Namibia Capital Market
Fixed Income Analysis
02 May 2019

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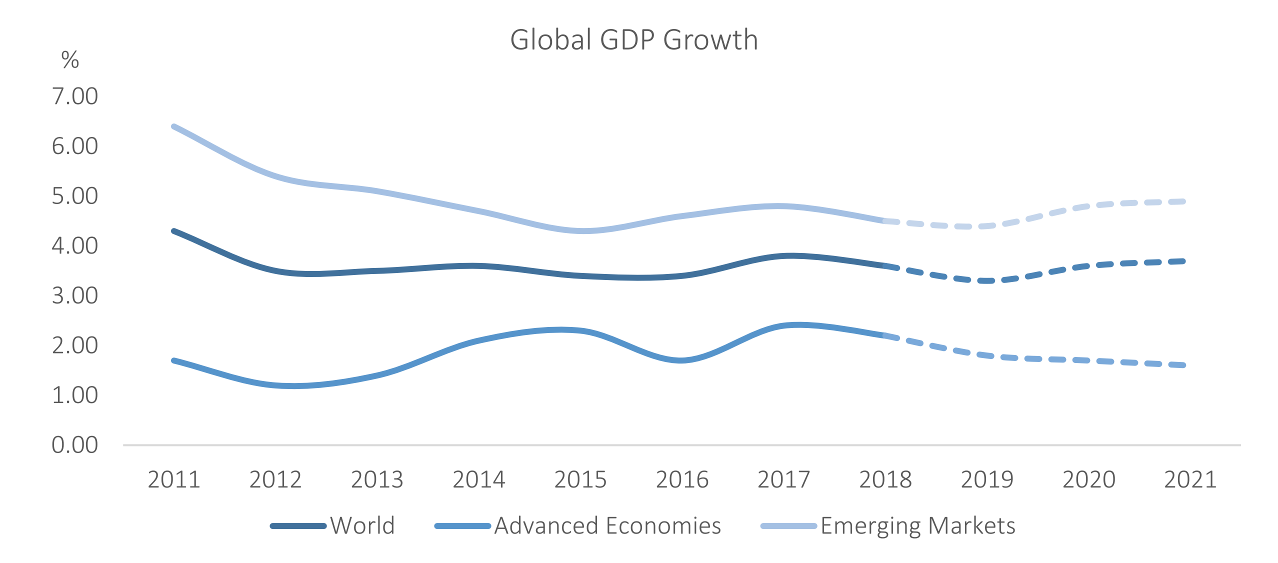
Global Macro

In its April 2019 World Economic Outlook ("WEO") titled "Growth Slowdown, Precarious Recovery" the International Monetary Fund ("IMF") highlighted a plethora of factors which has led to them revising their expectations for global growth in 2019 from 3.9% last year to 3.3%. According to IMF forecast, around 70% of the global economy (as measured by GDP) will experience a slowdown this year, making this the most synchronized slowdown in global growth since 2011.



Source: IMF

Some of these factors have been known for quite some time. The risks around Brexit remain high as uncertainty surrounding the terms of the departure persists and the likelihood of a no-deal Brexit increases by the day. Elsewhere in Europe, Germany's vehicle manufacturing contracted in the third quarter of 2018. Struggling to adjust to new emission testing standards, the industry dragged overall economic growth into negative territory. German production of motor vehicles and their components in the second half of 2018 was 7.1% lower than in the first half, while growth in the German automotive industry in 2019 has been negative thus far on a seasonally adjusted basis. This is bad news for Europe's largest economy, and risks dampening the entire Euro area's growth prospects for 2019.

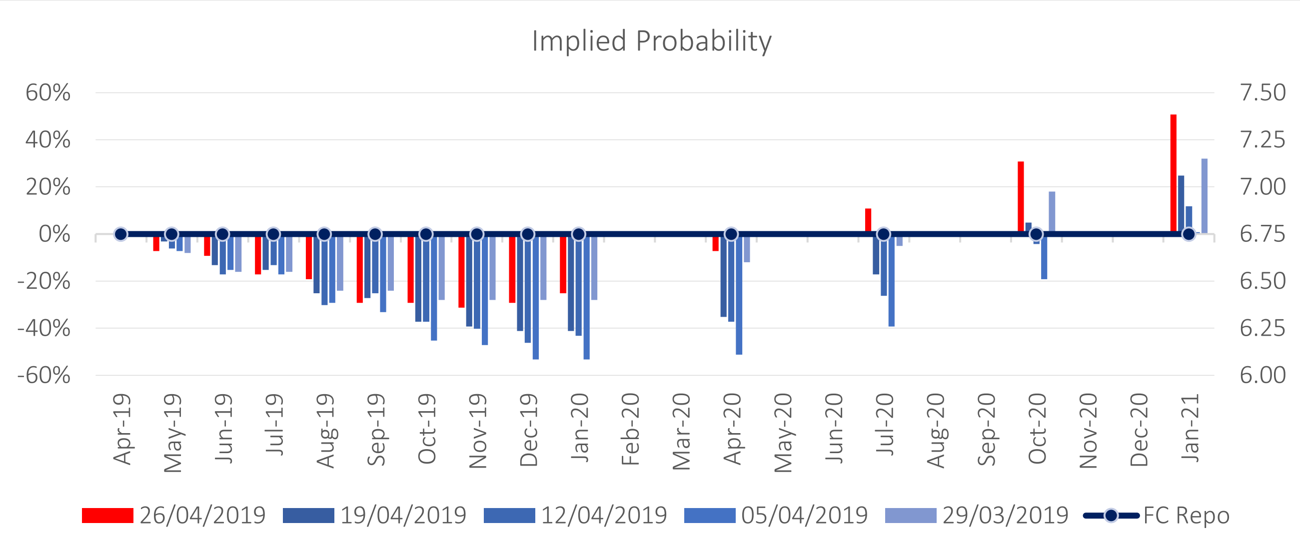
In other developed markets, news is also not overly positive. The US-China trade dispute has seen the US impose tariffs on roughly US$250 billion worth of Chinese products in 2018, with Beijing retaliating in kind. After some hostility, talks started in December 2018 and have been dragging on since. Although "good progress has been made" there is no deadline for discussions to conclude. Additionally, there has been no indication on whether any of the newly imposed US tariffs on Chinese goods would be reversed.

China's domestic economy is also under pressure, largely due to tightening regulation aimed at reining in soaring corporate debt. The rationale for credit tightening was to constrain shadow banking and place Chinese growth on a more sustainable footing. The immediate effect of the changes was slower domestic investment, specifically in the infrastructure sector. These measures, combined with lower exports to the US as a result of higher tariffs in the second half of 2018, contributed to slowed growth of 6.0% from 6.8% in the first half of 2018. Other emerging markets such as Turkey and Argentina also saw policy tightening aimed at reducing financial and macroeconomic imbalances. General sentiment around emerging markets has weakened and sovereign spreads have been rising for many EM issuers.

