Sub-Saharan Africa (SSA) Eurobonds: H1’2020 Performance

A. Background

Africa’s appetite for foreign-denominated debt has increased in recent times with the latest issues in H1’2020 being Gabon and Ghana. 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 deficit

This note analyses SSA’s Eurobond performance in H1’2020 with the aim of painting a picture of the investor sentiments risk tolerance, and an outlook on yield performance for the year 2020. The analysis will be broken down as follows:

I. Background of Eurobonds in Sub Saharan Africa in H1’2020,
II. Eurobond Performance in Sub-Saharan Africa,
III. Outlook on SSA Eurobonds.

Section I. Background of Eurobonds Issued in Sub Saharan Africa

I. Analysis of New H1’2020 Issues:

Collectively, H1’2020 saw the Sub-Saharan Region raise USD 4.0 bn through Eurobond issues. The new instruments attracted a lot of interest as evidenced by the oversubscription in all the issues, with the Ghana issues recording the highest oversubscription of over 4.7x. This underlines the demand by premium investors to hold riskier assets, partly because, by comparison, African sovereign debt offers the highest yields to investors globally. According to Bloomberg, African bonds recorded total returns of 26.8% as at June 2020, higher than the 22.4% returns recorded by S&P 500 during the same period. African Eurobond issuers possess different risk characteristics depending on the issuer and the tenor of the bonds. Such risks include political, economic and therefore credit risks. Key to note is that there was no Eurobond issue by Sub-Saharan countries in Q2’2020, all the issues highlighted below occurred in Q1’2020. The unfavorable global financial markets caused by the Coronavirus saw an increase in the yield curve as investors attached a higher risk premium in the region with investors demanding for compensation from the extra risk emanating from the virus. In the recently published Sub-Saharan Regional Economic Outlook by IMF saw the regions GDP growth lowered to a contraction of 3.2% from the earlier projection of 1.6% recorded in April 2020. This was mainly attributable to the uncertainty around the tenor of the pandemic and its implications around the various SSA economies given the acceleration of the virus despite the measures taken by most governments to contain its spread. Countries like Nigeria, which had plans of issuing a new Eurobond worth USD 3.3 bn for budgetary purposes and to refinance loans have had to postpone their issue due to the high yields in the market which would increase borrowing costs especially given that the country is highly reliant on oil exports whose prices have been subdued. Additionally, Nigeria recorded high debt service to revenues ratio of 99.0% in Q1’2020. With the depressed government revenues, Nigeria will rely heavily on external debt to fund its operations. The table below summarizes the Eurobonds issued in H1’2020:

Sub-Saharan Africa (SSA) Eurobonds Issued in H1’ 2020									
Country	Amount Issued USD millions	Issue Tenor (Years)	Issue date	Maturity Date	Coupon	Yield at Issue Date	Subscription Rate	Yield as at 30th June 2020 (%Points)	Issue date to 30th June Yield Change(% points)
Gabon	1,000	11	6/2/2020	6/2/2031	6.6%	6.4%	3.5x	8.3%	1.9%

Ghana	1,250	7	11/2/2020	11/2/2027	6.4%	6.3%	4.7x	7.9%	1.6%
	1,000	15	11/2/2020	11/2/2035	7.9%	7.9%		9.1%	1.2%
	750	41	11/3/2020	11/2/2061	8.8%	8.7%		9.7%	0.9%
Total	**4,000**								

Below are the key take outs form the issues:

i. Gabon

Gabon issued Africa's maiden Eurobond in 2020, a USD 1.0 bn, 11-year instrument, with a 6.6% coupon rate. The issue received bids worth USD 3.5 bn translating to a 3.5x subscription rate. The bond was earmarked for financing the country's efforts in diversifying its exports by venturing into logging and agriculture to reduce the country's over dependence on the world demand for Manganese and Oil, and hence reduce exposure to the impact of fluctuating crude oil prices. The Oil sector has accounted for 80.0% of its exports, 60.0% of its fiscal revenue and 45.0% of its GDP over the past 5 years, however Gabon has been facing a decline in its oil reserves in addition to the recent price wars that have caused oil prices to plummet. Gabon, which had a 56.4% debt to GDP ratio in 2019, was as of 3rd April 2020 downgraded by Fitch Ratings to CCC from B, in its Long-Term Foreign-Currency Issuer Default Rating (IDR). This was to reflect the fact that risks to the sovereign debt repayment capacity have risen significantly due to liquidity pressures from the fall in oil prices. According to Reuters Gabon has an additional USD 35.0 mn in external debt that is expected to mature this year, USD 736.0 mn in 2024 and USD 700 mn in 2025.

