<u>Sub-Saharan Africa (SSA) Eurobonds: Q1’2021 Performance</u>

A. Background

According to the International Monetary Fund’s (IMF) Regional Economic Outlook Update April 2021, the Sub-Saharan region economy is projected to have contracted at a rate of (1.9%) in 2020, but is expected to rebound in 2021 by registering a 3.4% growth, which is 2.6% points below the global projected growth of 6.0%. IMF anticipates the region to continue feeling the effects of the recent second wave of the pandemic, which seems to be stronger than the first one. The IMF further expects regional recovery to tag along pandemic-related risks such as; access to extrenal financing by governemnts and other persistant factors like political instability and domestic security. However, the effectiveness of vaccine distribution and inculation will boost the regional near term growth prospects.

Africa’s appetite for foreign-denominated debt has increased in recent times with the latest issues in Q1’2021 being Benin and Ivory Coast. Optimism about global recovery has come on the back of continued economic fiscal stimulus support by governments in developed economies coupled with the increased global rollout of COVID-19 vaccines that has driven yields further downwards in developed markets. Hence prompting investors to look for higher returns among the global’s lower-rated sovereigns. In order to finance their budget deficits and refinance existing debt, Countries such as Nigeria, Ghana and Kenya are expected to return to the market later in the year for further issuances. The increased affinity for foreign currency-denominated debt by African countries continues to be attributed to:

I. Financing of maturing debt obligations,
II. The need to finance heavy development infrastructure projects,
III. Reduced financial aid to African countries by Western donor nations,
IV. The need to bridge the widening fiscal budget deficits, and,
V. The need to revive the African economies that have been negatively impacted by COVID-19 pandemic.

This note analyses Sub-Saharan Africa‘s (SSA) Eurobond performance in Q1’2021 painting a picture of the investor sentiments, risk tolerance, and an outlook on yield performance. The analysis will be broken down as follows:

a. Background of Eurobonds in Sub Saharan Africa in Q1’2021,
b. Eurobond Performance in Sub-Saharan Africa, and,
c. Outlook on SSA Eurobonds.

Section I. Background of Eurobonds Issued in Sub Saharan Africa

Collectively, Q1’2021 saw two countries in the the Sub-Saharan Region raise USD 2.1 bn through Eurobond issues. The new instruments attracted a lot of interest as evidenced by the oversubscription in all the issues, with the Ivory Coast issues recording the highest oversubscription of over 3.4x. 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.

Some of the countries that issued papers in Q1’2021 include Benin which became the first African country to issue a Euro denominated Eurobond by issuing a dual-tranche paper in February 2021, raising an equivalent total of USD 1.2 bn. The issue had tenors of 11.0 years and 31.0 years, with coupon rates of 4.9% and 6.9%, respectively. The issue received bids worth USD 3.6 bn translating to a 3.0x subscription rate. The bond will enable the early repayment of 65.0% of the nominal amount of the country’s 2026 Eurobond and also assist in financing of the 2021 budget on flagship Government Action program Projects. Ivory coast also went in to the market by reopening a dual tranche Eurobond that raised USD 850.0 mn. The paper comprised of 11.0 and 27.0

-year instruments, with a 4.8% and 6.8% coupon rates, respectively. The issue received bids worth USD 2.9 bn translating to a 3.4x subscription rate. The bond was earmarked for financing the country's budget.

The table below summarizes the various Eurobond issued in Q1'2021:

Country	Amount Issued USD millions	Issue Tenor (yrs)	Issue Date	Maturity Date	Coupon	Yield at Issue Date	Subscription Rate	Yield as at 31st Mar 2021	Issue date to 31st Mar Yield Change(% points)
Benin	849.0	11	1/19/2021	1/19/2032	4.9%	5.2%	3.0x	5.5%	0.4%
Benin	364.0	31	1/19/2021	1/19/2052	6.9%	7.0%		6.9%	(0.1%)
Ivory Coast	600.0	11	9/2/2021	9/2/2032	4.8%	4.3%	3.4x	4.5%	0.2%
Ivory Coast	250.0	27	9/2/2021	9/2/2048	6.8%	6.1%		7.2%	1.1%
Total	**2,063.0**						**3.2x**		
Q1'2020 Issues	**4,000.0**						**4.1x**		

