Namibia Capital Market
Fixed Income Analysis
April 2020

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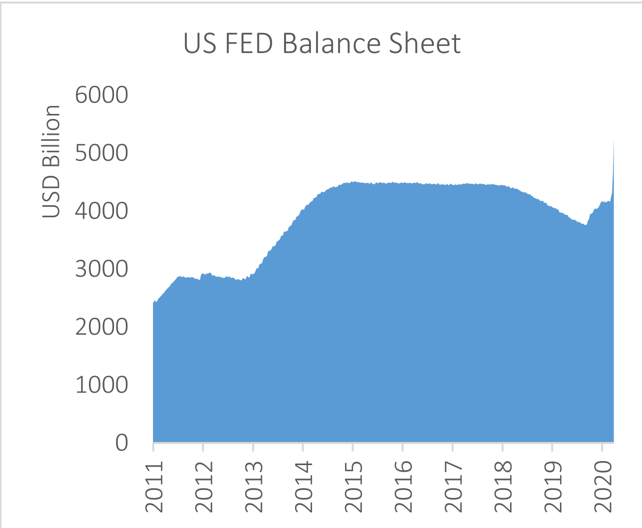
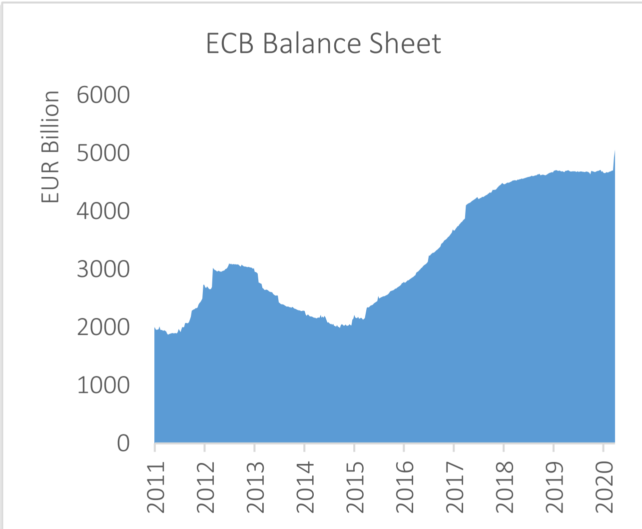
Global Macro

Since the beginning of 2020 a lot has changed. COVID-19 has transformed from a news story somewhere on the other side of the world into a global pandemic affecting the lives of nearly every person on the planet. The impact on the global economy is expected to be one of the largest shocks on record as both demand and supply sides have been severely disrupted following global lockdowns and travel restrictions. Expectations of modest growth in 2020 have been replaced by a range of views, where the base case varies between 0% to 1.6% global real GDP growth. However, there seems to be little consensus on how severe the slowdown will be as the duration of the disruption remains unknown. Additionally, the virus will have different impacts on different parts of the globe, and it is highly likely that many emerging markets will find it difficult to contain and suffer the worst burnt of the shock.

Most countries have turned aggressively to expansionary monetary policy. Central banks have launched massive programs for asset purchases, and financial regulators have eased requirements to allow banks to continue to support customers in distress and the economy more broadly. This has released a massive amount of liquidity into the system, and interest rates in the developed world have never been lower. The US is back at the 0% lower bound for the Fed target rate, and the market expects it to remain there for at least another two years. This is combined with unlimited and open-ended asset purchases. The European Union have kept their negative rates steady while introducing massive amounts of assets purchases, most notably, the "bazooka" Pandemic Emergency Purchase Programme (PEPP) which will add €750 billion to the European Central Bank's already enlarged Balance Sheet, on top of the already existing QE programme.



