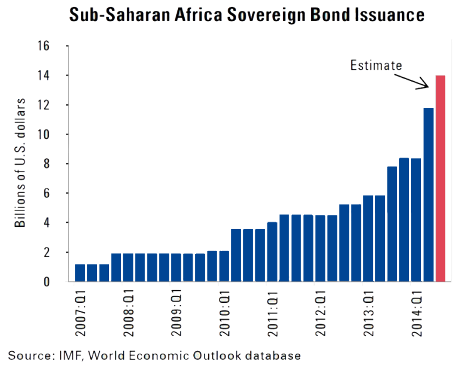
IDA AFRICA WATCH
Volume 9
August 6, 2015

SOVEREIGN DEBT—A THREAT TO THE AFRICAN GROWTH STORY?

By George F. Ward

During the past several years, sub-Saharan African countries have increasingly turned to the international sovereign debt market for their capital needs. Recently, some of the countries that issued sovereign debt have run into fiscal problems. The cost of borrowing in international markets has risen sharply. One potential new entrant to the sovereign debt market canceled its plans. These developments have sparked renewed debate over the sustainability of Africa's debt burden and the effectiveness of sovereign debt in promoting economic development. *more...*

Ambassador (ret.) George F. Ward is editor of Africa Watch and a Research Staff Member at the Institute for Defense Analyses.



Graph adapted from Paul Adams, "Africa Debt Rising," Counterpoints (Africa Research Institute, January 2015), http://www.africaresearchinstitute.org/newsite/wp-content/uploads/2015/01/ARI-Counterpoint-SovereignBond-download.pdf.

JULIUS MALEMA'S ECONOMIC FREEDOM FIGHTERS PARTY TURNS 2

By Dr. Janette Yarwood

The Economic Freedom Fighters (EFF), one of South Africa's newest political parties, recently had its two-year anniversary. The EFF's first anniversary was marked by surprise and optimism as the party earned 1 million votes during the 2014 elections. How has the party fared in its second year? Will the EFF continue its momentum and increase the party's share of the votes during the 2016 local elections? *more...*

South African Economic Freedom Fighters leader Julius Malema, center, after he and supporters disrupted the official opening session of Parliament in Cape Town, South Africa, Thursday, Feb. 12, 2015. Security guards removed the opposition lawmakers who interrupted an annual address by President Jacob Zuma and demanded that he answer questions about a spending scandal. (Source: AP Photo/Nic Bothma, Pool.)

Dr. Janette Yarwood is a Research Staff Member in the Africa Program at the Institute for Defense Analyses.

About IDA

The Institute for Defense Analyses is a non-profit corporation operating in the public interest.

IDA's three federally-funded research and development centers provide objective analyses of national security issues and related national challenges, particularly those requiring scientific and technical expertise.

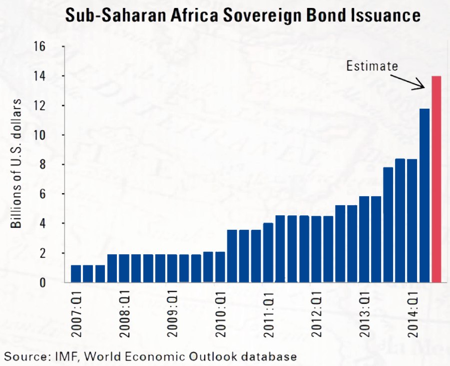
IDA's Africa team focuses on issues related to political, economic, and social stability and security on the continent.

4850 Mark Center Drive – Alexandria, VA 22311-1882
www.ida.org

SOVEREIGN DEBT—A THREAT TO THE AFRICAN GROWTH STORY?

By George F. Ward

During the past several years, sub-Saharan African countries have increasingly turned to the international sovereign debt market for their capital needs. Recently, some of the countries that issued sovereign debt have run into fiscal problems. The cost of borrowing in international markets has risen sharply. One potential new entrant to the sovereign debt market canceled its plans. These developments have sparked renewed debate over the sustainability of Africa's debt burden and the effectiveness of sovereign debt in promoting economic development.



Graph adapted from Paul Adams, "Africa Debt Rising," Counterpoints (Africa Research Institute, January 2015), http://www.africaresearchinstitute.org/newsite/wp-content/uploads/2015/01/ARI-Counterpoint-SovereignBond-download.pdf.

The African Rush to Sovereign Debt

The stock of sub-Saharan African government bonds on the international market (sovereign debt) grew from less than $1 billion in 2008 to more than $18 billion by 2014. The IMF reported in May 2013 that 11 sub-Saharan African countries had accessed international sovereign bond markets in the previous decade. Since that report, an additional six sub-Saharan African countries have issued international sovereign debt.