Key take-outs:

i. The region's Q1'2021 issues raised USD 2.1 bn, compared to USD 4.0 bn raised over a similar period in 2020, a decline of 48.2%, due to the reluctance of regional governments to tap into the market in a period characterised by weak soverign ratings which may see investors demanding a premium and therefore making issuing more expensive for Sub-Saharan countries,
ii. The issues in Q1'2021 recorded an average oversubscription of 3.2x, lower than Q1'2020's issues oversubscription of 4.1x. 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,
iii. Since issuance at the beginning of the year, the yields on the Benin 31 – year Eurobond issue declined to 6.9% as at 31st March 2021, from the 7.0% recorded on 19th January, 2021. Of the four issues, the long term 27-year Ivory Coast issue recorded the highest increase of 1.1% points, indicating that investors are attaching a higher risk premium to Ivory Coast's economy due to political tensions following a heated election period in late 2020, and,
iv. The Ivory Coast's 11-year issue was priced at a historical record-low yield for regional issuers of 4.3% and still recorded the highest oversubscription rate of 3.4x in 2020. This is attributed to investors' hunt for high yields following massive monetary easing in developed markets, which unlocked liquidity in financial markets and consequently resulted in declining yields. The low supply of Sub-Saharan Eurobonds in the market also contributed to the oversubscription. The oversubscription of Ivory Coast's issue highlights the high appetite for Sub-Saharan Eurobonds in despite the country issuing another Eurobond in November 2020 which was also oversubscribed 5.0x raising USD 1.2 bn. The country is however supported by a low debt to GDP ratio, projected at 41.7% in 2020, which is 23.9% points lower than the region's projected ratio of 65.6%.

Section II: Analysis of Existing Issues

Yields on African Eurobonds recorded a mixed performance in Q1'2021, with most of them recording upward pressure. The increase in yields is an indication of wanning investor confidence as the region grappled with a second wave of COVID-19 infections during the quarter leading to investors attaching a higher risk premium on the region due to an anticipation of further adverse effects of the pandemic. Yields on Kenyan and Zambian Eurobonds declined in Q1'2021 by 0.4% and 0.9% points to 3.6% and 19.5%, from 3.9% and 20.4%, respectively, recorded in December 2020. Yields on the Zambia Eurobond remain relatively high, owing to the high risk attached to the country as it failed to honour its service obligations of a USD 42.5 mn Eurobond coupon in

November 2020 and is still struggling with high debt levels which are currently at 8.0% to GDP. On the other hand, yields on the Senegalese Eurobond increased by 1.2% points to 6.8% in Q1'2021, from 3.3% recorded in December 2020, attributable to the economic decline due to the COVID-19 pandemic with the tourism and transport sectors being some of the hardest hit sectors. The table below highlights the performance of select African Eurobonds in Q1'2021.

