

Quarterly Frontier Markets Recap

Frontier Market Recovery Modest as Challenges in Public Finances Persist

A recovery from last year's pandemic-induced recession is underway but will be modest against a low base, as GDP growth is constrained by limited fiscal space in most frontier markets (FMs). Risks from the pandemic persist due to slow vaccination rates across all regions, with renewed COVID-19 waves continuing to hamper external receipts, public finances, employment and GDP growth. However, the impact on sovereign creditworthiness should be less severe, as economies have adapted, allowing for more targeted COVID-19 containment measures.

Positive Rating Actions Slightly Outweigh Negative Actions

There were four Outlook changes in 2Q21, three of which were positive, and one rating change.¹ Azerbaijan and Cameroon's Outlooks were both revised to Stable from Negative. While the former's rating change was driven by much reduced downside risks to fiscal and external balances, reflecting the rebound in energy prices from last year's shock, Cameroon's Outlook revision reflects that the deterioration in its public finances last year was only mild. Vietnam's Outlook was revised to Positive, reflecting the continued resilience of its economic growth and public finances to the pandemic shock – it was one of only a few countries to experience GDP growth in 2020. On the other hand, Ghana's Outlook revision to Negative was triggered by weakening public finances, with its deficit more than doubling, primarily due to COVID-related spending. Finally, Suriname was downgraded again to RD, after failing to service its debt on 31 March.

External Liquidity Strains Easing for Some FMs

In many cases, import compression due to lockdowns and a hit to personal income more than offset the impact on current account balances in 2020 from a drop in exports and tourism receipts last year. The exceptions tended to be FMs dependent on either oil exports, such as Angola, Gabon, Iraq and Azerbaijan, or tourism receipts, such as Jordan, Georgia and the Maldives (not in JP Morgan's NEXGEM index). While most of the former have seen a significant improvement in external balances in 2021 due to higher oil prices, the latter are still grappling with large current account deficits, as tourism remains scarred by the pandemic. For example, Georgia's tourism revenues in 2021 are expected to reach only 30% of 2019 levels. Other tourism-dependent FMs, like Jamaica and Costa Rica, have benefited from resilient remittances due to growth in host countries, the use of more formal delivery channels while travel restrictions apply, and overseas workers' tendency to increase their financial support when families face hardships at home. Remittances also remained strong in Pakistan, with inflows up 33.5% yoy in May 2021, mitigating the sharp increase in its trade deficit in 1Q21, which was partly driven by the higher cost of oil imports.

In Guatemala, where agricultural products represent a large portion of total shipments, exports have remained resilient throughout the pandemic. This, combined with robust remittances has led to a widening in the country's current account surplus, with FX reserves now covering 10 months of current external payments, almost twice the 'BB' median of 5.4 months. Iraq also benefits from high FX reserves, in addition to low debt service obligations and strong international financial support. Official reserves have risen in most Asian FMs over the last six months, with Sri Lanka being the only exception.



Key Sovereign Rating Actions

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

Mongolia's Proposed USD Bond Assigned a 'B' Rating

Kenya's Proposed USD Bonds Assigned a 'B+' Rating

Azerbaijan's Outlook Revised to Stable; Rating Affirmed at 'BB+'

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

Vietnam's Outlook Revised to Positive, Rating Affirmed at 'BB'



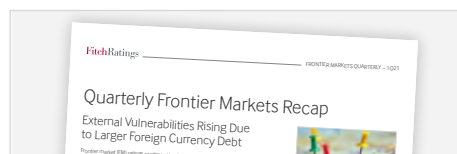
Webinars/Podcasts/Videos

Fitch on Centroamérica

External Liquidity Strains Ease in Some APAC Frontier Economies

Fitch on Asian Frontier Economies 2021

Fixed Interests – EM Taper Tantrum Risks



Previous Reports

Frontier Markets Recap – 1Q21

¹ Tunisia was downgraded in 3Q21 (on 8 July) and Zambia's LC IDR was upgraded in April, but its FC IDR remains on 'RD'.

Frontier Market Recovery Modest as Challenges in Public Finances Persist **(continued)**

In Vietnam, strong export demand due to a surge in demand for high-tech components and continued trade diversion from China have led to rising FX reserves. On the other hand, Bolivia's reserves could remain under pressure in 2021. A deep recession reduced its current account deficit to 0.5% of GDP in 2020, from a 4.9% average between 2015-2019, but the external relief was offset by negative FDI and capital flight.

Fiscal Scars a Legacy of the Pandemic

Public finances were the key negative rating driver for most FMs, as the pandemic exacerbated underlying weak fiscal trends predating 2020. Government deficits and debt burdens increased across all regions, with Iraq, Tunisia, Ghana, Mozambique, Namibia, Zambia, El Salvador, Bolivia, Suriname, Azerbaijan and Mongolia showing the largest deterioration in 2020. Economic recovery, higher commodity prices, and in some cases withdrawal of fiscal relief packages should lead to a decline in fiscal deficits or a return to fiscal surpluses (Azerbaijan and Angola) in 2021. Among the few exceptions are Suriname, Kenya, Ethiopia and Uzbekistan. Armenia's fiscal deficit is also expected to remain high, as the Nagorno-Karabakh war may have lasting effects on fiscal finances and domestic politics.

