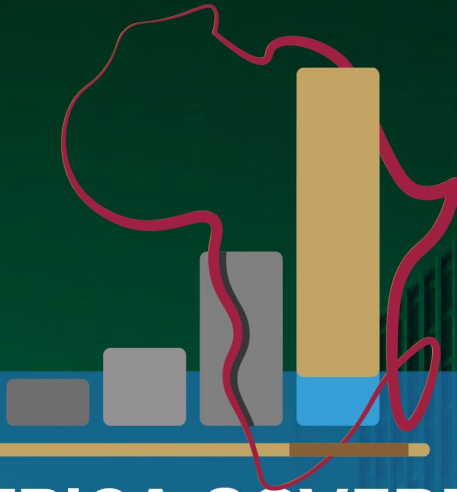




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AFRICA SOVEREIGN CREDIT RATING REVIEW

**2023 Year-End
Outlook**

An Institution of the
**African
Union**



8TH EDITION



ECA

**Africa Peer Review Mechanism
Continental Secretariat**
Directorate of Governance & Specialized Reporting
in Collaboration with the
United Nations Economic Commission for Africa (UNECA)

ABOUT THIS REPORT

This report analyses the long-term foreign currency sovereign credit rating actions in Africa by the three dominant international credit rating agencies (CRAs) – Moody's Investors Service, Fitch Ratings and S&P Global (S&P) Ratings – during the second half of 2023 (2023H2) and makes recommendations to both CRAs and African governments on how credit ratings can be improved.

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■ INTRODUCTION

The trend of negative sovereign credit ratings continued to dominate in the 2023H2 due to the growing fiscal pressure in a number of African countries coupled with concerns over the ‘wall of Eurobond maturities’ in 2024. The continent faces a period of huge principal maturities, peaking in this year, as investors are expecting to redeem a combined estimate of US\$11.3 billion in outstanding Eurobonds. With limited access to international financial markets, the elevated maturities increase financing and liquidity pressures. The African Union economic policy organ – the Specialized Technical Committee (STC) of Ministers of Finance, Monetary Affairs, Economic Planning and Integration – during its 6th Ordinary Session in Nairobi, Kenya, attributed the deteriorating financing conditions to the failure of the global financial architecture to support emerging economies on their efforts towards structural and productive transformation. The existing architecture has been unable to support the mobilization of affordable stable and long-term financing at a scale of investments needed to combat poverty, inequality and unemployment.

During the inaugural session of the 2023 Africa Climate Summit (ACS), President William Ruto of Kenya questioned¹ operations of the international CRAs, criticising them for making it difficult for the ‘junk’ rated countries to attract investments. Poor credit ratings, amongst other challenges faced by African sovereigns, has renewed the momentum towards implementing various initiatives aimed to address fiscal vulnerabilities. It is based on this observation that the 6th Ordinary Session of the STC adopted a Declaration endorsing the ‘establishment of a private sector driven African Credit Rating Agency, based

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¹ <https://kenyanwallstreet.com/activities-of-credit-rating-agencies-under-scrutiny/#:~:text=President%20Ruto%20said%20the%20agencies,it%20difficult%2C%E2%80%9D%20said%20Ibrahim.>

on self-funding and sustaining' to provide alternative rating opinions to the dominant three international CRAs. The Africa Debt Monitoring Mechanism (ADMM)² and the Africa Financial Stability Mechanism³ are the other programs adopted by the African Union policy organs for immediate implementation to build the capacity for effective debt management. The restructuring of Gabon's debt is also an example of the solutions being implemented to address the issues of debt and climate change.

² Established during the Africa Climate Summit in September 2023 where African leaders agreed to adopt the ADMM by June 2024. The mechanism will serve as a platform for the AU to access information on debt to help countries engage in debt negotiations in line with Agenda 2063

³ Established to complement the global safety nets offered by the IMF to offer liquidity support for countries in crisis.

