Repo market

UN launches African repo market in bid to lower borrowing costs

Short-term lending facility could save governments $11bn a year in interest costs, body says

Vera Songwe of UNECA: 'Cash is king, and you don't get cash very fast from a lot of African bonds. We need to create a repo market' © Minasse Wondimu Hailu/Anadolu Agency via Getty

Tommy Stubbington 19 MINUTES AGO

The UN has launched a new short-term lending market for African bonds in a move that it says could trim billions of dollars from government borrowing costs across the continent.

The liquidity and sustainability facility (LSF) will allow investors to use African debt issued in foreign currencies such as dollars and euros in repo transactions, the organisation said on Wednesday at the COP26 climate conference.

Repo is a key feature of market plumbing in the developed world, but is less common in developing economies. It allows market participants to access funding by exchanging bonds for cash in transactions that are typically considered to be ultra-safe.

An initial $200m transaction is planned for early next year with funding expected to be provided by Africa Export-Import Bank, and investors including French asset manager Amundi interested in participating.

Backers of the project are seeking additional sources of funding to scale up the facility. The funding is expected to include a slice of the $650bn of special drawing rights created by the IMF in August to help low and middle-income countries weather the pandemic. The size of the facility could reach $30bn, according to the UN Economic Commission for Africa (UNECA).

Vera Songwe, executive secretary of UNECA, said the launch of a repo market for African debt would make it more attractive to investors, lowering borrowing costs for governments.

“Cash is king, and you don’t get cash very fast from a lot of African bonds,” she said. “We need to create a repo market.” The LSF could save African countries $11bn in interest costs over the next five years, UNECA estimates.

“African governments have historically faced a high cost of borrowing” said Mohamed Maait, Egypt’s finance minister and Ken Ofori-Atta, Ghana’s finance minister, in a joint statement.

“Developed countries have long enjoyed the existence of large repo markets for their government bonds, facilitating the creation of stable and additional funding sources. Our aim is to be able to provide the same sort of liquidity-supportive environment to African governments and private investors alike.”

The facility also aims to encourage the issuance of green bonds or sustainability-linked bonds by Africa governments, by offering investors favourable terms for using them as collateral in repo transactions. Such debt currently comprises just 1 per cent of the total bond market across Africa and the Middle East.

“Today Africa needs more liquidity than ever before to finance its recovery and to invest in a bold, and sustainable environment,” Songwe said.

African bonds — along with other emerging market debt — plummeted in price during the early stages of the coronavirus crisis in March 2020 as panicked investors fled to the safety of cash. Even debt issued by countries with sound finances was punished disproportionately, said Jay Collins, vice-chair of banking, capital markets and advisory at Citi, which is advising UNECA on structuring the LSF.

“Asset stabilisation mechanisms have come from central banks in the developed world, so the hope is to create appropriate, systemically important liquidity mechanisms for the emerging markets, beginning in Africa,” Collins said. “If we do this right, it can catalyse more sustainability bonds.”

The facility will focus on countries who are not judged by the IMF to be at high risk of fiscal distress, Songwe said. Several African countries have returned to debt markets this year, with Ivory Coast, Rwanda and Benin all selling bonds this year. Others, such as Zambia, which is in the midst of restructuring its debt, remain shut out of markets for now.

"Our universe is about 20 countries to start with," she said.