One of the biggest signs of how much the outlook for the global economy has changed is the turnaround in stance of the US Federal Reserve. The Fed at its March meeting left its key policy rate unchanged and trimmed its rate hikes outlook this year from two to none, with most Federal Reserve officials believing that economic conditions warrant keeping the Fed's benchmark policy rate unchanged for the rest of this year. Similar accommodative monetary policy seems to be the mantra of central bankers across developed markets such as the UK, Eurozone and Japan, seeing as inflation remains well below most central banks' targets.

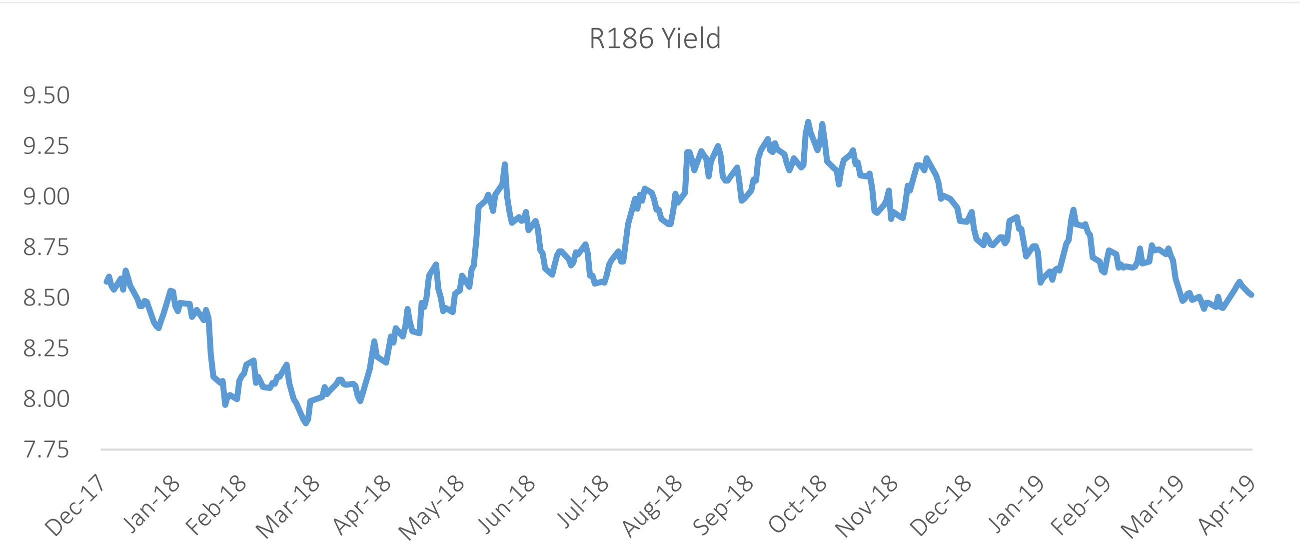
South Africa

The South African domestic growth forecast for 2019 has also been trimmed by the IMF, declining from 1.4% in October 2018 to 1.2% in the April 2019 update. Business and consumer confidence remain low as electricity constraints have weighed on the growth outlook. Additionally, the IMF have highlighted that continued policy uncertainty after the May 2019 elections remains a real risk to growth as gradual fiscal consolidation is required to stabilize public debt.

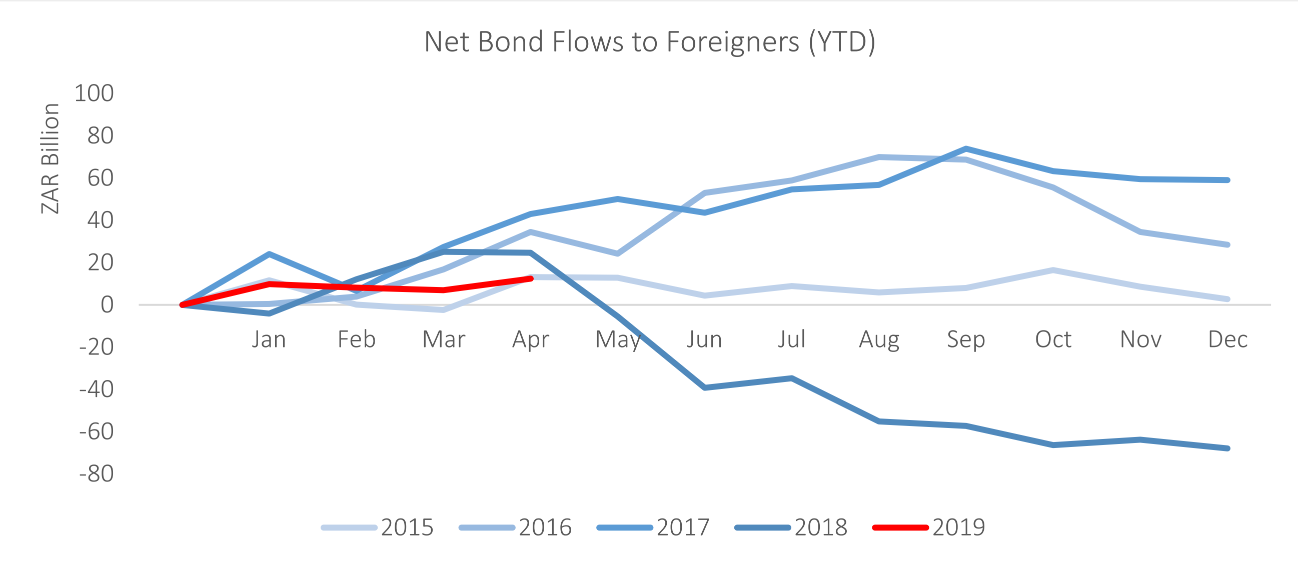


Source: Bloomberg, IJG

Although inflation risks remain skewed to the upside, the outlook remains relatively subdued, and inflation is expected to average 4.8% in 2019 and 5.3% in 2020. Combining low inflation with low levels of growth and more accommodative monetary policy globally, monetary policy in South Africa is also set to remain accommodative. Both the forward rate agreement ("FRA") curve and the SARB forecast are expecting no change in the repo rate in the near term.



Following a record sell-off in 2018, seeing roughly ZAR67.9 billion flowing out of South African bonds, non-resident South African sovereign bond holdings dropped to the lowest levels in almost two years. The decline in demand saw South Africa's benchmark R186 bond yield increase from below 8.0% to over 9.0%. From the start of this year the yield has moderated to settle around the 8.5% level, as some international demand has returned. Foreign flows have been marginally positive year-to-date.

