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African Markets Revealed

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Ruth Everard-Haden, (1904 – 1992). Landscape In Natal, Undated, Oil On Canvas, 74.5x95.5cm

Ruth and Rosamund Everard were the daughters of Bertha Everard, who with Bertha's sister Edith King, made up the remarkably creative family of women painters who lived in Mpumalanga (formerly Eastern Transvaal) during the first half of the 20th Century and became known as the Everard group. Isolated from artistic communities and living in a rural location, the extraordinary output has only recently received renewed attention and their significant contribution to South Africa art history acknowledged. Ruth was the first daughter of her artistic mother, Bertha Everard and was born in 1904 at Nottingham Road in KwaZulu-Natal.

Ruth worked in oil and watercolour to produce mainly landscapes, in addition to still life and portraits. Ruth was influenced by the new movements in European art such as Cubism, Vorticism, Futurism and the work of earlier Expressionist painters. Her work is confident, bold and controlled using simple outlines to convey shape and format. She stopped painting in 1956 because of failing eyesight. She exhibited her work in South Africa through the 1930s, 40s and 50s participating in the Everard Group exhibitions of 1931 and 1935, the Overseas Exhibition of South African Art which toured from 1948 to 1950 and the historical exhibitions to mark van Riebeeck's Tercentenary in 1952 and Pretoria's Centenary in 1955.

Source: Standard Bank Corporate Art Collection

Back to the future

- We have come full circle. The African economic narrative of the past two to three years was heavily weighted towards the FX supply problems that some economies experienced. Given that these problems are largely behind us, we argue that the overriding narrative will likely revert to the structural reforms that many of these economies need to undertake. Take Nigeria for instance. Rising oil prices is a double-edged sword for the economy. Even as rising oil implies that the BOP pressures that the economy faced will ebb, rising oil also exposes weaknesses in the fuel pricing mechanism, something that led to fuel shortages towards the end of 2017.
- We also argue that FX rationing amounts to devaluation by stealth. In contrast to conventional devaluation, such rationing actually restrains economic growth.
- Of course, devaluation was not available to any of the members of the Central African Monetary and Economic Community (CEMAC) that use the XAF. The appropriate policy response for these economies should have been fiscal restraint to restore macroeconomic balance, something that hasn't quite happened. Rising oil prices may well bail out policymakers.
- Of the other currencies of commodity producers, the AOA has only just started being devalued. Policymakers could easily underestimate the magnitude of devaluation required to restore macroeconomic balance, with the risk that the economy would keep struggling to grow. The EGP was devalued rather belatedly, with the exchange rate floated as well. Arguably, although the Egyptian economy is still going through the adjustment process, it will break free from the shackles that hemmed growth to an average below 4.0% y/y since the Arab Spring. Similarly, the Nigerian economy is on the mend, structural deficiencies notwithstanding.
- There are probably very good reasons to sell deliverable USD at spot rather than forward in Mozambique. We can't come up with any. We even like selling USD/MZN NDFs. We are still happy with the carry in EGP, KES, GHS, NGN and ZMW.
- The local bid for NGN duration was strong towards the end of 2017. The trade might be worth another look early this year as the CBN will likely resume mopping up liquidity. We will keep EGP, GHS and ZMW duration in our shadow portfolio, even though the latter might lead to large mark-to-market swings.
- Global risk appetite will likely remain elevated, providing an environment conducive for African Eurobonds to continue rallying. We are overweight Angola, Ghana, South Africa, Zambia.

A more constructive global backdrop

The global backdrop to Africa's economic growth still looks very positive. The upward momentum in global economic growth will likely be sustained, creating a supportive environment for commodity prices. Additionally, the BOP problems that beset many of the continent's commodity-exporting countries are mostly behind us, thanks in part to recovering commodity prices and some bold policy measures taken in some countries. Admittedly, there are still signs of long-running structural deficiencies that would likely restrain the medium-term recovery path. But, overall, we still believe that the outlook for growth in Africa is positive.

Going by the IMF's Oct edition of the World Economic Outlook (WEO), global economic growth is likely to be edging towards 4.0% y/y by 2018. Specifically, the IMF forecasts global economic growth to be 3.7% y/y from what it estimates was 3.6% y/y in 2017 and 3.2% y/y in 2016. There were broad-based upward revisions in the euro zone, Japan, emerging Asia, emerging Europe and Russia, that more than offset downward revisions to forecasts for the US and the UK.

The Fund still pointed to a downside bias to the medium-term outlook despite the ongoing cyclical upturn. Among the key challenges that the Fund identified as needing to be tackled were policies to boost potential output, indicating that inflation remains

USD performance, Dec-16 to Jan-18

Asset class	Return, %
FX	
Africa 8, spot (with carry)	-0.2 (12.2)
Africa 10, spot (with carry)	2.4 (13.6)
EM 10, spot (with carry)	10.9 (17.0)
Bloomberg USD index, spot	-11.8
Local bonds	
Africa 8	33.4
Africa 10	21.4
EM 10	20.5
Bloomberg DM	9.2
Credit	
Africa (ex SA)	17.9
Africa	16.4
EMBI Global	9.1
Bloomberg Global HY Corporate	12.0
Equity	
MSCI Frontier Africa (ex SA)	29.8
MSCI Africa	41.4
MSCI EM	46.0
MSCI DM	27.5

Source: Bloomberg; Standard Bank Research

very low in a number of advanced economies. Nominal wage growth is markedly lower than in the period leading to 2008, due to a combination of productivity slowdown, low inflation expectations, and labour market slack.

The IMF's Oct forecast for Sub-Saharan Africa featured some downward revisions, compared to the Jan 17 WEO Update. It lowered the 2017 forecast by 0.2 percentage points (ppts) to 2.6% y/y and the 2018 forecast by 0.3 ppts to 3.4% y/y. It estimates growth in 2016 was 1.4% y/y. Nonetheless, broadly speaking, even the IMF's forecast confirms the essence of our narrative. There is a notable improvement in economic growth among the continent's commodity exporters.

We still maintain that there is a strong likelihood that economic growth will surprise to the upside. Specifically, the chances of a meaningful pickup in growth in the economies that have seen their currencies depreciate or be devalued sharply are very strong. Our contention remains that these economies' BOP challenges also restrained economic growth. This situation was exacerbated by the refusal of these countries' policymakers to devalue their currencies.

The significance of the appropriate currency adjustment following a BOP shock is perhaps clearest when one compares the experience of Mozambique and Zambia, with that of Egypt, Nigeria and Angola. Both the MZN and ZMW were allowed to depreciate sharply when global growth subsided in 2014/2015, depressing commodity prices as well. The upshot was that the hit to economic growth was much less than otherwise would have been. Even the complication of a debt crisis in Mozambique did not plunge that economy into recession, barely slowing down below 4.0% y/y in 2016 from an average of over 7.0% y/y in the prior 5-y.

The contrast with Angola and Nigeria could not be any starker. Both economies plunged into recession in 2016, and the recovery since has been tepid. Of course, while Nigerian policymakers finally devalued and segmented the NGN, their Angolan counterparts have only just begun to devalue the AOA. As a consequence, it seems very likely that growth in Nigeria will accelerate much faster than in Angola. Having said that, it is highly probable that the AOA will be devalued sufficiently to restore macroeconomic balance in that country, something that would ultimately boost economic growth.

Devaluation by stealth

In the Sep 17 edition of the *African Markets Revealed* we argued that African policymakers use a number of capital controls that render the FX market inefficient, thereby obviating the need for currency devaluations as would be predicted by models of balance of payments (BOP) crises. These models show how a fundamental macroeconomic imbalance ultimately leads to an abandonment of a currency peg. These models also show this outcome can eventuate as a self-fulfilling prophecy, even if there is no fundamental misalignment, or a policy pre-commitment to a fixed exchange rate.

At issue is a willingness of central banks to prevent commercial banks from quoting and trading FX at exchange rates that would clear the market once a BOP shock hits. Consequently, FX 'shortages' arise, something that precipitates a slump in economic activity.

But, what about those FX shortages? Is it enough to just note that they are a manifestation of market inefficiency?

There is more to it than just that, especially from the perspective of an importer in such an economy. What essentially transpires in such circumstances is a devaluation by stealth; highly inefficient, of course, leading to a slump in economic activity.

Why do we refer to prevalence of FX shortages as devaluations? Because of the time value of money. It is almost always the case that the FX rationing that prevails in these circumstances leads to FX being made available after significant delays. So, even though FX may be made available at the official exchange rate, FX buyers have to wait, sometimes very long periods, before obtaining that FX. In Nigeria an importer who has to wait two to three months to obtain FX from the CBN's FX auctions and ends up paying a USD/NGN rate of 340 is not saving much relative to the spot IEFX window rate of 355 – 365.

So, while a central bank may refuse to devalue a currency, it effectively achieves that by compelling FX buyers to wait to obtain that FX. Of course, this stealth devaluation is highly inefficient. It doesn't affect FX market players the same way, and ultimately leads to a disruption of economic activity, contrary to a conventional devaluation.

Commodity prices: rising trend de-emphasises structural reforms

Angola is perhaps the only country that is still experiencing FX problems. Even there policymakers are on the way to devaluing the currency significantly.

One of the notable developments of the past 6-m or so is that the rising trend in commodity prices has gathered momentum. In all likelihood, prices will rise further from current levels, especially given the brightening outlook for global growth. The copper price has eclipsed USD7,000/ton, and the upward momentum appears unlikely to end soon.

Oil prices are also seemingly on a rising trajectory. While our view was that the rising trend would elicit a supply response from US shale producers, this hasn't actually materialised thus far. With Brent seemingly heading above USD70.0/bbl and WTI settling in comfortably above USD60.0/bbl, it is no longer improbable that we would be speaking of USD80.0/bbl oil again.

Figure 1: Commodity prices are rising

Source: Bloomberg; Standard Bank Research

Such a rising trajectory will have considerable influence on economies of commodity (oil and metals) exporters. As we have maintained, BOP pressures will ebb further, with deficits replaced by surpluses. This should also mean that the pressures on currencies will ebb markedly.

With respect to oil exporters especially, fiscal pressures will ease considerably. Countries that were struggling with fiscal deficits will see those pressures easing significantly. It was fairly clear that some of these countries would need to implement serious structural adjustments, for example to lower recurrent expenditure by cutting the proportion going to salaries while increasing capital expenditure.

All of that risks falling by the wayside. Relieved of the pressure to cut fiscal deficits, many governments will probably turn to populist policies. For example, it will be interesting to see how many countries will reverse the reforms to fuel pricing that removed the government subsidy. Remember that governments in countries such as Egypt and Mozambique made explicit commitments to remove those subsidies.

Curiously, fuel retailers were complaining about the pricing formula in Nigeria. Some reported not being able to import fuel at the government mandated exchange rate, arguing that the retail price needs to be lifted. Fuel shortages arose towards the end of 2017 as only the NNPC was in a position to supply fuel. Interestingly, the electoral calendar is challenging for all 3 countries, making it all the more likely that governments could renege on the reform commitments they have made.

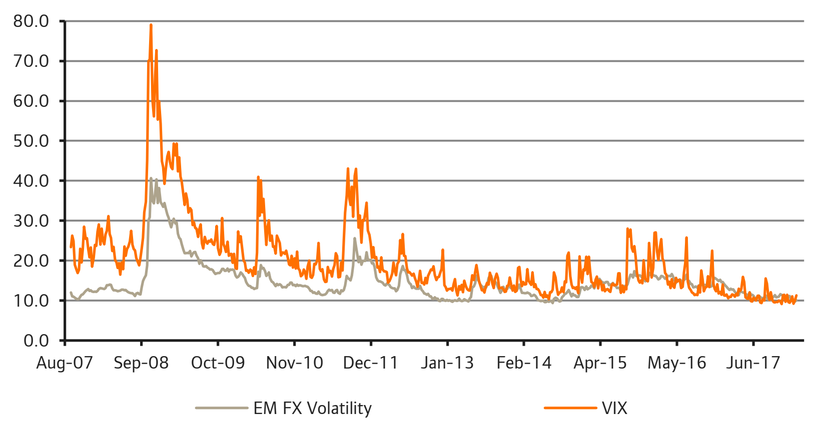
Rising commodity prices will likely turn the spotlight on commodity importers, with some market commentary likely to emphasise the consequences that these increases would have on the BOP positions of these countries. Some may wonder whether currencies such as the East African shillings will depreciate as a consequence of the rising trajectory in oil prices.

We find no reason to share any such concerns, were they to crop up. Granted, fuel imports will be boosted by the increase in oil prices. But so long as domestic demand in these economies is not rising sharply, we see no reason to believe that such a boost to fuel imports would lead to a durable deterioration in these countries' BOP. As we will discuss later on, we have some concerns about the medium-term outlook for these currencies, but those concerns would still be there, even with oil at USD50.0/bbl.

Global risk appetite: higher for longer

There can be no denying that there will come a time when the current bullish run in risk assets will turn substantively, with risk assets crashing as a result. Is there any reason to believe that such an eventuality will come in the next 4-m? Not as far as we can tell.

Figure 2: Sustainably low volatility?



Source: Bloomberg; Standard Bank Research

Risk appetite remains elevated, with the VIX index, our preferred measure of global risk appetite, at multi-year lows. We wouldn't rule out further declines in the coming months. Nonetheless, we acknowledge that there are plenty of unknowns globally, some of which would plausibly result in negative market outcomes, were they to eventuate. Sabre-rattling by North Korea and the United States will probably not die down completely. Similarly, we doubt that Middle East tensions will thaw soon. The passage of the US tax reform legislation aside, there are still notable policy execution risks, not just in the US, but among other developed countries as well.

Even then, we are still inclined to believe that the bull run will keep going. The Dow Industrial Average is at all-time highs, as are other US equity measures. A year ago the Dow at 30,000 might have seemed a dream. But with the index having gone past 24,000 before the end of 2017, that looks to be within touching distance now.

Admittedly, there will be numerous occasions in the coming 4-m when risk aversion will rise, leading to sell-offs of risky assets. But recall that many of the feared events over the past 8-y – like the European debt crisis in 2011, Taper Tantrum in 2014, Brexit vote in 2016 – turned out to have only a transient impact that did not alter the bull market in stocks and other risk assets. That pattern will likely prevail for a while still.