Yield Changes in Select SSA Eurobonds Issued Before Q1'2021							
Country	**Issue Tenor (yrs)**	**Issue Date**	**Maturity Date**	**Coupon**	**Yield as at Year Open**	**Yield as at March 2021**	**Q1'2021 change (%Points)**
Zambia	12	30/7/2015	30/7/2027	9.0%	12.2%	11.2%	**(1.0%)**
Kenya	12	23/05/2019	23/05/2032	8.0%	5.9%	7.1%	**1.3%**
Kenya	10	24/6/2014	24/6/2024	6.9%	3.9%	3.6%	**(0.4%)**
Nigeria	12	23/2/2018	23/2/2030	7.1%	6.0%	6.8%	**0.8%**
Senegal	10	13/5/2011	13/5/2021	8.8%	4.7%	8.5%	**3.8%**
Ghana	10	8/7/2013	8/7/2023	7.9%	4.1%	3.2%	**(0.9%)**
Kenya	8	22/5/2019	22/5/2027	7.0%	4.9%	5.6%	**0.7%**
Senegal	30	13/3/2018	13/3/2048	4.8%	6.0%	7.2%	**1.2%**
Kenya	10	28/2/2018	28/2/2028	7.3%	5.2%	6.3%	**1.1%**
Nigeria	30	28/11/2017	28/11/2047	7.6%	7.2%	7.9%	**0.7%**
Kenya	30	28/2/2018	28/2/2048	8.3%	7.0%	8.0%	**0.9%**
Benin	6	26/03/2019	26/03/2026	5.8%	4.3%	3.9%	**(0.5%)**
Senegal	10	30/7/2014	30/7/2024	6.3%	3.3%	3.8%	**0.6%**
Gabon	11	6/2/2020	6/2/2031	6.6%	6.2%	7.2%	**1.0%**
Ivory coast	12	30/11/2020	30/1/2032	4.9%	4.6%	5.2%	**0.6%**
Ghana	6	15/9/2016	15/9/2022	9.3%	3.3%	3.0%	**(0.3%)**
Ghana	31	16/5/2018	16/6/2049	8.6%	8.4%	9.4%	**0.9%**
Ghana	31	26/03/2019	26/03/2051	9.0%	8.6%	9.5%	**0.9%**
Ghana	7	11/2/2020	11/2/2027	6.4%	5.5%	7.2%	**1.8%**
Ghana	15	11/2/2020	11/2/2035	7.9%	7.6%	8.8%	**1.2%**
Ghana	41	11/2/2020	11/3/2061	8.8%	8.5%	9.5%	**1.0%**
Zambia	10	14/4/2014	14/4/2024	8.5%	19.6%	19.5%	**(0.1%)**
Zambia	10	20/9/2012	20/9/2022	5.4%	21.5%	44.3%	**22.7%**

From the table above,

a) Yields on most of the Sub-Saharan Eurobonds increased in Q1'2021 attributable to high demand for regional issues coupled with low supply of issuances, and,

b) Zambia recorded the highest increase in Eurobond yields, with the 10-year instruments for the 2012 issue increasing by 22.7% points to 44.3% from 21.5%, while the yield on the 12-year bond issued in 2015 declined by 1.0% points to 11.2% from 12.2%. This makes Zambia's 10-year Eurobonds the worst performing in Sub Saharan Africa, due to concerns of a widening fiscal deficit and deteriorating credit worthiness on the back of a default after missing a USD 42.5 mn coupon payment on its 2024 note. The country is currently in negotiations with the IMF over the appropriate policy instrument to help manage its public debt. On the other hand, the yield on the 12-year issue was the largest decliner in the region, signifying investor confidence of a recovery in Zambia's debt profile in the long term, supported by international institutions such as the IMF.

Since Eurobonds are denominated in foreign currency, the depreciation of a country's local currency means that they will incur a relatively higher cost to purchase foreign currency used to service outstanding debt obligations. Below is a summary of the performance of the different resident currencies for Q1'2021:

Select Sub Saharan Africa Currency Performance vs USD					
Currency	**Mar-20**	**Dec-20**	**Mar-21**	**Last 12 Months change (%)**	**YTD change (%)**
Ghanaian Cedi	5.7	5.8	5.8	(0.9%)	1.6%
Nigerian Naira	360.0	380.7	380.6	(5.4%)	0.04%
Tanzanian Shilling	2,308.0	2,314.0	2,314.0	(0.3%)	0.0%
Kenyan Shilling	104.7	109.2	109.5	(4.6%)	(0.3%)
Ugandan Shilling	3,785.0	3,647.0	3,660.0	3.4%	(0.4%)
South African Rand	17.8	14.7	14.8	20.8%	(0.5%)
Malawian Kwacha	729.3	763.2	776.3	(6.1%)	(1.7%)
Botswanan Pula	11.8	10.8	11.0	7.2%	(2.2%)
Mauritius Rupee	39.1	39.6	40.7	(3.8%)	(2.7%)
Zambian Kwacha	18.1	21.1	22.1	(17.7%)	(4.2%)

