Sub-Saharan Africa (SSA) Eurobonds: H1'2019 Performance

A. Background

Africa's appetite for foreign-denominated debt has increased in recent times with the latest issues in 2019 being Ghana, Egypt, Benin and Kenya. The increased affinity for foreign currency-denominated debt continues to be attributed to:

i. Financing of maturing debt obligations,
ii. The need to finance heavy infrastructure projects,
iii. Reduced financial aid to African countries by Western donor nations, and
iv. Covering for budget deficits.

Collectively, H1'2019 saw the African continent as a whole raise USD 12.4 bn through the various Eurobond issues as highlighted below.

Africa H1'2019 Eurobond Issues						
	Amount Issued (USD millions)	coupon	Issue date	Maturity Date	Tenor (Years)	Subscription
Kenya	900	7.0%	22/05/2019	22/05/2027	7.0	4.5X
	1,200	8.0%	23/05/2019	23/05/2032	12.0	
Benin	567	5.75%	26/03/2019	26/03/2026	6.0	2.3X
Ghana	1,250.0	8.13%	26/03/2019	26/03/2032	12.0	7.0X
	750.0	7.88%	26/03/2019	26/03/2027	7.0	
	1,000.0	8.95%	26/03/2019	26/03/2051	31.0	
Egypt	1,500.0	8.70%	26/02/2019	01/03/2049	30.0	5X
	1,750.0	7.60%	26/02/2019	01/03/2029	10.0	
	750.0	6.20%	26/02/2019	01/03/2024	5.0	
	1,020.7	4.75%	11/04/2019	11/04/2025	6.0	4X
	1,701.1	6.38%	11/04/2019	11/04/2031	12.0	
Total	**12,388.8**					

The new instruments attracted a lot of interest as evidenced by the oversubscription in all the issues, with the Ghana issue recording the highest oversubscription of over 7.0x, underlining the sustained investor confidence in the African debt market. This may partly arise because, by comparison, African sovereign debt offers the highest yields to investors globally. Data from Bloomberg indicates that Africa offers an average dollar-bond yield of 6.0%, higher than the Emerging Market average of 5.5%, as well as the North American average of 4.5%; and the Asia Pacific average of 4.0%. This note analyses SSA's Eurobond performance in H1'2019 with the aim of painting a picture of the investor confidence and risk tolerance.

B. Eurobond Performance in Sub Saharan Africa

Analysis of the H1'2019 Issues

There were three new Eurobond issues in Sub Saharan Africa (excluding Egypt) in H1'2019, with the issuers being Kenya, Benin and Ghana who collectively raised a total of USD 5.7bn. Below is an analysis of the various issues:

i. Kenya:

Below is a table with the summary of the Kenya Eurobond issue:

Kenya 2019 Issue				
Amount Issued (USD millions)	coupon	Issue date	Tenor (Years)	Subscription
900	7.0%	22/05/2019	7.0	4.5X
1,200	8.0%	23/05/2019	12.0	
2,100				

In H1'2019, Kenya issued its 3rd Eurobond, raising USD 2.1 bn (Kshs 210.0 bn) through a dual-tranche Eurobond of 7-year and 12-year tenors, value dated 15th May 2019 and maturities in 2027 and 2032, respectively. The issue was 4.5x oversubscribed attracting orders worth USD 9.5 bn. The Eurobond was priced at 7.0% for the 7-year tenor and 8.0% for the 12-year tenor with the proceeds expected to go towards:

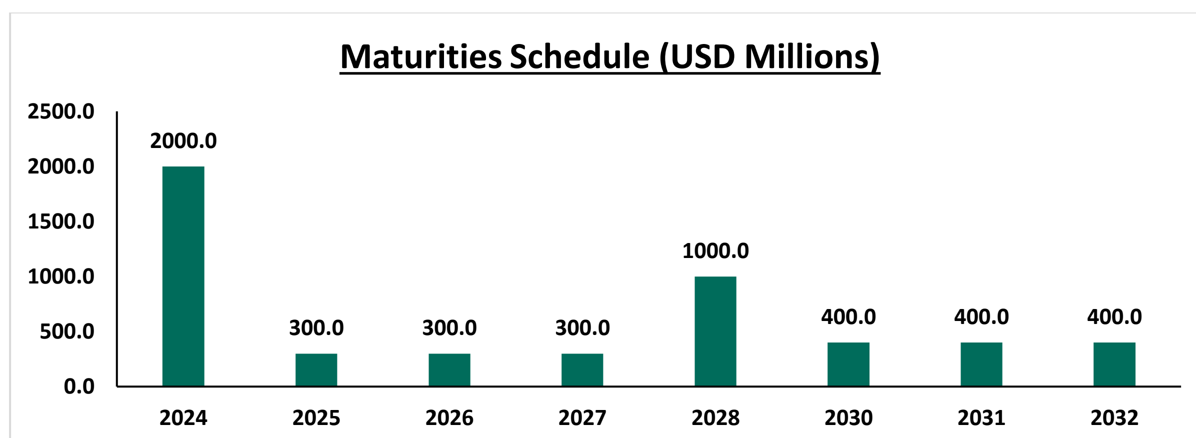
i. Refinancing the obligations outstanding from the USD 750.0 mn Eurobond issued in 2014, which matured on 24th June, 2019, and,

ii. Financing development infrastructure projects as well as the general budgetary expenditure.