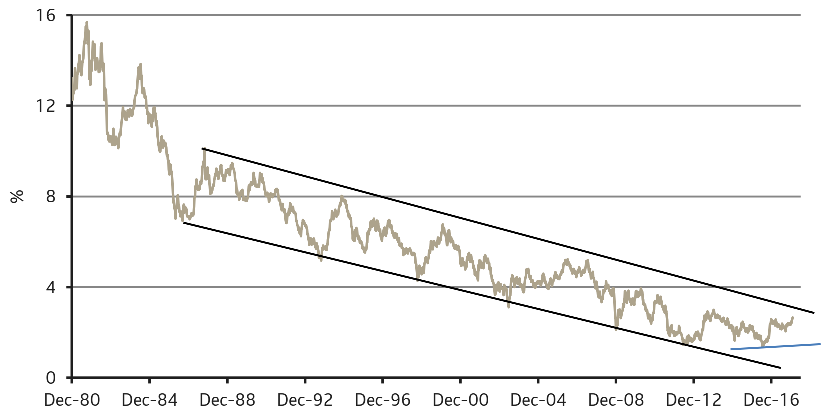
Central banks in the developed world have turned out to be adept at countering exogenous shocks that have hit those economies, even when policy rates were not far off from zero. The introduction of quantitative easing to the policy toolkit proved to be timely and effective. There are many commentators who worry, of course, that the policy stimulus provided by central banks has been excessive and will result in other bubbles developing.

But it is hard to ascertain what asset classes could possibly be bubbly at this point. Sure, if it turns out that the cryptocurrency craze is just that, a craze, then with hindsight one could argue that the unjustified loss of confidence in paper money that led to that bubble inflating was due to perceived policy errors committed by central banks that had provided large amounts of liquidity to the global economy over many years.

Global rates: waiting for US Treasuries to climb to 3.0%

As the experience of 2008/09 showed, as well as the Japanese experience, the reason to fear asset bubbles that burst is the impact that these have on the economy. So, even if cryptocurrencies are a bubble, and were to pop, it is unlikely that this would have much of an impact on the real economy since central banks would probably be capable of dealing with such an outcome.

Figure 3: US Treasury 10-y yields: hovering near 2.0%



Source: Bloomberg; Standard Bank Research

We still worry that the substantive headwinds for the markets would come if the markets were to get concerned about the appropriateness of monetary tightening, especially by the US Federal Reserve.

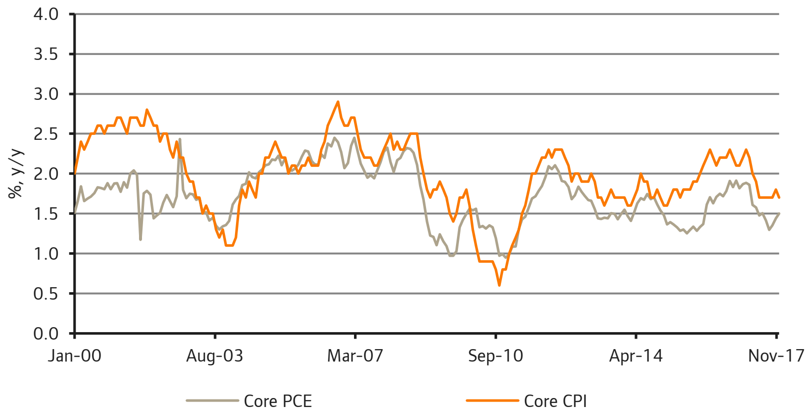
However, one has to admit that we have seen this on many occasions in the past 8-y, including the Taper Tantrum. Here is the concern. Thus far the experience has been that the markets worry about Fed policy, risk aversion rises, 10-y Treasuries rise, equities fall. In response, the Fed demonstrates its determination to be 'data dependent', by adopting a more dovish tilt, even slowing the pace of increases to the Fed Funds rate.

The markets cheer, and the rally moves on. Why is this a concern? There will likely be many market participants that become conditioned to the Fed coming to the rescue whenever there is a blip in risk appetite, pushing market valuations ever higher.

Having said that, it is worth noting that the Fed consistently communicated its willingness to raise policy rates by more than the market expected in 2017, but the rally persisted. With respect to 2018, FOMC members are yet again seemingly communicating a slightly more hawkish message, forecasting one more rate hike than the market is forecasting.

What is undeniable is that inflation has kept low, even lower than target. This is not just a problem for the Fed, but for other developed country central banks too. FOMC members have been predicting that inflation would get to the 2.0% y/y target since 2014. But the personal consumption expenditures core deflator, the Fed's favoured measure of inflation, has not recorded a single reading of 2.0% y/y or more over the past 3-y.

Figure 4: US core PCE deflator and core CPI inflation



Source: Bureau of Economic Analysis; Bureau of Labor Statistics

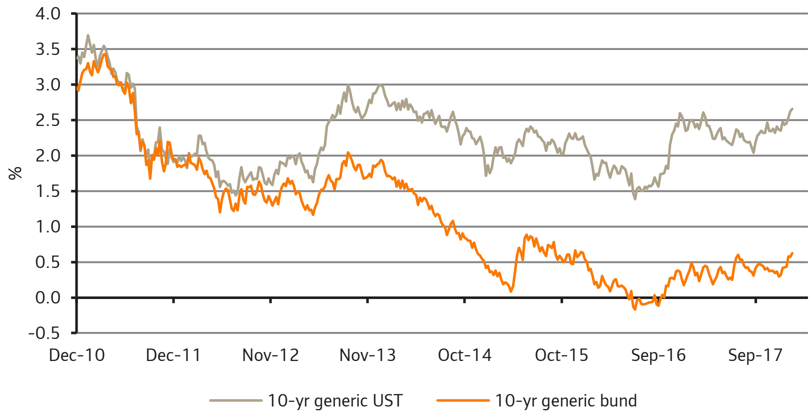
Persistence of inflation below target is perhaps one reason the market has not been persuaded that the Fed would keep increasing interest rates as fast as the Fed has been communicating. It is possibly a reason the market has not pushed the 10-y yield much above 2.5% over the course of the past 12-m. Nonetheless, the broad market consensus is that the 10-y Treasury yield will rise closer to 3.0% by the end of this year.

With inflation still stuck in the sub-2.0% region, we would not rule out the possibility that the market would revise its expectations lower over the course of the year, just like it eventually did during the course of last year. It was also curious that the passing of the tax reform legislation had no notable impact on the market, despite expectations that it would lead to higher fiscal deficits in the coming years. Perhaps the market is more focused on the inflation outlook rather than fiscal deficits, explaining why the yield curve has flattened.

Just 5 of about 32 analysts polled by Bloomberg expect the European Central Bank to change its policy stance over the course of the next 12-m. The consensus (median) expectation is that the bank will leave its policy rate unchanged this year and next year. At some point the ECB will reduce the size of its asset purchases, ultimately stopping to add to its balance sheet. Nonetheless, even with an unchanged policy rate, the market expects 10-y Bund yields to grind higher but remain below 1.0%.

Since our last AMR edition in Sep, the spreads of emerging market bonds, as measured by the JP Morgan EMBI Global spread, have trended broadly sideways. During the course of 2017, this spread tightened by some 52.7 bps to just under 311 bps. Bear in mind that during H1:13 and mid-2014, the spread was below 300 bps. It is hard to argue that it would not fall to those levels again over the coming 4-m. Of course, during the pre-credit crisis bull market, the spread fell below 200 bps.

Figure 5: 10-y generic US Treasury and German bund yields



Source: Bloomberg; Standard Bank Research

Figure 6: EM 10-y average bond yields versus US Treasury 10-y yields

Source: Bloomberg; Standard Bank Research

Political risks: a light electoral calendar in 2018

H2:17 saw some notable elections on the continent. Eduardo Dos Santos stepped down as the president of Angola, paving the way for Joao Lourenço to succeed him as president. The ruling party saw its electoral advantage wane, with 61% of the vote, compared with 72% the last time round. Even though Lourenço committed to not changing policies drastically, he has stamped his authority with some notable, high-profile personnel changes, including the leadership of the central bank and Sonangol, the country's national oil company that was chaired by Dos Santos' daughter. It is hard to believe that these would not be a prelude to significant policy changes.

The Kenyan Supreme Court nullified the original presidential election results, finding numerous irregularities and illegalities in the counting of ballot papers. This was clearly a big moment in the country's history, with the judiciary calling into question the processes and systems that the electoral commission uses to conduct polls. But then the opposition candidate for the presidency, Raila Odinga who was the plaintiff in the case, went on to call on his supporters to boycott the constitutionally mandated re-run of the presidential election, handing victory to incumbent President Kenyatta.

Even though there have been noises made by Odinga and the opposition regarding an economic boycott and establishment of a People's Assembly, for all intents and purposes political noise will likely ebb. Of course, the electoral commission's bungling of the vote count intensified secessionist sentiment in parts of the country, especially those that typically favour the opposition.

The Rwanda presidential election was largely uneventful, yielding no unexpected results. Rwandans will go back to the polls later this year for parliamentary elections. Don't count on any surprises there either. But the ruling party could well not get support of over 90%, same as the president.

Notionally, the Egyptian presidential elections later this year present some risks, security risks to be precise. Militant groups could well use these to launch some high-profile attacks. But in all likelihood the government will increase its security presence. Preparations for the polls began in earnest when the president signed into law a bill stipulating formation of an electoral commission that will have a board composed of judges.

Although President el Sisi has not announced whether he will run again, the only real question is if there will be a challenger. In the 2014 elections he garnered nearly 97% of the votes. The largest party in parliament has already endorsed his second term. Bear in mind also that parliament is fractured, with political party representatives limited to just 120 in the 596 seat house and 75% being independents.

Mozambique will have municipal elections in Sep. These will be crucial, and in all likelihood will be a prelude to the presidential and parliamentary elections to be held in 2019. Recall that the main opposition, Renamo, boycotted the 2013 polls. The party demanded greater regional autonomy, to allow it to appoint governors in the areas in which it had electoral dominance rather than having the central government do that. Of course, that boycott ultimately led to an escalation of conflict that has since stopped due to a ceasefire. Naturally, if there is no progress on regional autonomy, then there is a risk of hostilities resuming. With natural gas production likely to commence during the term of the next president, the political stakes are surely high over the next 20 months.

Consider the position of Nigeria's President Buhari. He won the 2014 election promising a clean government. But his crackdown on corruption is probably not going to be the most memorable aspect of his term in office. The commencement of his presidency coincided with a collapse in oil prices that created severe economic problems. His administration spent much of the first 2-y trying to frame a cohesive ideological basis for his approach to dealing with these problems. Having initially ruled out a devaluation of the NGN, he ultimately acceded to a convoluted process that led to a devaluation of the NGN and a segmented FX market.

The next election is not until Feb 2019, but campaigning will begin fairly soon. Already some notable political heavyweights are making their moves. With oil prices having increased significantly and the FX supply problems largely resolved, one would think that economic challenges are not going to cloud the last year of his term. But, as the fuel supply shortages towards the end of last year showed, this may not be the case. The temptation of adopting a populist stance – leading to an increase in fuel subsidies for example – while foregoing difficult structural reforms, must be very strong.

Events in the DRC have the potential to destabilise neighbouring countries. It is not entirely clear when general elections will be held, if at all. The electoral commission and the government have been consistently pointing to a lack of funds to conduct the exercise. Meanwhile, conflict in parts of the country have the potential to draw in neighbouring countries, like Rwanda and Uganda, that have traditionally expressed security concerns due to the presence of rebel groups in the country. Even the United Nations has seen its fair share of casualties, with Tanzanian peacekeepers killed last year when they were ambushed. The key concern is that it could become untenable for the UN to continue working with a discredited government, even if to improve security.

FX strategy: still selective in our choice of carry exposure

An examination of our trading record since we commenced keeping tabs on our trading recommendations is revealing. Since late May 14 we have only made one recommendation to buy USD against any of the currencies in our coverage, if one excludes the pair trades we have recommended. That was against the GHS last year. Sure, there are plenty of opportunities, especially since most of the currencies in our coverage tend to depreciate in a step-wise fashion, hardly ever appreciating. Nonetheless, the carry offered by these currencies tends to be sufficient to cover the risk of depreciation most of the time.

We could not resist selling a 2-m USD/AOA NDF in Dec. As we entered the month we saw implied NDF yields pushing higher dramatically. Seemingly the market was betting that the AOA would be devalued, perhaps around 1 Jan as happened the last time there was a major devaluation in 2016.

However, our investment thesis on Angola was that the FX reforms were likely to resemble those adopted by Egypt rather than Nigeria. Given the personnel changes that the president brought about since being elected, major policy changes were probably afoot. With respect to the currency, while we concurred with the market’s assessment of an AOA devaluation, we were not so convinced that this would be that quick in coming. We believed that the authorities would ensure that they resolved the BOP problems that have beset the economy. Bear in mind that there is still a backlog of FX demand, perhaps in excess of USD5.0bn, that needs to be cleared. A devaluation of the AOA, without a credible commitment to clear that backlog, would not alleviate the problems.

So, by our reckoning, the authorities would look for a solution that would ensure that there would no longer be a shortage of FX, no backlog of FX demand, and an improvement in capital inflows. That means that they would actively seek to attract capital inflows, say by issuing a Eurobond and attracting foreign portfolio inflows into the local bond market, as well as find a market clearing level for the exchange rate. It would, naturally, help if all that were underpinned by a funded IMF program.

Issuance of a Eurobond, or any other external financing, probably wouldn’t happen until parliament reconvenes after the Christmas break. In the past we observed that these considerations ensured that the government does not issue domestic paper in Jan and Feb, only resuming once parliament has approved the government’s borrowing plans for the year. Similarly, it would take time to negotiate and conclude a funded program with the IMF. All this suggested to us that a devaluation of the AOA would not happen in Jan.

While all of this sounded reasonable, it turned out to be wrong. The BNA and government indicated very early in Jan intentions to introduce a new mechanism for auctioning FX. The rate, EUR/AOA, would be determined by the weighted average of winning bids in these auctions. Prior to each auction the central bank would determine an upper and lower bound of acceptable bids, keeping those bounds to itself. Of course, before doing any of this the BNA made it known that it believed the AOA was overvalued. No surprises then that it took only two auctions, with EUR/AOA clearing rates of 221 and 248 from 202 at the last auction in 2017, before bids spiralled outside the undisclosed upper bound of the BNA’s acceptable range.

Back to our concerns about an FX devaluation without a credible plan to satisfy pre-existing demand for FX. Ordinarily, central banks that devalue a currency can always count on encouraging macroeconomic rebalancing by inflicting pain on FX buyers as well. This works in two ways. Firstly, by increasing the cost of new imports, thereby reducing future FX demand. Secondly, by reducing the FX amount that those with pre-existing demand for FX can obtain.

Our concerns in Angola are with respect to the second aspect. Recall that the government sold FX-linked bonds as a means to provide a hedge for importers. This was meant to relieve concerns about a devaluation of the AOA, hopefully prompting these businesses to continue importing products into the country, even as FX was not made available instantaneously.

Well, these now present a policy problem. Assuming that a reasonable proportion, if not all, of this pre-existing demand for FX is hedged, then this demand will not be affected by AOA devaluation. The magnitude of this pre-existing FX demand could be in excess of the equivalent of USD5.0bn. That could be more than 33% of FX reserves. Even this might be a conservative estimate. No matter what rate the BNA takes EUR/AOA to, this demand will not change. So to count on the rebalancing process to occur via diminished future imports only implies that the economy will not recover soon.

