SEPTEMBER 2025
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A New Debt Deal for Africa: Moving Up the Ladder

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Executive Summary

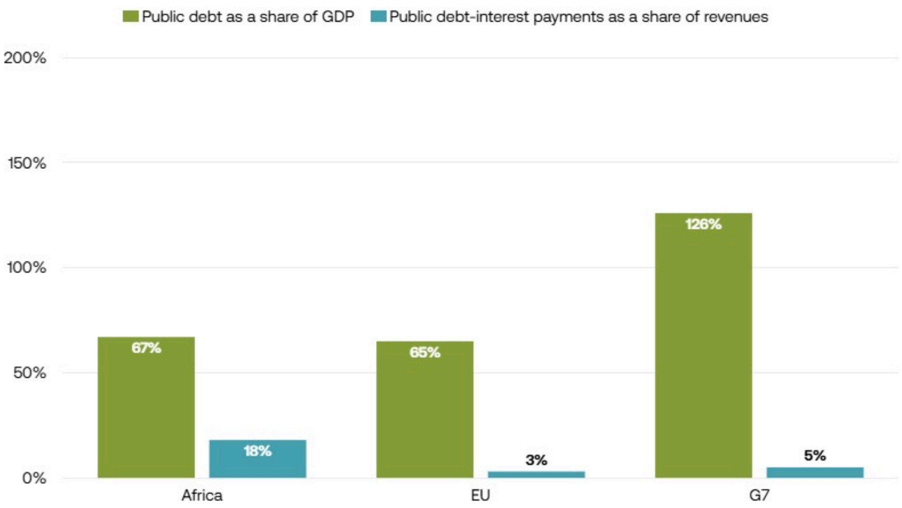
In February 2025, the Tony Blair Institute for Global Change published *A New Debt Deal for Africa: Breaking the Vicious Cycle*. This paper addressed the current, unjust debt challenge facing many African nations and called for a new global debt deal.

Despite significantly lower debt-to-GDP ratios than the G7, African countries face interest costs that are four to five times higher than those of G7 member countries. Because of this, on average African governments spend 18 per cent of all government revenues on interest alone: money that could be used instead to invest in roads, ports, skills, schools and hospitals.

The current global financial system, shaped through the activities of the global banking system, investors and credit-rating agencies, enforces a negative risk-perception cycle for African countries. This cycle starts with African countries being labelled as higher-risk investments and therefore having higher interest rates imposed upon them. Higher interest rates mean governments have less ability to invest in schools, skills, basic infrastructure and economic development, and local businesses face higher borrowing costs to invest in innovation, forcing them to remain uncompetitive. This results in weaker economies, fewer jobs, slow growth and depreciating currencies, feeding higher inflation, which in turn results in weak tax revenue, enhancing the perception that the government will be unable to repay debts – a self-fulfilling negative risk-perception spiral.

FIGURE 1

African interest payments outstrip EU/ G7 interest payments, while African debt is equal or lower



Source: TBI analysis based on UNCTAD data

This issue pervades all economic-development efforts, across every sector. The high cost of debt impairs African countries from investing in renewable power, trade infrastructure, basic education and health care, agriculture productivity, digital-technology adoption and economic-sector development. A solution must be found.

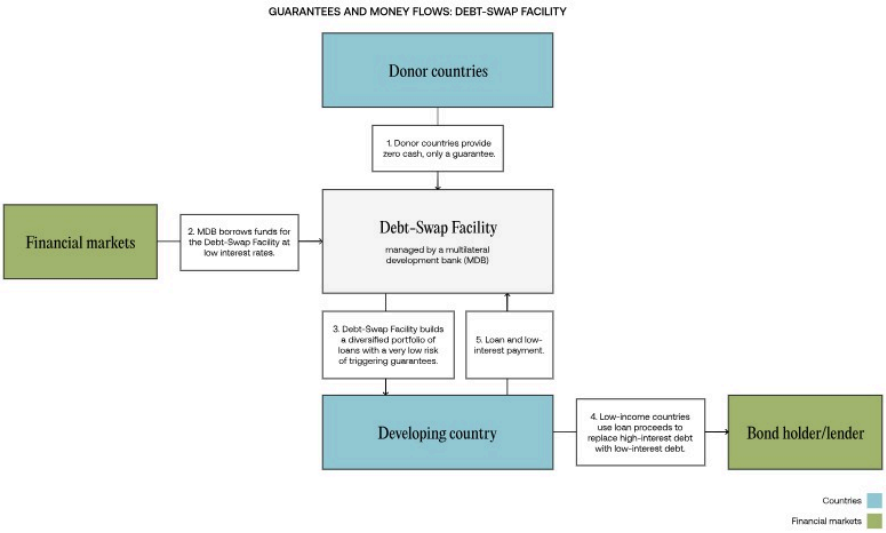
As part of a "New Debt Deal for Africa", TBI has previously called for the international community to collaborate to develop new tools to provide African leaders with a lower cost of debt to refinance their high-interest-paying debt.