As part of its Research and Advisory function⁴, the APRM has severally pointed out the material weaknesses in the Environmental, Social and Governance (ESG) rating criteria which include subjectivity, inconsistencies and lack of transparency. In a positive development, S&P Global Ratings announced⁵ its decision to drop ESG scores from its debt ratings, which signals a recognition of the challenges and limitations of subjectivity, the lack of standardized measurement in methodologies associated with these metrics as noted in previous editions of this report.

⁴ <https://www.pacci.org/africa-sovereign-credit-rating-review-2022-end-of-year-outlook/>

⁵ https://www.spglobal.com/_assets/documents/ratings/esg_credit_indicators_mr.pdf

GENERAL RATING OUTLOOK

The outlook in 2023H2 remained negative, extending the downward rating trend in the first half of 2023 (2023H1) when no single African country was upgraded during that period. African governments again experienced more credit rating downgrades and negative changes in outlooks than upgrades and positive outlooks. Out of the 23 sovereign rating actions by the three international CRAs during the 2023H2 period, 17 were negative (downgrades and negative

change in outlooks), distributed amongst 10 countries. Congo was the only sovereign to be upgraded whilst 4 countries – Benin, Eswatini, Nigeria and Rwanda – had a positive change in outlook during this period, compared to 5 that were downgraded. This reverses the gains made during the same period in 2022H2, when 5 countries were upgraded while 6 had a positive change in outlooks. The rating actions are summarized in Table 1 below.

Table 1: Summary of sovereign credit rating actions (Jul – Dec 2023)

Sovereign	Moody's			S&P			Fitch		
	Previous	Current	Direction	Previous	Current	Direction	Previous	Current	Direction
UPGRADES									
1. Republic Congo				CCC+ (stable)	B- (stable)	↑			
Total						1			
DOWNGRADES									
1. Cameroon	B2 (stable)	Caa1 (stable)	↓	B- (stable)	CCC+ (stable)	↓			
2. Egypt	B3 (negative)	Caa1 (stable)	↓	B (negative)	B- (stable)	↓	B (negative)	B- (stable)	↓
3. Ethiopia	Caa2 (negative)	Caa3 (stable)	↓	CCC (negative)	SD (n/a)	↓	CCC-	RD (NR)	↓
4. Niger	B3 (stable)	Caa2 (under review)	↓						
5. Uganda				B (negative)	B- (stable)	↓			
Total		4			4			2	
POSITIVE CHANGES IN CREDIT RATING OUTLOOKS									
1. Benin				B+ (stable)	B+ (positive)	↑			
2. Eswatini	B3 (stable)	B3 (positive)	↑						
3. Nigeria	Caa1 (stable)	Caa1 (positive)	↑	B- (negative)	B- (stable)	↑			
4. Rwanda	B2 (negative)	B2 (stable)	↑				B+ (Negative)	B+ (Stable)	↑
Total		3			2			1	
NEGATIVE CHANGES IN CREDIT RATING OUTLOOKS									
1. Cameroon							B (stable)	B (negative)	↓
2. Gabon	Caa1 (stable)	Caa1 (negative)	↓				B- (stable)	B- (negative)	↓
3. Kenya	B3 (under review)	B3 (negative)	↓				B (stable)	B (negative)	↓
4. Mozambique	Caa2 (positive)	Caa2 (stable)	↓						
5. Niger	Caa2 (under review)	Caa2 (negative)	↓						
Total		4						3	

Source: Authors' compilation using data from primary sources, 2023

Ethiopia became the latest African country to default on its single outstanding US\$1 billion sovereign bond, joining Zambia and Ghana, which defaulted in 2020 and 2022, respectively. Ethiopia was downgraded three times by Fitch Ratings due to a material decline in external liquidity, increasing external financing gaps and the government's participation in the G20 Common Framework (CF) debt relief initiative. However, there are some disparities in the interpretation of the default events in the three countries amongst the three international CRAs. Rating agencies define defaulting as failure by the issuer to honour a portion of its debt obligations. Whilst S&P downgrades defaulting countries to 'the selective default' rating, for Moody's most sovereign issuers

that are assigned Caa ratings usually receive these ratings after they have defaulted. Hence, S&P holds Ethiopia, Ghana and Zambia in 'selective default', whilst Moody's have not yet classified these countries as defaulting and still hold Zambia at Ca (stable) since April 2020, Ghana at Ca (Stable) since November 2022 and Ethiopia at Caa3 (Stable) since September 2023.