But this need not be the case, of course. The FX problems will be resolved at some point. Who would be natural buyers of those FX-linked bonds at that time? After all, it is reasonable to believe that once companies can obtain FX, they will no longer find these bonds useful. We would suggest that there are plenty of portfolio investors, who couldn't buy enough of the Angolan Eurobonds last year, who would happily buy these bonds. Some may even be willing to eschew the currency protection offered by these bonds, and buy T-bills unhedged instead. In the process, the inflows of capital would resolve the BOP crisis much quicker, ensuring a quick recovery in economic growth too.

Having witnessed depreciation of the ZMW at over a 30% annualised pace between Jul and early Dec, we reasoned that the carry was attractive, and added a 12-m short USD/ZMW NDF position to our shadow portfolio. Historically, the ZMW hardly ever depreciates in a straight line. Furthermore, there is no reason to believe that the country's BOP will be under much pressure over the coming 12-m. Copper prices eclipsed USD7,000/ton in Dec. Even as the BOZ is easing the policy stance, there is still no indication that import demand is picking up. Sure, with credit contraction ebbing, domestic demand will eventually pick up sufficiently to boost imports. But, even then, the recovery in copper prices and growth in production should prove supportive.

It is hard to believe that USD/GHS would fall below 4.00 again. But having witnessed the pair spiralling upwards during the course of Nov, we took the opportunity to enter another rebound trade by selling a 6-m USD/GHS NDF in Dec. Even though we believe that the pair will keep heading higher over the course of the next 12-m, we believe that the GHS will receive significant support in the near term. As we have argued repeatedly, the heavy positioning of foreign portfolio investors in the GHS bond market suggests that these investors will continue to buy these bonds whenever there is a sharp spike in USD/GHS. The last bond auction in Dec seems to bear this out.

We will retain the other carry positions that we have in our shadow portfolio. The short USD/XAF position will likely benefit from rising EUR/USD. Steve Barrow, our head of G10 strategy, believes that the latter is heading to a range of 1.30 – 1.40. We retain our view that there is very little chance that the XAF or the XOF will be devalued against the EUR.

If we didn't already have a position in USD/MZN, we would happily enter it at prevailing prices. We don't see much of a chance that the pair will head higher. Some may wonder if political noise will not end up exerting upward pressure on the pair as confidence wanes in the period leading up to municipal elections. We don't think so, especially given the dramatic depreciation the currency has experienced since 2014. Even without that, the general experience among currencies in our coverage is that politicians, as do central banks, see the value of maintaining a stable currency leading up to elections. From a ruling party's perspective, there is nothing to be gained by getting the electorate riled up by a massive currency depreciation just before polls. Almost invariably, central banks tend to redouble their efforts to deliver that stability. We have no reason to think any differently on the MZN.

The MWK has proven to be stable even in the lean period after the tobacco marketing season ended. We are still just over 3-m from the commencement of the next tobacco marketing season. Towards the end of that season, the same political calculations, with elections in Apr 19, will come to bear on the exchange rate.

We don't believe that elections will matter much for the EGP and NGN. Investor behaviour might matter, though. Both currencies attracted plenty of foreign investor money, in excess of USD10.0bn in each market, since the respective policymakers introduced reforms to their FX markets. Those investors have made plenty of money, just as we have in our shadow portfolio. Some of those investors may just decide to take precautions ahead of elections.

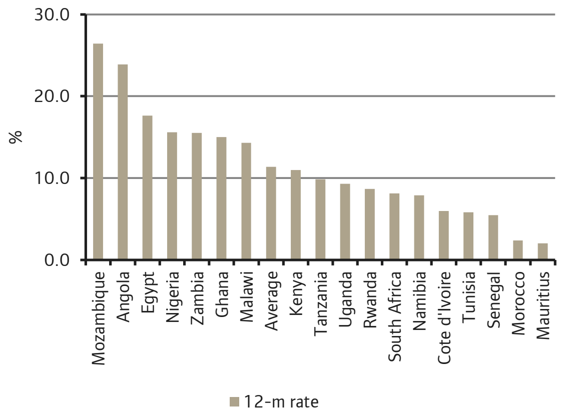
As we already argued, Egyptian elections are probably nothing to be concerned about. Investors may just opt to take money off the table. But bear in mind that the central bank changed the pricing for accessing its repatriation mechanism for portfolio investors in an effort to encourage more FX trades to happen in the interbank market. Curiously, the immediate impact of this was for USD/EGP to rise from nearly 17.60 in late Nov to nearly 17.85 by the end of Dec. This can't possibly be a durable move. Indeed, if there were to be any meaningful portfolio outflows – and the pair were to push even higher, say close to 18.25 – that would probably prompt some of the investors who came in via the repatriation mechanism last year to come back without using the mechanism.

It is much harder to be unflinchingly constructive on the NGN, if only due to the segmented nature of the FX market. As we have pointed out, inflows in the investors' and exporters' FX window come from portfolio investors. There has always been trepidation about this imbalance, with investors worrying that these could dry up, leading to the same dysfunction that had characterised the FX market before the introduction of the IEFX window.

But, we are not as concerned. After all, 'FX shortages' would be incompatible with an autonomous market. Granted, there are plenty of inefficiencies in the manner in which the market functions. But there is nothing preventing two counterparties from agreeing on a price. Additionally, it is worth reiterating that the combination of an increase in oil prices and production, while import demand is somewhat restrained, will bolster the C/A balance, perhaps leaving it in surplus. Of course, we must also acknowledge that FX reserves have risen by close to USD10bn since the introduction of the IEFX window. True, this mainly reflected portfolio inflows. Third, and most crucial, it would not be in the interests of the incumbent president to have a recurrence of FX dislocation with an election less than a year away.

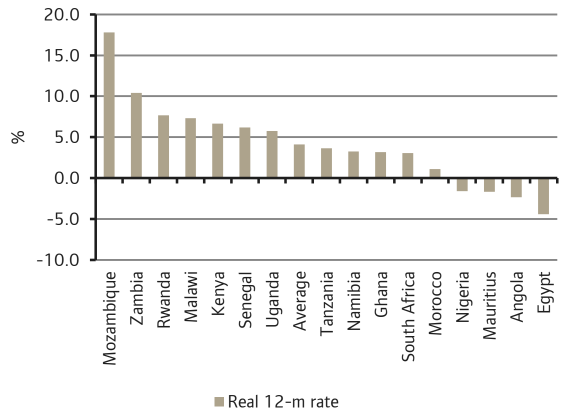
Given everything we've said above, we are convinced that the CBN has the means, and incentives, to ensure that the FX market operates efficiently, even if USD/NGN were to rise meaningfully in the IEFX window. In fact, any such meaningful increase in USD/NGN would most likely end up attracting fresh portfolio inflows into the market.

Figure 7: 12-m T-bill yields



Source: Various central banks

Figure 8: Real 12-m T-bill yields



Source: Various central banks; various statistical agencies

Exposure to the UGX and KES has typically guaranteed returns of 1% per month, with hardly any volatility to speak of. This is likely to continue in the near term; hence, we are happy to retain exposure to both currencies. In Kenya, there is likely to be a resumption of normal economic activity following the protracted electoral process. This would boost import demand sufficiently to push USD/KES higher. But in the near term, the pair will likely remain range-bound. We took advantage of a spike in USD/KES after the annulment of the presidential election results to enter an NDF position in Aug. The UGX has been similarly quiescent. We are happy to keep the bond we bought in 2016, and which will mature later this year, for the carry.

While the near-term outlook for both currencies is positive, we are not so sure about the medium-term outlook. We expect that the Kenyan government will be keen to boost economic activity. But with the interest rate cap still in place, there isn't much scope for such a boost to be delivered by monetary policy. So, the government may well look to fiscal policy instead. This could ensure that import demand picks up enough to cause the KES to depreciate.

Growth considerations are top of mind for Ugandan policymakers, too, as the table below attests. The African growth story of the last 5-y is most easily told by differentiating the experience of commodity and non-commodity producing countries. Non-commodity producers weathered the storm caused by lower commodity prices in the last 5-y to record growth in line with the 10-y average. Uganda is the notable exception, with growth in the last 5-y 3.4 ppts lower than in the prior 5-y. Only Angola (6.4 ppts decline) and Nigeria (4.2 ppts) fared worse among the countries in the table.

Comparisons of the African growth experience until 2016

	GDP growth (%, y/y)		GDP per capita (USD)	Inflation (%, y/y)	10-y annualised FX performance	
Period	**5-y average**	**10-y average**	**2016**	**10-y average**	**31-Oct-17**	**29-Dec-10**
Kenya	5.5	5.2	1 550	8.3	-4.3	-0.3
Uganda	4.2	5.9	614	8.6	-7.2	-2.7
Ethiopia	9.5	10.2	750	16.8	-10.4	-6.8
Rwanda	7.2	7.4	700	6.3	-4.4	-5.0
Tanzania	6.7	6.7	959	9.0	-6.4	-5.8
Nigeria	3.5	5.6	2 195	10.7	-10.3	-3.3
Ghana	5.9	6.8	1 514	12.4	-14.1	-6.9
Ivory Coast	8.7	4.9	1 348	2.2	-2.3	3.4
Senegal	4.8	4.1	990	1.7	-2.3	3.4
Angola	2.9	6.1	4 277	13.5	-7.8	-15.9
Mozambique	6.4	6.7	411	7.8	-8.3	-6.2
Zambia	5.2	6.5	1 316	10.3	-9.3	-0.6
South Africa	1.6	2.2	5 653	6.3	-7.5	1.3

Source: National statistical agencies; Bloomberg; Standard Bank Research

We highlight the fact that Ugandan policymakers typically seek to maintain a competitive exchange rate, not allowing the real exchange rate to appreciate over time. The disappointing growth experience could very well prompt them to conclude that the

UGX is somewhat overvalued, and they may therefore opt to intervene to actively weaken it.

What about the TZS? If the KES and UGX were to depreciate in the medium term, then the TZS would likely follow suit. Indeed, among the three East African shillings, the KES has a tendency of depreciating by the least over long periods, as the table above shows. But you wouldn't say that by looking at NDF pricing. One could buy a 3-y USD/TZS NDF at an implied yield close to 8%, while it would be close to 12% for the USD/UGX and USD/KES NDFs. Although we won't recommend any trade right now, buying the KES/TZS pair – selling a 3-y USD/KES NDF against buying a 3-y USD/TZS NDF has positive carry of 10 bps per month – is an attractive trade.

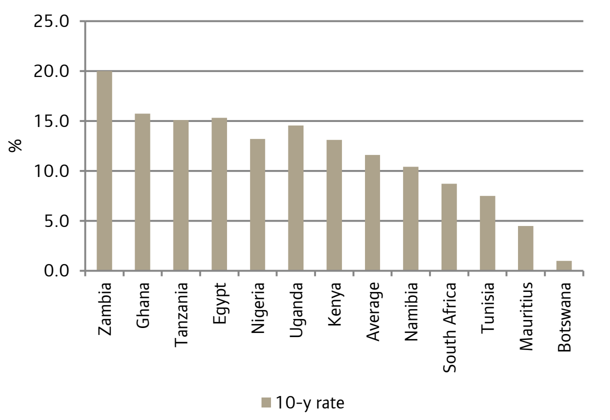
Fixed income strategy: buy EGP duration

There aren't a lot of markets offering bond yields of over 16.0%. Zambia, Ghana and Egypt are the only ones in our coverage. We already have exposure to those markets in our shadow portfolio and are happy to recommend them all. Certainly, over the coming 12 to 18 months, investors will have to be comfortable with bond yields below 15% in many markets.

The Monetary Policy Committee of the Central Bank of Egypt can't be too far off from commencing the easing of its monetary policy stance. Inflation is on track to be in the mid-teens by Q1:18 and closer to 10.0% y/y by Dec 18. Thus, for most of H2:18, inflation would be within the 10.0% to 16.0% y/y target range that the CBE aims to achieve in Q4:18. It is highly probable that inflation will decline to single digits by early 2019.

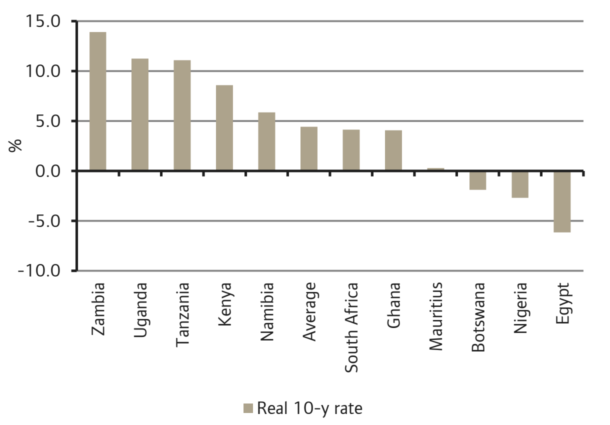
We like EGP bonds, having entered our position at a yield just below 16.0%. We believe that, with the MPC poised to lower its policy rates by 400-500 bps in 2018, bond yields will drop off dramatically over the course of the next 12-m, with the curve dis-inverting as well.

Figure 9: 10-y bond yields



Source: Various central banks

Figure 10: Real 10-y bond yields



Source: Various central banks; various statistical agencies

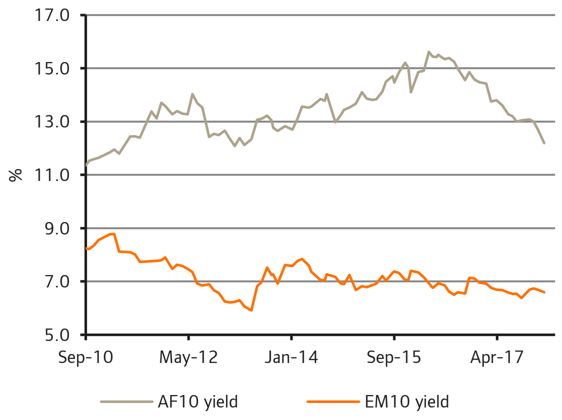
We are happy with Zambian duration, intending to keep the position we have for quite some time. Inflation is becoming stable just above 6.0% y/y, with little chance that it will rise meaningfully. The central bank is continuing to ease its policy stance. Even if it were not to lower the policy rate further from current levels, it would most likely allow liquidity conditions to ease further. Thus, there is likely to be a consistent bid for bonds from domestic investors.

Ghana still has some of the highest real yields among the countries in our coverage. It is also the one trade that most international investors seem to be comfortable with. The central bank, which has maintained a high real policy rate, will likely continue to ease its policy stance in coming months. We might disagree with the MPC's assessment of the inflation outlook, but even if we turn out to be correct and inflation has a 14% handle by mid-2018, the MPC would still have a case to ease its policy stance.

Having said that, we don't see scope for yields to decline much from current levels. Volatility of bond yields will likely be minimal, with much of the return volatility likely to be accounted for by the exchange rate. We will look for opportunities to mitigate those FX risks over the course of the year. After all, the currency has detracted more than 10% per year from the return on the bond position in our shadow portfolio.

