing to reduce high dependency on expensive loans
- Explore non-debt creating financing options for public investments such as PPPs
- Increasing efficiency of public spending to avoid waste
- Refinancing expensive debt with debt on more favorable terms
- Frequent reporting and monitoring use of borrowed funds

There is also a need for each of the EAC countries to conduct a detailed study that captures returns from expenditures (investments) through increased exports, taxes, and faster economic growth.

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