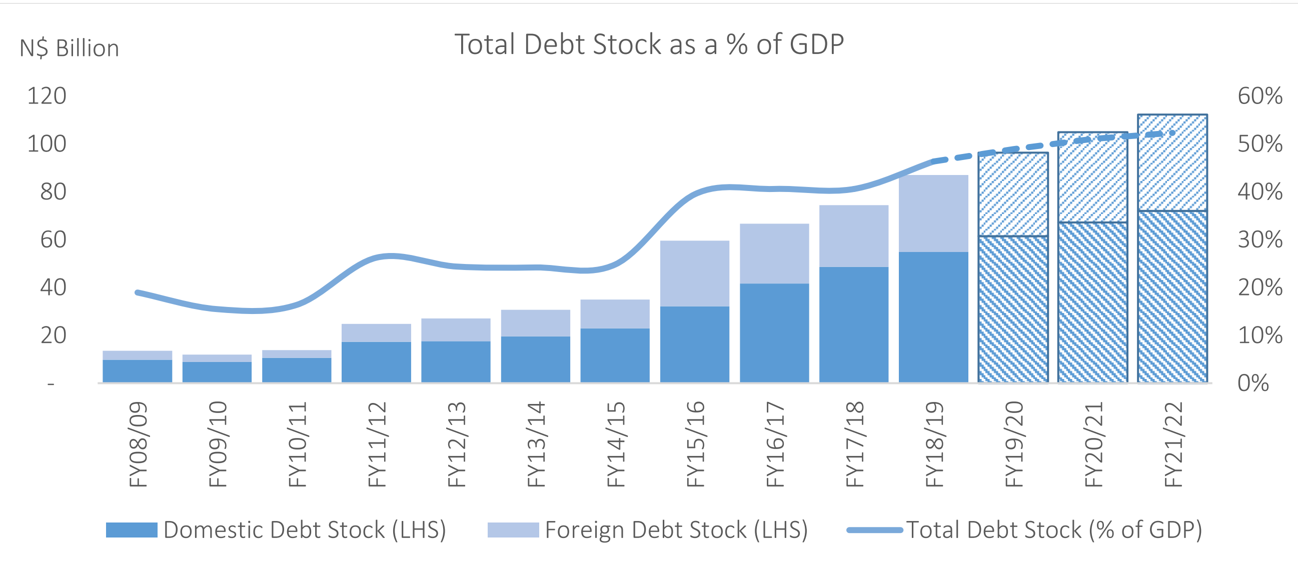


Source: Bloomberg, IJG

This demand will likely continue to be supported by the deferral of Moody's Investors Service's review, which will see the country retain its investment grade rating until November at the least. Additionally, a re-weighting of the JPMorgan Government Bond Emerging Markets index which saw South African debt assigned a higher weighting, should increase appetite from passive fixed income investors which should be supportive of bonds in the short term.

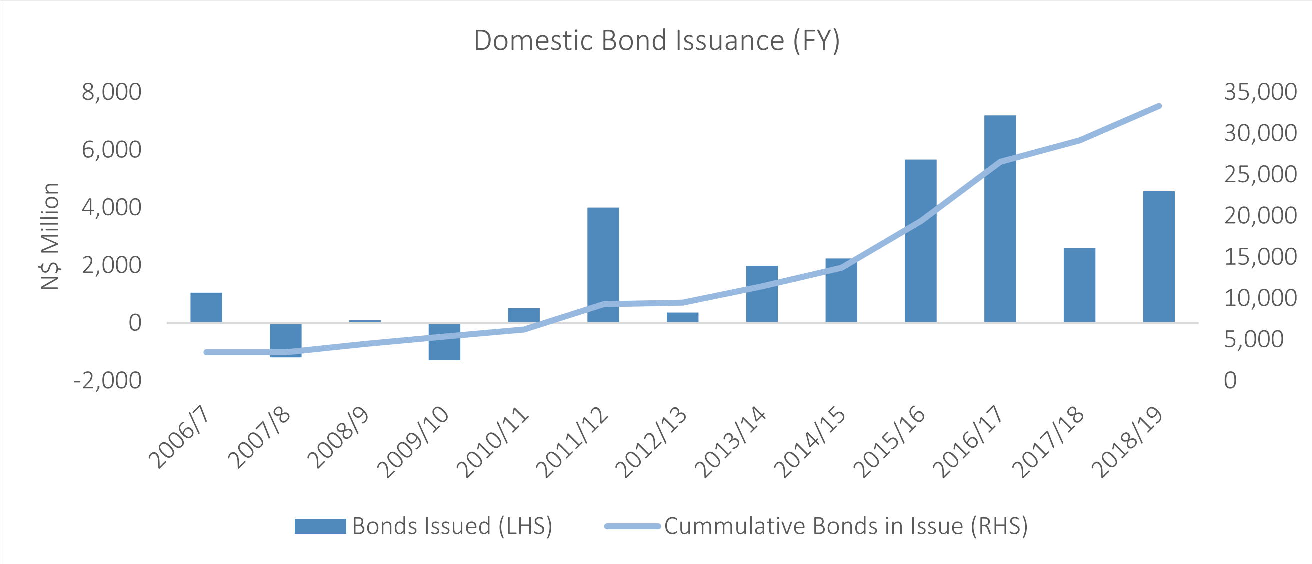
Namibia

Namibia remains in the midst of "pro-growth" fiscal consolidation. With the country's growth outlook also quite muted over the medium term, fixed income remains an attractive source of real return. Additionally, amendments to the pension fund regulation has seen domestic asset requirements increase to 45% of total portfolio value. This has been creating artificial demand for Namibian assets.



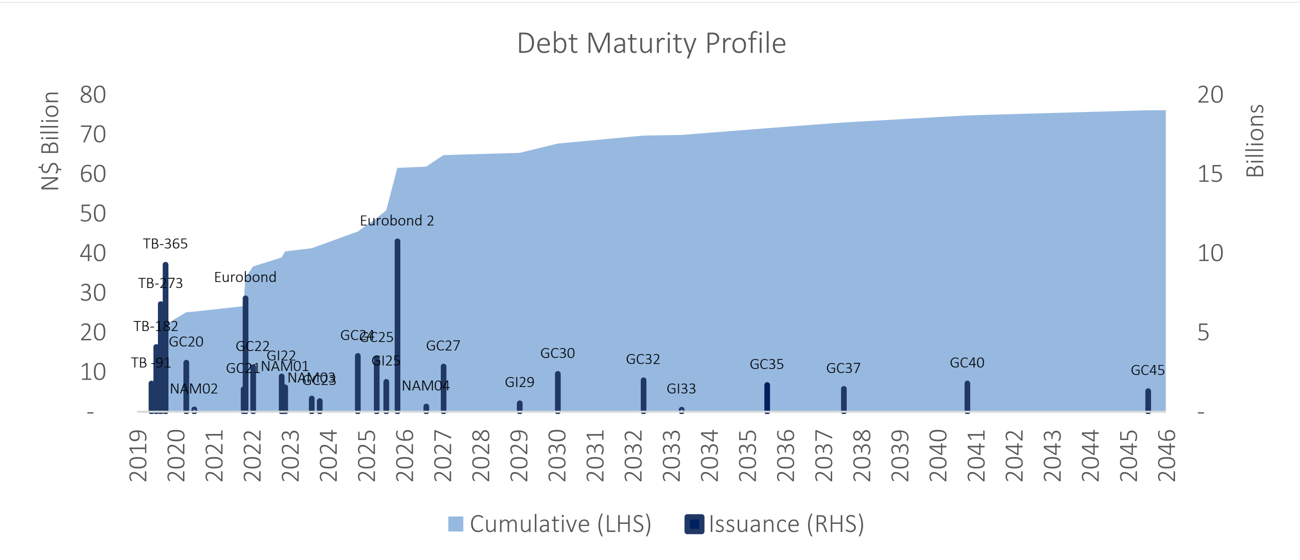
Source: MoF, IJG

As per the March 2019 budget, the financing requirement for the next three financial years amount to N$9.2bn, N$8.6bn and N$7.4bn for FY19/20, FY20/21 and FY21/22 respectively. Roughly two thirds of this will be sourced from the domestic market which indicates that domestic net issuance will increase from N$5.3bn in N$2018/19 to N$6.5bn in 2019/20, and is expected to gradually taper off from there. This means there will be a continued supply of domestic bonds for the next couple of years.