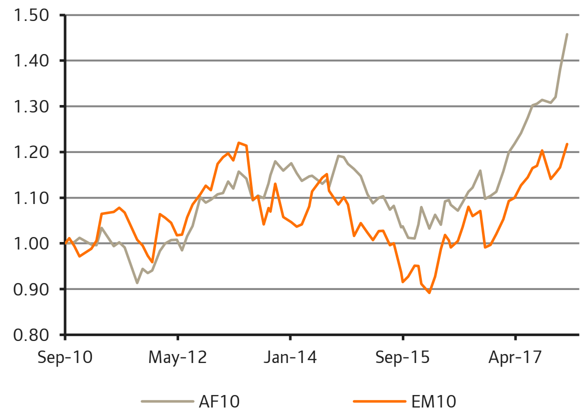
We are somewhat torn about our KES bond exposure. The trade was motivated by our expectation that the bond's yield would decline by some 50 - 70 bps after issuance, to more or less where similar paper was trading in the secondary market. Now that it is nearly there, what do we do? Selling it means giving up nearly 95 bps of carry a month. We don't really see impetus for yields to rise meaningfully in the near term, so we will hold this position.

Figure 11: EM10 versus AF10 average 10-y bond yield



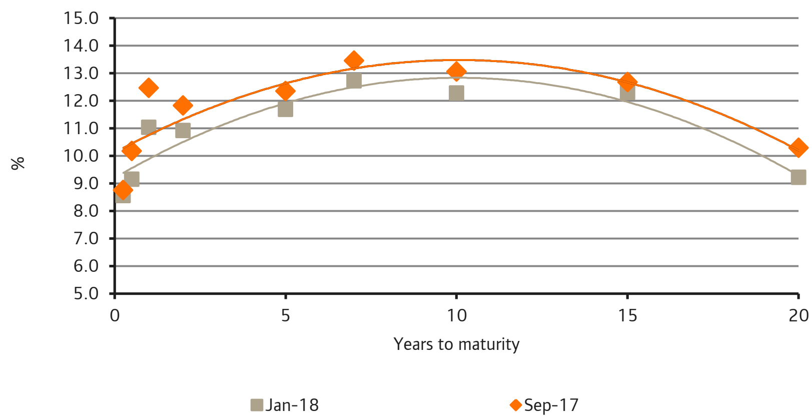
Source: Bloomberg; Standard Bank Research

Figure 12: EM10 versus AF10 average 10-y bond return



Source: Bloomberg; Standard Bank Research

Figure 13: AF10 yield curve: simple yield average



Source: Bloomberg; Standard Bank Research

Nigeria will be a tough market in 2018. There was a strong local bid for paper towards the end of 2018 that depressed yields. In part this was due to the CBN not mopping up

NGN liquidity as much as it was doing earlier in the year. Indications from the CBN are that they are happy to see yields fall further from current levels. Nonetheless, inflation is still elevated, and foreign portfolio investors may get twitchy with elections around the corner. In any event, the reason for the CBN not mopping up liquidity towards the end of the year may have more to do with operational rather than policy considerations. It seems as if the CBN fully utilised the available budget for open market operations. Hence, it is plausible that it would resume mopping up liquidity early this year, providing some impetus for yields to rise somewhat and better entry levels. Even then, 16.0% yields may not be readily available in this market.

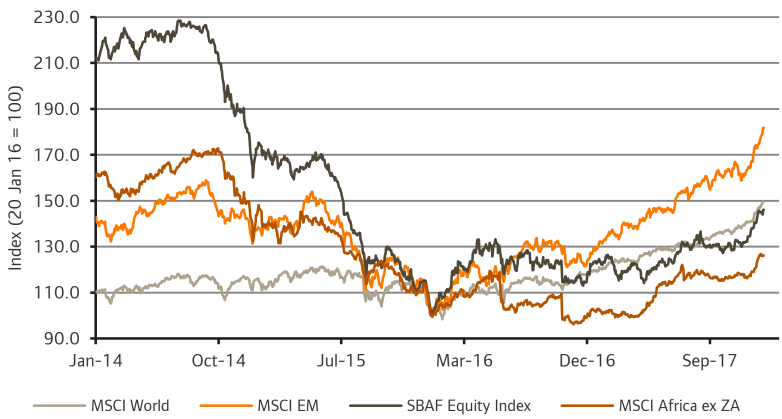
African equities: still playing catch-up

African equities, as measured by the Standard Bank Africa Equity Index, have finally caught up with developed market equities, as measured by the MSCI World index. Most of this outperformance has occurred since Nov 17.

The macroeconomic challenges Nigeria and Egypt faced, challenges that encompassed FX shortages, have ebbed. Over the coming two to three years, we are likely to see these markets recovering considerably, matching the improvement in these countries' economies.

It is hard not to be optimistic about the positive impetus that might come from the improvement in Egypt's economy. For more than 5-y, the economy has struggled to deliver growth of 5.0% y/y consistently. FX constraints were telling, with FX reserves waning. Almost overnight, the situation has improved, with FX reserves at record highs. The central bank will surely ease the monetary stance over the course of the year.

Figure 14: African equities underperforming EM equities



Source: Bloomberg; Standard Bank Research

Similar sentiment characterises our view on Nigerian equities. True, one might make the point that perhaps the market has been front-running the revival in corporate earnings. But chances are very strong that this revival will not disappoint, ensuring that the market continues to attract healthy inflows over the course of the next 12-m. The Nigerian All Share Index is up over 15% since the beginning of the year in USD terms.

Kenyan equities haven't quite recovered since being jolted by the Supreme Court ruling. Perhaps the market is focusing on any indication that there might be a relaxation of the interest rate cap law. Certainly, as the PMI has shown, economic activity is likely to normalise, and with that corporate earnings are likely to receive a boost. But there is still no indication that the end of the electioneering period has boosted investor sentiment enough to support the market. Nonetheless, at this stage we are still inclined to believe that portfolio inflows into the market will still be sufficient to support the overall BOP.

African Eurobonds: stay overweight the oil sovereigns

EM bond spreads languished over the past 4-m, with the JP Morgan EMBI Global spread remaining just above 310 bps as it was 4-m ago. In contrast, African Eurobond spreads fell appreciably, with the Standard Bank Africa Sovereign Bond Index spread falling by some 40 bps.

Strategically, we are still inclined to believe that spreads will tighten further on a multi-month basis. However, tactically we would like to take some risk off the table. Given the magnitude of the rally, it is likely that spreads will widen first. Hence, we will bring the overall positioning of the portfolio to 2% underweight relative to the benchmark and shorten our duration exposure. We will also make some notable country reallocations.

We have a very strong view that reform momentum in Angola will prove to be beneficial for those bonds. As we have argued in previous pages, there is a very strong likelihood that policymakers will implement reforms that will address the FX problems that have beset that economy, even if doing so solely by devaluing the AOA. Coupled with the rally in oil prices, it seems likely that the Angola '25s will continue to outperform. We will maintain our 2%overweight position.

In all, we like oil credits, but not all of them equally. Although we are tempted to establish an overweight position on Gabon, we will retain the 1% underweight. We will leave both RepCon and Cameroon at benchmark weight. There is a case to be made for one to establish overweight positions on Gabon and RepCon. The rally in oil prices will make a big difference in the fiscal and BOP positions of Angola, Gabon and RepCon, but not as much for Nigeria and Cameroon. Even though we leave the Nigeria overweight position unchanged, valuation concerns argue for an underweight position on Nigeria. By our valuation yardstick of choice, the spread per unit of duration, Nigerian bonds are tighter than comparable bonds of other oil sovereigns in our universe.

We have high conviction on Ghana and Zambia, leading us to retain our 1% overweight positions in each. Even though there were revenue disappointments during 2017, the Ghanaian government still illustrated its willingness to restrain spending in order to arrest the budget deficit. The market will likely remain constructive over the near term. That the Zambian Finance Ministry is still talking about an IMF program suggests that it is still looking to embed expenditure restraint on the spending ministries. At the very least, the government is likely to restrain expenditure successfully.

Even though the bond has rallied a lot, a 1% overweight position on Mozambique probably would pay off. We have no reason to expect the government and bondholders to agree a restructuring of external debt anytime soon. By all accounts, there are no negotiations taking place. In part, this may be due to perceptions that the government's financial position has improved markedly, especially after the capital gains tax it received following the sale of a stake in ENI's project to Exxon Mobil.

On valuation concerns, there is a case for establishing underweight positions on Côte d'Ivoire, Morocco, South Africa and Senegal. The security concerns that were triggered by mutinies in Côte d'Ivoire may not recur, but we doubt if this will provide much support for the country's bonds. Similarly, the market has breathed a sigh of relief after the African National Congress elective conference but it is hard to see much upside for South African Eurobonds. Namibia seems to offer better value over South Africa.

Kenya will surely come to market during H1:18. We are not particularly constructive about the fiscal outlook. Part of the reason the second review of the IMF's Precautionary Facility fell through in Apr 17 could very well have been failure of the government to meet fiscal targets. The review will likely be revisited during Q1:18, and the discussions could well turn out to be tough.

The IMF has hardly tried to hide its displeasure at the promulgation of the interest rate capping law. But repeal appears to be out of the question. An amendment that would lift the lending ceiling could take some time to be concluded. Spending pressures mounted in H2:17, even if one excludes the presidential election re-run, against a backdrop of somewhat disappointing revenue collection. There is still the chance that the government would look to boost spending after the election in an effort to stimulate the economy.

The market has elected to focus on the positive story stemming from a successful and peaceful electoral process, with yields on the '24s dropping below 5.5%. We are not inclined to be that bullish. We suspect that the market will re-focus its attention on the spending pressures and the reality of an incomplete review of the IMF facility. For this reason, we maintain the 1% underweight position in our portfolio.

If there is one country whose macroeconomic performance is likely to improve such that credit rating upgrades could ensue in the next 5-y, it is Egypt. There is very little chance that the upcoming elections will lead to a departure in macroeconomic policy conduct.

It is easy to understate the significance of the FX reforms that policymakers have introduced, but they will probably turn out to be significant. ENI's offshore gas project is about to deliver natural gas onshore, further bolstering the BOP. It is very likely that growth will rebound well above the 4.0% y/y average of the post-Arab Spring period. With it, government revenues are likely to receive a boost. The disinflation process is well underway, with the central bank about to embark on an extended easing cycle. That will also set the stage for the government's interest expenditure to fall.

Even with all of these considerations, we are inclined to remain neutral for the time being. There may well be opportunities to reassess our stance in the coming 4-m.

Hedging CNY exposure

Trade consummated between Africa and China is still predominantly conducted in USD. Yet, for importers, it is often cheaper to hedge CNY exposure than to hedge USD exposure. Standard Bank offers forwards that allow African importers to hedge CNY exposure.

Indicative CNY forward prices

	Historical FX levels				Forward prices		
	-12m	-6m	-3m	spot	3-m	6-m	12-m
CNY/BWP	1.54	1.52	1.59	1.51	1.51	1.50	1.50
CNY/GHS	0.64	0.65	0.67	0.71	0.74	0.77	0.81
CNY/KES	15.12	15.47	15.66	16.15	16.25	16.40	16.70
CNY/MUR	5.18	4.96	5.26	5.08	5.07	5.06	5.04
CNY/ZAR	1.96	1.96	2.13	1.89	1.90	1.92	1.95
CNY/UGX	521.86	537.37	551.62	571.10	574.19	578.84	592.28

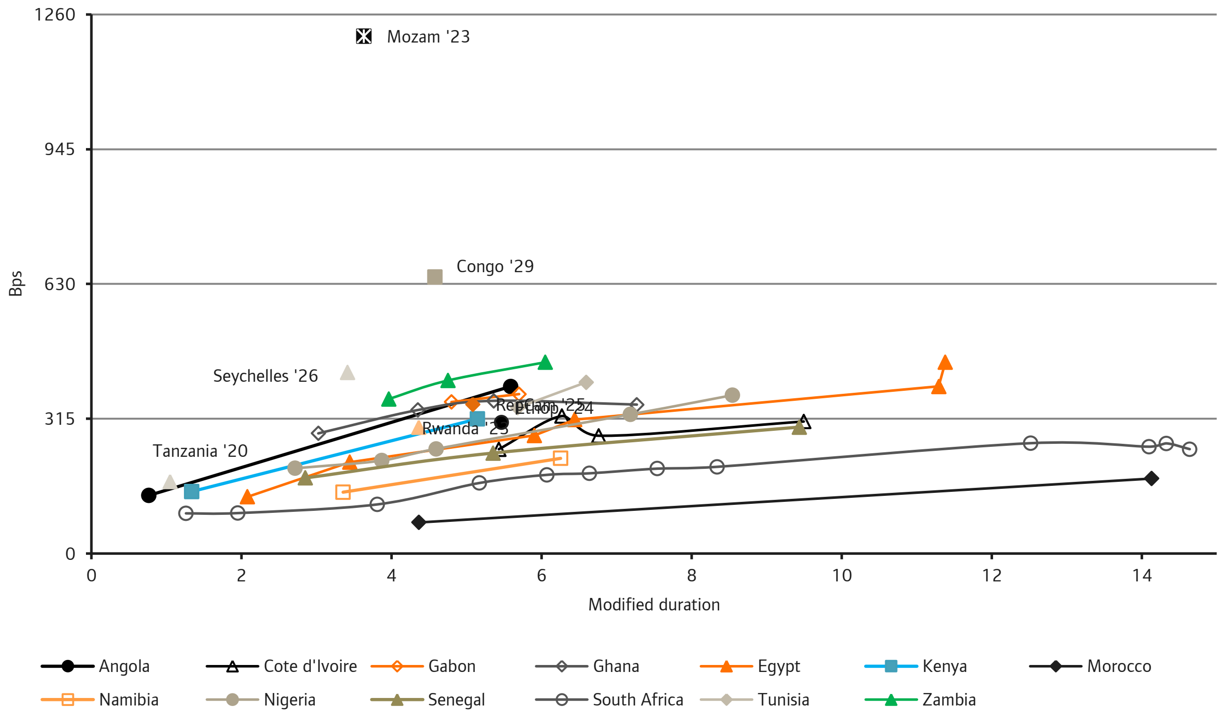
Source: Bloomberg; Standard Bank Research