These should be powered by a new, cost-efficient $100 billion Debt-Swap Facility.

In this follow-up piece, we outline the details of one key instrument – which we call "Moving Up the Ladder" – that facilitates this model of debt-swapping. Informed by many discussions with African leaders, ministers and their staff, and linked to improvements in public financial management, this instrument offers a path out of the current debt trap by reducing borrowing costs, improving fiscal governance and restoring investor confidence – without requiring major new aid commitments from donor countries.

FIGURE 2

The Debt-Swap Facility



Source: TBI

As a feature of the wider Debt-Swap Facility, "Moving Up the Ladder" allows African leaders to follow a reputation-enhancing pathway out of distress, grounded in reforms rather than reliance.

01

The Challenge: Huge Investment Needs, High Debt Costs and Lower Development Aid

African leaders are caught between a rock and a hard place. They want to deliver change for their citizens by investing in economic growth, job creation, security and measures to deal with cost-of-living pressures and external shocks. However, they are severely constrained by the high cost of debt-financing in their countries compared to high-income countries due to a "negative risk-perception cycle", in which high borrowing costs stifle economic investment, weak economies struggle to meet debt obligations and risk perceptions deepen further. This cycle undermines public investment and private-sector lending, creating a drag on economic growth.

- In 2023, African governments spent 18 per cent of revenues on interest payments, compared to just 3 per cent in the EU and 5 per cent in G7 economies. Some African countries spend up to $1 of every $4 collected as tax on paying interest.
- High domestic interest rates further constrain private investment, business development, job creation and economic diversification.
- The cost of debt is exacerbated by declining development assistance, pushing African countries to rely more heavily on their own revenues and market-based financing.

Many African leaders try to take full control and responsibility for financing development. They wish to follow a reputation-enhancing pathway out of distress, grounded in reforms rather than reliance. This is not a regional call for a one-off debt relief or grants to provide short-term fiscal space. African leaders wish to tackle the persistently high-risk premiums caused by weak confidence in the governance of public finances – but it is difficult to do so when the credit-rating agencies and wider financial system impair them with punishing interest rates, regardless of the quality of their investments. Africa must be enabled to invest in its future.

02

The New Debt Deal Proposal: A Debt-Swap Facility Linked to Performance

To drive the New Debt Deal, we propose the creation of a $100-billion Debt-Swap Facility. One feature of the facility is a new debt-swap instrument, monikered "Moving Up the Ladder". This instrument integrates debt swaps driven by reforms to public financial management.

It reduces interest in two ways:

- Through debt swaps – replacing existing high-interest debt (external or domestic) with lower-cost concessional debt.
- By improving indicators of public financial management, potentially positively impacting credit ratings and risk perceptions.

This approach provides countries with greater access to lower-interest debt by reforming budget systems, improving expenditure-control and strengthening financial oversight. In doing so, it aims to reduce borrowing costs across the board – public and private, domestic and international.

How the Instrument Would Work

OBJECTIVE

To reduce borrowing costs in Africa by linking access to concessional financing with improvements in public financial management – creating a self-reinforcing cycle of better governance, stronger creditworthiness and lower risk premiums.

KEY FEATURES

- **Creation of a new cost-efficient $100 billion Debt-Swap Facility.** The facility could be administered by any number of international agencies, including the African Development Bank (AfDB) or the World Bank Group (WBG) and its newly established, fully integrated “one-stop shop” guarantee programme. Contributing countries would provide a financial commitment to back the Debt-Swap Facility with debt guarantees, which international institutions such as the WBG or AfDB would use to obtain loans and deploy the funds in a risk-managed portfolio of debt deals.

By using guarantees, donor countries would not be required to simply transfer billions to the administrator. The funds would only be called upon should a signed guarantee be called or triggered, for example in the case that a failure occurs and an underwritten financial claim is made. The fiscal impact on donor countries will be limited to the probability of default and if the portfolio risk is managed properly, the probability of a call will be low, making the ultimate fiscal cost to donor countries equally low. The immediate impact of a guarantee on the fiscal deficit and debt of donor countries will be null, depending on the accounting system and probability of default.