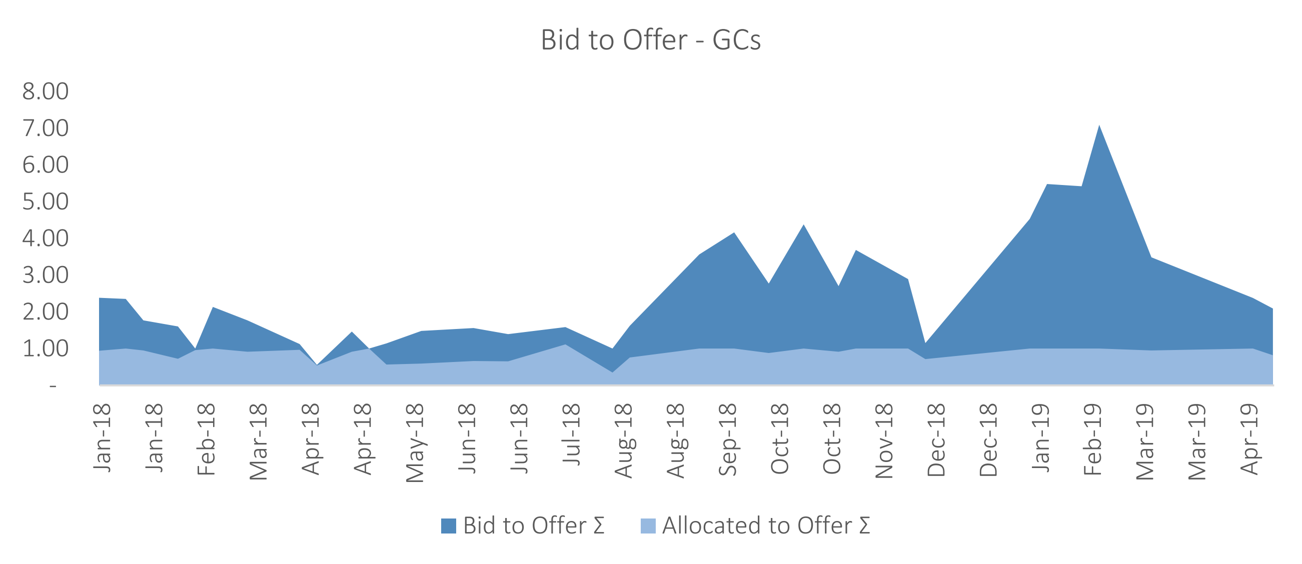
Source: MoF, IJG

The Namibian debt maturity profile remains very steep as roughly 80% of the country's sovereign debt will mature before the end of 2025. Roughly 29% of total government debt is made up of TBs which will be rolled on a continuous basis. This opens government up to the risk of spikes in funding costs should demand for short term securities fall and government is unable to redeem their short-term borrowings.



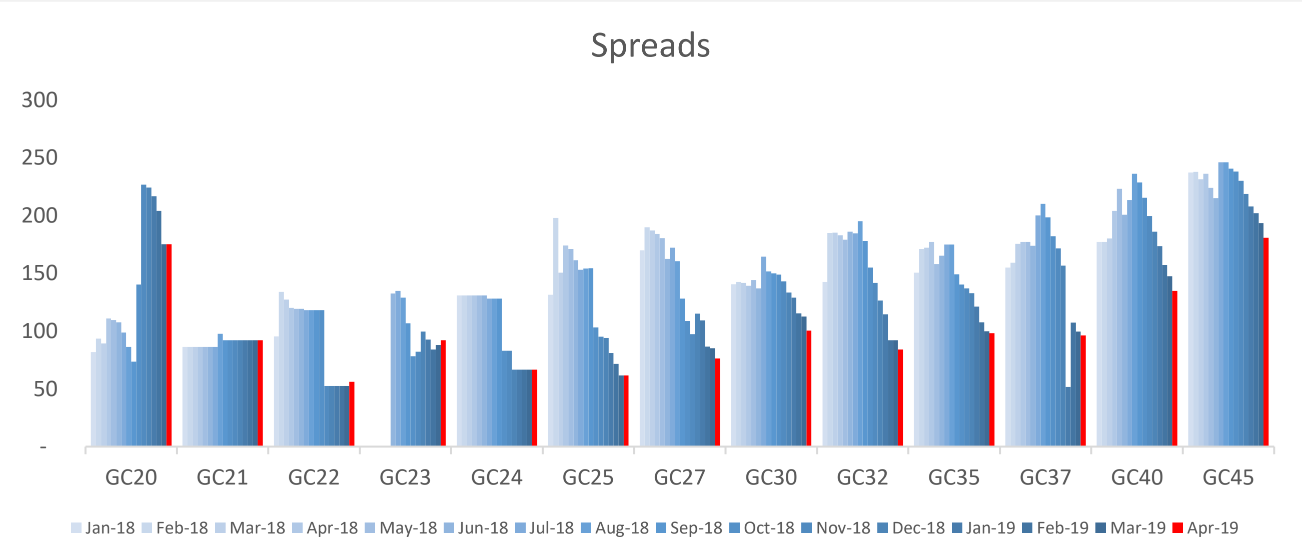
Source: BoN, IJG

Another concern is the maturities of the two large Eurobonds, one amounting to US$500m maturing in 2021 and another of US$750 million maturing in in 2025. The sinking fund balance for redemptions currently stands at only US$340 million, which makes the probability that these issuances will have to be rolled quite likely.