While higher oil prices will aid fiscal balances of most oil exporters, in Gabon, these will be offset by further declines in oil production. Namibia's fiscal deficit, which doubled in 2020, will remain high and lead to a continued rise in government debt, but fiscal financing risks are limited due to a well-developed domestic financial sector. On the other hand, Mongolia's budget deficit is projected to nearly halve in 2021, after spiking to 9.5% in 2020, and government debt/GDP is expected to decline, facilitated by a continued growth recovery. In the Americas, Jamaica's fiscal consolidation is happening faster than anticipated and we are now projecting a balanced budget for FY21/22.

Mongolia, Iraq, Angola, Gabon, Jamaica and Suriname will be among the few FMs to exhibit a drop in government debt ratios this year, but debt levels will generally remain high, with Angola, Jamaica and Suriname's still in the vicinity of 100% of GDP. Public debt stabilization will elude most FMs, as the pandemic has exacerbated pre-existing fiscal challenges from low revenue bases and rising spending pressures. With the pandemic still hampering structural consolidation, and several countries re-imposing restrictions due to a rebound in infections in 1H21 (e.g., Jordan, Vietnam, Sri Lanka, Mongolia and most European FMs), fiscal consolidation may be less of an immediate priority in IMF negotiations, although medium-term debt sustainability, structural reforms and revenue mobilization will still be encouraged.

New IMF Disbursements and Supportive Financial Conditions Boost Available Funding

FMs will benefit from the new allocation of the IMF's special drawing rights (SDR), which is expected to be approved by its board in August. The planned USD650 billion allocation will raise FX reserves for IMF member states without creating new debt or requiring conditions to be met. In addition, there are proposals for richer members to use their new SDR to support low-income countries (LICs), with the US, China and several European countries already expressing support.

Most IMF loans to LICs last year were under the Rapid Credit Facility (RCF), without conditionality, but further lending will increasingly fall under regular programmes such as the Extended Credit Facility (ECF), with conditionality. A large number of regular programmes are likely to be concluded over the next year, with Kenya and Gabon already locking in a deal and Cameroon reaching a staff-level agreement so far this year. There are also negotiations underway with Zambia and El Salvador, although uncertainty has risen for the latter due to governance concerns after February's election, which has led to a weakening in the country's checks & balances, and its sudden adoption of bitcoin as legal tender. Increased IMF financing could also incentivise some countries at high risk of distress to restructure under the G20 Common Framework (CF).

After an initial delay due to debt sustainability concerns, Ethiopia has passed its first two IMF reviews but is still awaiting formation of a creditor committee for treatment under the CF, leaving uncertainty about implications for private creditors. Pakistan has benefited from disbursement under its EFF in March and from Saudi Arabia's oil-assistance package in June. Sri Lanka agreed to a currency swap with Bangladesh in May, which if finalized, would build on existing loan and swap agreements with China. Both Pakistan and Sri Lanka would also see a significant boost in reserves from the IMF's SDR allocation.

Supportive global financial conditions have allowed a number of countries to (continue to) access international bond markets at benign conditions during 1H21, including Pakistan (July '21 & March '21), Cameroon (June '21), Mongolia (June '21 & Sept.'20), Kenya (June '21), Ghana (March '21), Cote d'Ivoire (Feb. '21) and Paraguay (Jan. '21). However, risks could arise from a sudden tightening of financial conditions, with FMs in Latin America and the Caribbean being most exposed to a rise in US bond yields, due to their generally greater reliance on international capital markets and shallow local markets. On the other hand, European FMs are more insulated from rising US interest rates, as these access the market relatively infrequently. Many sovereigns in the Middle East and Africa are also somewhat insulated by their high reliance on official financing, but given already elevated vulnerability due to high overall debt levels, several of them would still be exposed to a surge in international bond yields.

Newsreel



New Infection Wave Raises Pandemic Risks for African Sovereigns

A new wave of Covid-19 infections in a number of African countries, exacerbated by the Delta variant, has increased the risk of pandemic-related setbacks for rated sovereigns in Africa. Slow progress on vaccination suggests that pandemic risks will persist until at least 2022. The number of confirmed infections relative to populations has risen in Mozambique, Namibia and Zambia among Fitch-rated FMs.



Bitcoin Could Increase Regulatory, AML Risks for El Salvador Banks

El Salvador's recent legislation establishing bitcoin as a legal tender would increase financial institutions' regulatory, financial and operational risks, including the potential of violating international AML and terrorist financing standards. Regulators have yet to announce detailed implementation guidance, however, the high level of bitcoin price volatility will challenge its use as a store of value and means of payment.