The performance of the issue was commendable considering the market conditions at the time, with the International Monetary Fund (IMF) having withdrawn their stand-by credit facility in 2018, coupled with the downgrading of Kenya's growth prospects by both the IMF and the World Bank. Key to note is that, unlike the previous issues, with expected bullet payments on the maturity date, both the 7-year and the 12-year tenors are sinkable which means that the repayment of the principal will be amortized equally, at USD 300 mn and USD 400 mn, respectively, per year in the last three years to maturity, as opposed to a full repayment of the principal at maturity. This will avoid a spike in repayments in one particular year. Concerns however remain on the use of the proceeds. For a country to be able to refinance its debt obligations, funds ought to be directed to projects whose economic rate of return is higher than the cost of debt. The debt is however expected to repay maturing obligations as well as fund infrastructure projects whose economic rate of return continue to be in contention. The maturity profile of the debt also raises concerns as its relatively short, which raises maturity concentration risk as the country will be in a continuous state of maturing obligations between 2024 and 2028 since:

i. The 10-year Eurobond issued in 2014 will be maturing in 2024,
ii. There will be the yearly repayments of USD 300.0 mn for the 7-year Eurobond issued in 2019 will be maturing in May 2027, whose repayments, are set to start in 2025, and,
iii. The 10-year Eurobond issued in 2018 will be maturing in 2028.

Below is a chart showing the maturities schedule:



ii. Benin

Below is a table with a summary of the Benin Eurobond issue:

Benin 2019 Issue				
Amount Issued (EUR)	coupon	Issue date	Tenor (years)	Subscription
500	5.75%	26/03/2019	6.0	2.3X

Benin raised Eur 500.0 mn (USD 567.0 mn) in its debut Eurobond sale on 26th March 2019, the same day that Ghana had touted their USD 3.0 bn Eurobond. Benin's amortizing Eurobond, with a final maturity in 2026 and average life of six years was priced at 5.8%, lower than the initial estimates of around 6.4%. The repayment profile of the issue will be amortised over three years (2024, 2025, 2026), in a bid to limit refinancing risk in line with the Government's prudent public debt management policy. The issue was over-subscribed, with the transaction's order book surpassing the Eur 1.0 bn mark in less than two hours, reaching a peak of Eur 1.3 bn during the day. The proceeds from the issue are expected to be channelled towards supporting the approximately Eur 14.0 bn, 2016-2021 Government Action Programme (GAP), financing priority projects in infrastructure, electricity and the digital economy. The issue was commendable as it achieved its set objectives which included:

(i) Diversifying the government's sources of debt as the country was accustomed to borrowing from domestic bonds from the regional financing market and from multilateral development banks, and
(ii) Extending their debt maturity profile to closely match its domestic spending ambitions with the key focus being on the 2016-2021 Government Action Programme (GAP).

iii. Ghana

Below is a table with a summary of the Ghana Eurobond issue:

Ghana 2019 Issue				
Amount Issued (USD millions)	coupon	Issue date	Tenor(Years)	Subscription
1,250.0	8.13%	26/03/2019	12.0	7.0X
750.0	7.88%	26/03/2019	7.0	
1,000.0	8.95%	26/03/2019	31.0	
3,000				

Ghana successfully managed to raise USD 3.0 bn during H1'2019 with the issue date set at 26th March 2019. The issue was 3 tranches of 7-years, 12-years and 31-years tenors. The bonds were priced at 7.9% for the 7-year tenor, 8.1% for the 12-year bond and 8.95% for the 31-year tenor. The issue was 7x oversubscribed attracting orders worth USD 21.0 bn, the largest ever in Africa Year to date a clear indication of the increased investor appetite for Africa's sovereign bonds. About USD 2.0 bn of the proceeds are expected to fund the country's 2019 budget while the remaining USD 1.0 bn is to be used to refinance the Eurobonds maturing in 2023, 2026 and 2030.

C. Analysis of Existing Issues

This section analyses the H1'2019 performance of some of the Eurobonds issued in Sub Saharan Africa before 2019.