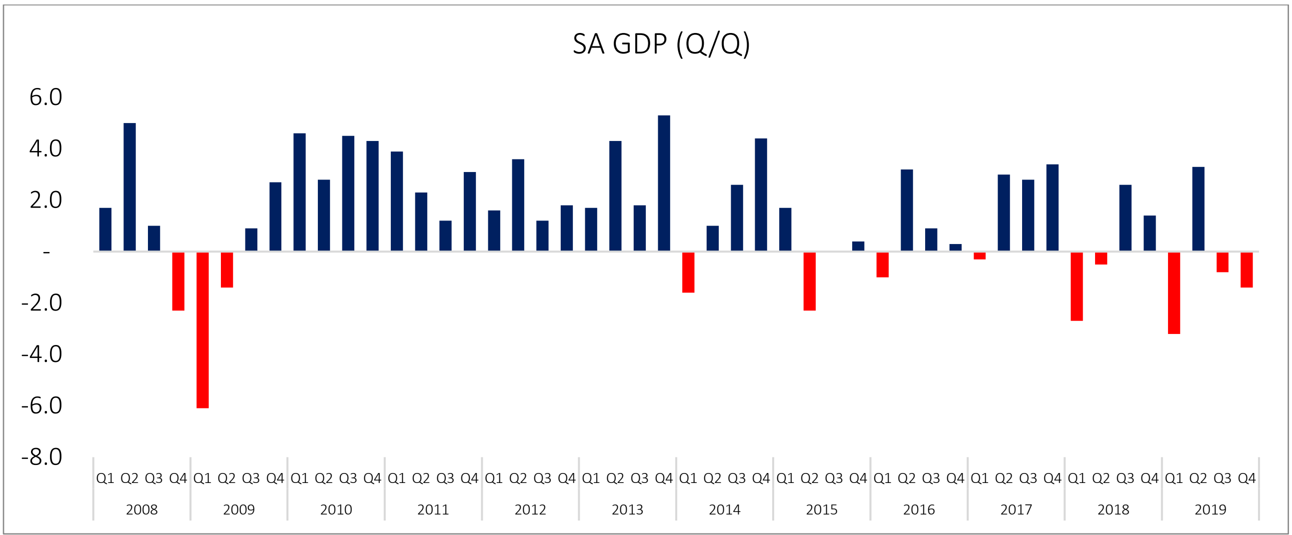


Source: Bloomberg

This monetary easing had been combined with various fiscal measures, The U.S. Senate passed a US$2 trillion stimulus package including a US$500 billion fund to help hard-hit industries and a comparable amount for direct payments of up to US$3,000 apiece to millions of U.S. families. Many more countries have implemented similar measures, including the suspension of loan and mortgage repayments for companies and households. Clearly, we live in extraordinary times.

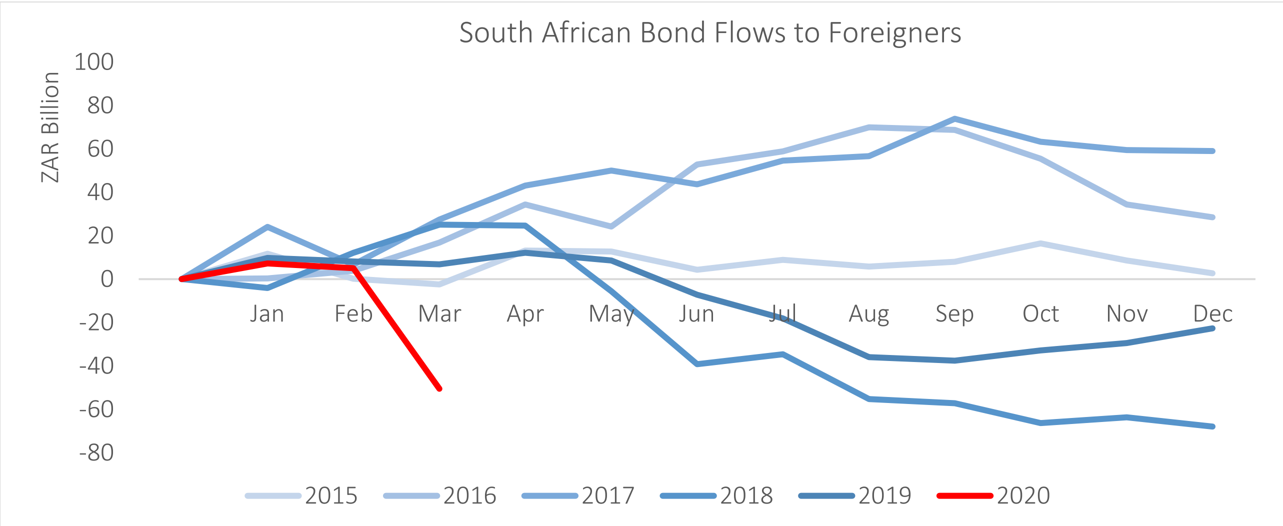
South Africa

The South African economy was already on poor footing when this crisis hit. Pre-COVID expectations were for a meagre 0.8% real growth. However, severe lockdown measures have strangled an already fragile economy into certain contraction, with initial estimates pointing to a roughly 7% drop in GDP for 2020. Given an already poor outlook for debt to GDP, the crisis is set to see South Africa surpass the 80% level by 2025.