- **For developing countries, access to a new pool of low-interest financing that is systematic, sustainable and performance-driven**. Across Africa, nations are already investing in improving their public financial management, using modern financial-management systems to track transactions and manage spending and revenue. The International Monetary Fund and World Bank already periodically assess the reliability, transparency and effectiveness of every country in the world’s public financial management, and grant each country a Public Expenditure and Financial Accountability (PEFA) score. The “Moving Up the Ladder” instrument is designed so that, as developing countries improve their PEFA scores – including by increasing reliability in expenditure management and forecasts, and making improvements to their tax systems and revenue generation – they will be granted access to up to (on average) a total of $2 billion per country in new tranches of lower-cost financing.

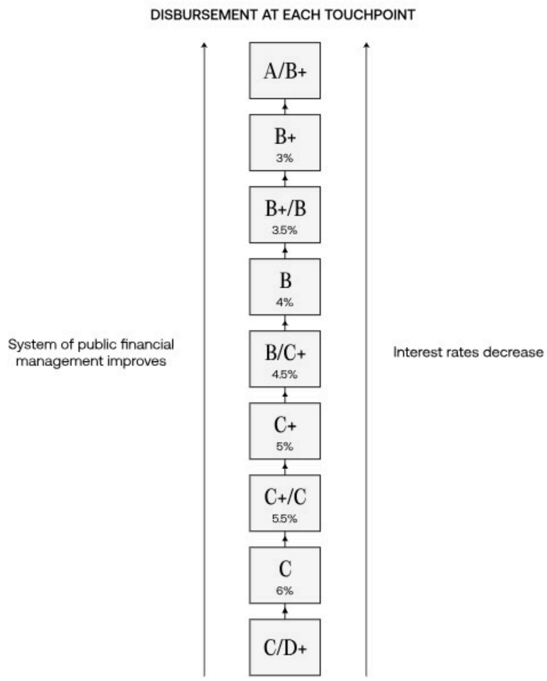
MECHANISM IN PRACTICE

Use of the “Moving Up the Ladder” instrument in practice is visualised in Figure 3. As a developing country improves its public financial management, with that improvement reflected in its PEFA score moving from, for instance, C/D+ incrementally upwards to A/B+, that country would access incremental amounts of low-cost debt, and at declining interest rates. For example:

- A country improves its public-financial-management score by 10 per cent and moves from C+/C to C+. The country receives access to a $250 million line of credit with 4.5 per cent interest costs, which can be used to swap out higher-interest debt.
- Another 10 per cent improvement qualifies the country for another $250 million at 4.0 per cent.
- Over time, this structure could refinance on average $2 billion in debt per country at rates significantly below market levels.

FIGURE 3

Moving up the ladder improves public financial management and provides cheaper funding



Note: Each box represents a new tranche at a lower interest rate

Source: TBI

The use of PEFA scores is important as this:

- Provides a rigorous, transparent framework with 31 indicators across seven pillars (for example, budget reliability, expenditure control and audit).
- PEFA indicators measure public-financial-management activities within each country's control – budget forecasts, reliability, control and audits – excluding indicators that countries cannot control, such as global commodity prices.

- Scores are derived from documented methodologies and public reporting.
- Most countries have a PEFA assessment, so a base line is available.
- Additional indicators for improving debt management, such as a debt-repayment account, could also be included.
- Importantly, PEFA scores correlate, albeit modestly, with credit ratings – higher PEFA scores can be an indicator of improved credit ratings and hopefully can disrupt the negative risk-perception cycle.

To address the infrequency of PEFA assessments (which currently take place every five to six years), the proposal includes interim verification steps based on selected indicators, similar to the performance-based disbursement models used in global development finance. It is advisable to also verify the use in practice of PEFA-score improvements to avoid improvements in public financial management existing on paper only.

POTENTIAL IMPACT

If implemented at full scale, the "Moving Up the Ladder" instrument could refinance $100 billion in debt and generate substantial fiscal savings for developing countries. The instrument is:

- **Transparent and systematic.** Developing countries would have access to a new tool to lower their debilitating interest payments and allow them to better invest in economic growth. The transparency and predictability associated with the availability of the instrument incentivises countries to improve the quality of their public financial management without expensive negotiations and bespoke deals with donors and agencies.
- **Sustainable and agnostic.** The improvement in the quality of public financial management will continue to pay dividends for countries into the future, supported by an improvement in financial health and a lower cost of capital for the government and private sector alike in the long term. Crucially, the instrument does not force countries into specific spending: it is agnostic about the use of the fiscal savings, with the instrument tied only to improvements in public financial management.

- **Capable of creating real fiscal space for developing countries.** The instrument will lower interest costs for developing countries, creating tens of millions of dollars annually in fiscal budget space – funds that can be used to build infrastructure and investment in education, health care and economic development, or to support the sustainability of government finances. In a world where development aid is falling, this fiscal space is invaluable.
- **Cost-efficient.** For donor countries, the Debt-Swap Facility utilises the multiplicative benefits of financial instruments. By managing such debt on a portfolio basis, and requiring only guarantees, donor countries can support real interest-cost relief to developing countries with minimal risk and cost.

