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SSA Eurobonds (finally) taking a bath

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"If it looks like a duck, swims like a duck, and quacks like a duck, then it probably is a duck."

The Duck test, coined by James Whitcomb Riley

SSA Eurobonds are being hammered today, in line with sharply lower energy and soft commodity prices, following yesterday's surge in VIX, and Eurozone periphery debts that are under sharp pressure today. Ghana 2023 is leading on the downside with losses of 2.7%, followed by Nigeria 2023 that is down 2.2% on the session. Kenya 2024, Zambia 2024 and Rwanda 2023 are down around 1.4% each.

On the first table below of key African Eurobonds, first column is price, followed by daily percent change, and Ytd percent change. Note that north Africa is holding firm, this is a SSA specific sell-off.

Summary

It's a sea of red across SSA Eurobond screens today. An overdue correction is finally playing out.

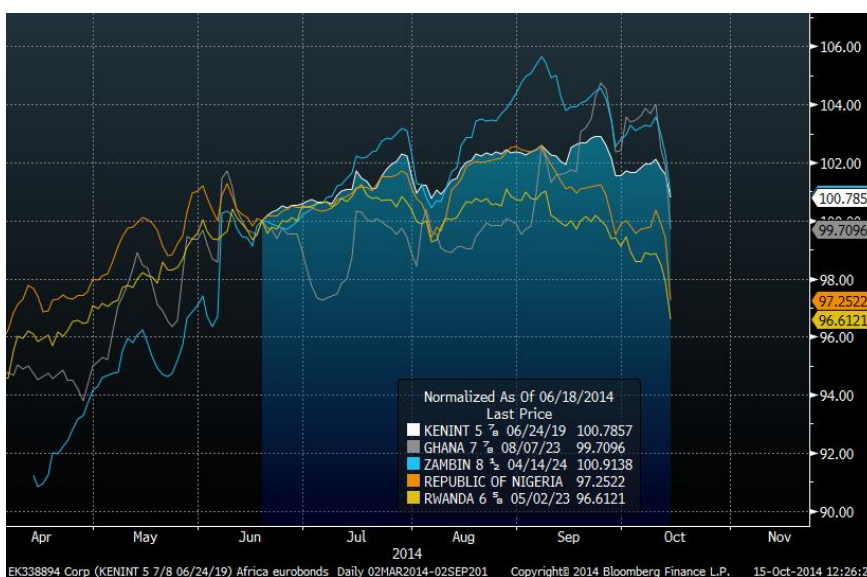
Investment Implications

SSA Eurobonds have behaved more like investment grade bonds in the last few months, in contrast to their high yield peers. The current correction makes fundamental sense, and should restore the market to health.

AFRICA EURO BONDS			
REP OF NIGERIA (NGER)	↑104.686	-2.22%	+1.183%
KENYA REP OF (KENINT)	↓103.687	-1.44%	
GHANA REP OF (GHANA)	↓97.632	-2.66%	+1.591%
ZAMBIA REP OF (ZAMBI)	↑112.227	-1.42%	
REPUBLIC OF RWAN (RI)	↓100.490	-1.28%	+5.999%
ARAB REP EGYPT (EGYF)	↓106.101	+0.09%	+10.92%
MOROCCO KINGDOM (M)	↑102.639	-.02%	

Source: Bloomberg

The following chart reflects SSA Eurobond prices, rebased to 100 on June 18, 2014. The heavens have opened up. Watch out below.



The sell-off is in line with the fall of high yield corporate bonds in general, as captured by the HYG and JNK ETF's (of the same tickers on Bloomberg). It is interesting to note that energy companies now account for 15% of US high yield

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bonds, up from 9.7% at end-2007, which is supporting the sell-off of high yield corporate bond ETF's, according to Bloomberg.

With oil prices under significant pressure, the corporate bonds of energy companies are facing an equal, and sometimes greater, amount of selling pressure. Regarding some of these energy companies, Bloomberg point to the cases of Hercules Offshore Inc. and Samson Investment, the former a Houston-based drilling company and the latter an Oklahoma-based oil and gas explorer and producer, which have seen their corporate bonds drop from 100 cents to 59.8 cents, and 103.5 cents to 78.5 cents on the dollar respectively in the last few months. Therefore it's no surprise that the Nigeria 2023 Eurobond is down nearly as much as Ghana 2023 today, despite a much sounder fiscal position than Ghana.

The Nigeria 2023 Eurobond (and other SSA Eurobonds) have continued to gain in the last few months, but as we argued in "A Kenya Eurobond exchange, already," September 2, 2014 ([download](#)), this was not bound to last:

"Kenya Eurobonds have performed more like IG bonds than HY bonds in the past two months (and noting chart two below, so have Zambia and Nigeria Eurobonds). If the government wants to refinance these bonds at cheaper rates, it should do so soon, before these bonds start behaving in line with HY bonds again. There are also several macro risks that could weigh on Kenya Eurobonds in the near term that could bring about this underperformance."

The tide is now moving out for SSA Eurobonds that performed in line with investment grade bonds in recent months, despite being speculative and junk grade bonds. The recent window that opened for SSA governments Kenya and Ghana to issue Eurobond debts looks as if it's now again closed. The global market landscape is net bearish for the performance of African Eurobonds, a trend that is likely to persist in the next few months.

This isn't a change of heart on our part, we have been expecting Africa Eurobond weakness (see "A Kenya Eurobond exchange, already?" September 2, 2014). It's a good thing Ghana and Kenya tapped USD 1bn and USD 2bn from international bond markets when they had the chance, as they managed to secure external financing at lower coupons than they'd fetch today or in the next few months. Looking ahead, we don't expect the current correction of benchmark global equities to turn into a bear market just yet, but see the correction as a much-needed cyclical sell-off that will help restore the market to health from excessive bullishness, at which point buying opportunities will once again present.

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