Quarterly Frontier Markets Recap

Frontier Market Credit Risks Still High, after Record Negative Actions

Global lockdowns of varying lengths and degrees curtailed domestic economic activity and hampered international trade, tourism and remittances during 1H20. This, combined with plummeting commodity prices, currency depreciation and a drop in investor appetite, has led frontier markets (FMs) to experience an unprecedented wave of negative rating actions, mostly in April and May.

Of the 19 FM sovereigns that experienced rating and/or outlook changes during 1H20, half saw ratings downgraded, while the other half experienced a negative change in Outlook (either from Stable to Negative or from Positive to Stable). Most of these changes affected sovereigns in the Middle East and Africa (7 in SSA and 3 in MENA), while in the Americas, three sovereigns were downgraded (Suriname 3x, Guatemala and Costa Rica) and one experienced a change in Outlook to Negative (El Salvador)[1].

FM Asia experienced the lowest proportion of negative actions (2:4) among all regions, with 1 downgrade (Sri Lanka) and 1 Outlook revision from Positive to Stable (Vietnam). Europe recorded zero FM downgrades, but of the five European FMs included in the NEXGEM index, three (Armenia, Azerbaijan and Georgia) had Outlooks revised to Negative in April. (*For more information on these and other rating actions that took place during the first four months of this year, please refer to our previous edition - the link can be found at the bottom of this page*).

Weakened Pre-Pandemic Fiscal Positions Deteriorating Further. As the impact of containment measures and commodity price shocks became clearer throughout the second quarter, Fitch continued to revise its projections for economic growth downward and government debt ratios upward, reflecting the severe effect these shocks are having on both fiscal and external accounts. Many FMs, particularly in MEA and LatAm, started the pandemic with an already weakened fiscal position, limiting their countercyclical policy flexibility and ability to support post-crisis recoveries. In 2019, all LatAm & Caribbean countries, except for Jamaica, reported fiscal deficits, which in many cases were large (Bolivia, Costa Rica, Suriname), and all countries except Jamaica reported higher government debt compared to 2008. In SSA, government debt burdens are rising at a faster pace and to a higher level than in any other FM region, with Angola, Mozambique and Zambia expected to surpass 100% of GDP by the end of this year.

Sub-Saharan Africa (SSA) will experience its first contraction in decades as a result of the coronavirus pandemic and the commodity price shock. Six out of 11 SSA frontier markets will experience a decline in GDP this year. While the main oil-exporting FMs Angola, Gabon and Nigeria will be hit particularly hard, sovereigns dependent on tourism and remittances, mining and agricultural products will also face significant challenges. Repeated droughts in Namibia and Zambia and locust infestations in Ethiopia and Northern Kenya have damaged crops in these countries. Disruptions to mining activity, for example in Namibia and Zambia, and potential disruptions caused by terrorism or political instability (Mozambique, Cameroon, Ethiopia, Tunisia) add further pressure.

[1] Jamaica's change in Outlook to Positive in January was reversed to Stable in April, leaving the outlook unchanged by the end of 1H20 versus Dec.'19.

Key Sovereign Rating Actions

Kenya's Outlook Revised to Negative; Rating Affirmed at 'B+'

Namibia Downgraded to 'BB'; Outlook Stable

Costa Rica Downgraded to 'B'; Outlook Negative

Tunisia Downgraded to 'B'; Outlook Stable

Jordan's Outlook Revised to Negative; Rating Affirms at 'BB-'

Georgia's Outlook Revised to Negative; Rating Affirmed at 'BB'

Sri Lanka Downgraded to 'B-'; Outlook Negative

Webinars

Global EM Sovereign Rating Vulnerabilities and Outlook

Impact of COVID-19 and oil price collapse on Middle East and Africa Sovereigns

Latin America Sovereign Outlook

Previous Reports

Frontier Market Newsletter - 1Q20

Frontier Market Credit Risks Still High, after Record Negative Actions **(continued)**

In the Middle East and North Africa (MENA), all three FMs are expected to record a sharp contraction in GDP during 2020, ranging from -4.5% in Tunisia and -5% in Jordan, to -9% in Iraq. Low growth and high unemployment present risks of social unrest, adding to the region's already high geopolitical and security issues. While these countries' government debt/GDP is expected to exceed 80% this year, Jordan and Iraq boast high albeit declining levels of international reserves, and all three sovereigns enjoy strong support from international donors and official creditors, which mitigates high current account deficits and increasing net external debt. However, official support was not sufficient to offset Tunisia's large macroeconomic imbalances, leading to its downgrade in May.