The vast majority of the select currencies depreciated against the US Dollar in Q1'2021 continuing the trend witnessed in FY'2020, with only the Ghanaian Cedi and the Nigerian Naira gaining by 1.6% and 0.04%, respectively. The Ghanaian Cedi performance is partly attributable to recovering global oil and cocoa prices as well as the subsequent increase in trade and investment activities in the country. The Zambian Kwacha was the worst performer in Q1'2021 as it depreciated by 4.2% against the dollar. The performance is partly attributable to high demand for hard currency from investors and the government as it seeks to meet its debt repayment obligations. The Zambian Kwacha depreciation was however mitigated by rising global copper prices; having increased by 15.6% to USD 4.1 from USD 3.5 per pound. The Kenya Shilling depreciated by 0.3% in Q1'2021 to close at Kshs 109.5 against the US Dollar, compared to Kshs 109.2 recorded at the end of 2020.

Section III: Outlook on SSA Eurobonds

From the analysis, most of the Eurobond yields in Sub-Saharan Africa increased in Q1'2021, 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 recovery and a slow vaccine inoculation rate. Notably, African debt has been on the rise mainly due to a slowdown in commodity prices, given that most economies are commodity driven, which has affected revenue generation as most African countries. To bridge the fiscal deficit gap, most countries have been forced to re-enter the international fixed income market to raise funds to fund their budget deficits as well as refinance existing debt obligations as seen by Benin's issue in February 2021 to partly repay part of the 2026 Eurobond. The deficit has also been widened by ambitious and expensive infrastructure investment promises made by the elected governments and the huge interest payments fom existing debt obligations. Countries such as Nigeria, Ghana and Kenya are expected to return back to the Eurobond market, however Eurobond issuance is expected to remain lower than in previous years partly due to availability of the cheaper concessional and multilateral debt coupled with demand for higher premiums by international market on developing countries' papers.

There are a few points to note:

a) **Public debt**- The COVID-19 pandemic has elevated the debt distress of most economies, with most governments now faced with the dilemma of whether to satisfy creditors or spend money on public health and on bailing out the economy, a situation that may lead to debt defaults. Zambia, for instance, became the first African country to default on its debt in the COVID-19 era after missing a USD 42.5 mn coupon payment on its 2024 note. According to the IMF's Regional Economic Outlook: Sub-Saharan Africa, released in April 2021, the region's public debt is projected to be 56.2% of GDP in 2021, a 1.6% points decline from the 57.8% recorded in 2020. The decline is mainly attributable to an expected 1.5% narrowing in fiscal deficits as governments across the region try and restore the health of public balance sheets through fiscal consolidation. The pandemic has exposed macroeconomic vulnerabilities in the region, with most countries recording declines in revenue collection, export revenues and diaspora remittances as well as depreciation of local currencies thus elevating the region's debt challenges. As such, as the pandemic continues to have a grip on the region's economic growth, with most governments being necessitated to borrow further to plug in fiscal deficits,

b) **Debt Sustainability**: According to the World Bank's Africa's Pulse April 2021, SSA's public debt is projected to rise further to 69.0% of GDP in 2021. Most African countries have resorted 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 given the high debt burden as well as the change in the composition of the region's public debt profile to sovereign bonds. Countries with higher debt service and riskier debt profiles are expected to face debt sustainability issues. The participation of several African countries in the Paris club Debt Service Suspension initiative (DSSI) in the second half of 2020, alarmed some investors following the uncertainty over what the debt relief could translate to in terms of repayments for both private bonds and African sovereigns. According to the IMF's Regional Economic Outlook, seventeen countries were in debt distress which is one more than before the pandemic. This is due to significant shortfalls in revenue collection and depreciating local currencies which in turn make debt servicing more expensive. As the pandemic continues to affect the region's economic growth, we project further deterioration of the SSA's debt sustainability, and,

c) **Subdued Economic Growth**- In 2020, the Sub-Saharan region experienced its first recession in 27 years, with the IMF projecting that the regional economy contracted by 1.9% in 2020. However, according to the World Economic Outlook released in early April 2021, the region is expected to bounce back in 2021 by registering a 3.4% growth owing to the reduced effects of the pandemic. The outlook also estimates that the substantial downturn in economic activity caused by the pandemic cost the region at least USD 115.0 bn in output losses in 2020 and could potentially erase at least five years of economic progress.