The international bond market has been attractive to African countries for several reasons. It provides an alternative to concessional lending by donor countries, which often comes with strings attached, and to domestic bond markets, which are in almost all cases small. Even though all African sovereign bond issues have been rated at less than investment grade, interest rates have been surprisingly low. In 2014, for example, a bond issue by Cote d'Ivoire was set at a level not much greater than the sovereign debt of the United Kingdom. These favorable terms have been available because Western investors have turned to so-called frontier markets to obtain more attractive yields and because they have been willing to accept relatively small surcharges to compensate for the increased risk.

Bumps in the Road

Despite some of the advantages of sovereign debt, its recent history in Africa has not been entirely positive. The experiences of a number of countries have highlighted the risks associated with sovereign debt:

- To attract international investors, sovereign debt is issued in foreign currencies, either in dollars or euros. This means that the debt is subject to *currency risks* if the currency of issuance strengthens relative to the currency of the issuing country. In 2014, the currencies of countries such as Ghana and Angola declined sharply in value, largely due to the decline in prices for natural resources, especially oil. The additional Ghanaian cedis and Angolan kwanzas needed to service debt denominated in dollars and euros represented a significant new economic burden for both countries. In part because of this burden, Ghana was obliged to turn to the IMF for assistance. According to Judith E. Tyson of the Overseas Development Institute, if comparable exchange rate losses were to be repeated across the region, the total impact would amount to a value over time equivalent to 1.13 percent of sub-Saharan African GDP.
- *Interest rate risks* have also emerged on the African debt market. Record-low borrowing costs in 2014 facilitated sovereign bond sales by several African countries, including Ethiopia, which paid 6.63 percent for its debut offering of $1 billion in December 2014. Beginning in 2015, investors appear to be taking a more jaundiced view of the African scene. On July 23, 2015, Zambia paid 9.38 percent for the sale of $1.25 billion in debt. That was the highest yield ever paid for an African issuer on the Eurobond market and almost 4 percent higher than Zambia's first Eurobond in 2012.

- In part due to past debt relief programs, *the overall level of African government debt* has remained relatively stable at around 30 percent of GDP. Upward revisions to the GDPs of countries such as Ghana, Kenya, and Nigeria due to updated statistics have helped to lower debt-to-GDP ratios. Nevertheless, the IMF has warned African countries not to go overboard in contracting new debt. The IMF's advice has not always been heeded, and debt in four countries—Cote d'Ivoire, Ghana, Mozambique, and Seychelles—has reached a moderate level of risk on the IMF's scale of debt sustainability.

- A final type of risk relates to the differences between sovereign debt and concessional debt. In the case of the latter, negotiations over debt issuance typically take place over a lengthy period of time during which issues such as the term of the debt, its sustainability, and its developmental impact are explored in detail. In contrast, sovereign international debt is often contracted rapidly. The borrower's intentions regarding the use of the debt principal are generally not binding. The term of the debt is generally 5 to 10 years, in contrast to the 30-year terms often employed in concessional lending. The looser arrangements associated with sovereign debt have led some countries to use the funds obtained for purposes that have little or no development impact. In Ghana and Mozambique, for example, funds were used to increase the salaries of public sector employees.

Time to Check the Fire Alarm, But Perhaps Not to Ring It

After reviewing a study from the Overseas Development Institute, Amadou Sy of the Brookings Institution concluded, "it is not yet time to sound the alarm on these risks. Rather, it is time to check the fire alarm and make sure that African governments can properly and rapidly identify, measure, and manage the risks from their increased external indebtedness." Other views have been more negative. One African country—Uganda—in 2014 declared that it would not issue sovereign debt after all. Its central bank governor warned of the dangers of debt and said that African countries would "never again get debt relief." A Policy Research Working Paper published by the World Bank Group in June 2015 concluded that in contrast to foreign direct investment, sovereign borrowing does not have a positive effect on economic growth in sub-Saharan Africa.

The bottom line is that African governments should heed cautionary notes such as the ones above. Even at a time of increasing interest rates, sovereign debt may be appropriate to address some problems. For example, borrowing to finance high-impact infrastructure projects that are likely to produce significant rewards at low risk might be justified. On the other end of the scale, governments should probably avoid issuing sovereign debt for purposes that promise low returns, such as financing current expenditures, increasing government salaries, or purchasing military hardware.

Ambassador (ret.) George F. Ward is editor of Africa Watch and a Research Staff Member at the Institute for Defense Analyses.

JULIUS MALEMA'S ECONOMIC FREEDOM FIGHTERS PARTY TURNS 2

By Dr. Janette Yarwood

The Economic Freedom Fighters (EFF), one of South Africa's newest political parties, recently had its two-year anniversary. The EFF's first anniversary was marked by surprise and optimism as the party earned 1 million votes during the 2014 elections. How has the party fared in its second year? Will the EFF continue its momentum and increase the party's share of the votes during the 2016 local elections?