Large External Financing Needs Rising in MEA and LatAm. Widening current account deficits in many countries are increasing external funding pressures, with MEA's external financing needs expected to nearly double over 2020-2021. These needs will largely be met through a combination of official borrowing and reserve drawdowns, as global capital markets have become prohibitively costly for many FMs (Guatemala and Paraguay are some of the exceptions) and local markets are generally shallow. Borrowing constraints and a steep amortization schedule were among the factors that triggered Costa Rica's downgrade in May. Financing constraints from increased reliance on short-term debt, limited additional local market funding and uncertain access to external markets also played a major role in El Salvador's Outlook revision to Negative.

Suriname's debt sustainability has been a concern for a while, as debt/GDP approaches 90% this year and the government's USD1 billion debt was issued at a steep interest rate of 9.5%. Distressed financing conditions and the "consent solicitation" to defer a 30 June principal payment, an effective debt restructuring, led to a third downgrade of Suriname this year to 'RD' on 13 July. The sovereign was upgraded to 'CC' on 16 July, following the completion of the "consent solicitation".

Official Creditors Provide Some Relief. In response to the crisis, the IMF has announced emergency balance-of-payment support, besides providing additional funding under its more normal lending arrangements, which could pave the way for renewed market access and crowd-in financing from other official lenders. A G20 Debt Service Suspension Initiative (DSSI) covers bilateral debt service in 2020 and is open to 77 eligible developing nations. While helpful, these initiatives are small in scale (around 1% of GDP each) and not designed to address debt stock and medium-term risks to debt sustainability. However, China's involvement in the G20 initiative could play a substantial role in easing liquidity strains, as China accounts for over 25% of total external debt of DSSI-eligible countries, making it their single largest bilateral creditor.

In frontier market Asia, to date, only Pakistan & Mongolia have accessed emergency funding from the IMF. The ratings of both sovereigns were affirmed with a Stable Outlook during 1H20. In the case of Pakistan, continuing support from the IMF and other official creditors should help finance the country's large fiscal deficit, estimated at 9.5% of GDP for FY20 (general government balance), and contain risks with its fragile external position. For Mongolia, the impact of the coronavirus shock should largely be temporary, with the economy rebounding strongly (by about 7.9%) due to rising commodity exports as China recovers, and government debt/GDP starting to decline again in 2021. The strong majority retained by the incumbent party in June's parliamentary election bodes well for policy continuity, favouring continued access to multilateral credit facilities.

Sri Lanka's prospects are more precarious, as its stressed external liquidity position is set to remain a credit weakness. The country's external liquidity ratio, at around 60% in 2019, is among the lowest in its rating category. After its downgrade in April, Sri Lanka's rating Outlook remains Negative, as the country faces hurdles in securing external financing. Sri Lanka's three-year EFF with the IMF expired in early June, after going off track late last year, when the new government's tax cuts went against the programme's revenue-based consolidation strategy. Vietnam, on the other hand, continues to stand out among Asian frontier markets, with GDP growth projected at 2.8% this year and general government debt/GDP estimated at 42% in 2020, which, while rising, is still well below the 'BB' median of 59%. With only one out of four FMs on Negative Outlook, Asia is currently the most stable of all FM regions.

In frontier market Europe, only Belarus and Uzbekistan's ratings were affirmed with Stable Outlook, with the rest of the FMs' Outlooks revised to Negative (*see 1Q20 edition for more details*). Despite its heavy commodity dependence, Uzbekistan is the only European FM forecast to record positive growth this year. The rating is supported by robust fiscal and external buffers, with higher gold prices cushioning the drop in external demand and boosting international reserves. In addition, external funding has been secured, supporting the government's anti-crisis response. Belarus' rating ('B') is lower than Uzbekistan's ('BB-'), reflecting weak growth prospects, low FX reserves, government debt that is highly exposed to foreign currency risks, a weak banking sector, high external indebtedness and weak governance indicators relative to peers.

Heightened Downside Risks Remain. FMs' unprecedented wave of negative rating actions during 2Q20 has led to an exceptionally high number of sovereigns rated 'CCC' or lower and a record share of Negative Outlooks, suggesting heightened risk of further downgrades and/or outright defaults. This risk is most acute in MEA, as 10 out of 14 MEA sovereigns are either on Negative Outlook or rated 'CCC' or lower, where Fitch does not assign Outlooks. FM Europe has the second-highest proportion of Negative Outlooks (3:5), but ratings there tend to be much higher, typically falling in the 'BB' category. In the Americas, 3 out of 7 FMs are on Negative Outlook while 1 is rated 'CC' with no outlook assigned. Globally, only one frontier market, Côte d'Ivoire, is currently on Positive Outlook.

