



SOUTHERN AFRICA

Regional Debt Profile



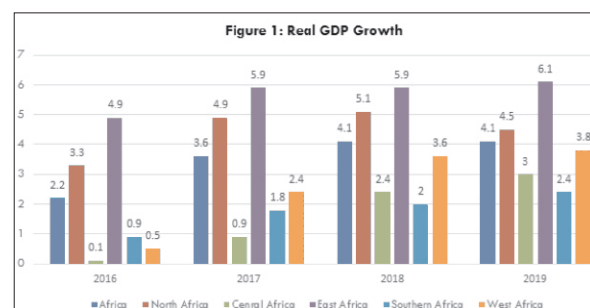
2018

1. Introduction

It's almost four decades since the establishment of the Southern African Development Community (SADC). Initially SADC was formed as a development coordinating conference (SADCC) in 1980 and in 1992 it was transformed into SADC when the SADC Treaty was signed in Windhoek, Namibia which redefined the basis of cooperation among member states from just being an association to being a legally binding arrangement. The Southern Africa sub-region is made up of the following member states: Angola, Botswana, Lesotho, Malawi, Mauritius, Mozambique, Namibia, South Africa, Swaziland, Zambia and Zimbabwe. AFRODAD sub-regions follow United Nations Economic Commission for Africa (UNECA) categorizations. Although most of sub-region member countries belong to the Southern African Development Community (SADC), countries like Tanzania are excluded in this profile. SADC has its genesis in the political liberation of the region and focuses on mobilizing and strategically utilizing resources for the benefit of southern Africa. SADC is committed to Regional Integration and poverty eradication within Southern Africa through economic development and ensuring peace and security. SADC works closely with the African Union and other Regional Economic Communities to achieve Continental and Regional Integration. As an inter-governmental organization, it aims to promote sustainable and equitable economic growth and socio-economic development through efficient production systems, deeper co-operation and integration, good governance and durable peace and security among the member states.

2. Southern Africa Regional Economic Outlook

The African continent is susceptible to varying social, economic and political factors which largely impacts on the macroeconomic environment and the economic performance at large. The instability in the region has a historical context in the sense of civil wars and the threat of political instability which is ever present across the continent. Against all odds the African economies has been resilient to negative shocks as the continent has been registering some positive economic growth rates according to the African Economic Outlook 2018. Average real GDP growth in Africa is estimated at 3.6 percent in 2017, up by 1.4 percent from the 2.2 percent in 2016. The real GDP growth is projected to grow by a constant 4.1 percent in 2018 and 2019. This improvement in the real GDP growth is attributed largely to improving commodity prices, increased agricultural production, improved global macroeconomic conditions, sustained domestic demand and better macroeconomic management amongst other factors.



Compilation based on World Bank data 2018

A close look at the real GDP growth rates across the sub-regions of the African continent shows real output is up in most sub-regions, reflecting generally good macroeconomic policies, progress in structural reforms (especially in infrastructure development), and generally sensible policy frameworks. East Africa has been recording the highest real

GDP growth rate for over a decade with an estimate of 5.9 percent in 2017 and projected to reach 6.1 percent by 2019. Southern Africa has been the 2nd lowest in terms of real GDP growth rates in 2017 and the sub-region is even projected to have the lowest growth rate in 2018 and 2019 when compared against the other four sub-regions of the African continent.

Table 1: Macroeconomic developments in Africa, Real GDP growth (%)

	2008-12	2013	2014	2015	2016	2017 (e)	2018 (f)
North Africa	4.4	1.7	1.5	3.3	3.3	5.0	5.1
Central Africa	4.9	4.0	6.0	3.6	0.8	0.9	2.6
East Africa	5.6	7.2	5.9	6.5	4.9	5.6	5.9
Southern Africa	3.1	3.7	2.8	1.9	0.9	1.6	2.0
West Africa	6.2	5.7	6.1	3.3	0.4	2.4	3.6

Against the global average, Africa's real GDP growth rate was below par in 2016 and it grew at the same rate with the global economy in 2017. However, the population growth in the African continent surpasses rate of economic growth which implies the per capita growth was below the average growth. There is basically an improvement across the continent in regards to economic performance and this cannot be singled out to a certain factor but the excelling global economy; improving international market or commodity prices and the improving access to global markets.

