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Sovereign bonds in developing countries: Drivers of issuance and spreads[☆]

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Abstract

In the last decade there has been a new wave of sovereign bond issuances in Africa. What determines the ability of developing countries to issue bonds in international capital and what explains the spreads on these bonds? This paper examines these questions using a dataset that includes 105 developing countries during the period 1995–2014. We find that a country is more likely to issue a bond when, in comparison with non-issuing peers, it is larger in economic size, has higher per capita GDP, a lower public debt, and a more effective government. Spreads on sovereign bonds are lower for countries with strong external and fiscal positions, as well as robust economic growth and government effectiveness. We also find that primary spreads for the average Sub-Saharan African issuer are higher than in other regions. With regard to global factors, our results confirm the existing evidence that issuances are more likely during periods of global liquidity and high commodity prices, especially for Sub-Saharan African countries, and spreads are higher in periods of higher market volatility.
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1. Introduction

Over the past decade or so, a number of low-income developing countries (LIDCs)[1] have issued sovereign bonds in the international capital markets, driven in part by African frontier markets.[2] Given the declining trend of aid flows,[3] sovereign bonds could represent a sizeable source of external finance, which can contribute to the financing of investment projects, helping LIDCs make progress in closing the infrastructure and development gap. Since 2005, 15 LIDCs have issued international sovereign bonds, 11 of which are in Sub-Saharan Africa (SSA). In 2013, LIDCs issued sovereign bonds amounting to US$4 billion, and this trend continued in 2014, with Côte d'Ivoire, Ethiopia, Ghana, Kenya, Senegal, Vietnam, and Zambia having issued bonds totaling about US$8 billion (Table 1). In 2015, partially reflecting worsening global conditions and lower commodity prices, the number of issuances slowed down and countries that have been able to issue sovereign bonds

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[1] The definition of income groups follows the IMF World Economic Outlook (WEO), which distinguishes advanced economies (AEs) and emerging market and developing economies (EMDEs, here called also developing countries). Low income developing countries (LIDCS)—60 countries in all—are a sub-group of lower income EMDEs, defined in IMF (2014). Frontier markets—14 countries in all—are LIDCs that have some degree of access to international capital markets (see IMF, 2014 for further discussion).

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[2] See IMF (2013), Standard and Poor's (2013), AfDB, OECD and UNDP (2014), Gueye and Sy (2015) and te Velte (2014).

[3] According to the 2015 OECD DAC bilateral aid (excluding debt relief) to the least-developed countries fell by 8% in 2014. See OECD at: http://www.oecd.org/development/development-aid-stable-in-2014-but-flows-to-poorest-countries-still-falling.htm.

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Table 1
International sovereign bond issuances by LIDCs, 1995–2014.

Issuer	Issue date	Yield at issue	Tenor	Amt (USD mn)	Spread (bps)	S&P rating at issue
Moldova	12/10/96		3	30		
Moldova	6/6/97	9.88	5	75	340.0	Not rated
Vietnam	10/27/05	7.25	10	750	256.4	BB−
Ghana	9/27/07	8.50	10	750	387.0	B+
Republic of the Congo	12/7/07	8.77	22	480	458.0	Not rated
Senegal	12/15/09	9.47	5	200	691.0	B+
Vietnam	1/26/10	7.07	10	1000	332.7	BB
Côte d'Ivoire	4/8/10	17.35	23	2330	393.0	Not rated
Nigeria	1/21/11	7.13	10	500	372.0	B+
Senegal	5/6/11	9.34	10	500	596.4	B+
Zambia	9/13/12	5.63	10	750	383.6	B+
Bolivia	10/22/12	4.88	10	500	306.0	BB−
Côte d'Ivoire	11/15/12		20	187		Not rated
Mongolia	11/29/12	4.17	5	500	358.0	BB−
Mongolia	11/29/12	5.19	10	1000	358.0	BB−
Tanzania	2/27/13		7	600	600.0	Not rated
Honduras	3/12/13	7.50	11	500	547.9	B+
Rwanda	4/25/13	7.00	10	400	515.7	B
Nigeria	7/2/13	5.45	5	500	381.0	BB−
Nigeria	7/2/13	6.74	10	500	393.0	BB−
Ghana	7/25/13	8.00	10	750	540.0	B
Ghana	7/25/13		10	250		
Bolivia	8/15/13	6.25	10	500	347.5	BB−
Zambia	4/14/14	8.63	10	1000	592.6	B+
Kenya	6/24/14	6.88	10	1500	429.0	B+
Kenya	6/24/14	5.88	5	500	418.0	B+
Kenya	12/24/14	5.00	10	500		B+
Kenya	12/24/14	5.90	5	250		B+
Côte d'Ivoire	7/23/14	5.63	10	750	308.9	
Senegal	7/30/14	6.25	10	500	379.3	B+
Ghana	9/11/14	8.25	11	1000	572.0	B−
Vietnam	11/6/14	4.80	10	1000	238.7	BB−
Ethiopia	12/4/14	6.625	10	1000	435.6	B

Source: Bloomberg. Updated to end-December 2014.

(Cameroon, Cote d'Ivoire, Ghana, and Zambia) did so at higher yields.

What determines the ability of developing countries to issue bonds in the international capital markets? What are the factors that influence the spreads on these bonds? Do the recent bond issuances by African countries respond to different factors? What can LIDCs learn from the experience of other developing countries (and emerging markets) that have market access? To address these questions, this paper examines the experience of 105 EMDEs during the period 1995–2014, including 52 countries that had issued sovereign bonds at least once in the international capital markets, with the remainder having never issued (Table 2).

The analysis builds on a very extensive literature on international debt markets in developing countries; see Eaton and Taylor (1986) and Eaton (1993) for an overview. The existing literature on market access by emerging and developing countries considers the probability that a country has access to international markets issuing sovereign bonds and/or contracting syndicated loans—and possibly the amounts borrowed. Overall, this literature has underscored the importance of global factors, macroeconomic stability, fiscal discipline, economic diversification, and policies and institutions for accessing international capital markets.

Grigorian (2003) focuses on first time and subsequent issues by emerging economies over the period 1980–2002 and finds that both external and internal factors matter: countries with better fiscal position, lower inflation and higher per capita GDP are more likely to issue, and this finding holds better in years when global conditions improve (i.e., international interest rates are lower and US GDP growth is stronger). Thomas (2009) shows that poor credit rating and political instability adversely affected access to international capital markets by LIDCs during 1970–2006; his analysis also suggests that debt relief provided under the Heavily Indebted Poor Countries (HIPC) Initiative has significantly raised market access by low-income countries. This is consistent with SBI by LIDCs being mainly concentrated among HIPCs (IMF, 2014). Gelos et al. (2011) examine a sample of 150 developing countries over the period 1980–2000 and define market access to cover sovereign bond issues or borrowing through private syndicated bank loans. Their analysis shows that larger and richer countries are more likely to access credit markets; the perceived quality of the institutional setting is also a key driver of market access, while countries more vulnerable to shocks are less likely to tap international markets. Two recent papers investigate also the costs of issue sovereign bonds, with a specific focus on African countries. Gueye and Sy (2015) examine the importance of push and pull factors in

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