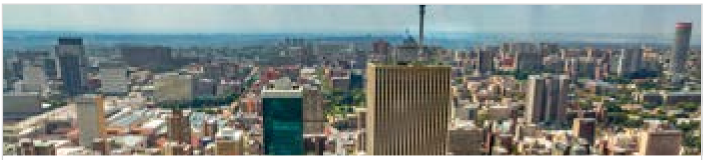
Newsreel

Remittances: Transmission of US Economic Shock to Central America and the Caribbean

The decline of remittances will magnify the economic downturn in emerging countries. Remittance flows into low-income countries support household consumption, finance trade deficits, maintain reserve level adequacy and provide fiscal revenue by boosting value-added and sales tax. In the case of LatAm, these flows come predominantly from the U.S, with the largest FM receivers relative to economic size being El Salvador (21% of GDP), Jamaica (15.2%) and Guatemala (13.7%).

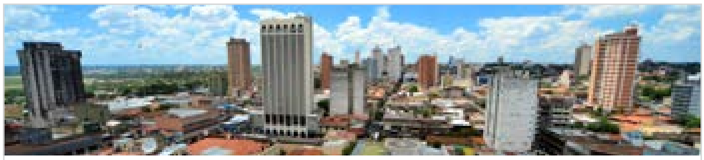
Pakistan's Public Finances Set to Remain a Rating Weakness

Pakistan's fiscal consolidation targets presented in its FY21 budget will be challenging to meet amid the economic shock and health crisis associated with the coronavirus pandemic. Public finances were a key credit weakness even before the health crisis. Nevertheless, continuing support from the IMF and other official creditors should help the government finance its budget and contain risks associated with the country's fragile external position.



Debt Distress Rising in Sub-Saharan Africa

SSA government debt burdens are rising at a faster pace and to a higher level than for other EMs, heightening the risk of further downgrades and defaults. The agency forecasts the median government debt/GDP ratio for the 19 Fitch-rated SSA sovereigns to reach 71% at end-2020, from 57% at end-2019 and 26% in 2012. Fitch forecasts median real GDP to fall by 2.1% in 2020 and the budget deficit to widen to 7.4% in 2020, from 4.9% in 2019, causing a 14pp jump in the median debt ratio this year.



Paraguay Fiscal Rule Suspension May Herald Permanent Changes

The government suspended the fiscal responsibility law, which sets a deficit limit of 1.5% of GDP and growth in current expenditures at 4%, after announcing a fiscal package worth close to 4% of GDP to combat the coronavirus pandemic. The package includes measures to support the healthcare system, to expand the social safety net through cash transfers and to provide loans to small and medium-sized enterprises.

Frontier Vision – 2Q20

Economic activity indicators for frontier markets have deteriorated significantly in recent months as the coronavirus crisis has disrupted domestic economies and reduced external demand and trade, says Fitch Ratings in its latest "Frontier Vision" chart pack. GDP fell year on year in 1Q in Belarus, Belize, Honduras, Jamaica, Mongolia, Namibia and Tunisia.

The economic impact of the coronavirus pandemic in frontier markets has become even more pronounced with exports and imports declining dramatically in Armenia, Azerbaijan, Barbados, Belarus, El Salvador, Jordan, Mongolia, Sri Lanka, Uzbekistan and Vietnam.

Worsening economic conditions and fears of unprecedented recession have prompted many central banks to cut interest rates, with easing almost across the board, including in Armenia, Cameroon, Costa Rica, Gabon, Guatemala, Mongolia, Nigeria, Papua New Guinea, Paraguay and Uzbekistan.

Fitch's quarterly "Frontier Vision" chart pack tracks high-frequency macroeconomic data for the 36 countries included in NEXGEM. The charts cover five years of historical data and the choice of data series has been harmonised as far as possible across all countries to facilitate comparisons. The index comprises 36 countries representing sub-Saharan Africa, Latin America, the Caribbean, the Middle East, Europe and Asia.

Regional Commentary

Europe

Belarus Affirmed at 'B'; Outlook Stable

Outlook on Azerbaijan Revised to Negative; Ratings Affirmed at 'BB+'

Uzbekistan Affirmed at 'BB-'; Outlook Stable

Outlook on Armenia Revised to Negative

Latin America & The Caribbean

Suriname's LT-FC IDR Upgraded to 'CC'

Suriname's LT-FC IDR Downgraded to 'RD'

El Salvador's 2052 USD Bonds Rated 'B-'

Suriname's Long-Term Foreign Currency IDR Downgraded to 'C'

Presentation: Bolivia: Sovereign Rating Outlook 2020

El Salvador Affirmed at 'B-'; Outlook Revised to Negative

Paraguay's USD1 Billion Bond Rated 'BB+'