The southern Africa sub region though increasing in economic performance, it is projected to have the list real GDP growth rates in 2018 and 2019. This is mostly due to the fact that the sub region is prone to vulnerabilities and there are mixed results regarding progress in the fiscal consolidation. Also of key note is the dwindling South African economy, which is the heart of the Southern Africa economic performance, attained 0.3 percent growth in 2016. South Africa, more than doubled its growth in 2017, Zambia whose growth rate was estimated at 4.1 percent in 2017 and Angola which have increased its output by more than 2.0 percent are the major drivers of the economic development noted

in the region. However, this is only an issue of medium-term as South Africa which is the core of the Southern Africa economy is currently characterized by policy uncertainty which delays the much needed fiscal adjustments and this will have significant spillovers on the performance of other economies in the region such as Zimbabwe, Mozambique and Zambia.

Overall, there has been an improvement in the macroeconomic environment in the region with most economies being resilient to the negative shocks. Hence, the inflation rate has been receding and there is more flexibility in the exchange rate systems. The regional growth continue to thrive on the key sectors, that is, extractive, energy and agricultural sectors. However, full beneficiation from such key sectors and the other relevant sectors such as manufacturing and services is constrained by the decreasing ODA in the region and low contribution of tax to GDP in most countries due to factors such as illicit financial flows and corruption as well as increasing debt servicing and interest payments.

3. Regional Public Debt Trends

African debt continues to be an issue of great concern as public debt ratios, especially in the Southern African countries, are on the rise. Looking at the time period 2003 to 2017, about 40 countries in the sub-Saharan Africa region recorded an increase in external debt and only nine experienced otherwise.

Based on the IMF 2018 Regional Economic Outlook, about 40 percent of the SSA low income countries are either in debt distress or have been assessed as being at high risk of debt distress. External debt crisis has been and continues to be a main feature in most of the Southern Africa sub-region countries of Angola, Lesotho, Malawi, Mozambique, Swaziland, Zambia and Zimbabwe. By 2016, four of the Southern African countries, that is, Angola; Malawi; Mozambique and Zambia have benefited from the 1996 IMF and World Bank Heavily Indebted Poor Countries (HIPC) Initiative

and the Multilateral Debt Relief Initiative (MDRI) which aimed to ensure that countries do not have debt burdens they cannot manage. Regardless of the HIPC and MDRI, debt crisis continues to be an issue of great concern and significance in the region with the median level of public debt in SSA at the end of 2017 exceeding 50 percent of GDP. Of the beneficiaries of the HIPC and MDRI, alongside with Zimbabwe, Mozambique and Angola are in debt distress and Zambia has moved from moderate to being in high risk of debt.

Contrarily, there is developing domestic debt market in the Africa at large. Of major concern is the fact that the domestic debt markets have become a destination for foreign investment. For instance in the domestic government bonds market in South Africa, non-residents hold about 40 percent of the bonds.

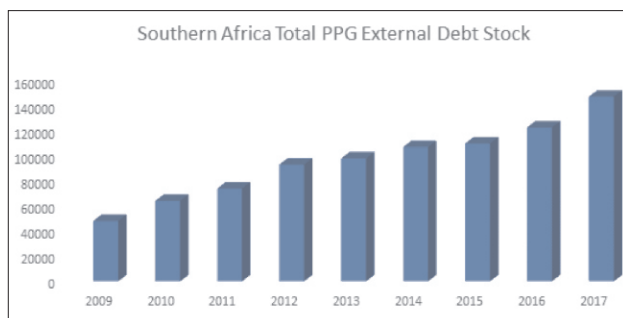
Table 2: External Debt Stock in the Southern African Region (public and publicly guaranteed),