ii. Ghana

Ghana issued Sub Saharan Africa's longest-ever selling amortized Eurobond, a USD 750 mn tranche that with an average effective tenor of 40 years, offering an 8.9% coupon. Additionally, the country also issued a 14-year and 6-year Eurobond with 7.9% and 6.4% coupons respectively, raising USD 1,000.0 and USD 1,250 for the 14-year and 6-year Eurobonds, respectively. The entire issue raised USD 3.0 bn, with bids received totaling to USD 14.0 bn translating to a 4.7x oversubscription. The Eurobonds are to be used to restructure the country's obligations to independent power producers since the country was in talks to re-negotiate the supply deals from the current take-or-pay agreement that means that the government is billed even for unused electricity, to retire more expensive debt and hence reduce the interest costs, as well as to fund infrastructure projects. Ghana had a 60.0% debt to GDP ratio in 2019 with Moody's changing its outlook from positive to negative while affirming the B3 rating balances, in April 2020, reflecting the rising risk emanating from the coronavirus pandemic to the country's debt service capabilities. The country is more vulnerable to global shocks particularly due to its overreliance on external debt.

II. Analysis of Existing Issues

Yields on select African Eurobonds as indicated in the table below, increased in H1'2020 after a decline in 2019. This was attributable to the COVID-19 health crisis, with investors attaching a higher risk premium on the affected regions due to the anticipation of slower economic growth.

Yield Changes in Select SSA Eurobonds Issued Before H1'2020							
Country	**Issue Tenor (yrs)**	**Issue Date**	**Maturity Date**	**Coupon**	**Yield as at Year Open 2020**	**Yield as at 30th June 2020**	**H1'2020 change (%Points)**
Senegal	30	13/3/2018	13/3/2048	4.8%	6.7%	7.0%	**0.3%**
Kenya	30	28/2/2018	28/2/2048	8.3%	7.7%	8.4%	**0.8%**

Nigeria	30	28/11/2017	28/11/2047	7.6%	7.8%	8.7%	**0.8%**
Ghana	31	16/5/2018	16/6/2049	8.6%	8.7%	9.6%	**0.9%**
Ghana	31	26/03/2019	26/03/2051	9.0%	8.7%	9.8%	**1.1%**
Ghana	10	8/7/2013	8/7/2023	7.9%	5.0%	6.2%	**1.2%**
Senegal	10	30/7/2014	30/7/2024	6.3%	3.7%	5.0%	**1.2%**
Kenya	12	23/05/2019	23/05/2032	8.0%	6.9%	8.2%	**1.3%**
Nigeria	12	23/2/2018	23/2/2030	7.1%	6.8%	8.2%	**1.4%**
Kenya	10	28/2/2018	28/2/2028	7.3%	5.9%	7.5%	**1.6%**
Kenya	10	24/6/2014	24/6/2024	6.9%	4.8%	6.5%	**1.6%**
Kenya	8	22/5/2019	22/5/2027	7.0%	5.6%	7.3%	**1.7%**
Senegal	10	13/5/2011	13/5/2021	8.8%	2.5%	5.0%	**2.5%**
Benin	6	26/03/2019	26/03/2026	5.8%	4.8%	7.7%	**2.8%**
Ghana	6	15/9/2016	15/9/2022	9.3%	3.8%	9.1%	**5.3%**
Zambia	12	30/7/2015	30/7/2027	9.0%	17.0%	24.5%	**7.4%**
Zambia	10	14/4/2014	14/4/2024	8.5%	19.6%	30.0%	**10.4%**
Zambia	10	20/9/2012	20/9/2022	5.4%	21.5%	38.7%	**17.2%**

From the table above,

a) Yields on all Sub-Saharan Eurobonds rose in H1'2019 attributable to the ongoing Coronavirus pandemic and the uncertainties involving the impact that it will have on the economy, with investors attaching a higher risk premium on developing countries, and,

b) Zambia recorded the highest increases in Eurobond yields, with the 10-year instruments for both the 2012 and 2014 issues increasing by 17.2% and 10.4% points respectively, while the yield on the 12-year bond issued in 2015 increased by 7.4% points. This makes Zambian Eurobonds the worst performing in Sub Saharan Africa, due to concerns of a widening fiscal deficit and deteriorating credit worthiness on the back of high debt levels. Zambia's increasing debt levels estimated at 74.4% of GDP ratio, coupled with the 28.6% depreciation of the Kwacha YTD presents the risk of rising debt-service costs for the economy, hence necessitating demands for higher premium on sovereign debt issued by the country.

