SSA Q3'2021 Eurobond Performance Note

A. Background

According to the September 2021 Africa's Pulse Report, the World Bank projects that the Sub-Saharan region will grow at a rate of 3.3%, higher than their earlier projection of 2.3% in April 2021, driven by the continued economic recovery in the region. Despite the recovery of commodity prices, global trade and the relaxation of the COVID-19 containment measures in most parts of the region, the World Bank notes that SSA's economic recovery will be weighed down by the emergence of new strains of the virus and the slow vaccine inoculation. The International Monetary Fund's (IMF) on the other hand projects a 3.4% growth rate in the region, unchanged from their earlier projections in April 2021.

During the third quarter of 2021, Africa's appetite for foreign-denominated debt continued, with the latest issue being Nigeria who raised a total of USD 4.0 bn in September after receiving bids worth USD 12.2 bn, translating to a subscription rate of 3.1x. The oversubscription was mainly driven by the yield hungry investors and also the positive outlook of Nigeria's economic recovery. 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 Q3'2021 painting a picture of the investor sentiments, risk tolerance, and an outlook on the yield performance. The analysis will be broken down as follows:

a. Background of Eurobonds in Sub Saharan Africa in Q3'2021,
b. Eurobond Performance in Sub-Saharan Africa, and,
c. Outlook on SSA Eurobonds.

Section I. Background of Eurobonds Issued in Sub Saharan Africa

Q3'2021 saw only one country in the Sub-Saharan Region raise USD 4.0 bn through Eurobond issues. The new instrument attracted a lot of interest as evidenced by the oversubscription of 3.1x. The issue had tenors of 7.0 years, 12.0 years and 30.0 years, with coupon rates of 6.1%, 7.4% and 8.3%, respectively. The issue received bids worth USD 12.2 bn translating to a 3.1x subscription rate. This is attributable to the yield hungry investors seeking for high yields and also the positive outlook of Nigeria's economic recovery. The Eurobond issue was specifically for the purpose of raising finances to fund government spending for the 2021 fiscal year and to partially finance the 5.6 tn naira budget deficit. The table below summarizes Nigeria's Eurobond issued in Q3'2021:

Country	Amount Issued (USD bns)	Issue Tenor	Issue Date	Maturity Date	Coupon	Yield at Issue Date	Subscription Rate	Yield as at 30th September	Yield Change
Nigeria	1.3	7.0	21/9/2021	21/9/2028	6.13%	6.13%	3.1x	6.11%	(0.02%)
Nigeria	1.5	12.0	21/9/2021	21/9/2033	7.38%	7.38%		7.37%	(0.01)%
Nigeria	1.3	30.0	21/9/2021	21/9/2051	8.25%	8.25%		8.26%	(0.01%)
Total	**4.0**					**7.25%**		**7.25%**	

Section II: Analysis of Existing Issues

Yields on African Eurobonds recorded mixed performance in Q3'2021, with most yields readjusting upwards as investors attached a higher risk premium on the regions affected by the third wave of the pandemic. Yields on the Benin, Kenyan and Senegalese Eurobonds declined in Q3'2021 by 0.3%, 0.2% and 0.1% points to 3.1%, 3.1% and 2.4%, from 3.4%, 3.3% and 2.5%, respectively, recorded at Q2'2021. The yields on the Benin Eurobond declined due to the positive expectations of strong economic growth in the country supported by a rebound in trade activities and improved control of the COVID-19 pandemic. The table below highlights the performance of select African Eurobonds in Q3'2021:

Yield Changes in Select SSA Eurobonds Issued Before 2021							
Country	Issue Tenor (yrs)	Issue Date	Maturity Date	Coupon	Yield as at June 2021	Yield as at September 2021	Q3'2021 change (%Points)
Benin	6	26/03/2019	26/03/2026	5.8%	3.4%	3.1%	(0.3%)
Kenya	10	24/6/2014	24/6/2024	6.9%	3.3%	3.1%	(0.2%)
Senegal	10	30/7/2014	30/7/2024	6.3%	2.5%	2.4%	(0.1%)
Kenya	10	28/2/2018	28/2/2028	7.3%	5.4%	5.3%	(0.1%)
Senegal	30	13/3/2018	13/3/2048	4.8%	6.7%	6.6%	(0.1%)
Kenya	30	28/2/2018	28/2/2048	8.3%	7.4%	7.5%	0.1%
Kenya	12	23/05/2019	23/05/2032	8.0%	6.3%	6.5%	0.2%
Kenya	7	22/5/2019	22/5/2027	7.0%	4.8%	5.0%	0.2%
Nigeria	30	28/11/2017	28/11/2047	7.6%	7.6%	7.9%	0.3%
Ivory Coast	12	30/11/2020	30/1/2032	4.9%	4.9%	5.2%	0.3%
Nigeria	12	23/2/2018	23/2/2030	7.1%	6.3%	6.7%	0.4%
Gabon	11	6/2/2020	6/2/2031	6.6%	6.5%	6.9%	0.4%
Ghana	41	11/2/2020	11/3/2061	8.8%	9.1%	9.7%	0.6%
Ghana	31	16/5/2018	16/6/2049	8.6%	9.0%	9.6%	0.6%
Ghana	31	26/03/2019	26/03/2051	9.0%	9.1%	9.8%	0.7%
Ghana	15	11/2/2020	11/2/2035	7.9%	8.1%	9.2%	1.1%
Ghana	10	8/7/2013	8/7/2023	7.9%	4.2%	5.4%	1.2%
Ghana	7	11/2/2020	11/2/2027	6.4%	6.2%	7.8%	1.6%
Zambia	10	14/4/2014	14/4/2024	8.5%	16.8%	19.7%	2.9%
Ghana	6	15/9/2016	15/9/2022	9.3%	2.2%	6.5%	4.3%

From the table above,

a. Benin recorded the highest decline in Eurobond yields signaling improved investor confidence, with the 2019 6-year instrument declining by 0.3% points, to 3.1% from 3.4% in June 2021. The improved investor confidence is attributable to the expectation that Benin's economy will rebound in the near term following the recovery seen in sectors such as Trade, Transport, Agriculture and Construction which are the major contributors to their GDP, and,
b. Ghana's 6-year Eurobond was the worst performer, with the yields increasing by 4.3% points to 6.5% from 2.2% attributable to the strict measures put in place to contain the spread of the pandemic which disrupted the on-going recovery and slowed economic activity during the quarter. The country's high debt to GDP ratio which stood at 78.0% as at the end of 2020 also presents the risk of rising debt-service costs for the economy, hence necessitating demands for higher premium on sovereign debt issued by the country.

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 Q3'2021:

Select Sub Saharan Africa Currency Performance vs USD					
Currency	**Sep-20**	**Dec-20**	**Sep-21**	**Last 12 Months change (%)**	**YTD change (%)**
Zambian Kwacha	20.0	21.1	16.7	**16.3%**	**20.6%**
Ugandan Shilling	3,712.0	3,647.0	3,543.6	**4.5%**	**2.8%**
Tanzanian Shilling	2,315.0	2,314.0	2,303.9	**0.5%**	**0.4%**
Kenyan Shilling	108.4	109.2	110.5	**(2.0%)**	**(1.2%)**
South African Rand	16.7	14.7	15.0	**10.1%**	**(2.2%)**
Ghanaian Cedi	5.7	5.8	6.0	**(6.0%)**	**(4.2%)**
Botswana Pula	11.7	10.8	11.3	**3.3%**	**(4.8%)**
Malawian Kwacha	743.9	763.2	815.2	**(9.6%)**	**(6.8%)**
Mauritius Rupee	39.7	39.6	42.4	**(6.9%)**	**(7.1%)**
Nigerian Naira	380.6	380.7	410.2	**(7.8%)**	**(7.7%)**