	2009	2010	2011	2012	2013	2014	2015	2016	2017
Angola	13635	15466	17525	19203	23349	27826	27304	34815	36683
Botswana	1387	1349	1890	1924	1804	1827	1687	1654	1528
Lesotho	681	700	719	747	757	758	765	775	827
Malawi	846	729	929	1025	1244	1364	1454	1507	1787
Mauritius	740	1007	1171	1368	1735	1812	1718	1628	1547
Mozambique	3165	3170	4032	4793	6826	7930	8903	9180	10628
South Africa	22315	36274	41551	56502	54586	56642	57598	62195	81161
Swaziland	402	397	373	335	311	283	273	339	398
Zambia	1200	1290	1884	3101	3266	4659	6375	6904	8877
Zimbabwe	3735	3664	3820	3884	3951	3708	3567	3483	3534
TOTALS	48105	64046	73893	92881	97829	106810	109646	122480	146970

2009-2017 in US\$ Millions

**Namibia external debt statistics not available. Compilation based on World Bank data 2018*

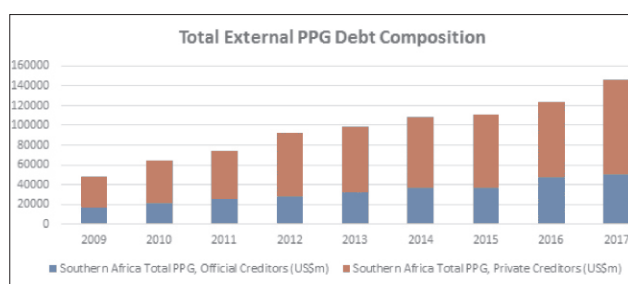
Figure 2: External Debt Stock in the Southern African Region (public and publicly guaranteed), 2009-2017 in US\$ Millions



Compilation based on World Bank data 2018

Public debt levels in the region as measured by the debt-to-GDP ratio as well as in nominal terms continue to deteriorate. Public and publicly guaranteed debt increased by more than 100% from \$48.105 billion in 2009 to \$146.970 billion in 2018. Angola, Mozambique, South Africa, Zambia and Zimbabwe have huge total debt stocks, rising since 2006/7, compared to other member countries of the region. Large percentage of South Africa's debt stock is made up of more domestic debt than external debt. Majority of Southern African countries received debt relief under the HIPC and MDRI initiatives, which saw their debt stocks reduced substantially around 2006 and 2007, but as end of 2017 countries such as Mozambique and Zambia are already in the debt distress category with total external debt stocks already surpassing pre-HIPC levels.

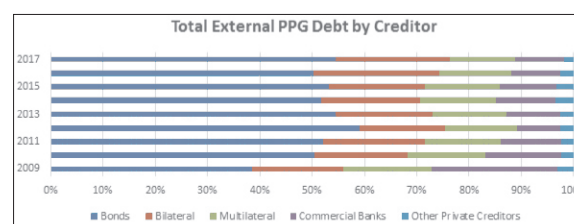
Figure 3: External Debt Stock composition in the Southern African Region (public and publicly guaranteed), 2009-2017 in US\$ Millions



Compilation based on World Bank data 2018

The Figure 3 above shows that PPG external credit in Southern Africa has largely been in the form of private creditors rather than official creditors. Most of the external debt acquired by Southern African countries between 2007 and 2016 has been through bonds and commercial banks. There is shift from traditional, concessional, sources of debt to commercial, domestic and non-traditional sources of debt which has increased exposure to market risk in Southern Africa and this has resulted in deterioration of debt sustainability in SSA as debt restructuring is more complex due to the different bondholders who might have diverging interests and jurisdictions.