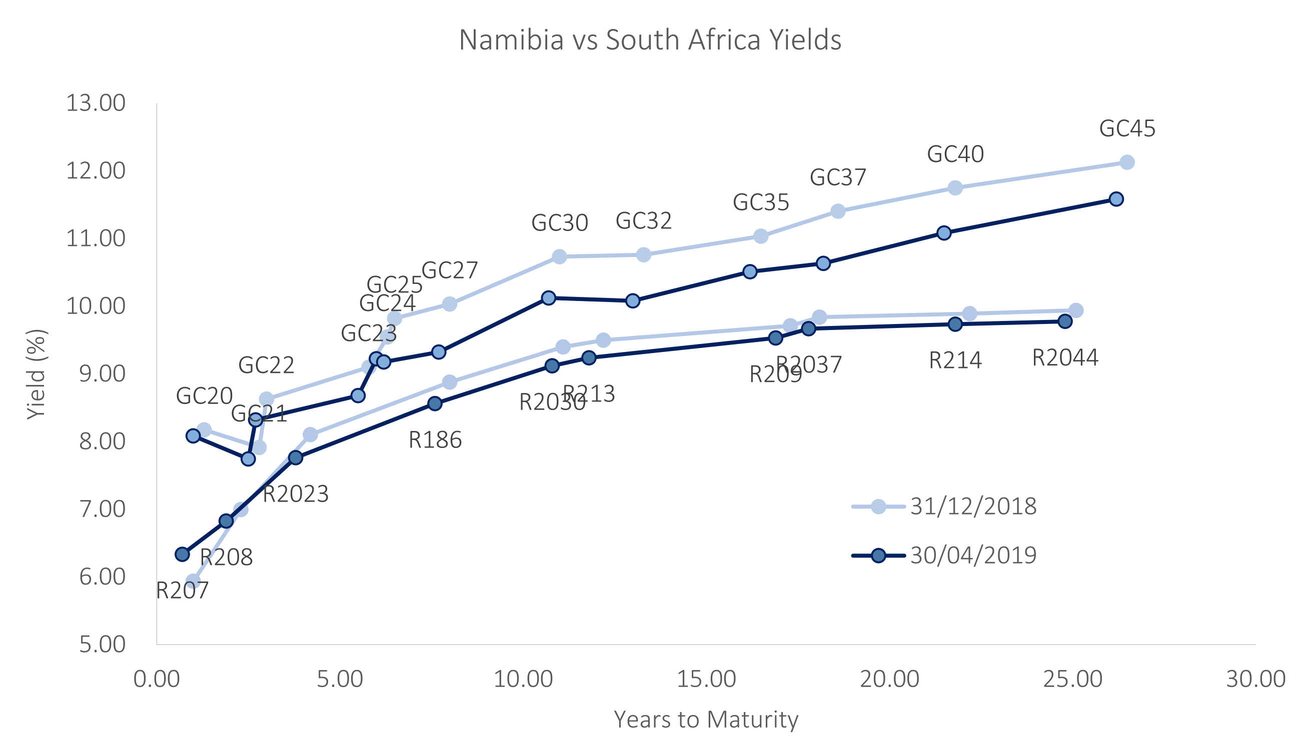
Source: BoN, IJG

Demand on recent GC auctions has been high. In the first quarter of 2019 auctions were 4.4x oversubscribed on average. As a result of the strong demand, spreads over the South African benchmarks have been declining. This demand was seen right across the curve, as the longer dated bonds, which normally receive less attention were also very well bid.



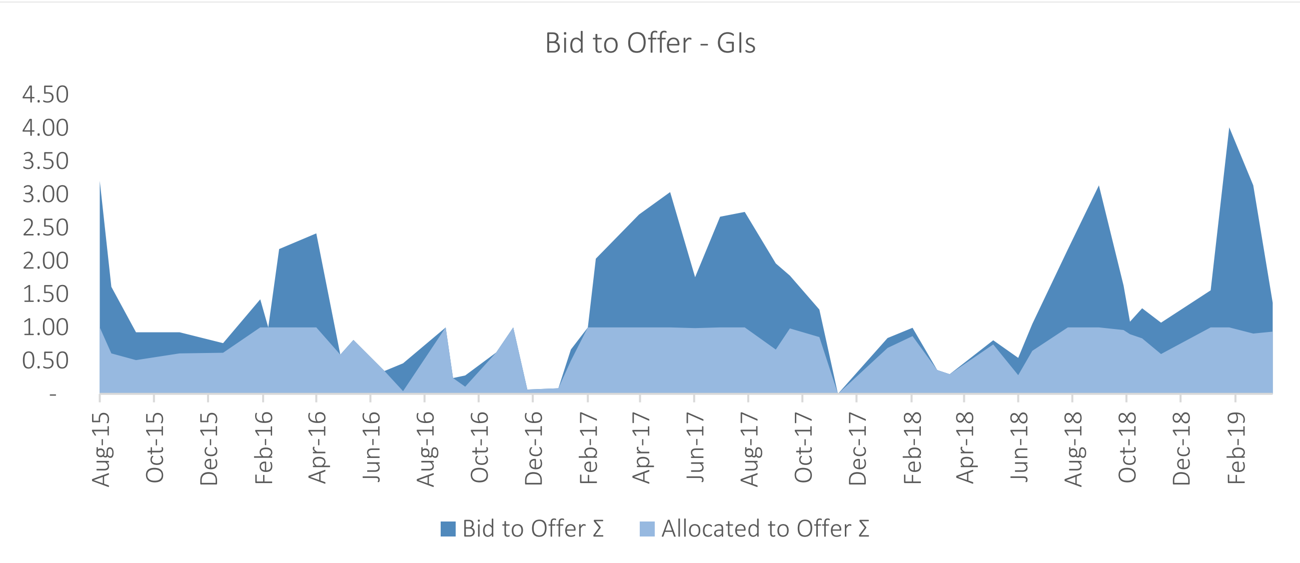
Source: BoN, IJG

South African benchmark yields declined over the first quarter of 2019. However, Namibian yields declined more as the spread between Namibia and South Afica also contracted.



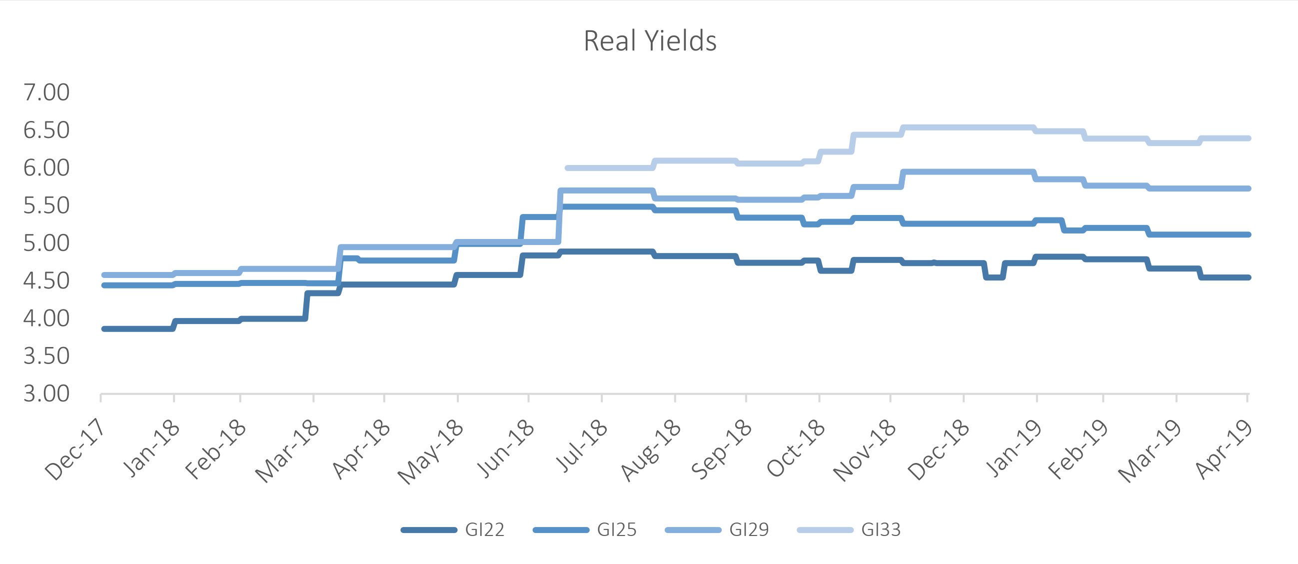
Source: Bloomberg, IJG Securities

Similarly, demand for inflation linked bonds has been quite high. The inflation linked auctions also saw a revival of demand at the beginning of the year. On average GI auctions have been 2.5x oversubscribed. Given the declines in spread on the GC bonds, GIs have become quite attractive on a relative basis.