South African Economic Freedom Fighters leader Julius Malema, center, after he and supporters disrupted the official opening session of Parliament in Cape Town, South Africa, Thursday, Feb. 12, 2015. Security guards removed the opposition lawmakers who interrupted an annual address by President Jacob Zuma and demanded that he answer questions about a spending scandal. (Source: AP Photo/Nic Bothma, Pool.)

Rise of the Economic Freedom Fighters

The EFF arose in the wake of the Marikana massacre (2012), when police shot and killed 34 striking black miners who were demanding higher wages, and it emerged onto the South African political scene in July 2013 after its leader, Julius Malema, was expelled from the ruling African National Congress (ANC) in 2012. The EFF declaration and founding manifesto explains that the party draws inspiration from Marxist and Leninist schools of thought, as well as the work of Frantz Fanon. The EFF describes itself as a radical, leftist, anti-capitalist, and anti-imperialist movement with an internationalist outlook anchored by popular grassroots formations and struggles.

The EFF quickly gained momentum with its populist message of redistribution of wealth and land and advocating the nationalization of South Africa's mines, banks, and other sectors of the economy. The party also aims to address corruption, unemployment, and broad inequality. This philosophy resonated among many in a society that remains deeply unequal. South Africa's GINI coefficient in 2011 was .65, the highest listed by the World Bank. (The Gini coefficient is a ratio between zero and one. The higher, or closer to one, a country's Gini coefficient is, the greater the level of inequality in that country.)

Malema and the EFF appeal to this disaffected sector of the population in a way that no other party does. EFF supporters wear Hugo Chavez-inspired red berets, and its parliamentary representatives wear red working men's overalls and domestic worker dresses, which they say symbolize solidarity with the working people the party represents and signal their intention to work hard in parliament to represent their constituency. The party has also attracted frustrated youths, who are often in attendance at protests wearing the signature red beret.

Nine months after its founding, the EFF won 6 percent, over a million votes, in the 2014 general election, becoming, with 25 seats, the third largest political party in the national assembly. It is now the official opposition in Limpopo and North West province. The 2014 election results showed that the ANC won the election with 62 percent of the vote and the Democratic Alliance (DA) consolidated its position as the official opposition with 22 percent of the vote, a 5 percent increase from 2009.

Year Two in Review

Political analysts in South Africa have varying views on the EFF's impact during its first two years, with most concluding that the political landscape continues to be dominated by the ANC. Theo Ventor of the University of the North West argues that the EFF has succeeded in making Parliament relevant again. The EFF certainly does have people watching what is going on in Parliament, but it may be more for the spectacle than a true engagement in politics. EFF members regularly disrupt Parliament and twice have been removed from Parliament by police for confronting South African President Jacob Zuma with questions about an investigation into a $23 million state-funded security upgrade to his home.

At the same time, the EFF continues to be marked by infighting. Shortly after the 2014 election, Malema was accused of removing those critical of him after key leaders were dismissed. EFF spokesperson Mbuyiseni Ndlozi denied the charges: "the restructuring was purely organizational and aimed at improving the overall functioning of the fledgling party's structures across the board." Then, in March 2015, the chairperson of the EFF in Gauteng, Zorro Boshielo, and deputy secretary of the province, Kim Heller, both resigned. Expulsions soon followed, with former party MPs Mpho Ramakatsa, Andile Mngxitama, and Khanyisile Litchfield-Tshabalala dismissed in April 2015 following their claims of misconduct and corruption against the party's leadership. In May 2015, seven senior members in Mpumalanga severed ties with the political party, citing financial mismanagement, exploitation of women, nonexistence of internal democratic processes, corruption, and thuggery as reasons for leaving. Mpumelelo Masina, who was the EFF Mpumalanga spokesperson at the time, summarized the party's problems: "The party has become a danger to the political fabric and economic stability of South Africa. The organization has turned into a *stokvel* led by corrupt individuals." (A stokvel is an informal savings pool or syndicate, usually among Black people, in which funds are contributed in rotation, allowing participants lump sums for various needs.) Finally, some claim that Malema and the EFF are opportunistic and capitalize on grassroots activism already underway. The party has been accused of parachuting into communities for service delivery protests rather than actually engaging in the struggles of the working class and poor.

Conclusion: Prospects for 2016

The EFF has had a rocky first two years. The party continues to center on Malema. Despite criticism of the party's confrontational methods during parliamentary sessions, Malema remains optimistic. At the two-year anniversary celebration, Malema said the party would contest all wards countrywide during the 2016 municipal elections. EFF spokesperson Mbuyiseni Ndlozi said the party immediately went to work to build structures in all provinces, regions, and subregions after the 2014 election. The party is also deploying party members around the country to increase membership. So far, doubts persist over the effectiveness of these efforts. Unless the party strengthens its base, its prospects will continue to rest on sustaining Malema's national popularity.

Dr. Janette Yarwood is a Research Staff Member in the Africa Program at the Institute for Defense Analyses.