African Eurobonds

					Spread, bps		Spread change, bps			Total return, %		
Name	**Moody's/Fitch**	**Mid Price**	**Mod Dur**	**Yield, %**	**Over UST**	**Z-Spread**	**1 wk**	**YTD**	**12mths**	**1 wk**	**YTD**	**12mths**
ANGOL 7% 16-AUG-2019	B2/-	103.000	0.8	3.14	136	98	-9	-6	-286	0.1	0.2	6.2
ANGOL 9.5% 12-NOV-2025	B2/B	118.375	5.6	6.46	390	385	-5	-72	-397	0.2	3.0	32.1
REPCAM 9.5% 19-NOV-2025	-/B	119.375	5.1	5.98	349	340	7	-15	-205	-0.5	-0.2	16.8
REPCON 3% 30-JUN-2029	-/CC	87.000	4.6	8.91	647	632	22	15	-626	-1.0	-1.2	41.5
EGYPT 5.75% 29-APR-2020	B3/B	104.938	2.1	3.45	133	113	-6	-32	-226	0.1	0.5	8.6
EGYPT 6.125% 31-JAN-2022	B3/B	106.063	3.4	4.45	214	197	-16	-59	-203	0.5	1.6	0.0
EGYPT 5.875% 11-JUN-2025	B3/B	103.250	5.9	5.33	276	273	-18	-63	-212	0.9	2.6	18.8
EGYPT 7.5% 31-JAN-2027	B3/B	112.250	6.4	5.74	313	309	-1	-48	-196	-0.1	1.8	0.0
EGYPT 6.875% 30-APR-2040	B3/B	102.938	11.3	6.61	391	385	-9	-40	-147	0.8	2.3	24.3
EGYPT 8.5% 31-JAN-2047	B3/B	115.938	11.4	7.18	448	443	-1	-29	-133	-0.1	1.1	0.0
ETHOPI 6.625% 11-DEC-2024	B1/B	105.750	5.5	5.61	307	301	9	-40	-299	-0.6	1.2	24.2
GABON 6.375% 12-DEC-2024	-/B	101.750	4.8	6.01	354	345	9	-24	-215	-0.5	0.3	17.1
GABON 6.95% 16-JUN-2025	B3/B	103.875	5.7	6.29	373	368	8	-25	-210	-0.6	0.4	19.1
GHANA 9.25% 15-SEP-2022	B3/B	113.625	3.0	5.07	281	262	4	-30	-305	-0.2	0.6	15.6
GHANA 7.875% 07-AUG-2023	B3/B	109.750	4.4	5.78	335	324	8	-21	-288	-0.4	0.2	19.7
GHANA 8.125% 18-JAN-2026	B3/B	111.375	5.4	6.09	357	350	7	-26	-268	-0.5	0.3	22.0
GHANA 10.75% 14-OCT-2030	B1/BB-	138.250	7.3	6.12	348	343	4	-32	-241	-0.5	0.8	25.1
IVYCST 5.375% 23-JUL-2024	Ba3/B+	102.250	5.4	4.96	244	238	3	-30	-144	-0.3	0.5	12.8
IVYCST 2.5% 31-DEC-2032	-/B+	99.625	6.3	5.81	321	315	2	-17	-128	-0.3	-0.2	13.1
IVYCST 6.375% 03-MAR-2028	Ba3/B+	107.125	6.8	5.37	275	272	5	-42	-148	-0.6	1.5	15.7
IVYCST 6.125% 15-JUN-2033	Ba3/B+	103.500	9.5	5.76	309	303	3	-42		-0.5	2.0	
KENINT 5.875% 24-JUN-2019	-/B+	103.313	1.3	3.43	145	118	-6	-23	-137	0.1	0.3	5.1
KENINT 6.875% 24-JUN-2024	-/B+	106.500	5.1	5.65	315	307	9	-21	-198	-0.6	0.1	16.5
MOROC 4.25% 11-DEC-2022	-/BBB-	104.875	4.4	3.16	73	64	1	-10	-84	-0.2	-0.4	6.0
MOROC 5.5% 11-DEC-2042	-/BBB-	114.000	14.1	4.55	176	177	2	-22	-49	-0.3	0.5	13.0
MOZAM 10.5% 18-JAN-2023	Caa3u/-	86.750	3.6	14.43	1,209	1,192	-13	-281	-882	0.6	10.2	59.2
REPNAM 5.5% 03-NOV-2021	Ba1/BB+	106.125	3.4	3.74	143	127	-2	-16	-75	0.0	0.0	5.2
REPNAM 5.25% 29-OCT-2025	Ba1/BB+	102.750	6.3	4.82	222	220	7	-37	-67	-0.6	1.0	8.2
NGERIA 6.75% 28-JAN-2021	-/B+	107.125	2.7	4.19	199	179	-7	-56	-234	0.1	1.1	11.2
NGERIA 5.625% 27-JUN-2022	B2/B+	104.250	3.9	4.55	217	205	-5	-32		0.1	0.6	
NGERIA 6.375% 12-JUL-2023	-/B+	107.000	4.6	4.90	245	235	-2	-39	-210	0.0	0.9	15.2
NGERIA 6.5% 28-NOV-2027	B2/B+	104.500	7.2	5.89	325	322	1	-28		-0.2	0.5	
NGERIA 7.875% 16-FEB-2032	B2/B+	113.875	8.5	6.36	370	364	0	-31		-0.2	0.9	
NGERIA 7.625% 28-NOV-2047	B2/B+	108.500	12.2	6.95	422	418	2	-31		-0.4	1.4	
RWANDA 6.625% 02-MAY-2023	-/B+	105.625	4.4	5.38	295	285	-5	-37	-161	0.1	0.9	12.3
SENEGL 8.75% 13-MAY-2021	Ba3/-	114.500	2.9	3.99	177	157	7	1	-210	-0.3	-0.4	10.2
SENEGL 6.25% 30-JUL-2024	Ba3/-	107.625	5.4	4.87	235	229	3	-18	-169	-0.3	-0.2	14.3
SENEGL 6.25% 23-MAY-2033	Ba3/-	106.000	9.4	5.63	296	290	3	-27		-0.5	0.5	
SEYCHE 3% 01-JAN-2026	-/BB-	105.024	3.4	6.55	423	404	13	-37	-145	-0.5	0.9	10.4
SOAF 6.875% 27-MAY-2019	Baa3 /*-/BB+	105.125	1.3	2.90	94	66	-12	-12	-56	0.2	0.2	2.7
SOAF 5.5% 09-MAR-2020	Baa3 /*-/BB+	105.000	2.0	3.03	95	74	-11	-20	-82	0.2	0.2	3.7
SOAF 5.875% 30-MAY-2022	Baa3 /*-/BB+	109.375	3.8	3.52	115	102	-11	-26	-67	0.3	0.3	4.8
SOAF 4.665% 17-JAN-2024	Baa3 /*-/BB+	102.688	5.2	4.15	165	158	-5	-30	-35	0.1	0.4	4.8
SOAF 5.875% 16-SEP-2025	Baa3 /*-/BB+	109.375	6.1	4.41	184	180	-8	-32	-29	0.3	0.7	4.9
SOAF 4.875% 14-APR-2026	Baa3 /*-/BB+	102.625	6.6	4.49	188	185	-4	-30	-22	0.1	0.5	4.8
SOAF 4.85% 27-SEP-2027	Baa3 /*-/BB+	101.688	7.5	4.63	198	196	-7	-30		0.3	0.6	
SOAF 4.3% 12-OCT-2028	Baa3 /*-/BB+	96.750	8.3	4.69	203	199	-6	-26	-33	0.3	0.3	6.5
SOAF 6.25% 08-MAR-2041	Baa3 /*-/BB+	112.375	12.5	5.31	258	253	-4	-30	1	0.2	1.3	5.3
SOAF 5.375% 24-JUL-2044	Baa3 /*-/BB+	101.125	14.1	5.30	250	252	-3	-27	11	0.1	1.0	5.0
SOAF 5.65% 27-SEP-2047	Baa3 /*-/BB+	103.875	14.3	5.39	258	261	-4	-33		0.3	2.0	
SOAF 5% 12-OCT-2046	Baa3 /*-/BB+	96.000	14.6	5.27	244	249	-6	-29	11	0.6	1.6	5.8
TNZNIA 6.4499% 08-MAR-2020	-/-	105.375	1.0	3.59	168	137	-6	-11	-127	0.1	0.4	4.6
BTUN 5.75% 30-JAN-2025	B1/B+	98.750	5.7	5.97	341	337	-8	-4	-82	0.3	-0.9	9.8
BTUN 8.25% 19-SEP-2027	B1/WD	111.500	6.6	6.62	401	396	-6	-38	-83	0.2	1.2	11.4
ZAMBIN 5.375% 20-SEP-2022	-/B	97.500	4.0	6.00	361	349	3	-14	-224	-0.1	0.0	15.5
ZAMBIN 8.5% 14-APR-2024	-/B	110.000	4.8	6.51	405	395	7	-14	-267	-0.4	-0.1	20.5
ZAMBIN 8.97% 30-JUL-2027	-/B	112.125	6.0	7.05	447	442	4	-28	-246	-0.4	0.6	23.1
SB Africa Eurobond (incl. SA)	B+		6.3	5.82	324	318	1	-28	-142	-0.3	0.8	15.4
SB Africa Eurobond (excl. SA)	B+		6.1	6.00	342	336	2	-28	-176	-0.3	0.8	17.1

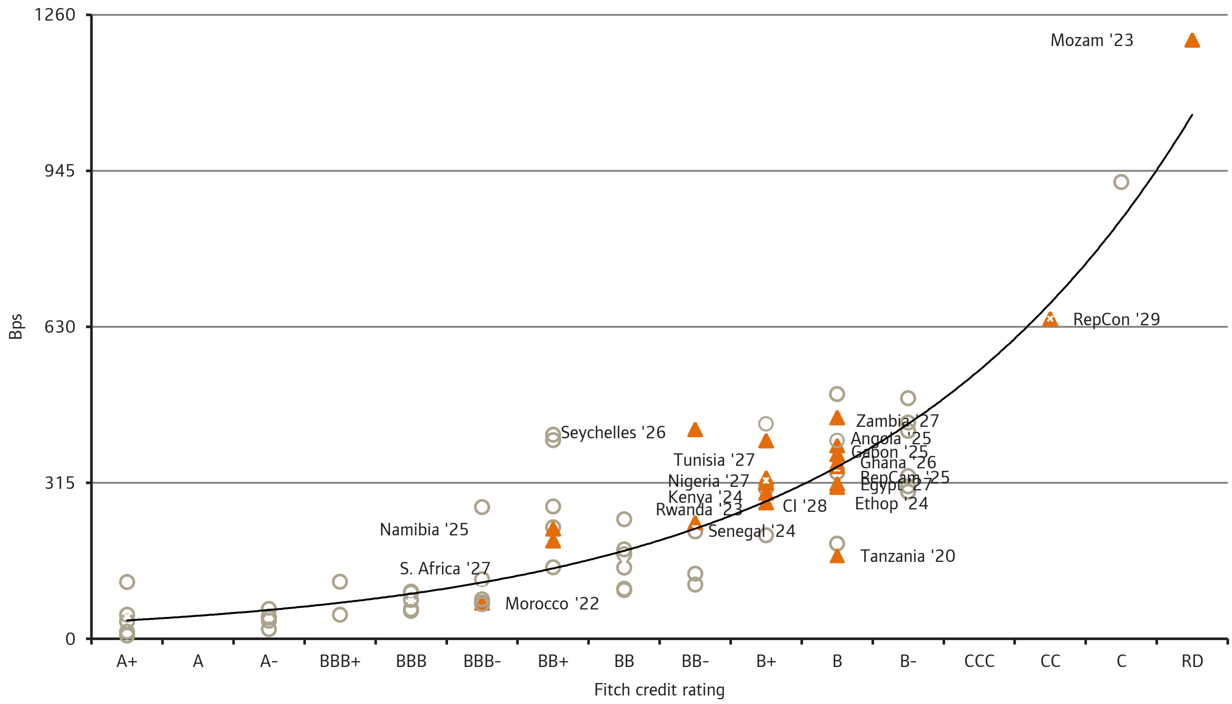
Source: Bloomberg; Standard Bank Research

Figure 15: African sovereign USD bonds (spread over US Treasuries versus modified duration)



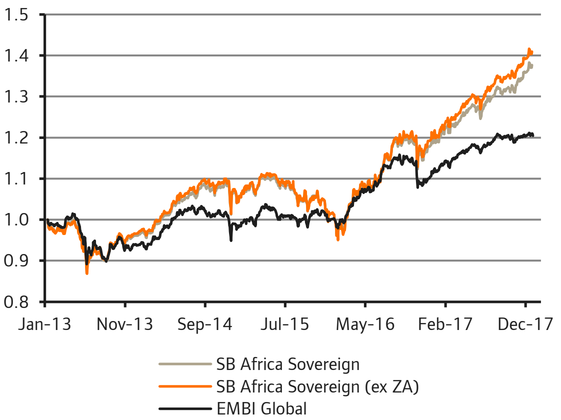
Source: Bloomberg; Standard Bank Research

Figure 16: African and broader EM bonds (spread over US Treasuries versus credit rating)



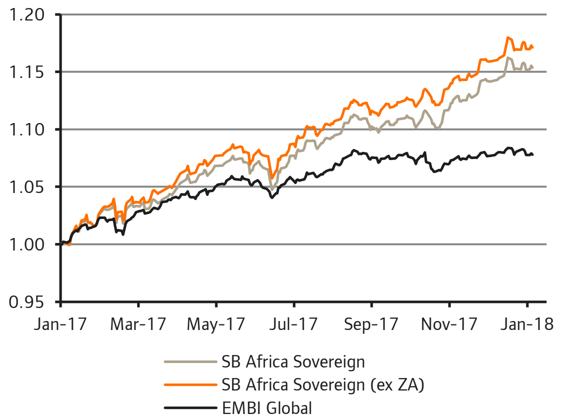
Source: Bloomberg; Standard Bank Research

Figure 17: African Eurobonds (5-y performance)



Source: Bloomberg; Standard Bank Research

Figure 18: African Eurobonds (1-y performance)

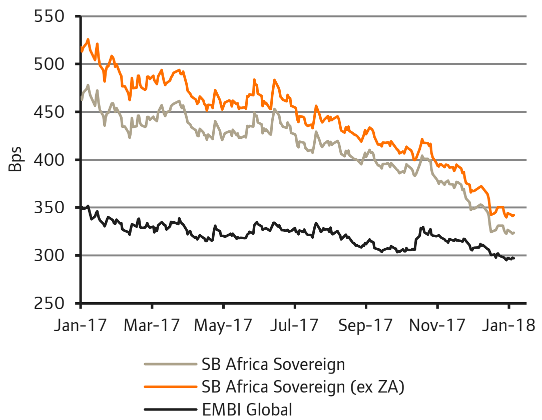


Source: Bloomberg; Standard Bank Research

Figure 19: African Eurobonds spread over UST (5-y)

