



**STRATHMORE BUSINESS SCHOOL**  
**MASTER OF SCIENCE IN DEVELOPMENT FINANCE**  
**END OF SEMESTER EXAMINATION**  
**MDF 8301: AID AND SOVEREIGN DEBT MANAGEMENT**

**Date:** Friday, 28th July 2023

**Time:** 3 Hours

**Instructions**

1. This examination consists of **FIVE** questions.
2. Answer Question **ONE** and **ANY OTHER TWO** Questions

**Question 1 (50marks)**

- a. There has been a lot of discussion in the media about the ever-growing public debt in Kenya and the risks that the country faces due to the huge debt. The following events are a major concern:
  1. Rising global interest rates due to inflationary pressures worldwide.
  2. Rising interest rates in the domestic debt market.
  3. Depreciation of the Kenyan shilling against the USD and other major currencies.
  4. Low tax revenue mobilization, with taxation mainly of the formal economic sector. The sector was adversely affected by the effects of Covid-19 health crisis and has yet to recover fully.
  5. Constant deviation from the borrowing mix specified in the Medium-Term Debt Management Strategy [MTDS] as evidenced below:

Debt		YR2019/2020	YR2020/2021	YR2021/2022
External	MTDS	38	28	27
	Actual	28	19	15
	Deviation	10	9	12
Domestic	MTDS	62	72	73
	Actual	72	81	65
	Deviation	-10	-9	-12

**Required:**

- i. Discuss six types of risks that Kenya faces due to the structure of its public debt and the factors highlighted above **[12marks]**
- ii. Apart from the events discussed above, describe five other factors that have the potential to worsen the debt situation in Kenya **[10marks]**

- b. Borrowing by State Owned Enterprises (SOEs) has negatively impacted public debt management especially in the African continent. Mozambique defaulted on its public debt due to fraudulent borrowing by three SOEs in that country, SOEs have also adversely affected the public debt of South Africa and other African countries leading to a down grade of the loan rating by international rating agencies.

Discuss the mechanisms that the affected countries can adopt to ensure that public debt is not affected by debts incurred by SOEs **[10marks]**

- c. Resource Based Lending (RBL) has also had an adverse effect on public debt in the African continent.
- i. Why are RBL loans a threat to proper public debt management in Africa? **[10marks]**
  - ii. How can the affected governments strengthen public debt management to reduce the threats posed by RBL loans **[8marks]**

### **Question 2 (25marks)**

The COVID-19 crisis led to a dramatic increase in sovereign debt, with average total debt burdens among low- and middle-income countries increasing by roughly 9 percent of GDP during 2020, compared with an average of 1.9 percent of GDP per year over the previous decade.

- a. Highlight the impact of covid-19 on the sovereign debt in Africa **[10marks]**

The IMF has developed a debt sustainability framework for low- income countries, however research has shown that these frameworks are rigid and narrow and misrepresent the debt situation among the low -income countries many based on the African continent.

- b. Why is it difficult to define debt sustainability? **[5marks]**
- c. Discuss the weakness of the IMF DSA framework for low -income countries suggesting the improvements required **[10marks]**

### **Question 3 (25marks)**

- a. Differentiate between a sovereign default and a corporate bankruptcy **[5marks]**
- b. In the last ten years several African countries have defaulted on their sovereign debt obligations and some have blamed Credit Rating Agencies (CRAs) for down-grades during difficult economic times which worsened the debt situation by increasing the cost of debt

**Required:**

- i. Highlight the short comings of CRAs in rating debt instruments of African Countries. **[10marks]**
- ii. Discuss the solutions that African countries can adopt to deal with the shortcomings identified in (a) above **[10marks]**

**Question 4 (25marks)**

- a. Domestic restructuring has been used rarely in the African continent until the recent case of Ghana. What factors should a country like Kenya carefully consider before opting for a domestic debt restructuring? **[5marks]**
- b. Going forward what mechanisms can Ghana adopt to revive and grow the financial sector? **[6marks]**
- c. A lot of progress has been made by the IMF and other concerned parties in improving the restructuring mechanism of external debt however a few concerns still remain.
  - i. Highlight the major problems that are inherent in the sovereign external debt market **[5marks]**
  - ii. Discuss three approaches that can be used to address the problems identified. Comment on the strengths and weaknesses of each approach selected **[9marks]**

**Question 5 (25marks)**

- a. Highlight the importance of debt management for a country like Kenya **[5marks]**
- b. The legislature plays a critical role in Public Debt Management which includes the enactment of the legal framework, approval, and oversight. In Kenya, parliament provides the checks and balances on government borrowing.
  - i. Has the Kenyan parliament adequately performed its roles as stated above? **[10marks]**
  - ii. What can the government do to improve debt management? **[10marks]**