Figure 4: Share of public and publicly guaranteed external debt, 2009-2017 in percentage



Compilation based on World Bank data 2018

Figure 4 shows that external debt has mainly been from bonds, comprising more than 50% of external debt since 2010. The share of commercial bank loans has been reducing since 2009 where it constituted about 24.0% to 9.4% of external debt in 2017. There has been a considerable increase in the use of bonds since 2009 to 2017 where bonds made up 38.4% of total PPG earlier and 54.5% at the end of 2017. The increased bond issuance for Southern African countries has largely been driven by Angola, South Africa, Zambia and Mozambique with South Africa contributing more than 75 percent of bond issuance in the Southern Africa region in 2016. Although multilateral credit has been widely viewed as effective and having a large impact on the economy there has been a limited use of it in Southern

Africa. Countries have been favouring commercial borrowing to raise large sums of money without heavy handed policy prescriptions. Servicing international sovereign bonds carries interest rate and foreign exchange risks as well as complex debt restructuring processes. If international interest rates raise debt rollover may not be feasible in the future and investor interest may shift to other instruments and markets. International sovereign bonds may be more difficult to restructure than bank loans since they are open to investors and investment banks there is a much larger number of creditors involved that must coordinate in the event of default and the introduction of collective action clauses may be required.

3.1 Drivers of Public Debt

Debt distress causes are country specific and vary across the region. However, most of the countries in debt distress in the region are those vulnerable to major export commodity price shocks. Some of the factors which have led to the increase in external debt stock in Southern Africa includes amongst others external shocks, below the line operations, persistent larger budget deficits, currency depreciation, infrastructure development and availability of new borrowing opportunities with less pre-condition.

Commodity prices volatility still remain obstacle of most countries growth and reveal countries' vulnerability to adverse shocks. Countries financed fiscal deficits through borrowing, either from external or domestic sources. Southern Africa countries have not made significant progress in diversifying their economies, which are still dependent on primary commodities, e.g. copper in Zambia, tobacco in Malawi, oil in Angola, and mining in Mozambique. The prices of commodities have been low in the recent past. These have led to higher deficits which might constrain debt servicing in future.

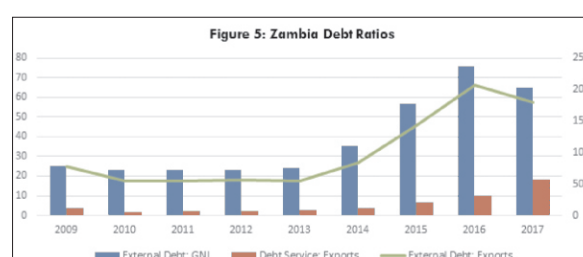
3.2 Selected countries with rising debt indicators

In selecting countries for further debt analysis debt ratios which indicate potential debt related risks were used. Debt ratios are considered in conjunction with key economic and financial variables such as expected growth and interest rates, which determine their trend in medium-term scenarios. For the purposes of this debt profile we shall consider 3 debt ratios, i.e. debt-to-exports, debt service-to-exports and debt-to-Gross National Income (GNI) ratio.

For individual country analysis, the analysis was based on countries whose debt ratios are signaling that debt service difficulties are likely to occur. These are countries whose external debt: to exports is above 150% or external debt to GNI is above 50%. In most cases countries with high external debt to exports ratio and high external debt to GNI ratios have a rising debt service ratio which can be regarded as a sign of an imminent debt crisis.

Zambia and Mozambique have already surpassed the external debt ratio thresholds above and have been in the debt discussion circles of late.