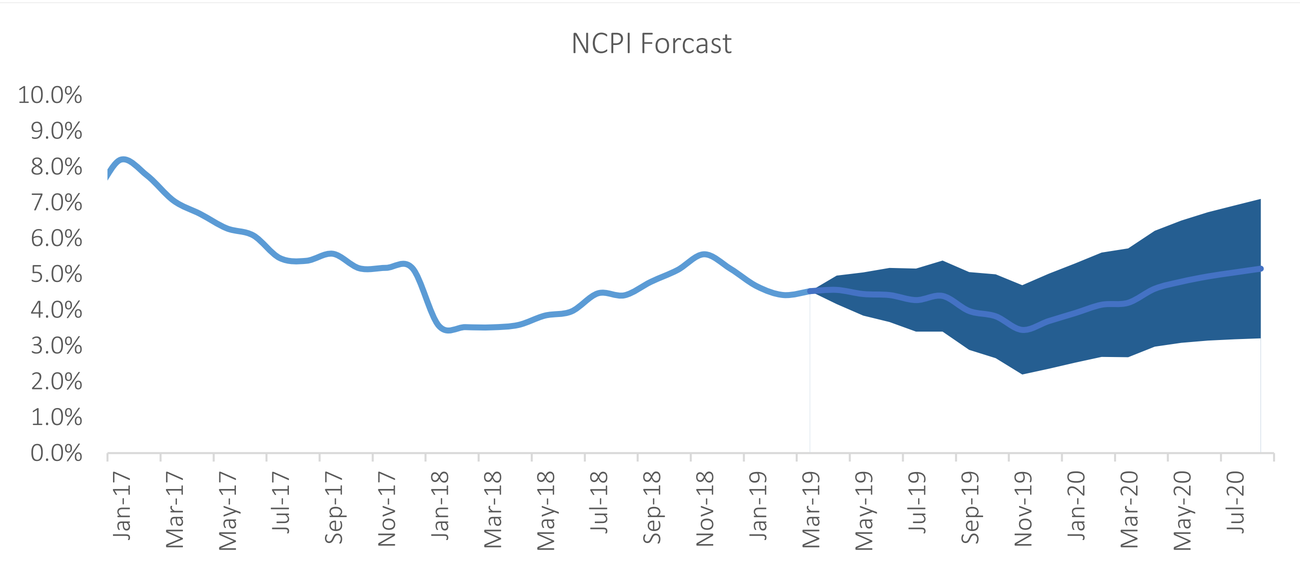
Source: BoN, IJG

The increase in demand resulted in yields declining slightly, although not by much. Real yield in Namibia also remains very attractive when compared with the South African counterparts, which yield between 2.8% and 3.3%, depending on maturity.



Source: BoN, IJG

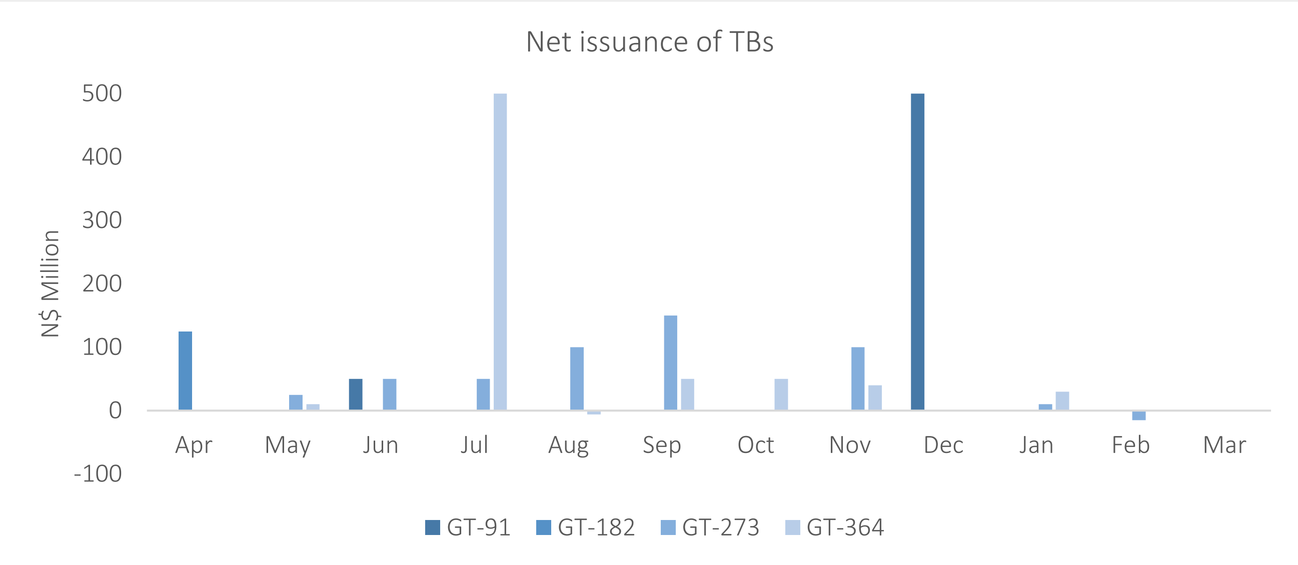
Namibian CPI is expected to remain subdued for over the next twelve months. However, increasing oil prices, and resultant increases in Namibian petrol prices remain a catalyst for inflation and risks remain skewed to the upside. As a result, GI bonds may be a lucrative play if one expects inflation to accelerate in the near term. The IJG model currently expects inflation to average 4.2% in 2019. Bank of Namibia forecasts inflation to average 4.7% in 2019.