Country	Issue Tenor (yrs)	Issue Date	Coupon	Yield as at the beginning of 2019	Yield as at the end of H1'2019	Current Yield	H1'2019 change (% Points)	YTD change (% Points)
Ghana	**31**	16/05/2018	8.6%	10.0%	8.6%	8.3%	(1.4%)	(1.7%)
Senegal	**30**	13/03/2018	6.8%	8.3%	7.3%	7.0%	(1.0%)	(1.4%)
Nigeria	**30**	28/11/2017	7.6%	9.2%	7.7%	7.4%	(1.5%)	(1.8%)
Kenya	**30**	28/02/2018	8.3%	9.8%	7.9%	7.7%	(1.9%)	(2.1%)
Zambia	**12**	30/07/2015	9.0%	14.7%	17.4%	14.7%	2.7%	(0.0%)
Nigeria	**12**	23/02/2018	7.1%	8.8%	7.1%	6.6%	(1.7%)	(2.2%)
Senegal	**10**	30/07/2014	6.3%	6.9%	4.7%	4.2%	(2.1%)	(2.6%)
Kenya	**10**	24/06/2014	6.9%	8.3%	5.5%	5.0%	(2.9%)	(3.4%)
Zambia	**10**	14/04/2014	8.5%	13.3%	19.4%	16.0%	6.0%	2.7%
Senegal	**10**	13/05/2011	8.8%	6.0%	3.7%	3.5%	(2.3%)	(2.5%)
Zambia	**10**	20/09/2012	5.4%	15.7%	20.7%	16.8%	5.0%	1.1%
Kenya	**10**	28/02/2018	7.3%	9.0%	6.8%	6.4%	(2.2%)	(2.6%)

Ghana	**10**	08/07/2013	7.9%	8.4%	5.7%	5.3%	(2.8%)	(3.2%)

From the table above,

a) Zambia was the only country that recorded a rise in Eurobond yields, with the 10-year instruments for both the 2012 and 2014 issues increasing by 5.0% points and 6.0% points, while the yield on the 12-year bond issued in 2015 increased by 2.7% points. Zambian Eurobonds were the worst performing in Sub Saharan Africa with the 10-year Eurobond issued in 2012 recording a high of 22.0%, 20.0% points more than U.S. Treasuries of an equivalent maturity, with similar dollar spreads and yields only being recorded in nations already in default globally, such as Venezuela. The performance has mainly been due to concerns of a widening fiscal deficit and deteriorating credit worthiness on the back of high debt levels. Zambia's increasing debt levels, coupled with the 8.1% depreciation of the Kwacha Year to date, present the risk of rising debt-service costs for the economy , given the significant proportion of debt denominated in foreign currency (at about 60% of the total), hence necessitating demands for higher premium on sovereign debt issued by the country. During the same period of review, Credit rating agency Moody's downgraded Zambia's credit rating long-term issuer ratings to Caa2 from Caa1 and changed the outlook to negative from stable. This was in addition to the three downgrades by the same agency in 2018. The downgrade is a reflection of increased liquidity and external pressures, which has elevated the risk of default over the near-term due to the impairment of the government's ability to service its debt over the medium term. The country's external position is currently vulnerable to external shocks due to narrow foreign exchange reserve buffers which stood at around USD 1.1 bn equivalent to 1.3 months of import cover, below the three-month of imports threshold commonly considered a minimum level of reserve adequacy as at the time of the rating in April. The declining reserves have been attributed to the significantly high external government debt service coupled with a high current account deficit.
b) Eurobond yields in other Sub-Saharan countries significantly declined during H1'2019. The trend has been replicated in other frontier markets, attributable to increased investor demand of the debt instruments due to the attractive returns compared to the low interest rates in the US and other advanced economies.

D. Summary

From the analysis, it is evident that Eurobond yields in Sub Saharan Africa declined in H1'2019, partly due to increased demand for emerging market fixed-income securities in the wake of the pause by the US Fed on its three-year cycle of tightening its monetary policy, which had made returns from fixed income securities more attractive. Specifically, African Eurobonds have posted impressive returns this year, generally out-performing the other emerging markets. Notably, African debt has been on the rise mainly due to a slowdown in commodity prices which has affected revenue generation as most African countries are commodity driven. To plug in the budget deficit most countries have been forced to dip in the international fixed income market to raise funds to fund their budget deficits as well as refinance existing debt obligations. The deficit has also been widened by expensive infrastructure investment promises made by the elected governments. The low interest rates in the US and other advanced economies has resulted in investors being attracted to frontier markets thus facilitating the capital raising by African countries as evidenced by the high subscription rates in most of the debt issuances. Going forward, we expect the yields to remain stable with a bias to further declines driven owing to expectations of loosening of monetary policy in advanced economies including the U.S and Eurozone as the Federal Reserve and European Central Bank take a dovish stance. This coupled with the easing of the China-U.S trade tensions which had increased investor risk perceptions due to expectations of a global slowdown is expected to stabilise yields going forward.