Mauritius, which only had an unsolicited rating from Moody's since March 1996, was assigned a BBB- with a stable outlook for the first time by S&P Global.

CONTINENTAL KEY RATING DRIVERS

The rating downgrades in 2023H2 were driven by the following underlying and emerging key risks. The emergence of cash management and liquidity challenges for some governments evidenced by delays in meeting external debt service payments, worsening debt affordability trend, the persistence of foreign currency shortages in the face of increasing external debt service payments, and the increasingly constrained policy options to rebalance economies without exacerbating social risk. A negative outlook in Gabon followed the military coup on 30 August 2023, which reflected a high political uncertainty, the risk of sanctions that could affect debt repayments. Revisions of ratings in Cameroon and Kenya reflected increased liquidity pressures related to the country's higher spending needs and challenging domestic and external market financing conditions. The positive rating actions were driven by the stabilising public debt/GDP and strong economic growth prospects.

AFRICA SOVEREIGN DEBT MARKET AND OUTLOOK FOR 2024H1

Ethiopia is the latest African country to default on its single outstanding US\$1 billion Eurobond

following the government's failure to pay the US\$33 million Eurobond coupon that was due on 11 December 2023. In 2023H2, no African country issued a sovereign bond, making Egypt and Morocco – which issued a combined US\$4 billion in 2023H1 – the only countries on the continent to tap into the international bond market the whole of 2023. The main reason for this outcome is the excessively high cost of borrowing, which has made financing through selling international bonds an unsustainable option. These developments have been interpreted by financial markets as 'Africa being shut-out of the international financial markets', raising their yields further as the perception of defaulting on outstanding bond obligations spike upwards. The fears from international investors that more developing countries could default in 2024 have annihilated the significant improvements in the macroeconomic environment of some countries in the 2023H1. We therefore project, at best, the ratings in the 13 African countries identified by the International Monetary Fund (IMF) as 'in debt distress'⁶ to remain unchanged.

Despite the limited financing options available to African countries, we expect some positive rating developments in the following countries during the 2024H1. First, we project Zambia to map a way through the contested conditions for restructuring its US\$3 billion Eurobonds agreeable with both official and commercial creditors to come out of default. Second, Cote d'Ivoire one of the five African countries amongst the 10 world's fastest-growing economies in 2023/24, will likely be upgraded based on

⁶ <https://www.imf.org/external/pubs/ft/dsa/dsalist.pdf>

significant improvement in the fiscal and debt metrics. Cote d'Ivoire registered a GDP growth rate of 7.2% in 2023 and is projected to have a 7.0% in 2024 owing to accelerated reforms and investments in the National Development Plan (NDP) 2021–2025 and commencement of production at the Baleine gas and oil field discovered in 2021–22⁷. Senegal and Rwanda, which are on a strong economic growth path, are also expected to receive positive rating actions in 2024H1.

CHALLENGES IN RATING SERVICES

Through mechanisms of open engagements with the international CRAs, there are prospects that several challenges including errors in publishing ratings and commentaries, analyst location, impromptu rating actions, and announcements could be addressed in the medium-term. There are however some areas that require immediate action:

⁷ <https://www.afdb.org/en/countries/west-africa/cote-d%E2%80%99ivoire/cote-divoire-economic-outlook>