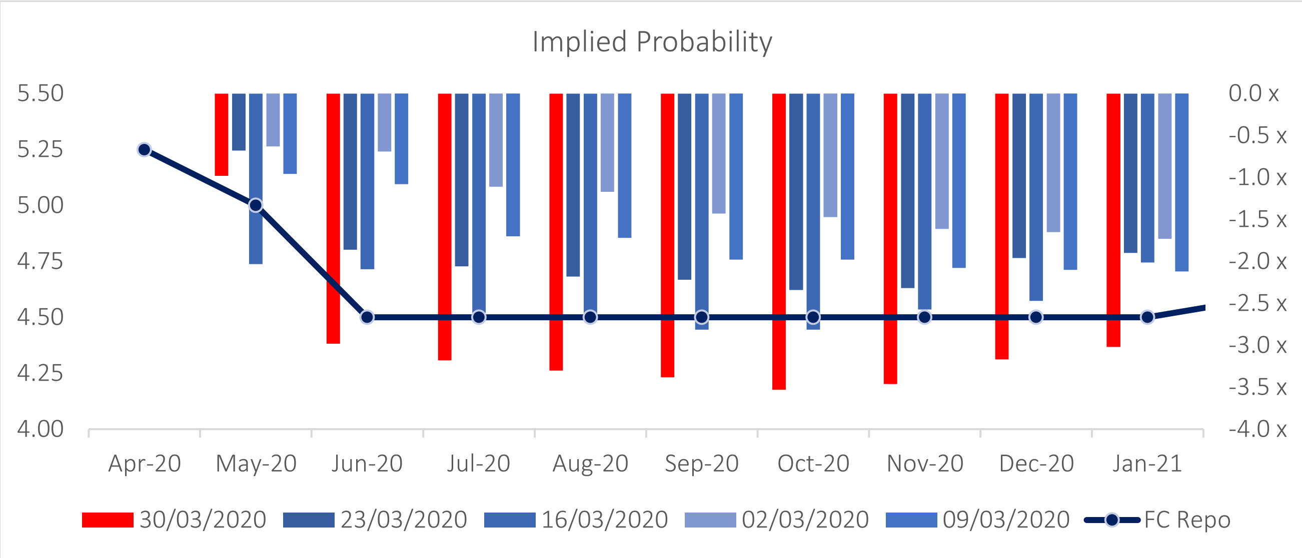
Source: StatsSA

Moody's downgraded South Africa's long-term foreign-currency and local-currency issuer ratings to Ba1 from Baa3 with a negative outlook late in March. Although Moody's downgrade made passing reference to the rapid spread of the coronavirus outbreak, it spoke more to the fundamental factors at play like the weak business confidence, low investment, unreliable electricity supply and high wage bill which continue to constrain economic growth.



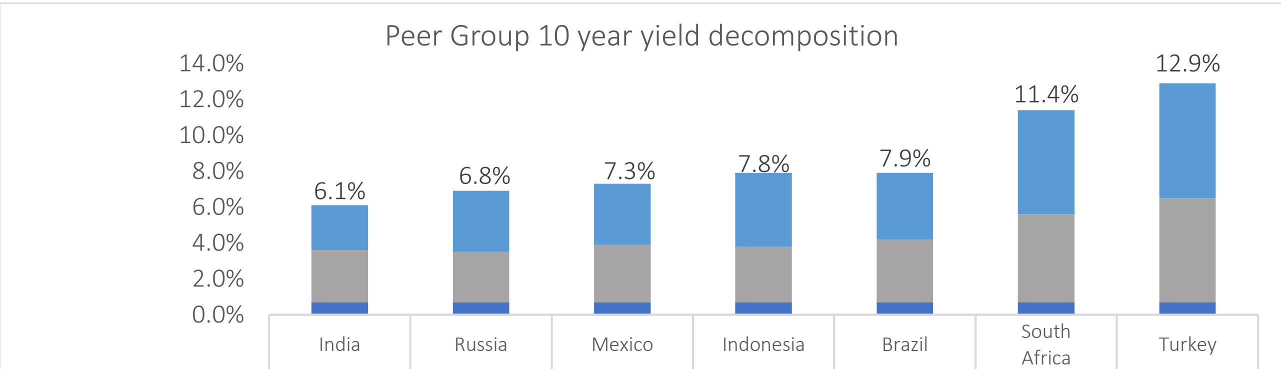
Source: Bloomberg, IJG

Foreigners sold off roughly ZAR 55.6 billion in March, bringing the year's cumulative outflow to ZAR 50.5 billion. Over the same period, the rand depreciated from about 14.01 to the US dollar to 17.84 by the end of the quarter, with most of the depreciation happening in March. Yields on the benchmark curve spiked drastically. The South African R2030, saw its yield increase by 193 basis points from 9.02% to 10.95%. The rest of the curve moved by an average of 131 bps, with the belly of the curve seeing the largest upward shift in yield. It should be noted, however, that South Africa will remain part of the World Government Bond Index until it is reconstituted. The rebalancing of this index has been postponed to the end of April. This means that there is still a large amount of bonds that will need to be sold out of in May, which could put further pressure on both yields and the currency.



Source: Bloomberg, IJG

The South African reserve bank responded strongly to the crisis in March. Firstly the repo rate was cut by 100 basis points, one of the largest reductions ever, dropping to 5.25% from 6.25% in a unanimous decision by the MPC. Most economists were expecting a cut of 50 basis points. Following this, the SARB stepped up its measures to ensure liquidity in the banking sector by providing lenders with cheaper access to funding and reorganising the way it injects liquidity into the financial system. The standing facilities borrowing rate was cut by 100 basis points to repo minus 2%, while the size and duration of repo auctions were increased to improve money market instrument liquidity. In its most unprecedented move, the SARB announced the purchase of government bonds on the secondary market, to support yields and inject further liquidity. Currently, another 75bps of repo rate cuts are expected in South Africa, as priced into the forward rate agreement market, which currently expects the repo rate at 4.5% for most of 2020.



	India	Russia	Mexico	Indonesia	Brazil	South Africa	Turkey
Currency Risk Premium	2.5%	3.4%	3.4%	4.1%	3.7%	5.8%	6.4%
Sovereign Risk Premium	2.9%	2.8%	3.2%	3.1%	3.5%	4.9%	5.8%
US 10 Year Yield	0.7%	0.7%	0.7%	0.7%	0.7%	0.7%	0.7%