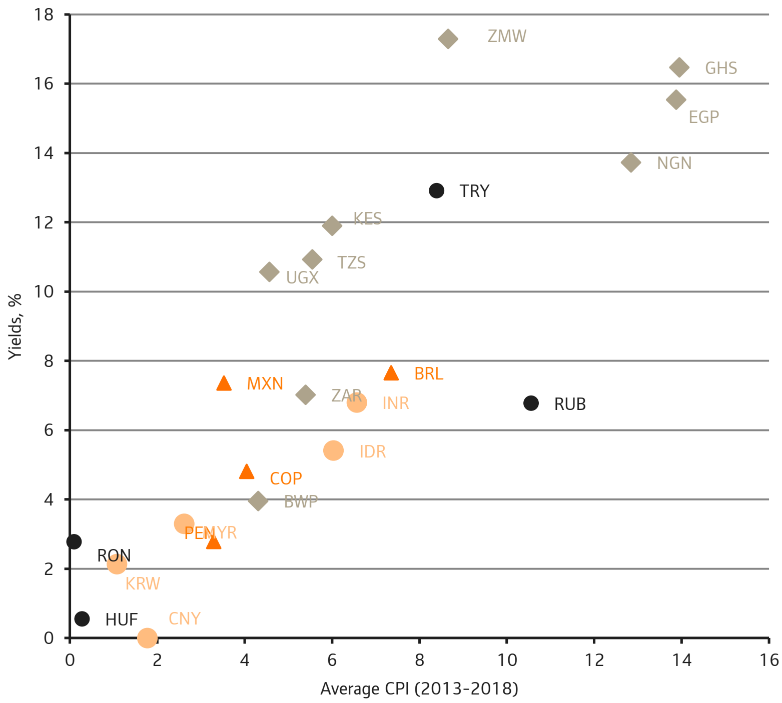
Source: Bloomberg; Standard Bank Research

Figure 20: African Eurobonds spread over UST (1-y)



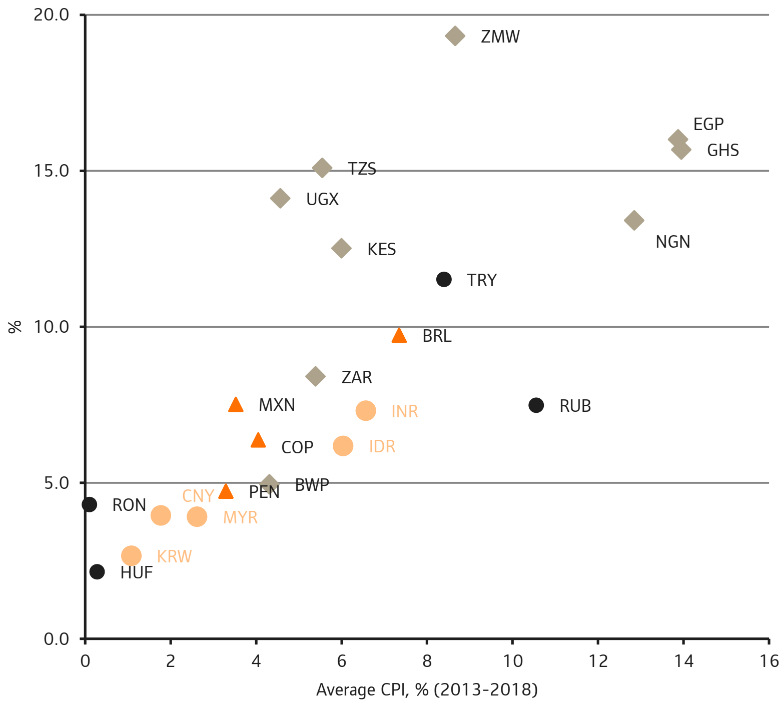
Source: Bloomberg; Standard Bank Research

Figure 21: Local 2-year bonds vs. past and forecast inflation



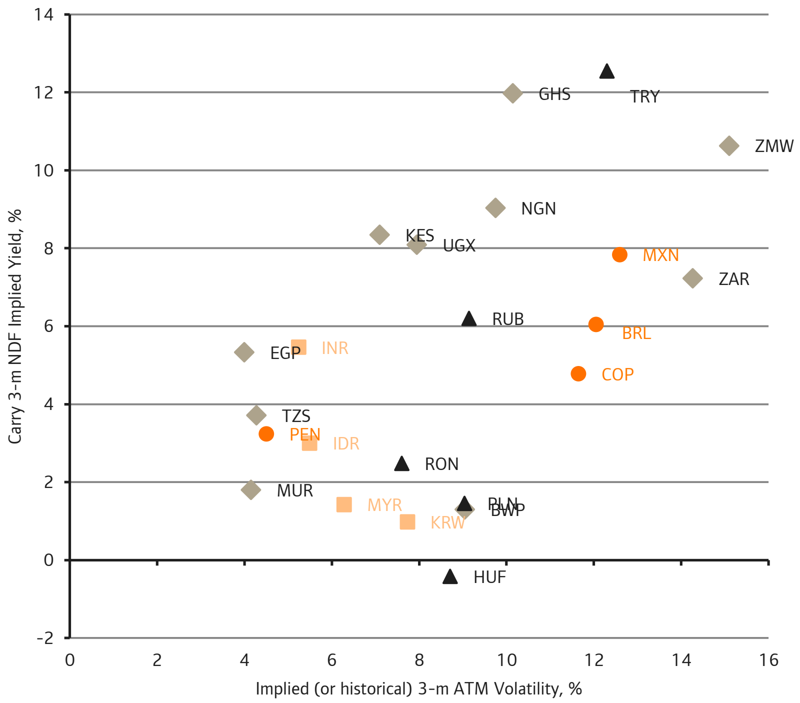
Source: Bloomberg; Standard Bank Research

Figure 22: Local 10-year bonds vs. past and forecast inflation



Source: Bloomberg; Standard Bank Research

Figure 23: NDF carry rates vs. implied vols



Source: Bloomberg; Standard Bank Research

Table of expected returns over the next 3 months

		Yield, %				Total return, %		
Country	**Tenor**	**Current yield**	**Slide**	**Forward**	**SB forecast**	**Slide**	**Forward**	**SB forecast**
Botswana	2Y	3.23	3.06	3.50	2.80	1.6	-0.4	1.6
	5Y	4.27	4.23	4.44	4.20	1.4	-0.3	1.4
	10Y	4.73	4.71	4.83	4.70	1.3	0.4	1.4
Egypt	2Y	15.88	16.14	15.68	15.60	3.6	4.3	4.4
	5Y	15.04	15.08	14.86	15.00	3.6	4.3	3.9
	10Y	15.00	15.05	14.90	15.25	3.5	4.2	2.5
Ghana	2Y	15.68	15.67	16.08	15.80	3.9	3.3	3.7
	5Y	15.91	15.90	16.08	15.70	4.0	3.4	4.6
	10Y	15.95	15.96	16.07	15.60	4.0	3.4	5.7
Kenya	2Y	12.29	12.21	12.92	11.6	3.2	2.1	4.2
	5Y	12.72	12.70	13.01	12.6	3.3	2.2	3.6
	10Y	12.84	12.84	13.04	13.1	3.2	2.2	1.8
Nigeria	2Y	13.52	13.68	13.27	13.60	3.1	3.8	3.3
	5Y	13.27	13.27	13.12	13.20	3.3	3.8	3.6
	10Y	13.33	13.33	13.24	13.10	3.3	3.8	4.6
South Africa	2Y	7.04	7.02	7.06	6.90	1.8	1.7	2.0
	5Y	7.67	7.62	7.72	7.55	2.1	1.7	2.4
	10Y	8.61	8.57	8.67	8.30	2.4	1.8	4.2
Tanzania	2Y	11.53	10.96	12.65	12.3	3.8	1.1	1.6
	5Y	14.18	14.08	14.90	14.1	3.9	1.1	3.8
	10Y	15.07	15.06	15.60	15.8	3.9	1.1	0.2
Uganda	2Y	10.39	10.22	10.64	12.4	2.9	2.2	-0.7
	5Y	12.23	12.10	12.45	13.6	3.5	2.3	-1.8
	10Y	13.87	13.82	14.09	14.6	3.8	2.3	-0.3
Zambia	2Y	16.56	16.11	17.74	16.20	4.8	2.4	4.7
	5Y	18.57	18.53	19.30	17.80	4.8	2.4	7.0
	10Y	19.01	18.99	19.53	18.20	4.8	2.5	8.2

Source: Bloomberg; Standard Bank Research

Notes: Yield curve scenarios: "Slide" = the bond yields slide along the unchanged yield curve, "Forward" = the yield curve evolves according to its embedded forward rates, "SB forecasts"= Standard Bank Research expectations

Asset class expected performance summary (3 months)

	FX	Rates	Credit	Equity
Angola	↓↓	↑	→	
Botswana	↑	→		↑
Côte d'Ivoire	↑↑	→	↑	→
Democratic Republic of the Congo	↑	→		
Egypt	↑↑	↑↑	↑	↑↑
Ethiopia	↓	→	↑	
Ghana	→	→	↑	→
Kenya	↑	↑	→	↑
Malawi	→	↓		
Mauritius	↑↑	↑		↑
Morocco	↑	→	→	↑
Mozambique	↑	↓	→	
Namibia	↑	↑	↑	↑
Nigeria	→	→	↑	↑
Rwanda	↑	↑	→	↑
Senegal	↑↑	→	↑	→
South Africa	→	→	↓	→
Tanzania	↓	→	→	↑
Tunisia	↓	↓	→	→
Uganda	→	→		↑
Zambia	↓	↑	→	→

Source: Bloomberg; Standard Bank Research

Notes: Arrows up (↑↑, ↑) = positive return on the asset class (significant and moderate, respectively), arrows down (↓↓, ↓) = negative return on the asset class (significant and moderate, respectively), horizontal arrows (→) = sideways. FX is against USD and including carry rates. Rates and Equity are in local currency. Credit is in USD.

Recommended trades: performance

Open trades

	Entry date	Entry yield, %	Entry FX	Latest yield, %	Latest FX	Total return, %	
Positions						**Since inception**	**1-month**
Uganda: buy UganGB '18	22-Feb-16	20.50	3440	10.50	3636	39.3	0.9
Ghana: buy GHGB '20	31-Oct-16	20.00	3.99	15.45	4.55	15.8	3.1
Zambia: buy ZAMGB '26	18-Nov-16	24.50	9.81	19.00	9.73	57.1	5.5
Malawi: buy 12-m T-bill	04-Apr-17	23.37	725.23	14.00	725.50	18.6	1.4
Mozambique: sell USD/MZN 12m NDF	12-Apr-17	8.80	66.48	10.58	59.47	18.9	1.3
Egypt: buy 12-m T-bill	02-May-17	18.99	18.06	18.36	17.69	14.4	2.7
Nigeria: buy 12-m T-bill	03-Aug-17	22.60	366.00	14.15	360.01	15.2	1.5
Kenya: sell USD/KES 6m NDF	15-Aug-17	9.06	103.72	7.35	102.30	5.6	1.9
Kenya: buy Kenya IS '24	22-Nov-17	12.23	103.45	11.80	102.40	4.6	2.2
Egypt: buy Egypt '27	23-Nov-17	15.88	17.69	15.20	17.69	5.7	7.6
BEAC: sell USD/XAF 2-y NDF	24-Nov-17	4.25	550.62	4.89	524.89	4.5	8.0
Angola: sell USD/AOA 2-m NDF	19-Dec-17	106.87	166.75	118.19	204.75	-11.0	
Ghana: sell USD/GHS 6-m NDF	19-Dec-17	12.30	4.53	12.22	4.54	1.0	
Zambia: sell USD/ZMW 12-m NDF	19-Dec-17	13.15	9.83	11.90	9.77	2.8	
Total portfolio internal rate of return since prev. AMR (14-Sep-2017)						**4.3**	

Source: Bloomberg; Standard Bank Research

Botswana: near-term weakness likely to persist

GDP growth: modest recovery

GDP growth is likely to recover modestly over the next 2-y to record 3.5% y/y and 3.7% y/y in 2018 and 2019 respectively from what we estimate was growth of 1.5% y/y in 2017. This will likely be driven by a recovery in domestic demand, especially investment spending. As that process unfolds, imports are likely to recover, too, leading to net exports detracting from overall economic growth. Indeed, it is not as if we are anticipating trade surpluses being replaced by deficits. It is just that those surpluses are likely to shrink.

The recovery in domestic demand was already in evidence through the course of 2017. Sure, overall domestic demand actually declined in the first 3 quarters. But this was due to declining investment spending and de-stocking. Neither of these components is likely to persist over the course of the next 2-y.

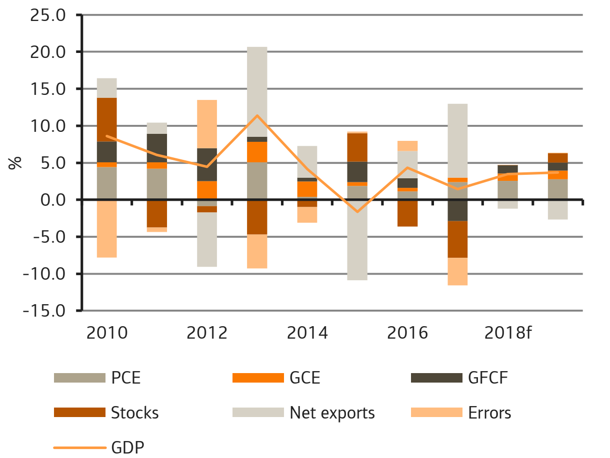
Indeed, even as overall GDP growth dwindled in H1:17, recording just 0.9% y/y, a far cry from 4.3% y/y in 2016, final consumption spending actually accelerated. Private consumption spending averaged just 1.1% y/y in 2016. In the first 3 quarters of 2017, it accelerated to an average of 2.2% y/y. Similarly, government consumption spending accelerated, but not as sharply as private consumption. It averaged 0.6% y/y growth, compared to 0.5% y/y in 2016.

Destocking detracted 5.7 ppts from overall average GDP growth in the first 3 quarters of 2017 after destocking detracted 3.6 ppts in 2016. It seems highly probable that the momentum will shift in 2018. To be sure, our forecasts imply that inventories will have a neutral effect on overall GDP growth this year, before adding 1.3 ppts in 2019.

As already pointed out, investment spending also detracted from overall GDP growth in the first 3 quarters of 2017. In all likelihood, this will not recur either. Macroeconomic conditions are still indicating that investment spending, which hasn't declined in any year since 2005, will recover again. Our forecasts envisage investment spending adding an average of 1.0 ppts over the next 2-y. As that recovery occurs, imports of machinery and equipment, the main component to depress imports in 2017, will recover, too. Hence, net exports are likely to detract from overall growth in the next 2-y.

Closure of the BCL copper mine may have something to do with these adjustments. Mining value added declined by an average of 21.5% y/y in H1:17, recovering to record growth of 4.4% y/y in Q3:17. Diamond production will likely remain a source of strength for overall mining output this year and next.