Many African countries have very diverse debt portfolios, with some debts that do not have to be paid back for a very long time: current governments may only pay interest, leaving future governments with large repayment liabilities (and potentially defaults). This could be prevented by "saving money" in a debt-repayment account for countries that wish to swap their debt. Other African countries have grants and very concessional debt, right up to the point that they are promoted to middle-income country status, when they then face much steeper costs of debt. The New Debt Deal for Africa could help them to transition into playing in the "Debt Premier League". The New Debt Deal should include technical support for better debt and arrears management as well as support to incorporate transparency in domestic debt for future swaps.

If translated to an average per country (assuming 50 countries benefit from the swap instrument):

- A debt swap resulting in a 3 per cent reduction in interest rates would save $60 million per country per year (steady state).
- Including domestic debt could increase savings to $100 million per country annually – a 5 percentage-point reduction in interest rates.
- Total annual savings could reach $3 to 5 billion across the African continent.

FIGURE 4

Substantial new fiscal room for manoeuvre will be generated

Current interest rate	Average swap interest rate	Average interest-rate benefit	Benefit per annum
Scenario at 11%	4%	7%	$140 million
Scenario at 10%	4%	6%	$120 million
Scenario at 9%	4%	5%	$100 million
Scenario at 8%	4%	4%	$80 million
Scenario at 7%	4%	3%	$60 million
Scenario at 6%	4%	2%	$40 million

Source: TBI

Beyond direct savings, the instrument is expected to:

- Improve credit ratings over time.
- Stimulate private investment by lowering economy-wide interest rates.
- Strengthen institutions and budget credibility.
- Reduce the transaction cost of individual swaps and avoid the use of benefits for sectors that are not the highest priority for African governments.

03

Country Examples: Côte d'Ivoire, Mozambique and Kenya

There is approximately $321 billion of African external debt owed to commercial and bilateral lenders (2023 data).[1,2] Each country borrows at a different rate depending on its circumstances. With a $100 billion swap facility, 31 per cent of each country's external debt could be refinanced at a lower rate.

Taking Côte d'Ivoire as an example, if the country were given the ability to refinance 31 per cent of its external debt from bilateral and private lenders to lower-interest debt with an average interest rate drop of 2.8 percentage points, it would be able to lower its annual interest payments by $190 million – funds that could be used to support other priorities.

With such a tool, Mozambique could refinance its $900 million Eurobond – currently set at a 9 per cent interest rate – which could allow the interest rate to be reduced to as low as 3 per cent, generating $54 million in benefits. Additionally, if part of its domestic debt could be swapped, the yearly benefit would increase to $90 million annually (6 per cent of $1.5 billion).

In Kenya, external debt data from the World Bank debt database show an international loan of $1.5 billion with interest payments amounting to 9.5 per cent. Refinancing the bank loan with a 3 per cent swap using the New Debt Deal instrument would save Kenya $97.5 million per annum. Swapping other external debt – up to 31 per cent of its portfolio – would create annual savings of $264 million.

In addition to these direct interest-rate benefits, future interest rates would also be lower, due to the improvements in fiscal governance and potentially sovereign-credit ratings. Also, the private sector would benefit from lower interest rates due to breaking the negative risk-perception cycle.

Conclusion and Call to Action

Moving Up the Ladder offers a bold, practical solution to Africa's debt crisis – targeting the systemic roots of high interest rates while strengthening public institutions. It empowers countries to reduce debt costs through reforms they control and delivers tangible fiscal benefits without significant donor costs.

Today, too many African nations are struggling to develop, hobbled by crippling interest rates. As high- and middle-income countries are speeding ahead with infrastructure development, broadband rollouts, energy-system transformations, digitalisation, data-centre creation and economic innovation, developing countries are being held back by interest rates that impact every part of their citizens' economic lives – from the cost of investing and growing a small business and purchasing new equipment to adopting new digital skills or buying a home.

We urge African leaders, international financial institutions and development partners to collaborate in designing and piloting this New Debt Deal architecture. TBI is committed to supporting governments through policy advice and reform implementation – ensuring that debt becomes a tool for development, not a barrier to it.

Endnotes

1 https://www.worldbank.org/en/programs/debt-statistics/ids

2 There is no comprehensive, reliable debt database comprising external and domestic debt; for external debt, there is the World Bank database, where a proxy for interest rates can be derived from interest payments and the outstanding debt. Therefore, the calculations in this paragraph should be seen as illustrations to provide a sense of the benefits per country.

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