3.2.1 Zambia

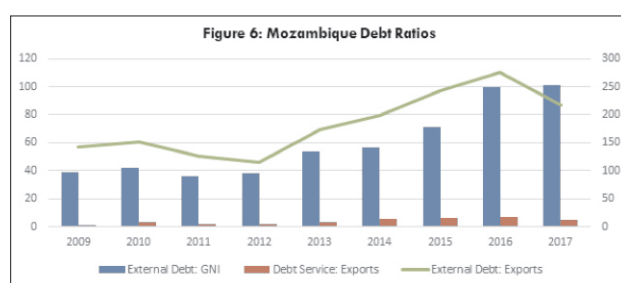


Compilation based on World Bank data 2018

Zambia has been a beneficiary of the HIPC in 2000 which reduced its external debt stock by 62.6 percent from the 1999 figure to \$0.9 billion. HIPC was intended to remove debt burden from the Zambian economy in terms of debt

servicing and repayment of loans. However, the Zambian public debt has been increasing since 2009 and as of 2016, Zambia's debt was standing at US\$13.3 billion representing 60.5 percent of the GDP. Public debt more than tripled from 21 percent of GDP at end-2011 to 60.5 percent of GDP at end-2016. External debt grew from US\$1.9 billion (8.4 percent of GDP) end of 2011 to US\$8.0 billion (36.5 percent of GDP) at end of 2016. Zambian Public Debt as a percentage of GDP has been on an increasing trend since 2011 surpassing the 40 percent threshold, mainly reflecting issuance of Eurobonds by the government and a rapid rise in private sector debt. The Eurobond Issuances in Zambia amounted to US\$3 billion just from 2012 to 2015. This, coupled with increase in bilateral loans as noted in the recent Zambia-China saga which has raised questions on China's debt stance towards Africa. The increase in external debt has been followed by a gradual increase in domestic debt. All these events has transformed Zambia from being rated as a moderate risk to a high debt risk country based on the IMF/World Bank debt sustainability analysis. The growing debt burden in Zambia implies straining of the domestic resources and it's a barrier to attainment of macroeconomic objectives.

3.2.2 Mozambique



Compilation based on World Bank data 2018

Mozambique just like Zambia, Malawi and Angola also received debt relief under HIPC and MDRI initiatives. Despite debt relief granted to Mozambique in 1999, external debt stock has been on the rise. Mozambique is one of the previously HIPC where debt has been growing rapidly since 2011. The period starting from 2011 is

characterized by a drastic increase in the eternal debt of Mozambique. As shown in Figure 6 above, the external debt to exports ratio has been rising sharply since 2012 reaching a high of 276.3% in 2016. PPG external debt increased by more than 200% between 2008 and 2016. This is way above pre-HIPC levels when its PPG external debt was \$5.983 billion in 1998. The increase in external debt between 2013 and 2016 is associated with the issuance of sovereign bonds. Besides the issuance of bond, Mozambique borrowed USD 1.4 billion over the period 2013 to 2015 in an undisclosed commercial debt. The level of debt took an explosive path with the contraction of the commercial loans between 2013 and 2016 making Mozambique one of the countries in Africa with the highest debt ratios. The onerous terms of the loans and the pace of currency depreciation has created severe liquidity constraints compromising Mozambique's capacity to meet debt service obligations. This has been exacerbated by weaker commodity prices and lower demand amongst trading partners that the country has been facing. Given that there has been a rapid increase in the country's liabilities yet the due diligence mechanisms to govern them remain lagging, Mozambique's debt sustainability now rests on the ability to restructure the debt.

4. Domestic Debt Levels Rising

Domestic debt has also been increasing in some of the Southern Africa countries in absolute amounts and as a proportion of total public debt and as a ratio of GDP.

Borrowing from the domestic market has become a viable option for most countries due to chronic annual budget deficits, drying up concessional lending, reduction in official development assistance (ODA) inflows, and impact of the global financial crisis of 2008 and 2009. Foreign aid is linked to project financing and hence cannot finance

governments with recurrent budget deficits therefore resort to domestic savings through issuance of domestic debt.