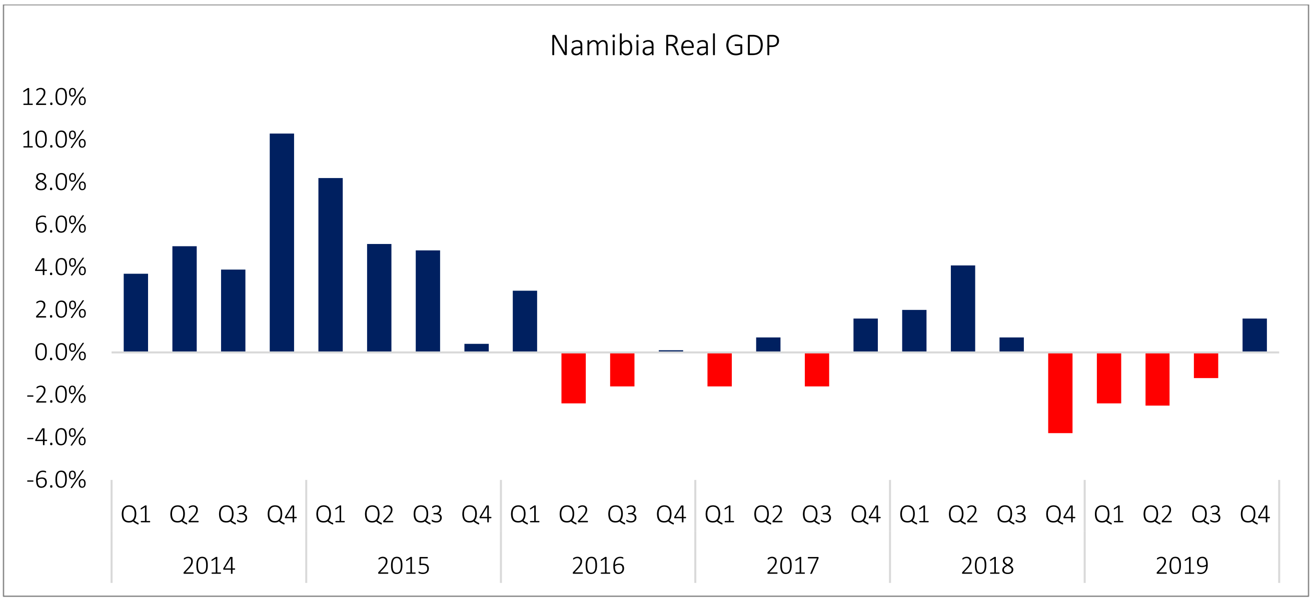
US 10 Year Yield · Sovereign Risk Premium · Currency Risk Premium

Source: Prescient investment management, Bloomberg

South African yields are well above the emerging market peer group, save for Turkey, which is yielding 1.5% more. However, decomposing the generic 10-year yields into sovereign and currency risk highlights the fact that a large portion of the South African yield is due to heightened currency risk compared to emerging market peers. However, South Africa, and by extension, Namibia's yields seem quite attractive compared to the rest of the emerging world.

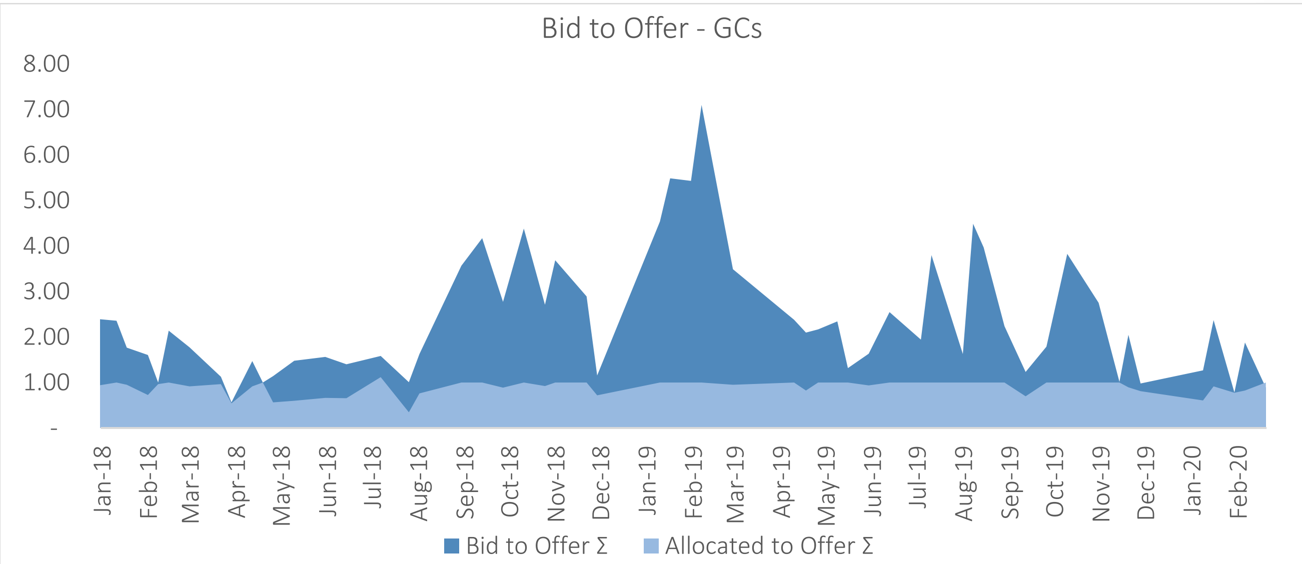
Namibia

Namibia has found itself in a strikingly similar position as South Africa. With an already frail economy, which has seen very little growth since 2016 and a steadily climbing unemployment rate, the corona pandemic has come at a particularly inopportune time. Expectations of moderately positive growth have also been replaced by a severe contraction, although the extent of the contraction will still have to be gauged, preliminary calculations point to a contraction of at least 3% for 2020.