- i. **Integrity of ratings and commentaries:** there were two countries that were assigned conspicuously contestable rating actions and commentaries in 2023H2. Moody's upgraded Nigeria's outlook from stable to positive, which indicates the likelihood of an upgrade in the country's credit rating on account of a positive impact on its credit risk profile in the short to medium-term. In its rating action, Moody's cited positive economic policy developments in Nigeria following the government's cuts to fuel subsidies and moves to drastically simplify and unify the country's various foreign exchange rates. However, largely the same factors were present when Moody's downgraded Nigeria in 2023H1, which was challenged by the government on the basis that the rating agency lacked an understanding of the country's domestic environment. Hence, the reversal of Nigeria's rating direction in the short-term could be interpreted as evidence in support of the government's claim that the rating agency erred in its analysis.

Box 1 : Moody's speculative comments on Kenya's planned Eurobond buyback

On 02 August 2023, Moody's Investors Service made comments in which the rating agency stated that it would treat Kenya's planned buyback of a portion of its Eurobond debt as a default. Moody's comments, which were made prematurely before the official details and the terms of the buyback were made public, mischaracterized Kenya's prospective Eurobond buyback as a 'distressed exchange which will result in economic losses to creditors'. The APRM viewed the comment as highly speculative and damaging as it had conveniently ignored the 'voluntary' nature of the proposed bond buyback program, which allowed investors the right not to participate. Moody's comment triggered a selloff in Kenya's Eurobonds, a spike in yield, and an associated decline in the domestic currency which derailed the government's fiscal efforts, diminished investors' appetite, and compromised the success of the buyback program. The APRM further considered Moody's speculative comments on Kenya's default event as a prejudicial pre-emptive rating action and equates it to a 'premature release of a credit rating to the public'.

Source : APRM Media Statement G&SR-CRA02/2023

ii. **Defective ESG rating score:** whilst ESG rating is important for sustainable and ethical investment decisions, its metrics are still misleading due to the risk of greenwashing and weaknesses in the methodologies. The move by S&P, the largest and oldest of the three international CRAs, to drop ESG scores from their debt ratings is a significant development that reflects the weaknesses and lack of effectiveness of such scores in assessing the creditworthiness of companies and governments. S&P should encourage the other dominant rating agencies to acknowledge the weaknesses in their ESG ratings and either revise their metrics or follow suit to drop the criterion.

iii. **Common definitions of default events:** disparities and contradictions across international CRAs in the critical definition of default present credibility challenges. On 08 August 2023, S&P lowered⁸ its long-term foreign currency sovereign credit rating on Cameroon to 'Selective Default' from B- due to late payment of coupon on commercial debt. This was reversed two days later⁹, upgrading the rating to CCC+ (Stable) after it was reported to the agency that Cameroon had met all commercial debt service obligations. On the contrary, Fitch Ratings did not treat this delay in coupon payment as a default as they applied a 30-day grace period for debt service payments. Moody's, although it considered the delayed payment as an incident of default, it only downgraded Cameroon's rating from B2 (Stable) to

Caa1 (Stable). The same happened on Ethiopia in which Fitch rating is 'default' whilst Moody's still rate the country 'Caa3' with a stable outlook. The differences in interpretation of default events raises questions around the credit ratings definitions, methodological weaknesses that do not account for the basics like grace period for debt service payments, causing some rating agencies to take a rating action quicker than others.

iv. **Weakness in information verification mechanisms:** international CRAs undertook rating actions on Cameroon in August of the 2023H2 based on unverified public information relating to late external debt service payments between January and November 2022. Rating agencies' reports^{10,11} on Cameroon's delayed debt service payments suggest that the CRAs did not have timely and factual official information regarding the status of the country's repayments on all commercial debt service obligations.