Composition of GDP growth by demand



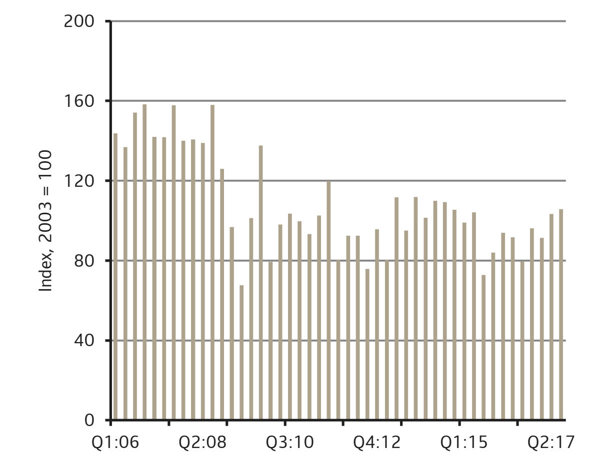
Source: Statistics Botswana; Standard Bank Research

Contribution to GDP by sector (% of total)

	2012	2 014	2 016
Agriculture	1.9	1.6	1.6
Mining	14.7	15.8	11.9
Manufacturing	6.4	5.9	6.0
Water & Electricity	0.5	0.3	0.8
Construction	7.7	7.1	7.5
Trade, hotels, restaurants	17.5	19.3	20.6
Transport & Comm.	5.4	5.5	6.0
Finance & Bus Serv.	14.6	14.0	14.8
General Gov	13.2	12.7	13.0
Soc & Per. Serv.	6.9	6.7	7.0
VA	88.8	89.1	89.2
Taxes on Imports	5.7	5.9	5.7
Other Taxes	6.0	5.5	5.5
Subs	-0.5	-0.5	-0.5
Total GDP	100.0	100.0	100.0

Source: Statistics Botswana; Standard Bank Research

Diamond production



Source: Markit; Bloomberg

Quarterly indicators

	Q1:16	Q2:16	Q3:16	Q4:16	Q1:17	Q2:17	Q3:17	Q4:17e	Q1:18f	Q2:18f	Q3:18f	Q4:18f
GDP (% y/y) pa	2.3	3.9	6.9	4.3	0.9	0.9	1.2	2.7	3.1	3.3	3.7	3.7
CPI (% y/y) pa	2.9	2.7	2.7	2.8	3.9	3.7	2.7	2.9	2.8	2.8	3.1	3.3
M3 (% y/y) pa	11.5	9.9	4.3	4.9	3.8	1.2	4.0	6.0	10.3	12.8	12.7	11.1
CA/GDP (%) pe	8.0	10.4	19.8	11.6	22.5	15.7	15.6	17.0	13.9	13.4	12.4	13.0
FX reserves (USD bn) pe	7.6	7.4	7.6	7.2	7.0	7.3	7.5	7.7	8.0	8.4	8.4	8.2
Import cover (mths) pe	14.7	14.4	14.8	14.0	16.7	17.3	17.7	18.2	14.2	15.1	15.1	14.6
3-m rate (%) pe	1.4	1.1	1.0	1.0	1.3	1.5	1.4	1.3	1.2	1.3	1.3	1.4
5-y rate (%) pe	4.4	4.4	4.0	4.3	4.3	4.4	4.2	4.1	4.3	4.4	4.4	4.5
USD/BWP pa	11.22	10.89	10.62	10.66	10.46	10.32	10.21	10.23	9.40	9.33	9.46	9.61

Source: Bank of Botswana; Statistics Botswana; Ministry of Finance; Standard Bank Research
Notes: pe – period end; pa – period average; na – not available

Political risks: minimal

We don’t see any policy or security risks over the course of this year.

Elections are not until 2019, but the coming year could see much in the way of political noise as various political figures and parties position for the upcoming polls.

There is a widespread desire among the opposition to unseat the long-ruling BDP. However, as was the case in 2014, it seems as if the opposition is not quite united. Back then, the BCP decided to shun the newly formed UDC, opting to contest the elections independently.

Now there is another party, the Alliance for Progressives (AP), keen to contest the elections outside the ambit of the UDC. As a coalition of various parties, the UDC would probably do better than the AP. But it is not entirely clear whether having two opposition parties fielding candidates in the elections would not split the opposition vote. In 2014, the opposition collectively garnered more votes than the ruling party, but the votes were split between the two parties.

Of course, looking at the overall figure may be misleading since these are parliamentary elections in which members of parliament are elected from various constituencies. Nonetheless, the 2014 outcome was an indication that even if the ruling party were to be unpopular, the opposition runs the risk of splitting the opposition vote.

Of course, one has to acknowledge that there may be no such thing as ‘the opposition vote’. Even unity within the UDC is not guaranteed. Some of its members may not be entirely happy with the BCP joining the coalition in time for the 2019 elections. Personality clashes could weaken the opposition coalition, making it hard for it to campaign effectively.

Election results (2014)

Legislative election	Seats	% of votes
Botswana Democratic Party (BDP)	37	46
Umbrella for Democratic Change (UDC)	17	30
Botswana Congress Party (BCP)	3	20
Independents	0	1
Indirectly-elected seats	-	6
Total	**57**	**100**

Source: Independent Electoral Commission

Botswana

Balance of payments: still healthy

It looks ever more likely that the C/A surplus is going to decline in the next 2-y. The factors that boosted it in 2016 appear unlikely to be repeated. Even then, we anticipate FX reserves rising somewhat over the course of 2018 to just over USD8.2bn, and remaining at that level in 2019.

Admittedly, the trajectory of imports over the coming 2-y could be a lot more volatile than we are forecasting. Hence, there is a risk that the trade surplus could decline by more than we are anticipating, should imports recover much more strongly than we anticipate.

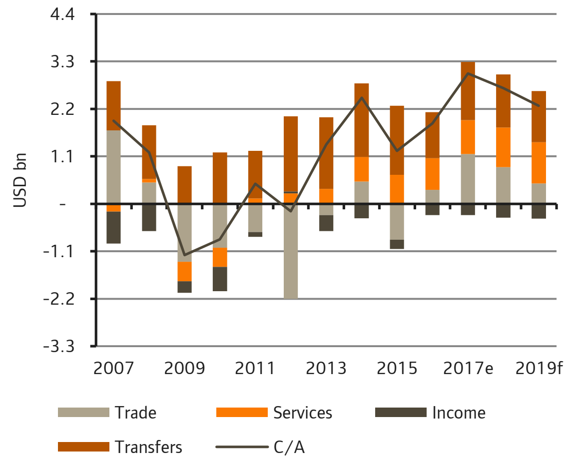
Mining production subsided in late 2016 and early 2017, mainly driven by copper/nickel and coal production. This inevitably dampened imports, especially of machinery and equipment. This subsidence is unlikely to be enduring. Sure, we are not anticipating a recovery in imports to the pre-2016 levels. But we believe that there will be a recovery from the levels in early 2017. As that happens, the trade surplus will likely diminish somewhat over the course of the next year.

We anticipate tourism inflows remaining robust, ensuring that the services balance improves over the course of the next 2-y. Together with strong net transfer inflows, the C/A will likely remain in surplus, even if moderating somewhat.

Financial outflows will likely predominate. Net FDI outflows tend to characterise the BOP. A lack of adequate opportunities also means that net portfolio outflows will likely dominate over the coming 2-y.

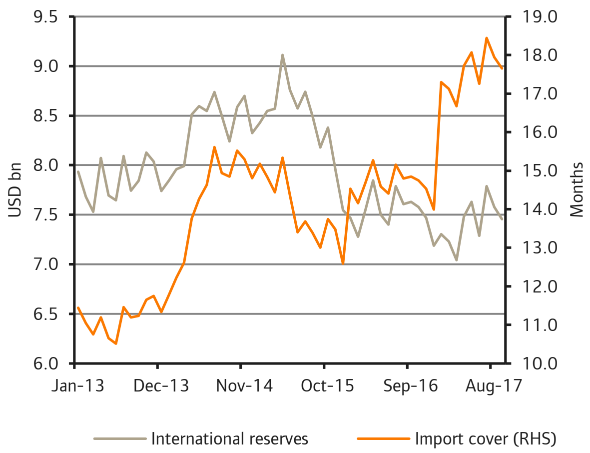
Given these developments, it is likely that FX reserves will rise to USD8.2bn by the end of this year, covering 14.6-m of imports.

Current account



Source: Bank of Botswana; Standard Bank Research

FX reserves

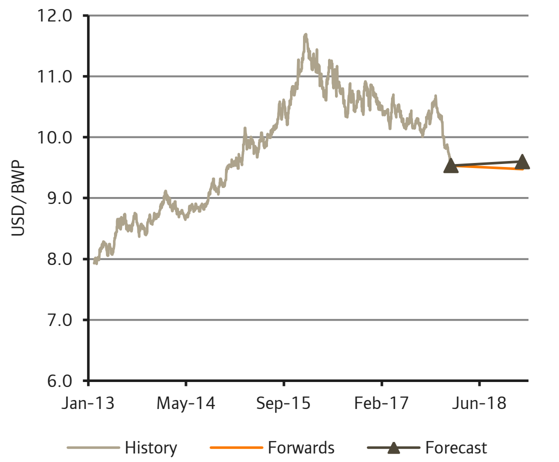


Source: Bonk of Botswana; Statistics Botswana; Standard Bank Research

FX outlook: the BWP to follow the ZAR

With effect from 1 Jan, the government decided to change the rate of crawl of the BWP. The BOB will manage FX policy in order to maintain an upward rate of crawl of 0.3% per annum. During 2017, the BOB managed FX policy so as to ensure a downward rate of crawl of 0.26%. In truth, chances are that FX market players are not going to feel much of an impact as a result of the change. The ultimate aim for exchange rate policy is to keep the real exchange rate stable, something that will likely continue to be achieved this year. At the end of Sep 17, the real effective exchange rate calculated by the BOB was 100.2, the same as it was at the end of2016, having reached a 2017 high level of 100.7 in Mar. Interestingly, the government decided to maintain the composition of the peg at 45% for the ZAR and 55% for the SDR. All this implies that the BWP will continue to follow the ZAR's lead over the foreseeable future.

USD/BWP: forwards versus forecasts



Source: Bloomberg; Standard Bank Research

Monetary policy: easing bias

The likelihood of the BOB's MPC lowering the bank rate again is very high. With economic activity stagnant and inflation pressures muted, there is plenty of justification for the MPC to lower the policy rate.

Strictly speaking, inflation registered 2.9% y/y in Nov, and is below the lower bound of the 3.0% - 6.0% y/y objective range. Indeed, it has been in the lower half of the range since Sep 14, averaging 3.1% y/y in that period.

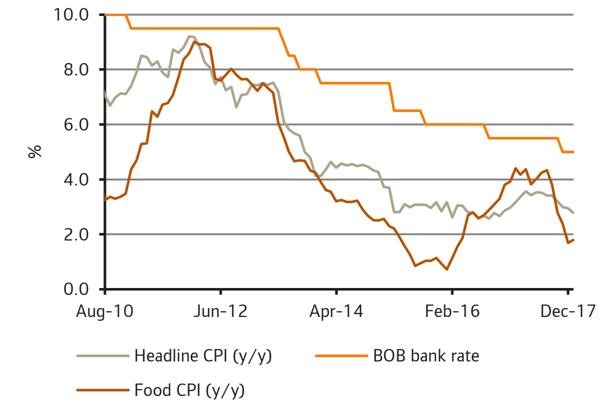
Our expectation is that it will remain below the 4.5% y/y mid-point of the objective range for the next 2-y. In fact, we expect it remaining below 3.0% y/y throughout H1:18.

Evidently, there are no indications that there are any underlying inflation pressures in the economy. The trimmed mean measure of inflation fell below 3.0% y/y in Aug, averaging 2.7% y/y since then. The trimmed mean CPI has registered average growth of just 0.1% m/m in the previous 6-m. Although the index rose by 0.3% m/m in Nov, it will likely remain quiescent for quite some time.

The inflation pressures, such as they were, that led to headline inflation rising to 3.6% y/y in Mar 17, the highest reading in 26-m, proved to be transient. Food inflation, rising to a peak of 4.4% y/y in Mar 17, was one of the factors that underpinned the rising trajectory in headline inflation. But that pressure has since dissipated, with food inflation declining to 1.7% y/y in Nov 17.

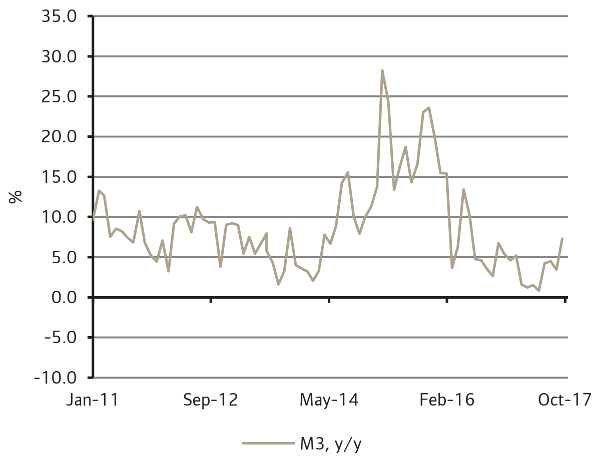
Administered prices were also another factor that underpinned the rising trajectory in headline inflation. Indeed, of the components of the CPI that were still rising at over 3.0% y/y in Nov, administered prices were probably a feature. Besides restaurants (food), those were education, alcohol and tobacco (due to sin taxes), and housing (electricity and water tariffs).

Inflation and interest rates



Source: Bank of Botswana; Statistics Botswana; Standard Bank Research

Money supply

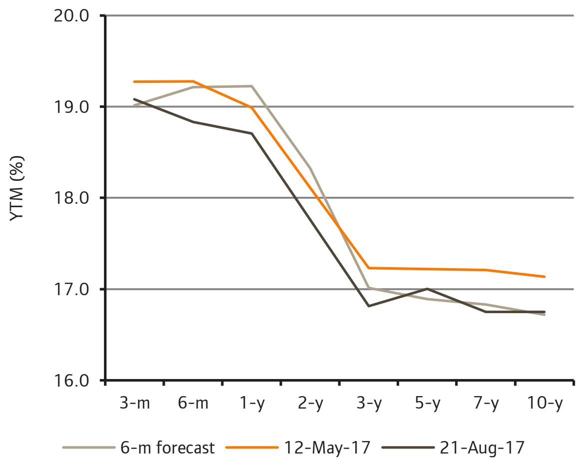


Source: Bank of Botswana

Yield curve outlook: marginal bull flattening

In absolute terms, yields are probably going to be largely unchanged over the next 4-m. Of course, there will likely be an auction of a 6-m T-bill and some bonds in early Mar when there will be an opportunity for price discovery. It would be at that auction that there would likely be a meaningful movement in yields. If we are correct in our view regarding the monetary policy stance, then the easing would likely occur in Q1:18, setting the stage for yields to decline, even if marginally, in the period leading up to the Mar auction. Of course, over the coming 4-m we will also get to hear the FY2018/19 budget presented. In truth, there is probably not be a significant departure from the conservative fiscal stance that the government has exhibited in the past 10-y. Hence, there is no reason to believe that the fiscal deficit will be so large as to prompt the government to increase the amount it borrows from the domestic market.