The increasing yields have further been affected by appreciation of most of the local currencies of the respective nations. Below is a summary of the performance of the different resident currencies for H1'2020:

Select Sub Saharan Africa Currency Performance vs USD					
Currency	**Jun-19**	**Dec-19**	**Jun-20**	**Last 12 Months change (%)**	**YTD change (%)**
Malawian Kwacha	762.1	729.1	728.4	**4.4%**	**0.1%**
Tanzanian Shilling	2295.0	2293.0	2313.0	**(0.8%)**	**(0.9%)**
Ghanaian Cedi	5.4	5.7	5.7	**(6.5%)**	**(1.2%)**
Ugandan Shilling	3690.0	3660.0	3719.1	**(0.8%)**	**(1.6%)**
Kenyan Shilling	102.3	101.3	106.5	**(4.1%)**	**(5.1%)**

Mauritius Rupee	35.5	36.2	40.0	**(12.7%)**	**(10.5%)**
Botswana Pula	10.7	10.5	11.9	**(11.0%)**	**(13.0%)**
Nigerian Naira	305.9	306.0	360.0	**(17.7%)**	**(17.6%)**
South African Rand	14.1	14.0	17.3	**(23.1%)**	**(23.7%)**
Zambian Kwacha	12.8	14.1	18.1	**(40.8%)**	**(28.6%)**

All select currencies depreciated against the US Dollar except for the Malawian Kwacha, which remained relatively stable against the dollar attributable to the high forex reserves, which continue to provide a buffer to the Kwacha against exchange shocks. The depreciation recorded by the currencies is partly attributable to the ongoing COVID-19 pandemic, which has seen a fast-falling demand for export commodities given the lockdown measures put in place. The depreciation of local currencies has the effect of making dollar denominated debt more expensive, hence increasing the danger of rising debt-service costs and ultimately triggering the default risks. For instance, credit rating agencies such as Moody's have flagged Zambia's default risks that emanates from the countries constrained external liquidity that is likely to increase their defaulting risks as well as exchange rate depreciation that is likely to push the country's debt burden to above 110.0% of GDP in 2020.

Section III: Outlook on SSA Eurobonds

From the analysis, it is evident that Eurobond yields in Sub Saharan Africa rose in H1'2020, attributable to the COVID-19 health crisis, with investors attaching a higher risk premium on the affected regions due to the anticipation of slower economic growth. 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 Eurobond window for Sub-Saharan Africa is effectively closed for now given the strong drop in commodity prices that has led to the region underperforming emerging market peers, and also because investors have a current preference for safe havens. There are a few points to note:

a) **Public debt**- The COVID-19 pandemic is likely to increase the vulnerability of debt distress in the region. High risk of debt distress being a baseline scenario that indicates a protracted breach of debt or debt service thresholds, but the country has not yet defaulted, countries in this category include The Republic of Congo and Zambia to mention a few. The spread of Coronavirus coupled with the plummeting commodity prices since January 2020 with the prices of Crude oil, Platinum and Copper of declining by 50.0%, 25.0% and 20.0%, respectively. The declines seen in the commodity prices is likely to increase the number of countries in debt distress with many governments now facing the decision on whether to satisfy creditors or spend money on hospitals and on bailing out the economy, a situation that may lead to debt defaults. Most governments in the region are expecting to record decreased revenue due to the slowdown in economic activities in the region necessitating the need to borrow further in order to plug in fiscal deficits,

b) **Debt Sustainability**: According to the World Bank, SSA's debt to GDP ratio has been gradually increasing since 2012 to 59.0% in 2019 from 37.0% recorded in 2019. Most African countries have resulted to expensive sources of financing as evidenced by the increased uptake of sovereign bonds as opposed to concessional loans, attributable to liquidity problems stemming from the global financial crisis and European debt crisis. Debt sustainability in the region continues to be a major concern in the region given the high debt burden as well as the change in the composition of the regions public debt profile to sovereign bonds. Countries with a higher debt service and risker debt profiles are expected to face debt sustainability issues. According to the world bank, a third of the African countries are at risk of debt distress mainly due to the ongoing COVID-19 pandemic, and,

c) **Subdued Economic Growth**- Sub-Saharan Africa is set for its first recession in 25 years, with the World Bank projecting economic activity in the region to contract by 2.8% with growth expected to rebound back to 3.1% by 2021 assuming the effects of the pandemic begin fading off in the second half of 2020. The World Bank expects the region to be heavily affected given the region's weak healthcare systems. Measures to curb the spread of the virus such as social distancing and self-isolation are difficult to be implemented in the region given that a majority of individuals work in the informal sector and depend fully on their daily income for survival. Most Sub Saharan economies do not have much wriggle in deploying fiscal policy to cushion economies, fiscal positions are likely to deteriorate even further.