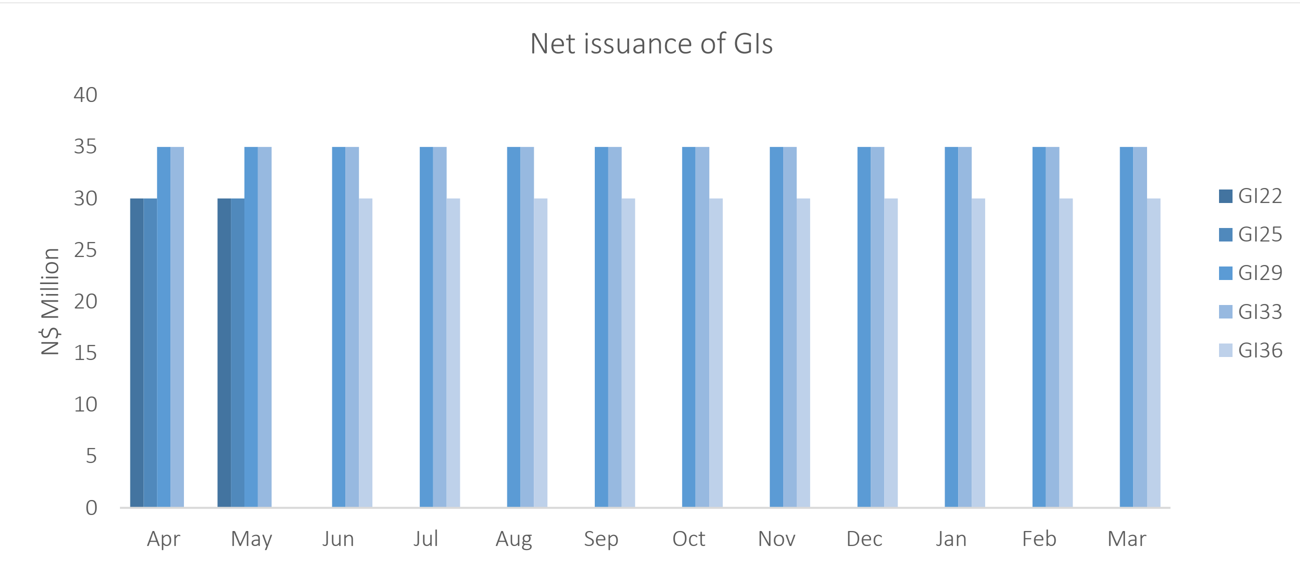
Source: NSA, IJG

Borrowing Plan

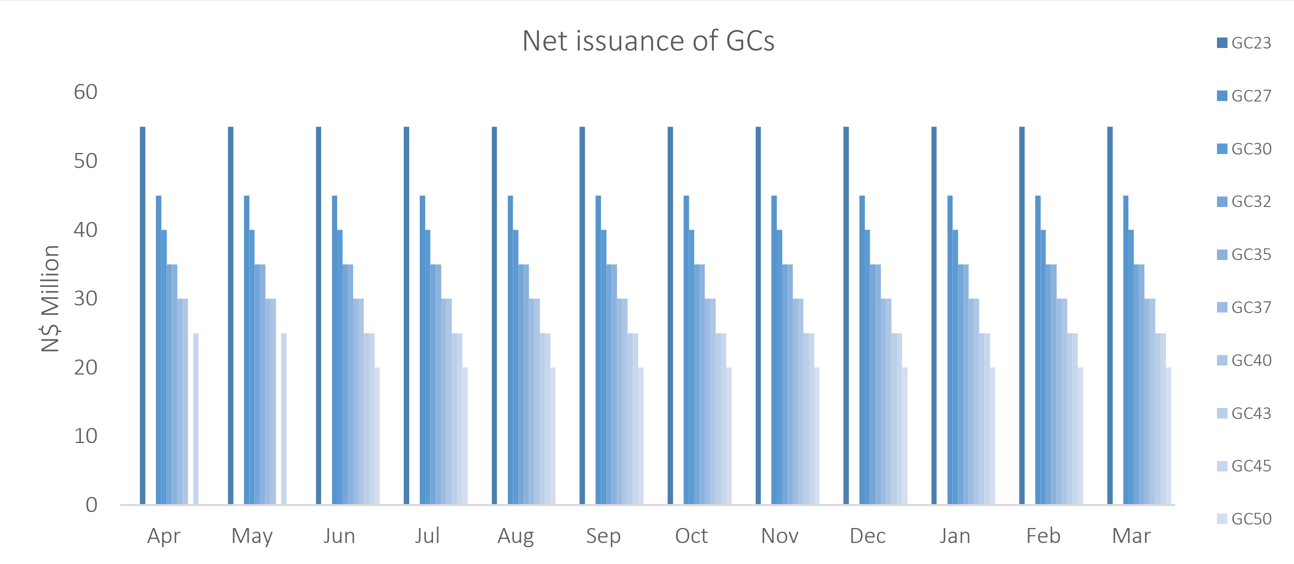
According to the Bank of Namibia's borrowing plan, the borrowing requirement for FY2019/20 amounts to N$10.1 billion, roughly N$900 more than the amount announced in the budget. Of this amount, N$7.1 billion will be raised domestically while the remaining amount of N$3.0 billion is to be sourced from regional markets. The N$7.1 billion will be raised via N$1.8 billion of treasury bills ("TBs"), N$1.3 billion of inflation linked bonds ("GIs") and N$4.0 billion of fixed rate bonds ("GCs").



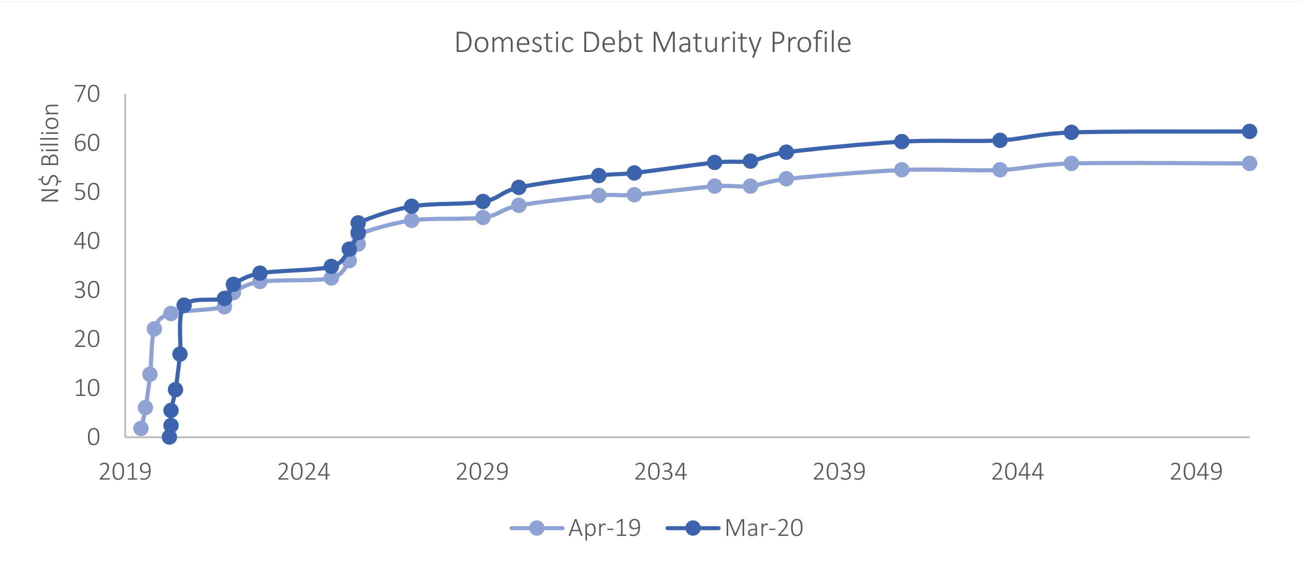
TBs will make up 26% of the borrowing requirement and N$1.0 billion of this will be raised through two tranches of new 91-day and 364-day paper, amounting to N$500 million each. The rest will be raised on increasing the issuance of existing treasury bills, while the existing balances on TBs will be rolled on a continuous basis.