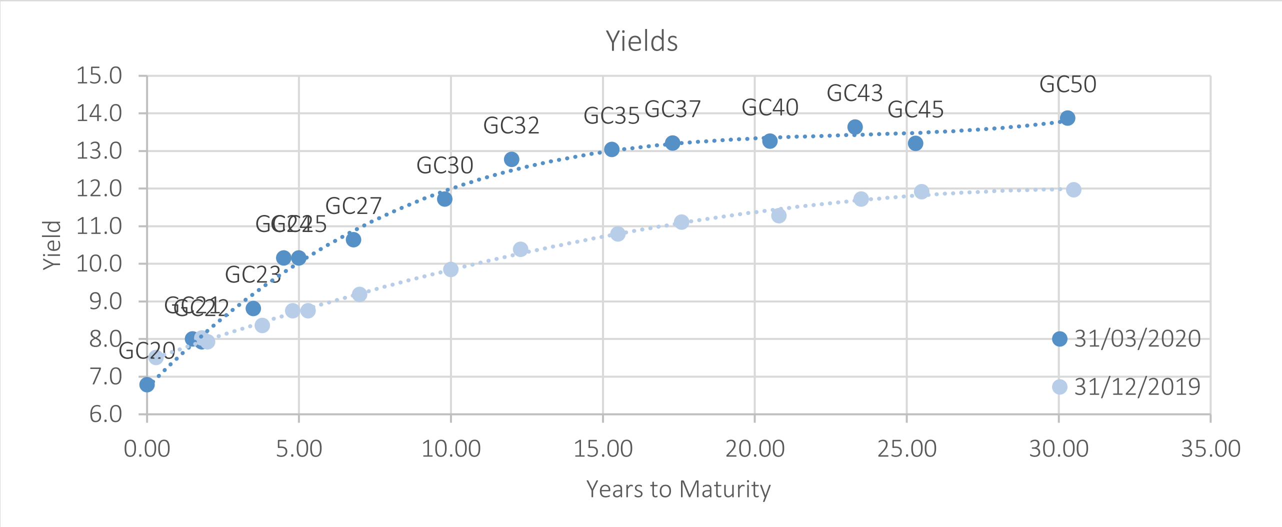
Source: NSA, IJG

Monetary policy was quick to react, following the South African repo rate lower with 100 basis points, while banking regulation has been relaxed to encourage lending to vulnerable sectors of the economy. Certain banks have offered payment holidays to cash strapped industries like tourism and hunting. On top of this, the government has announced an N$8.1 billion stimulus package (comprised of N$5.9 billion in direct support and N$2.3billion in contingent liabilities) which aims to keep corporations and households afloat during a 21-day lockdown of the Khomas and Erongo regions. The N$5.9 billion stimulus package and 3% in contraction alone would see our debt to GDP increase from 51% to 57%.



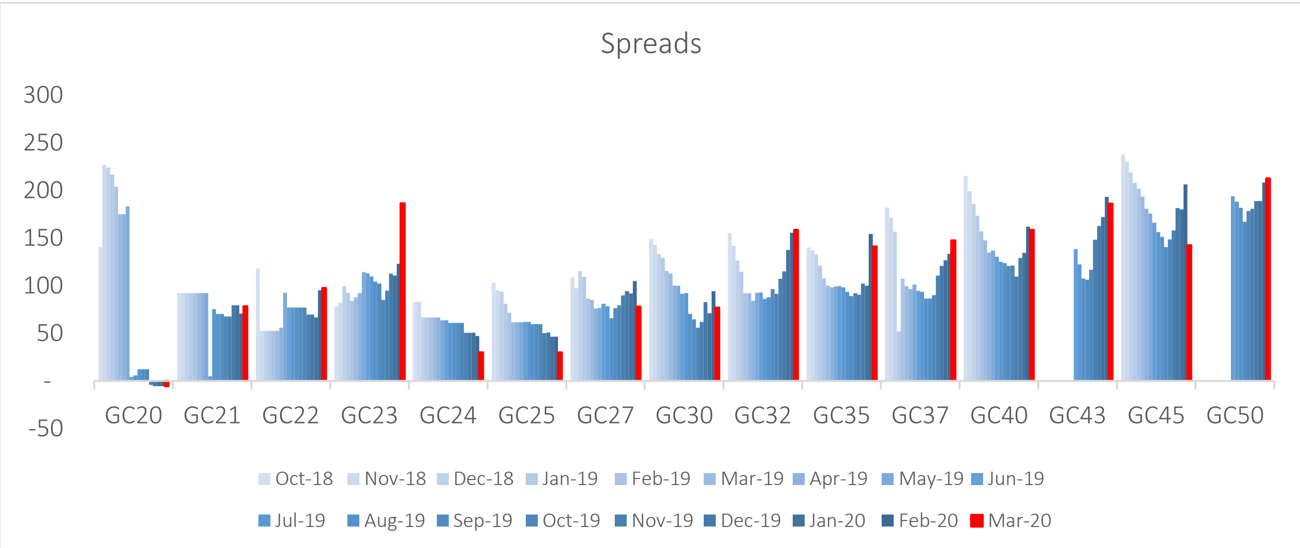
Source: BoN, IJG

Up until the beginning of March, the demand for government bonds has been decent, although we have seen a few undersubscribed auctions. Seeing as the last auction happened on the 4th of March, before much of the market moves happened, we expect to see increased demands on auctions going forward as we believe yields should be enticing, especially to local currency investors. We have already seen demand on the South African auctions pick up