Source: Cytonn Research

In the third quarter of 2021, we have seen most Sub-Saharan currencies depreciate against the US Dollar with the Nigerian Naira being the largest loser, depreciating by 7.7% on YTD basis. The Zambian kwacha registered significant recovery gaining by 20.6% compared to the 42.2% depreciation recorded in Q3'2020. The strong performance of the Kwacha is mainly attributable to the strong recovery in global copper prices which led to improved foreign exchange flows from the mining sector. The Malawian Kwacha is the largest decliner over the last twelve months, having lost 9.6%, attributable to changes in government policy including the removal of currency swap mechanisms which had previously held the Kwacha steady in times of low foreign exchange reserves. Going forward, the increase in commodity prices will see commodity driven economies perform better due to increased dollar inflows from the higher prices which will support their currencies.

Section III: Outlook on SSA Eurobonds

From the analysis, it is evident that most Eurobond yields in the region increased in Q3'2021, attributable to investors attaching a higher risk premium in the region as major economies in SSA experienced the third wave of the pandemic. Notably, African debt has been on the rise mainly due to the surge in government financing needs as a result of COVID–19 expenditure, cumulative depreciation in exchange rates, rising interest payments, and widened primary deficits. More African countries are expected to return back to the Eurobond market in an attempt to seek more funding to support their recovery process from the pandemic, however, due to the high premiums demanded by investors, they may resort to alternative sources of funding either from International Financial Institutions (IFIs) or through domestic currency borrowing.

There are a few points to note:

a. **Public debt**- The COVID-19 pandemic and the resulting global economic disruptions elevated the debt distress of most economies, with the World Bank highlighting that increased funding extended to African states on commercial terms has raised the exposure of SSA countries to interest rate, exchange rate, and rollover risks. These rising fiscal burdens are expected to result in significant debt sustainability concerns and the regions public debt is projected to hit a peak of 71.0% of GDP in 2021, from 65.0% in 2020. It is worth noting that the IMF in their Regional Economic Outlook highlight that during the pandemic, 17 African countries were in debt distress, which is one more than before the pre-pandemic times attributable to the significant shortfalls in revenue collection and the depreciating local currencies which has in turn undermined their ability to service maturing debt obligations. Most governments are now faced with the dilemma of whether to satisfy creditors, spend money on public health or bail out the economy, a situation that may lead to high default levels. We believe that African countries should come up with ways to mitigate debt vulnerabilities, strengthen the process of debt resolutions where necessary, and apply policy measures to improve debt sustainability metrics,

b. **Debt Sustainability** - With African governments having an increased interest in accessing foreign financial markets, the need for public debt sustainability on the continent's debt policies has to be emphasized. According to World Bank, SSA's public debt is projected to hit a peak of 71.0% of GDP in 2021, from 65.0% in 2020. 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. Increased reliance on more expensive sources of financing coupled with the depreciation of local currencies has pushed up interest payments in the region. In 2021, we saw countries partake the G20 Debt Service Suspension Initiative (DSSI), and although it was meant to lower debt servicing costs and ease the financing constraints of countries in debt distress, it has not yet been effective. As a result, some countries like Chad and Ethiopia have had to engage in talks to restructure their debts through the Common Framework for Debt Treatments beyond the DSSI to ensure debt sustainability, and,

c. **Economic Growth** - In 2020, the Sub-Saharan region experienced its first recession in 27 years, with the regional economy contracting by 1.8% according to the International Monetary Fund (IMF). The IMF projects that the Sub-Saharan Regional GDP growth for 2021 will come in at 3.4%, which is unchanged from their earlier projections while the World Bank's projection of 3.3% is an improvement from their earlier estimation of 2.3%. The region's growth will be driven by positive spill overs from strengthening global activity, improved control of the COVID-19 pandemic on the back of the increased rollout of vaccines in the region which has resulted to most countries re-opening their economies, and strong domestic activity in commodity exporting states. There are still risks to these outlooks given the given the resurgence in the number of infections and the rising COVID-19 death tolls in some countries brought about by the third wave of the pandemic.