Guatemala's 2032 USD Bonds Rated 'BB-'

Jamaica's Outlook Revised to Stable; Ratings Affirmed at B+

Guatemala Downgraded to 'BB-'

Coronavirus Hits Central America, Caribbean via Tourism, Remittances

Asia Pacific

Vietnam Outperforms Among Asia's Frontier Sovereigns

Mongolian Election Result Eases Policy Uncertainty

Sri Lanka's External Strains Set to Persist Beyond Elections

Coronavirus Compounds Sri Lankan Banks' Stresses

Mongolia Affirmed at 'B'; Outlook Stable

Outlook on Vietnam Revised to Stable; Rating Affirmed at 'BB'

Sri Lankan Banks' Risks to Persist Despite Regulatory Measures

Middle East & Africa

Jordan's USD Bonds Rated 'BB-'

Mozambique Affirmed at 'CCC'

Ethiopia Affirmed at 'B'; Outlook Negative

Namibia's Outlook Revised to Negative; Rating Affirmed at 'BB'

External Funding Pressures Rise for High-Yield MEA Sovereigns

Outlook on Sub-Saharan Sovereigns is Negative

Locusts Create Additional Downside Risk for East African Sovereigns

Outlook on MENA Sovereigns Turning Negative

Cote d'Ivoire's Affirmed at 'B+'; Outlook Positive

Private Sector Access to FX in WAEMU and CEMAC

Coronavirus Darkens Fiscal Outlook for MEA Sovereigns

Nigeria's Oil Output Cap to Weigh on Growth, External Finances

Namibia's National Rating Upgraded to 'AAA(zaf)'; Outlook Stable

Oil Price Slump Raises Pressure on CEMAC'sCurrency Peg

Cameroon's Outlook Revised to Negative; Rating Affirmed at 'B'

Ghana Affirmed at 'B'; Outlook Stable

Zambia Downgraded to 'CC'

Outlook on Iraq Revised to Negative; Rating Affirmed at 'B-'

Oil and Coronavirus Shocks Add Pressure for MEA Sovereigns

Kenya Coronavirus Measures Lead to Faster Increase in Debt

Nigeria Downgraded to 'B'; Outlook Negative

Gabon Downgraded to 'CCC'

Coronavirus Poses Downside Risks to Jordanian Banks

Nigerian Banks at Severe Risk from Oil Price Slump, Coronavirus

Regional Commentary

Country	Current Ratings	Last Rating Action	Outlook	Rating Action Type
Middle East & Africa				
Angola	B-	06-Mar-2020	▶	Downgrade
Cameroon	B	22-Apr-2020	▼	Affitmation
Cote D-Ivoire	B+	03-Jun-2020	▲	Affirmation
Ethiopia	B	30-Jun-2020	▼	Affirmation
Gabon	CCC	03-Apr-2020	–	Downgrade
Ghana	B	21-Apr-2020	▶	Affirmation
Iraq	B-	16-Apr-2020	▼	Affirmation
Jordan	BB-	08-May-2020	▼	Affirmation
Kenya	B+	18-Jun-2020	▼	Affirmation
Mozambique	CCC	09-Jul-2020	–	Affirmation
Namibia	BB	22-Jun-2020	▼	Affirmation
Nigeria	B	06-Apr-2020	▼	Downgrade
Tunisia	B	12-May-2020	▶	Downgrade
Zambia	CC	16-Apr-2020	–	Downgrade
Latin America & The Caribbean				
Bolivia	B+	21-Nov-2019	▼	Downgrade
Costa Rica	B	08-May-2020	▼	Downgrade
El Salvador	B-	30-Apr-2020	▼	Affirmation
Guatemala	BB-	03-Apr-2020	▶	Downgrade
Jamaica	B+	10-Apr-2020	▶	Affirmation
Paraguay	BB+	06-Dec-2019	▶	Affirmation
Suriname	CC	16-Jul-2020	–	Upgrade
Asia				
Mongolia	B	28-May-2020	▶	Affirmation
Pakistan	B-	13-Jan-2020	▶	Affirmation
Sri Lanka	B-	24-Apr-2020	▼	Downgrade
Vietnam	BB	08-Apr-2020	▶	Affirmation
Europe				
Armenia	BB-	03-Apr-2020	▼	Affirmation
Azerbaijan	BB+	17-Jul-2020	▼	Affirmation
Belarus	B	15-May-2020	▶	Affirmation
Georgia	BB	24-Apr-2020	▼	Affirmation
Uzbekistan	BB-	10-Apr-2020	▶	Affirmation

Legend
▲ (positive), ▶ (stable), or ▼ (negative)
Source: Fitch Ratings

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