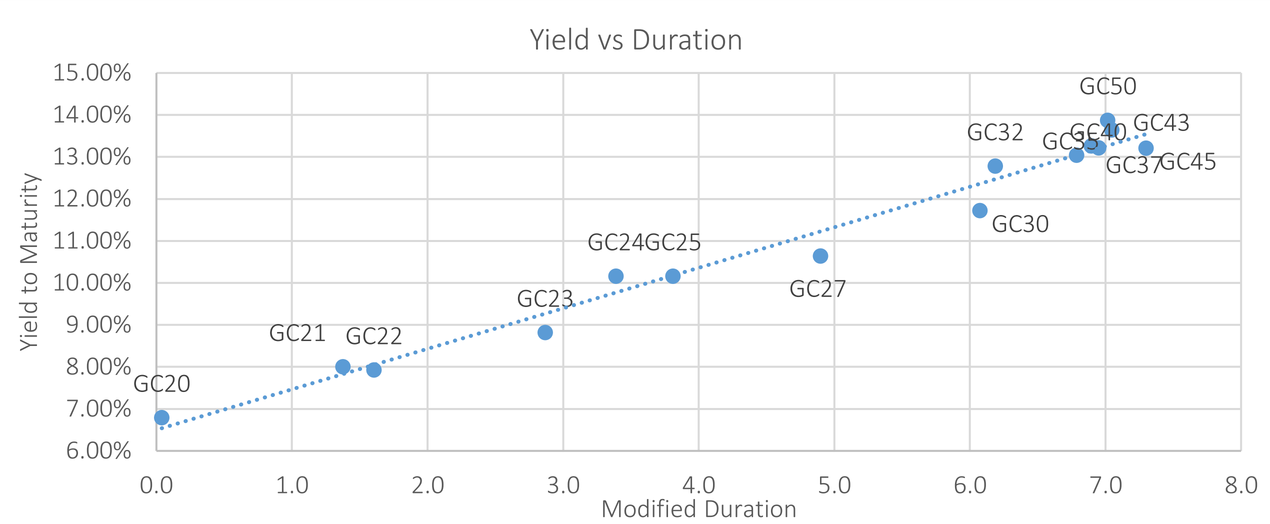
Source: IJG

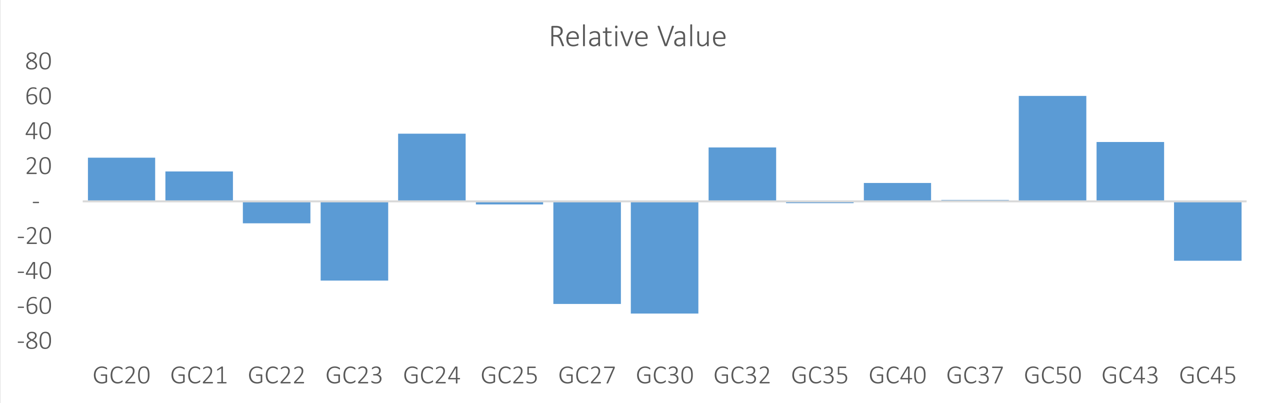
Lower short term rates have led to the short end of the curve being anchored at a lower rate than the start of the year. However, the rest of the curve has moved higher on the back of higher benchmark rates in South Africa. The shift has not been equal, and the belly of the curve has seen more of an increase than the rest of the curve.



Source: BoN, IJG

Spreads have increased on the short end and the long end of the curve, while spreads on the GC24 to GC30 have decreased since the start of the year. The exception being the GC45 which saw its spread contract by 39 basis points. We expect to see renewed interest at auctions in coming months as yields have risen substantially. As a result, we would expect to see downward pressure on spreads again.