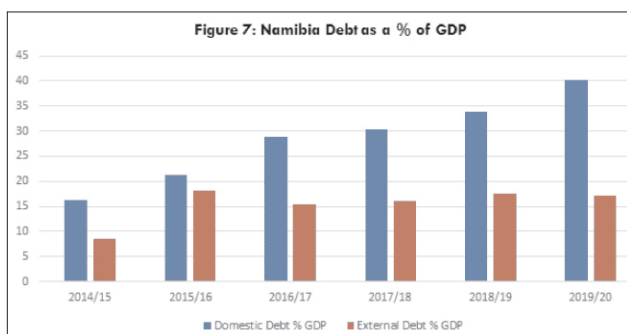
There are currently no internationally agreed thresholds for assessing domestic debt sustainability. However, the IMF describes the domestic debt burden as significant when the nominal domestic debt stock to GDP ratio is above 15% - 20%. It has already reached the critical threshold in countries such as Malawi, Mozambique and Zambia.

Although the rate of accumulation of domestic debt for most Southern African countries has been increasing since 2015, the majority of the sub-region members rely on external sources of finance to support their development, but South Africa, Namibia and Mauritius use their domestic debt markets more and this is reflected by the dominance of domestic debt in their total public debt portfolios.

South Africa`s domestic debt/GDP ratio continues to grow with the total net domestic debt of the national government of R2 242 billion at the end of 2017. The continuous increase in domestic debt is a consequence of significant increases of issuances of domestic marketable debt instruments. There is also an increasing domestic and foreign demand for long dated domestic securities. For 2017 as a whole, the acquisition of domestic debt and equity securities by non-resident investors almost doubled compared to 2016, reflecting the global search for higher investment returns. For instance non-residents hold about 40 percent of the domestic government bonds. The country's national budget was generally balanced up to 2008, thus putting minimum pressure on total debt accumulation. However, budget deficits have been recorded since 2009, due to the 2008/09 global financial and economic crisis. Consequently, the Total Debt to GDP ratio which had declined from 41.3% as of March 2004 to 25.3% as of March 2008 rose to reach 37.6% as of end March 2012, mainly driven by domestic debt. The dominance of South Africa`s domestic debt has continued to grow over

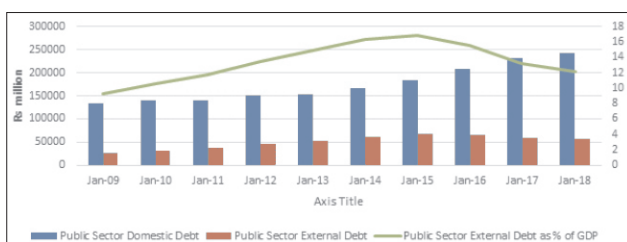
the years. By end of 2017 domestic debt accounted for more than 90% of total gross loan debt. The impact of the increasing domestic debt is notable on the increasing ratio of total public debt to GDP which is on increasing trajectory as it was 53% in 2017 from 51% in 2016. The South African debt composition is largely dominated by the commercial creditors in the form of bonds, which accounted for more than 80 percent of total debt in 2016.

Namibia`s the largest annual increase in the central government stock of debt was experienced between 2010 and 2011 when the total outstanding debt increased by 98.8% from N\$12 968.7million as of end 2010 to N\$25 787.6million as of end 2011. In a bid to address the country's high unemployment rate and also support strategic economic sectors in the face of the 2008 global and regional economic slowdown, the government of Namibia unveiled the Targeted Intervention Programme for Employment and Economic Growth (TIPEEG) in 2011. Given the huge funding requirements of this programme, the government turned to both domestic and international capital markets to source funding, resulting in a corresponding huge upsurge in the country's debt. Domestic debt as a percentage of GDP stood at 16% and 12% in 2012 and 2013 respectively whilst for external debt the ratio was 9% and 10% respectively for the same period reflecting the dominance of the country`s reliance on domestic debt. This trend is expected to continue going even into 2019/20 (see Figure 7 below) because since 2011/12 domestic short-term debt has averaged at about 42 percent of domestic debt and 27 percent of total debt. While the recent issuance of external debt has reduced the reliance of short-term debt, it has increased foreign exchange risks with non-rand foreign currency debt averaging about 32 percent of total debt at the end of 2016/17.