10 <https://www.fitchratings.com/research/sovereigns/cameroons-late-debt-service-payments-is-not-default-16-08-2023>

11 https://www.moody.com/research/Moodys-downgrades-Cameroons-rating-to-Caa1-from-B2-maintains-stable-Rating-Action-PR_478787?cy=aus&lang=en

8 <https://disclosure.spglobal.com/ratings/en/regulatory/article/-/view/type/HTML/id/3031661>

9 <https://disclosure.spglobal.com/ratings/en/regulatory/article/-/view/type/HTML/id/3033365>



DOMESTIC CREDIT RATINGS MARKET

The 2023H2 witnessed positive developments in the domestic credit ratings market, whose appetite for growth continues to expand. The Financial Regulatory Authority (FRA) of Egypt issued Resolution No. 151 for 2023 regarding criteria for obtaining a licence for credit rating of securities. This is aimed at encouraging prospective CRAs to apply for licensing, enhance the capabilities of the financial sector and increase competition to support the country's growing volume of bond issuances. By the end of 2023H2, the Authority had received three applications – a joint application from MGM Financial & Banking Consultants and India's Infomerics Ratings; a joint application from Beltone Capital and Italy's CRIF Ratings; and a joint application from the Egyptian Credit Bureau (I-SCORE) and S&P Global Ratings. If approved, these CRAs will bring competition to only

one Egypt-licensed credit rating agency, Middle East Rating & Investors Service (MERIS), a partnership between Moody's Investors Service and Egypt's Finance & Banking Consultants International (FinBi).

During the same period, the Mauritius-based CareEdge Ratings Africa launched a Sovereign Risk Assessment Framework as it expanded its business into the sovereign credit rating space. This is an important step towards diversity of credit rating opinions, providing alternatives to the three dominant international CRAs and accurately assessing the creditworthiness of African countries. Scope Ratings, a European rating agency, is also expanding its portfolio in Africa, assigning a BB+ with a stable outlook to Morocco, in addition to its B and BB+ for Egypt and South Africa, respectively.



RECOMMENDATIONS

The general concern over fiscal and external financing and liquidity pressures in Africa, coupled with constrained options for concessional external financing, and tightening domestic and external financing conditions, have heightened the negative risk perception amongst investors and rating agencies. As such, there is limited room left for governments to manoeuvre in trying to alleviate liquidity pressures on public finances and any market-based debt management operations are interpreted by CRAs as a sign of distress. There are however several ways to address some of these challenges;

i. Engaging rating agencies at all levels of government:

in addition to low levels of preparations, learning from other regions^{12,13}, African governments need to engage agencies at all levels of government. In addition to maintaining a competent credit rating liaison team, it is imperative for senior government officials to engage rating agencies, especially on issues to do with rule of law, policy certainty, judiciary independence and anti-corruption drive. This signals government commitment to addressing investor concerns and aide market confidence.

ii. Improve treasury and debt management:

it is important for governments to enhance their capacity to manage debt and avoid accumulating payment arrears, especially

to private creditors. Maintaining a track record of meeting external payment obligations, clearing domestic arrears and limited off-budget expenditures would be indicative of an improved liquidity profile and debt management capacity.

iii. Verify data before publishing rating opinions:

the underlying assumption in financial markets is that international CRAs utilise credible data to draw credit rating options and the instances of using unverified public information proves that, it is evidently not always the case. Despite the inaccuracies in the credit opinions, investors react to publications of such information. It is therefore important for rating agencies to utilise factual official information and latest data.

iv. Standardise the definitions of default events:

after decades of operating in the same market and subject to similar regulators, there has been no meaningful effort to agree on common definitions and parameters for critical aspects such as 'default'. This may also suggest that despite all three CRAs being registered and regulated in the European Union and United States of America, there is little evidence of effectiveness in these. It is thus necessary for rating agencies to redefine their rating definitions and interpretations to account for the basics such as debt defaulting and the grace period for debt service payments, to avoid analysts making pronouncements too quick.

¹² <https://www.euractiv.com/section/economy-jobs/news/frances-le-maire-goes-full-out-to-avoid-sp-credit-rating-downgrade/>
¹³ <https://www.i24news.tv/en/news/israel/economy/1694084124-netanyahu-meets-with-moody-s-rating-agency-amid-weakening-israeli-shekel>



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