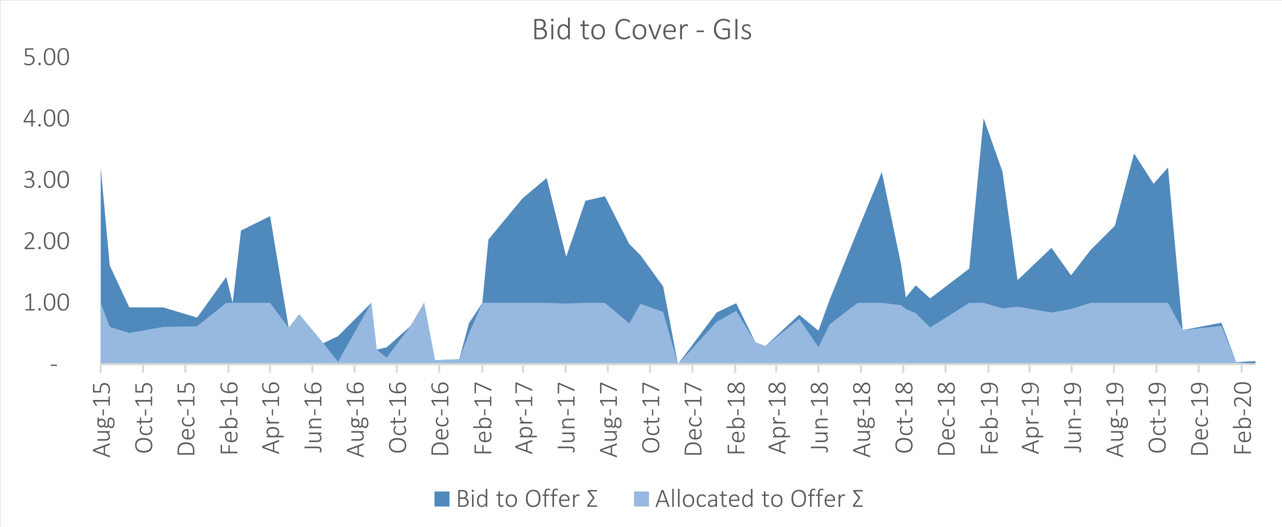


Source: IJG Securities

On a duration adjusted basis, we see relative value in the longer-term issues like the GC40, GC43 and GC50. This has also normally been the worst bid part of the curve and offers an opportunity on the primary auctions. The GC27 and GC30 seem to be the most overbought, as can be witnessed in their spread compression over the last three months.

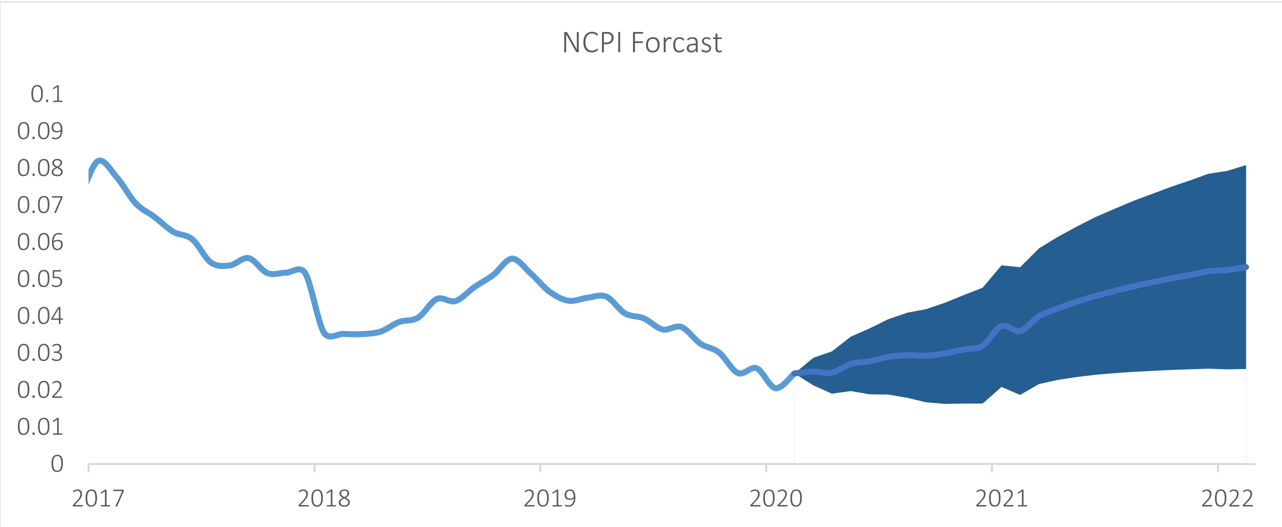
The GC32 seems to be relatively attractive and the GC21 also seems attractive, although off the run, relative to 365-day treasury bills, which are yielding 6.58%. The two off the run bonds, the GC21 and GC24 also show some value at their current yields.