N$1.3 billion, or 18% of the borrowing requirement, worth of inflation linked bonds will be issued in the current financial year. The GI22 and GI25 will only be on offer until May, after which they will be off the run. From June, the GI36, a new inflation linked bond will be on offer instead.



The remaining N$4.0 billion will be raised using fixed rate bonds. This represents 56% of net domestic borrowing. The shorter dated bonds namely the GC20 and GC25 will no longer be issued while two new GC bonds will be offered instead. The GC43 and GC50 will be issued for the first time in June.



As a result of the concerted effort to lengthen the average maturity of domestic debt, the debt maturity profile, which is already very steep up to 2025, will luckily not become any steeper. Additionally, the rolling out of GC20 and GC21 using switch auctions will further aide in this endeavor. Although increasing the duration of government debt will undoubtably lead to a higher cost of funding, this reduces the amount of roll risk. Given the numerous large maturities between 2021 and 2025, which includes two foreign currency Eurobonds, the maturity profile still remains quite daunting. However the acknowledgement of this risk and the steps taken to manage it has been quite a welcome development.

Instrument	Closing Date	Issue Date	Due Date
May-19			
IRS	Thursday, 02 May, 2019	Friday, 03 May, 2019	
273-day TB	Thursday, 02 May, 2019	Friday, 03 May, 2019	Friday, 31 January, 2020
364-day TB	Thursday, 09 May, 2019	Friday, 10 May, 2019	Friday, 08 May, 2020
IRS	Wednesday, 15 May, 2019	Thursday, 16 May, 2019	
273-day TB	Thursday, 16 May, 2019	Friday, 17 May, 2019	Friday, 14 February, 2020
G20 Switch Auction	Wednesday, 22 May, 2019	Thursday, 23 May, 2019	
91-day TB	Thursday, 23 May, 2019	Friday, 24 May, 2019	Friday, 23 August, 2019
182-day TB	Thursday, 23 May, 2019	Friday, 24 May, 2019	Friday, 22 November, 2019
364-day TB	Thursday, 23 May, 2019	Friday, 24 May, 2019	Friday, 22 May, 2020
ILBs	Wednesday, 29 May, 2019	Friday, 31 May, 2019	
273-day TB	Thursday, 30 May, 2019	Friday, 31 May, 2019	Friday, 28 February, 2020
Jun-19			
IRS	Wednesday, 05 June, 2019	Thursday, 06 June, 2019	
91-day TB	Thursday, 06 June, 2019	Friday, 07 June, 2019	Friday, 06 September, 2019
Book Closure (GC22, GI25, GC27, GI29, GC30, GC35, GC37 & GC45)	Friday, 14 June, 2019		
182-day TB	Thursday, 13 June, 2019	Friday, 14 June, 2019	Friday, 13 December, 2019
IRS	Wednesday, 19 June, 2019	Thursday, 20 June, 2019	
273-day TB	Thursday, 20 June, 2019	Friday, 21 June, 2019	Friday, 20 March, 2020
364-day TB	Thursday, 20 June, 2019	Friday, 21 June, 2019	Friday, 19 June, 2020
ILBs	Wednesday, 26 June, 2019	Thursday, 27 June, 2019	
Jul-19			
364-day TB	Thursday, 04 July, 2019	Friday, 05 July, 2019	Friday, 03 July, 2020
IRS	Wednesday, 10 July, 2019	Thursday, 11 July, 2019	
91-day TB	Thursday, 11 July, 2019	Friday, 12 July, 2019	Friday, 11 October, 2019
Coupon Payments (GC22, GI25, GC27, GI29, GC30, GC35, GC37 &GC45)	Monday, 15 July, 2019		
IRS	Wednesday, 17 July, 2019	Thursday, 18 July, 2019	
182-day TB	Thursday, 18 July, 2019	Friday, 19 July, 2019	Friday, 17 January, 2020
273-day TB	Thursday, 18 July, 2019	Friday, 19 July, 2019	Friday, 17 April, 2020
364-day TB	Thursday, 18 July, 2019	Friday, 19 July, 2019	Friday, 17 July, 2020
ILB	Wednesday, 24 July, 2019	Thursday, 25 July, 2019	
91-day TB	Thursday, 25 July, 2019	Friday, 26 July, 2019	Friday, 25 October, 2019
182-day TB	Thursday, 25 July, 2019	Friday, 26 July, 2019	Friday, 24 January, 2020

Instrument	Closing Date	Issue Date	Due Date
Aug-19			
182-day TB	Thursday, 01 August, 2019	Friday, 02 August, 2019	Friday, 31 January, 2020
272-day TB	Thursday, 01 August, 2019	Friday, 02 August, 2019	Thursday, 30 April, 2020
364-day TB	Thursday, 01 August, 2019	Friday, 02 August, 2019	Friday, 31 July, 2020
GC20 Switch Auction	Wednesday, 07 August, 2019	Thursday, 08 August, 2019	
IRS	Wednesday, 14 August, 2019	Thursday, 15 August, 2019	
182-day TB	Thursday, 15 August, 2019	Friday, 16 August, 2019	Friday, 14 February, 2020
273-day TB	Thursday, 15 August, 2019	Friday, 16 August, 2019	Friday, 15 May, 2020
IRS	Wednesday, 21 August, 2019	Thursday, 22 August, 2019	
91-day TB	Thursday, 22 August, 2019	Friday, 23 August, 2019	Friday, 22 November, 2019
273-day TB	Thursday, 22 August, 2019	Friday, 23 August, 2019	Friday, 22 May, 2020
364-day TB	Thursday, 22 August, 2019	Friday, 23 August, 2019	Friday, 21 August, 2020
ILBs	Wednesday, 28 August, 2019	Thursday, 29 August, 2019	
Sep-19			
IRS	Wednesday, 04 September, 2019	Thursday, 05 September, 2019	
91-day TB	Thursday, 05 September, 2019	Friday, 06 September, 2019	Friday, 06 December, 2019
Book Closure (GC20, GC21, GI22, GC23, GC24, GC25, GC32, GI33 & GC40)	Friday, 13 September, 2019		
IRS	Wednesday, 18 September, 2019	Thursday, 19 September, 2019	
91-day TB	Thursday, 19 September, 2019	Friday, 20 September, 2019	Friday, 20 December, 2019
182-day TB	Thursday, 19 September, 2019	Friday, 20 September, 2019	Friday, 20 March, 2020
273-day TB	Thursday, 19 September, 2019	Friday, 20 September, 2019	Friday, 19 June, 2020
ILBs	Wednesday, 25 September', 2019	Thursday, 26 September, 2019	
364-day TB	Thursday, 26 September, 2019	Friday, 27 September, 2019	Friday, 25 September, 2020

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