Mauritius, Figure 3 below shows a decomposition of Mauritius total public debt into domestic and external debt. Domestic debt is generally more dominant than external debt. External debt represented less than a quarter of total public debt and 15.6% of GDP as at June 2016. The dominance of domestic debt over external debt is in line with the country's 2008 debt management strategy which emphasizes the foreign currency risk associated with external debt. The strategy thus recommends limiting the size of the public sector external debt stock to a level that will result in an annual debt service of the external debt portfolio not exceeding 10% of export earnings. In this respect, the debt service ratio as at end of June 2016 stood at 3.6%. It has, in fact, remained within the range 3% to 8% over the period 2003 and 2016.

Figure 8: Domestic and External Public Debt, June 2009 to June 2018



Source: Mauritius Ministry of Finance and Economic Development

Sovereign Bond Issuance in Southern Africa

Conditionalities which come with traditional sources of finance coupled with favourable capital market conditions has

resulted in a shift in the debt composition in sub-Saharan Africa with an increase in participation in international markets for development funds. Prior to 2006, only South Africa was the major player in issuances of foreign currency dominated sovereign bonds.

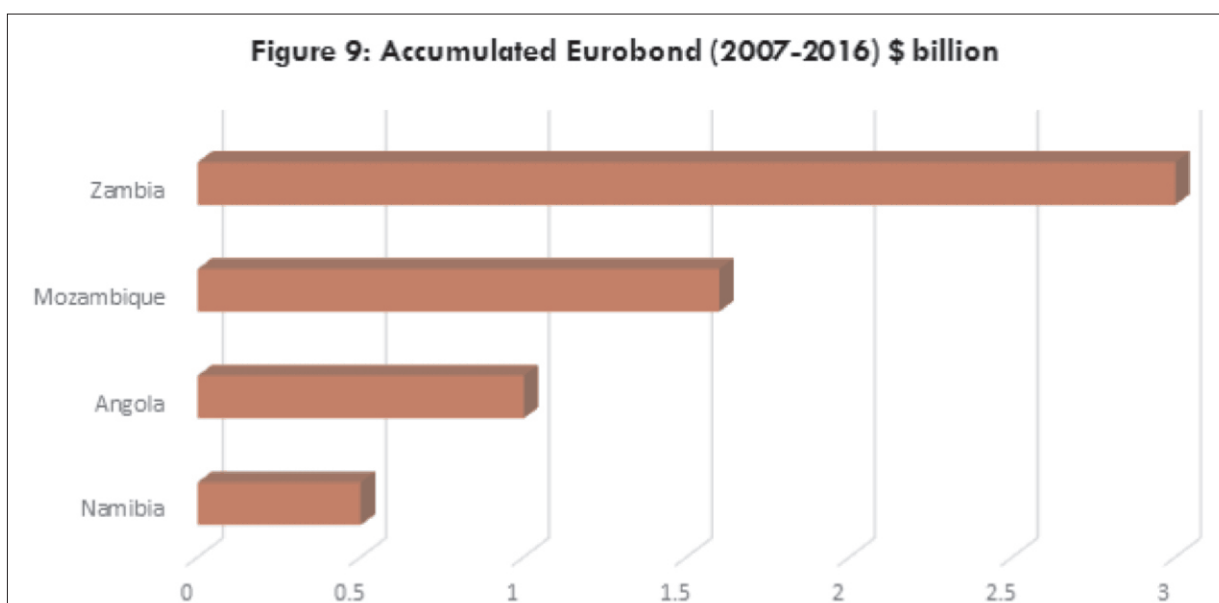
However, of late countries such as Mozambique, Zambia, Angola and Namibia amongst others have largely raised development funds through the international markets.