Changes in the yield curve



Source: Bank of Botswana; Standard Bank Research

Fiscal policy: expenditure restraint

Even though the budget balance was marginally in surplus in H1 of FY2017/18, the government seems to believe that the balance will worsen this fiscal year. In presenting the Budget Strategy Paper to parliament, the Finance Minister indicated that he expected the deficit for FY2017/18 to widen to BWP6.5bn from the originally budgeted BWP2.4bn.

Interestingly though, the cumulative balance in the first 6-m of the fiscal year amounted to a surplus of BWP106.9m. At BWP24.9bn, total revenue collection and grants was about 51.4% of the annual figure. Meanwhile, expenditure and net ending was just 49.2% of the budgeted annual total.

This is a familiar pattern by now, with the government proving to be far more conservative in expenditure execution that what is budgeted for. As a consequence, it seems highly probable that the government will maintain this conservative stance for the remainder of the year. Clearly, the main element of this outcome is expenditure restraint. However, it also still appears that revenue collection is somewhat better than the government may have anticipated.

Hence, we are inclined to believe that the signal provided by the Finance Ministry with regard to the FY2018/19 budget might just be a lot more expansionary than might turn out to be the case. The government anticipated that the fiscal deficit will widen to BWP8.0bn that year.

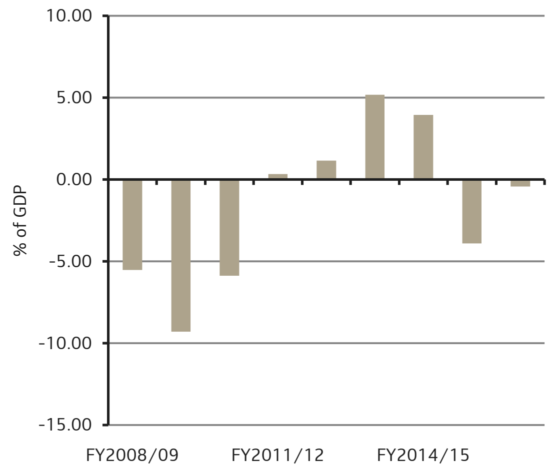
In part, our reticence to believe that the government would allow the deficit to widen that much is the determination of the government to limit fiscal deficits, as espoused in the National Development Plan. Secondly, in order to finance those deficits the government would probably draw down on its accumulated savings, potentially reducing reserves. This is something that might prove unacceptable, and prompt the government to restrict expenditure instead.

Central government budget

% of GDP	FY2015/16	FY2016/17	FY2017/18
Total revenue	33.0	30.7	29.2
Total expenditure	32.1	31.3	30.4
Recurrent	26.6	21.4	21.4
- wages	10.9	-	-
-interest	0.5	-	-
- development	7.5	8.1	8.4
Overall balance (+ grants)	-4.4	-0.5	-1.3
Overall balance (- grants)	-4.6	-0.6	-1.3
Net external borrowing	0.0	0.0	-
Net domestic borrowing	0.4	0.4	-
Donor support (grants)	0.2	0.2	-

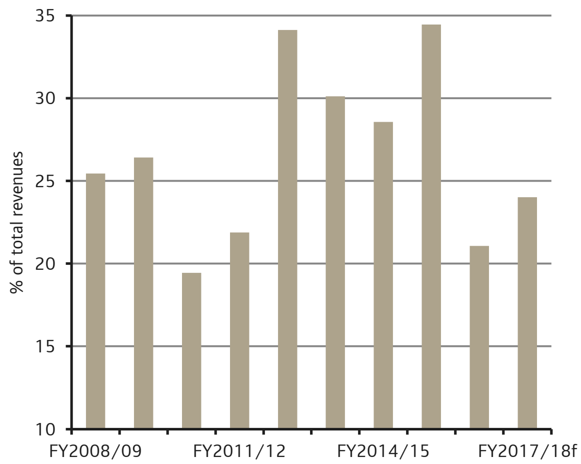
Source: Ministry of Finance and Development Planning

Fiscal balances



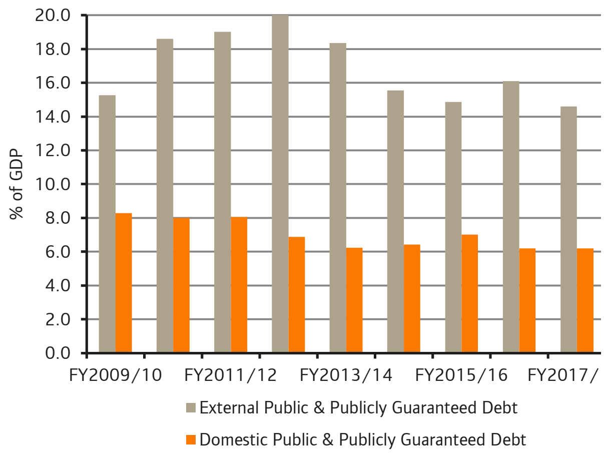
Source: Ministry of Finance and Development Planning

SACU revenues



Source: Ministry of Finance and Development Planning

External and domestic debt



Source: Ministry of Finance and Development Planning

Annual indicators

	2013	2014	2015	2016	2017e	2018f	2019f
Output							
Population (million)	2.1	2.1	2.1	2.1	2.2	2.2	2.2
Nominal GDP (BWP bn)	125.2	145.9	145.9	169.7	180.0	191.6	205.107
Nominal GDP (USD bn)	14.82	16.21	14.31	15.64	17.47	20.28	21.17
GDP / capita (USD)	7 211	7 846	6 892	7 499	7 939	9 218	9 622
Real GDP growth (%)	11.4	4.2	-1.6	4.3	1.4	3.5	3.7
Diamond production ('000 carats)	22 693	24 658	20 824	22 000	23 000	23 000	23 200
Coal (thousand tons)	1 496	1 712	2 066	2 100	2 200	2 300	2 200
Central Government Operations							
Budget balance (incl. grants) / GDP (%)	1.1	5.2	3.9	-4.4	-0.5	-1.3	-1.5
Domestic debt / GDP (%)	5.5	5.0	5.4	5.1	5.2	5.2	5.3
External debt / GDP (%)	17.5	15.2	17.2	14.8	14.0	13.6	13.4
Balance Of Payments							
Exports of goods and services (USD bn)	7.8	8.4	6.2	6.5	6.2	7.6	8.4
Imports of goods and services (USD bn)	8.1	7.9	7.0	6.2	5.1	6.7	8.0
Trade balance (USD bn)	-0.3	0.5	-0.8	0.3	1.2	0.9	0.5
Current account (USD bn)	1.37	2.45	1.23	1.86	3.02	2.68	2.27
- % of GDP	9.6	15.6	8.2	11.6	17.2	13.2	12.9
Capital & Financial account (USD bn)	-0.95	0.27	-0.73	-0.44	-1.61	-2.30	-2.57
- FDI (USD bn)	0.30	0.40	0.49	-0.58	-0.56	0.36	-0.18
Basic balance / GDP (%)	11.3	17.6	12.0	8.2	14.1	15.0	9.9
FX reserves (USD bn) pe	7.7	8.3	7.5	7.2	7.7	8.2	8.2
- Import cover (months) pe	11.5	12.6	12.9	14.0	18.2	14.6	12.4
Sovereign Credit Rating							
S&P	A-	A-	A-	A-	A-	A-	A-
Moody's	A2	A2	A2	A2	A2	A2	A2
Fitch	NR	NR	NR	NR	NR	NR	NR
Monetary & Financial Indicators							
Consumer inflation (%, y/y) pa	5.9	4.4	3.1	2.8	3.3	3.0	3.3
Consumer inflation (%, y/y) pe	4.4	4.1	3.1	2.8	2.9	3.3	3.5
M3 money supply (%, y/y) pa	6.0	7.8	18.6	7.7	3.8	11.7	7.8
M3 money supply (%, y/y) pe	4.0	10.0	19.9	5.4	6.4	10.7	7.6
BOB overnight lending rate (%) pa	8.6	7.5	6.8	5.8	5.4	4.3	4.3
BOB overnight lending rate (%) pe	7.5	7.5	6.0	5.5	5.0	4.3	4.3
3-m rate (%) pe	3.6	3.3	1.2	1.0	1.3	1.4	1.3
5-y rate (%) pe	4.9	5.0	5.5	4.3	4.1	4.5	4.5
USD/BWP pa	8.4	9.0	10.2	10.8	10.3	9.4	9.7
USD/BWP pe	8.7	9.3	10.9	10.7	10.2	9.6	9.7

Source: Bank of Botswana; Statistics Botswana; Ministry of Finance and Development Planning; Bloomberg; Standard Bank Research
Notes: pe – period end; pa – period average; na – not available; nr – not rated

Glossary

For brevity, we frequently use acronyms that refer to specific institutions or economic concepts. For reference, below we spell out these and provide definitions of some economic concepts that they represent.

14-d	14-day, as in 14-d deposit, which denotes 14 day deposit
10-y	10-year
16 Jan 13	16 January 2013
3-m	3 months
3m	3 million, as in USD3m, which denotes 3 million US dollars
3bn	3 billion, as in UGX3bn, which denotes 3 billion Ugandan shillings
3tr	3 trillion, as in TZS3.0tr, which denotes 3 trillion Tanzanian shillings
AOA	Angola Kwanza
BAM	Bank Al Maghrib
BCC	Banque Central du Congo (Central Bank of Congo)
BCEAO	Banque Central des États de L'Afrique de l'Ouest (Central Bank of West African States)
BCT	Banque Central de Tunisie
BM	Banco de Moçambique
BNA	Banco Nacional de Angola
BOB	Bank of Botswana
BOG	Bank of Ghana
BOM	Bank of Mauritius
BON	Bank of Namibia
BOP	Balance of payments – a summary position of a country's financial transactions with the rest of the world. It encompasses all international transactions in goods, services, income, transfers, financial claims and liabilities.
BOT	Bank of Tanzania
BOU	Bank of Uganda
BOZ	Bank of Zambia
BR	Bank Rate (Reserve Bank of Malawi)
BRVM	Bourse Régionale des Valeurs Mobilières (Regional Securities Exchange)

BWP	Botswana Pula
C/A	Current account balance. This is the sum of the visible trade balance and the net invisible balance of a country. The latter includes net service, income and transfer payments.
Capital account	Captures the net change in investment and asset ownership for a nation by netting out a country's inflow and outflow of public and private international investment.
CBE	Central Bank of Egypt
CBK	Central Bank of Kenya
CBR	Central Bank Rate
CDF	Congolese Franc
CPI	Consumer Price Index – An index that captures the average price of a basket of goods and services representative of the consumption expenditure of households within an economy.
Discount rate	Policy rate for Bank of Uganda
Disinflation	A decline in the rate of inflation. Here prices are still rising but with a slower momentum.
Disposable income	After tax income
DM	Developed markets
ECB	European Central Bank
EGP	Egyptian pound
EM	Emerging markets
ETB	Ethiopian Birr
Eurobond	A bond denominated in a currency other than the home currency of the issuer.
Exports	The monetary value of all goods and services produced in a country but consumed broad.
FMDQ	FMDQ OTC Securities Exchange, Nigeria
FX	Foreign Exchange
FY2016/17	2016/17 fiscal year
GCE	Government Consumption Expenditure - Government outlays on goods and services that are used for the direct satisfaction of the needs of individuals or groups within the community. This would normally include all non-capital government spending.
GDE	Gross domestic expenditure, the market value of all goods and services consumed in a country – both private and public – including imports but excluding exports. This is measured over a period of time – usually a quarter/year.
GFCF	Gross Fixed Capital Formation – this is investment spending, the addition to capital stock such as equipment, transportation assets, electricity infrastructure, etc to replace the existing stock of productive capital that is used in the production of goods and services in a given period of time, usually a year/quarter. Normally, the higher the rate of capital, the faster an economy can grow.

GDP	Gross Domestic Product – the monetary value of all finished goods and services produced in a country in a specific period, usually a year/quarter.
GHS	Ghanaian Cedi
H1:16	First half of 2016
Imports	The monetary value of goods and services produced abroad and consumed locally.
Inflation	The rate at which the general level of prices of goods and services are rising. It is usually measured as the percentage change in the consumer price index over a specific period, usually a month/year.
Invisible trade balance	The value of exports of services, income and transfers, less imports of same.
Jan 16	January 2016
KBRR	Kenya Bankers' Reference Rate
KES	Kenya Shilling
KR	Key Rate (Bank Al Maghrib)
KRR	Key Repo Rate
m/m	Month on month, in reference to a rate of change
MAD	Moroccan Dirham
MLF	Marginal Lending Facility
MOF	Ministry of Finance
MPC	Monetary Policy Committee, the committee that makes the decision on policy rates
MPR	Monetary Policy Rate
MUR	Mauritian Rupee
MWK	Malawian Kwacha
MZN	Mozambican Metical
NAD	Namibian Dollar
NBE	National Bank of Ethiopia
NBR	National Bank of Rwanda
NEER	Nominal Effective Exchange Rate. This is the weighted average rate at which a country's currency exchanges for a basket of currencies, usually trading partner currencies. It is measured in index format.
NGN	Nigerian Naira
Nominal GDP	The monetary value of all finished goods and services produced in a country in a specific period, usually a year/quarter, measured in current prices.
NPL	Non-Performing Loans

Parity	Refers to the par or nominal value of a debt instrument. This is usually the price at which the said instrument is redeemed on maturity.
PCE or HCE	Personal or Household Consumption Expenditure: The monetary value of household purchases of durable goods, non-durable goods, semi durables and services within a given period of time, usually a year/quarter.
PR	Policy Rate
Prime rate	key lending rate
q/q	quarter on quarter, in reference to a rate of change
Q1:16	First quarter of 2016
RBM	Reserve Bank of Malawi
Real GDP	The monetary value of all finished goods and services produced in a country in a specific period, usually a year/quarter, measured in constant prices.
REER	Real Effective Exchange Rate. This is the weighted average rate at which a country's currency exchanges for a basket of currencies - usually trading partner currencies – while taking into account any changes in relative prices between the host country and its trading partners. It is often measured in index format.
RWF	Rwandan Frank
SARB	South African Reserve Bank
SDF	Standing Deposit Facility (Mozambique)
SLF	Standing Lending Facility (Mozambique)
T-bill	Treasury bill – A short-dated, government backed security that yields no interest but is issued at a discount over a period of less than one year.
TND	Tunisian Dinar
Treasury bond	A marketable government debt security with a maturity of a year or longer
TZS	Tanzanian Shilling
UGX	Uganda Shilling
USD	US Dollar
VAT	Value Added Tax
Visible trade balance	The value of exports of visible goods less imports.
WAEMU	West African Economic and Monetary Union, also known as Union Economique et Monetaire Ouest Africaine (UEMOA)
XAF	Central African Franc
XOF	West African Franc
y/y	Year on year, in reference to a rate of change

Yield	The return on an investment, usually expressed as a percentage over a period of time, usually a year.
YTD	Year to date
ZAR	South African Rand
ZMW	Zambian Kwacha

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