Inflation-Linked Bonds



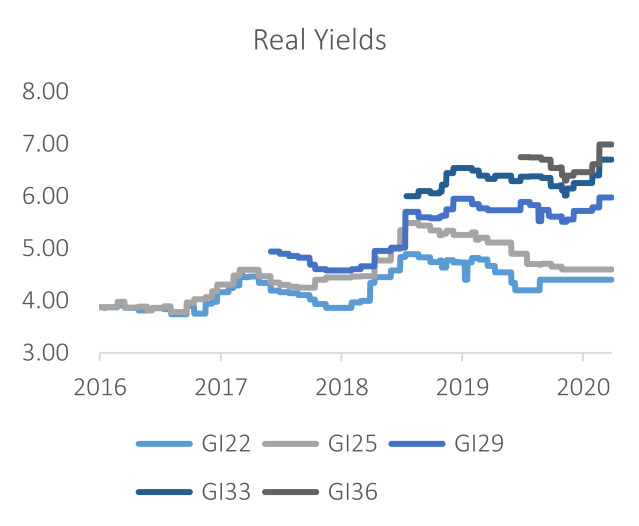
Source: BoN, IJG

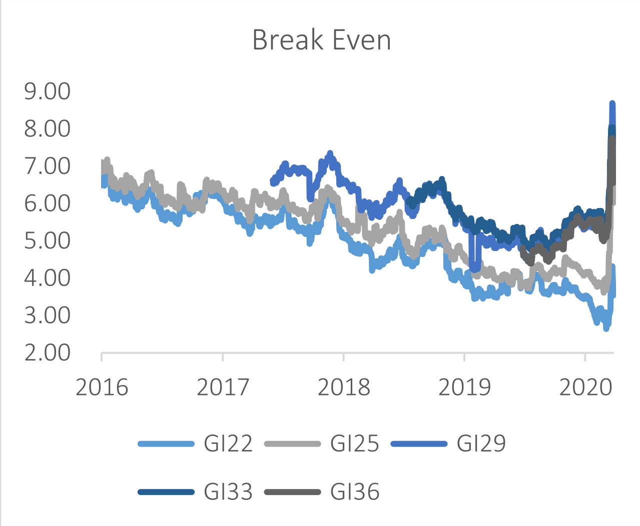
Demand for inflation-linked bonds has dropped significantly. The last auction held on the 18th of March saw only N$6 million in bids and zero allocated. This is likely due to the low inflation expectations over the next two years driven by much lower oil prices and deflation in rental prices. As well as this it is likely that BoN will not issue these bonds at much higher yields than the last traded yields.



Source: NSA, IJG

Over the last three months real yields have increased by 25bps, 45bps and 53bps on the GI29, GI33 and GI36 respectively. However, compared to the sharp increase in yields on nominal bonds, the break-even inflation rate on many of these bonds have increased sharply and a much higher real yield will be required to make these offers attractive relative to their nominal peers.





Source: BoN, IJG

The two shorter off the run bonds show the most value, however, this is due to the steep nominal curve and short term rates declining. Based on a long term expected inflation rate of 4.5%, the on-the-run bonds will have to see their real yields rise to over 9% to make them attractive relative to a nominal bond with similar duration.

Auction Calendar

Instrument	Closing Date	Issue Date	Due Date
Apr-20			
364-day TB	Thursday, 02 April, 2020	Friday, 03 April. 2020	Friday. 02 April, 2021
91-day TB	Wednesday, 08 April, 2020	Thursday, 09 April, 2020	Thursday, 09 July, 2020
IRS & ILBs	Tuesday, 14 April, 2020	Wednesday. 15 April, 2020	
coupon payments (GC20. GC21, G122, GC23. GC24, GC25, GC32. GI33 « GC40)	Wednesday, 15 April, 2020		
GC20 Redemption	Wednesday. 15 April, 2020		
182-day TB	Thursday, 16 April, 2020	Friday, 17 April, 2020	Friday, 16 October, 2020
273-day TB	Thursday, 16 April, 2020	Friday, 17 April. 2020	Friday, 15 January, 2021
91-day TB	Thursday, 23 April, 2020	Friday, 24 April. 2020	Friday. 24 July, 2020
182-day TB	Thursday, 23 April, 2020	Friday, 24 April, 2020	Friday, 23 October, 2020
364-day TB	Thursday, 23 April, 2020	Friday, 24 April. 2020	Friday, 23 April, 2021
274-day TB	Wednesday. 29 April 2020	Thursday, 30 April. 2020	Friday, 29 January, 2021
May-20			
IRS	Wednesday, 06 May, 2020	Thursday, 07 May, 2020	
364-day TB	Thursday, 07 May, 2020	Friday, 08 May, 2020	Friday, 07 May, 2021
IRS	Wednesday, 13 May, 2020	Thursday, 14 May, 2020	
273-day TB	Thursday, 14 May, 2020	Friday, 15 May, 2020	Friday, 12 February, 2021
91-day TB	Wednesday. 20 May, 2020	Friday, 22 May. 2020	Friday, 21 August, 2020
182-day TB	Wednesday. 20 May, 2020	Friday, 22 May. 2020	Friday, 20 November. 2020
364-day TB	Wednesday, 20 May, 2020	Friday, 22 May, 2020	Friday, 21 May, 2021
ILBs	Wednesday, 27 May, 2020	Friday, 29 May, 2020	
273-day TB	Thursday. 28 May, 2020	Friday, 29 May. 2020	Friday, 26 February, 2021
Jun-20			
IRS	Wednesday, 03 June, 2020	Thursday, 04 June, 2020	
91-day TB	Thursday. 04 June, 2020	Friday, 05 June. 2020	Friday, 04 September. 2020
182-day TB	Thursday, 11 June, 2020	Friday, 12 June, 2020	Friday, 11 December, 2020
273-day TB	Thursday. 11 June, 2020	Friday, 12 June. 2020	Friday, 12 March. 2021
Book Closure (GC22. GI25, GC27, GI29, GC30. GC35, GI36, GC37, GC43 & GC45)	Monday. 15 June, 2020		
GC21 Switch Auction	Wednesday, 17 June, 2020	Thursday, 18 June. 2020	
91-day TB	Thursday. 18 June, 2020	Friday, 19 June. 2020	Friday, 18 September. 2020
273-day TB	Thursday, 18 June, 2020	Friday, 19 June, 2020	Friday, 19 March, 2021
364-day TB	Thursday. 18 June, 2020	Friday, 19 June. 2020	Friday, 18 June, 2021
ILBs	Wednesday. 24 June, 2020	Thursday, 25 June, 2020	

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