Zambia alone according to the World Bank statistics have raised in excess of \$5 billion from 2012 to 2016 and from 2006 to 2014, thirteen African countries have issued a total of US\$15 Billion in international sovereign bonds, with five countries from Southern Africa (Judith E. Tyson 2015).

When compared against other sub regions of Africa, Southern Africa has been experiencing low economic growth and this has been a drawback when it comes to infrastructure development. On such a background, the international debt market presence a bridge to close the gap on financing development needs such as in infrastructure, education and health.

However, it also increases external debt, and bullet repayments will require strict fiscal management. A number of countries issued large Eurobonds and these are drastically increasing external debt, which may compromise the gains on debt sustainability.

Southern Africa member countries (excluding South Africa) raised \$6.1 billion from the international capital market between 2007 and 2016.



Apart from South Africa, which has Eurobonds in several currencies, all Eurobonds by Southern African countries have been issued in USD with maturities mostly around 10 years and most are listed at the London Stock Exchange. International debt issues incur repayment costs which might rise if the currency depreciates. International bonds with a bullet repayment structure can lead to phases of soaring debt servicing obligations and demand competent public debt management.

Sovereign bond issues are contributing to economic development. The use of funds varies in relation to its potential contribution to development goals. Some countries have used funds positively, such as for infrastructure. However some countries appear to have used funds for purposes with little or no developmental impact such as “pork barrel”, which is political spending on public sector salaries and military hardware. In Southern Africa bond proceeds were used for infrastructure investments by Namibia, Zambia and Angola while in Mozambique funds were used for public sector salary increases, financing of state-owned enterprises and purchases of military equipment.

5. Regional Outlook for Debt Sustainability

The recent (November 2018) IMF/World Bank debt sustainability analysis for all countries, low income countries and market accessing countries, showed that most Southern African countries had varying debt distress categories. Zimbabwe and Mozambique are classified as being under debt distress, Zambia being in high risk debt distress whilst Malawi and Mozambique are classified under moderate and low risk debt distress respectively. AFRODAD’s analysis classified Zimbabwe, Zambia and Mozambique as debt distress countries. Mozambique cause is supported by the recent cases of unveiled hidden loans and the defaulting and missing loan repayments whilst Zambia has been circled on China debt defaulting as she failed to meet her obligations posing threat to some national assets. Overall the sub-regional public debt is still sustainable despite the rapid debt accumulation. This is mainly due to the rising GDP growth rates, in member countries. However, the recent increase in commercial borrowing implies a new set of risks as this type of financing is associated with high interest rates and

shorter grace and maturity periods, thus raising concern about debt sustainability. Falling commodity prices, a rising dollar and the prospect of higher interest payments mean these debts may be harder to repay than ever.

6. Recommendations

Large portion of the African debt, especially in the Southern Africa region, is foreign currency dominated debt, hence, the debt dynamics are susceptible to fiscal policy slippages, tighter financing conditions and external exchange rate shocks. On that note, there is a call for prudent fiscal policy to rein in public debt.

African countries' governments needs to enact responsible borrowing in the financial system as in most cases the borrowed money is not productive. Therefore, debt must be deployed in productive sectors that yield income streams for self-financing and grow the economies which will allow to build capacity weaning the countries from foreign debt and distress.

The shift in the borrowing source from concessional to non-concessional loans (traditional to non-traditional sources of finance) is an issue of great concern to the region as it have significant implication on debt sustainability and debt risk. Hence, domestic debt markets should be part of the broader strategy to mobilize domestic finance in Africa.

There has been a significant rise in domestic debt in most of the Southern African countries and domestic debt now constitutes a large share of total debt. Domestic debt is much more expensive than external debt as it consumes a large percentage of government revenue given that domestic interest rates are higher than foreign ones. This has significant negative implications for private investment, fiscal sustainability, economic growth and poverty reduction. Governments need to formulate and implement prudent domestic debt management strategies to mitigate the effects of the rising debt on the economy.



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