BIZCOMMUNITY

Hunting for Eurobonds

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Attracted by the prevailing low interest rates, cash-strapped African countries looking to borrow money on international private markets are increasingly turning to Eurobonds as the instrument of choice. In 2006, Seychelles became the first country in sub-Saharan Africa, other than South Africa, to issue bonds. A year later Ghana followed, raising $750m in Eurobonds. Since then they have been joined by Gabon, Senegal, Côte d'Ivoire, the Democratic Republic of Congo, Nigeria, Namibia and Zambia.

In September 2012, Zambia made a splash on the international private market, launching a 10-year bond at $750m. The issue was oversubscribed by $11m and became a model for other African nations. Rwanda followed suit in 2013 with a $400m Eurobond issued on the Irish Stock Exchange. Zambia is considering issuing a $1bn Eurobond this year to finance its budget deficit. It also plans to spend over $600m on developing power, road and rail infrastructure. Kenya is finalising plans for its debut entry into the Eurobond market, seeking up to $1.5bn to finance infrastructure projects.

Sub-Saharan Africa's second-largest economy, Nigeria, first entered the markets in 2011 with a 10-year Eurobond. "We look to come [to the market] regularly, every two years," Finance Minister Ngozi Okonjo-Iweala told the *Financial Times*. In 2012, African countries raised about $8.1bn from issuing bonds, says Moody's, a global credit rating agency. In total, more than 20% of the 48 countries in sub-Saharan Africa have sold Eurobonds, according to the International Monetary Fund (IMF).

Moving away from traditional foreign aid

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For certain governments in sub-Saharan Africa, Eurobonds are a means of diversifying sources of investment finance and moving away from traditional foreign aid. Not only do these bonds allow such governments to raise money for development projects when domestic resources are wanting, they also help reduce budgetary deficits in an environment in which donors are not willing to increase their overseas development assistance.

Corporate entities in sub-Saharan Africa, like Guaranty Trust Bank in Nigeria and Vodafone Ghana, have also successfully issued Eurobonds. Global investors have been eager to purchase these bonds for higher yields amidst low returns in mature markets. It is a sign of the investors' endorsement of the region's buoyant economic prospects, observes Mthuli Ncube, chief economist and vice-president of the African Development Bank (AfDB). The developed world has been rocked by a series of economic and financial crises while Africa has displayed steady growth over recent years, averaging about 5% per annum. Analysts believe the incentive for investors is solely the prospect of higher gains.

Eurobonds have also given African countries an opportunity to integrate into global financial markets. Up until recently, according to the AfDB, access was limited for African countries apart from Morocco, South Africa and Tunisia, which entered the markets in the 1990s. In addition, bond issuances come with fewer strings attached than money from multilateral institutions. Governments also have more control over where they channel the money.

Other reasons behind the recent surge in borrowing by African countries, according to the IMF, are changes in the institutional environment, such as more flexibility for low-income countries with access to non-concessional borrowing, reduced debt burdens, large borrowing needs and historically low borrowing costs. But there are serious challenges to Africa's future in international markets, analysts warn. Buyers of African bonds raise concerns about the countries' vulnerability to commodity prices, political instability, fiscal irresponsibility, lack of reliable statistics and transparency, and poor histories of debt management. Therefore, sovereign bonds issued by resource-rich African countries are deemed risky assets by some investors.

Speculation causes sell-off

Recent speculation that the US Federal Reserve bond-buying programme would end in 2014, along with rising US treasury yields, sparked a sell-off in emerging markets, Angus Downie, the head of economic research at Ecobank, a pan-African bank, told *Business Daily* of Kenya. "Investors will want higher yields," he says. Since the beginning of 2014, the Federal Reserve has started cutting back on its bond-buying programme, leading to speculation that this might spark an increase in interest rates. Higher interest rates raise the cost of servicing the national debt. In a recent article, the *Wall Street Journal* showed Nigeria's Eurobond trading at a yield of 6.375%, up from 4% in late April, because of waning investor interest, adding that Rwanda is now trading north of 8%.

On the flip side, these bonds have not been the saving grace that African countries thought they would be. In an article entitled "First Borrow," Amadou Sy, deputy division chief of the IMF's Monetary and Capital Markets Department, points to some recent sovereign defaults in sub-Saharan Africa. The Seychelles defaulted on a $230m Eurobond in 2008, after a sharp plunge in tourism revenues and years of excessive government spending. Côte d'Ivoire missed a $29m interest payment after its 2011 election disputes forced it to default on a bond issued in 2010. Ghana and Gabon are struggling to find money for a $750m and $1bn bond, respectively, on 10-year Eurobonds that will reach maturity in 2017. But this has not deterred African countries from issuing bonds, although they are borrowing at high interest rates.

Joseph Stiglitz, a Nobel laureate in economics and Columbia University professor, questions in a blog for the *Guardian* this new trend for "private sector borrowing" by developing countries. The sovereign Eurobonds carry significantly higher borrowing costs than concessional debt, Stiglitz notes. He worries about "excessive borrowing" over the long term, which benefits only the banks because they "take their fees up front." African countries, Stiglitz believes, should have in place a "comprehensive debt-management structure"; they should also invest wisely and refrain from borrowing further in order to repay their debts.

Sustainability

Whether the "rash of borrowing by sub-Saharan African governments is sustainable over the medium-to-long term is open to question," echoes IMF's Sy. If the low-interest-rate environment changes, it could reduce investors' appetite for the bonds and "economic growth may not continue, making it harder for countries to service their loans," he adds.

Political instability is something else that could put a wrench in the whole process, lowering economic growth and increasing interest rates. It is no coincidence that countries such as Ghana, Kenya and Nigeria that have had political stability in recent years have been able to-or intend to-sell bonds of at least $1bn. A change in the political situation in such a country, resulting in bad governance, could drive back potential bonds buyers, says Larry Seruma, chief investment officer of Nile Capital Management, which invests in Africa. And for Sy, developing well-functioning domestic bond markets to attract domestic and foreign savings over time is the way to go.

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