On-Lending Could Amplify Positive Impact of IMF SDR Allocation

The main on-lending mechanism being considered is via the IMF's Poverty Reduction and Growth Trust (PRGT), which supports concessional loans such as the RCF and the ECF. Other mechanisms, including those via the World Bank and other MDBs, are also under debate but details are still vague. These could focus more on project-related financing - for instance for Covid-19 vaccination or climate-related projects.



ESG Investing in Sub-Saharan Africa Is Tied to Sustainable Development

The approach to ESG investing in SSA is closely linked to longer-term sustainable development benchmarks. This shapes how borrowers in the region frame sustainable investment opportunities and which types of issuers source financing through the international capital markets. Several African governments are planning to issue green or sustainability bonds in the next year.



Frontier Vision - 2Q21: Frontier Market Countries' Inflation Rates Are Still Rising

The trend of rising inflation in recent months has also been seen in Frontier Markets (FM), fuelled by higher commodity prices, supply-chain pressures and the gradual lifting of restrictions to curb the Covid-19 pandemic. Consumer price inflation continues to rise on a year-on-year basis among many frontier economies including Angola, Azerbaijan, Belize, Cote d'Ivoire, El Salvador, Ethiopia, Georgia, Iraq, Jordan, Mongolia, Pakistan, Sri Lanka, Vietnam and Zambia among others – this mirrors the global picture of rising inflation rates among many major economies covered in Fitch's Global Economic Outlook report.

Simultaneously, international trade has rebounded, in particular among commodity exporters, such as Azerbaijan, Mongolia and Papua New Guinea, but also other FM countries, such as Armenia, Belarus, Paraguay, Senegal, Sri Lanka and Tunisia. Fitch's quarterly 'Frontier Vision' chart pack tracks high-frequency macroeconomic data for the countries included in JP Morgan's Next Generation Markets (NEXGEM) Index. 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 countries representing sub-Saharan Africa, Latin America & the Caribbean, the Middle East & North Africa, Europe, Asia and Oceania.

Regional Commentary

Europe

Recovery from Covid-19 Pandemic Evident in Emerging Europe

Belarus Affirmed at 'B'; Outlook Negative

Uzbekistan Affirmed at 'BB-'; Outlook Stable

Middle East & Africa

Tunisia Downgraded to 'B-'; Outlook Negative

Tunisian Banks' Near-Term Prospects Still Very Challenging

Gabon's IMF Deal to Ease Near-Term Debt Repayment Risks

Jordan Affirmed at 'BB-'; Outlook Negative

Nigerian Banks' Near-Term Credit Risks Ease

Sub-Saharan Africa's Recovery Dampened by Weak Fiscals, Slow Vaccination

MENA Sovereigns Still Reeling from Covid-19, Weak Oil Prices

Financial Sustainability Next Challenge to African NDBs' Revival

Zambia's LC IDR Upgraded to 'CCC'; FC IDR Affirmed at 'RD'

Tunisia's Labour Union Deal a Step Towards Consensus on Reforms

Latin America & The Caribbean

Mexico, Central America & the Caribbean Face Challenges a Year into the Pandemic

Costa Rican Banks: 1H21 Review & Update

Guatemalan Banks: 1H21 Review & Update

Guatemala Affirmed at 'BB-'; Outlook Stable

El Salvador Affirmed at 'B-'; Outlook Negative

Return to Growth Not Sufficient to Repair Latin American Public Finances

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

Asia Pacific

Support Measures Ease Pressure on Mongolian Banks' Asset Quality

External Liquidity Strains Ease in Some APAC Frontier Economies

Risks for Sri Lankan Banks May Rise on End of Restriction on ISB Investments

Sri Lanka Affirmed at 'CCC'

Recent Vaccination Rise May Ease Pandemic Risks in Asia

Pakistan Affirmed at 'B-'; Outlook Stable

Mongolia Affirmed at 'B'; Outlook Stable

APAC Growth Outlooks Diverge amid Recovery from Pandemic Shock

Vietnam's Public Finances Outperform Peers Amid Pandemic Stress

Vietnam Banks: Chart of the Month - April 2021

New Border Disruptions Manageable for Mongolian Mining



Regional Commentary

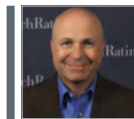
Country	Current Ratings	Last Rating Action	Outlook	Rating Action Type
Middle East & Africa				
Angola	CCC	04-Sep-2020	-	Downgrade
Cameroon	B	12-Apr-2021	►	Affirmation
Cote D'Ivoire	B+	17-Dec-2020	▲	Affirmation
Ethiopia	CCC	09-Feb-2021	-	Downgrade
Gabon	CCC	11-Dec-2020	-	Affirmation
Ghana	B	22-Jun-2021	▼	Affirmation
Iraq	B-	24-Mar-2021	►	Affirmation
Jordan	BB-	03-Jun-2021	▼	Affirmation
Kenya	B+	26-Mar-2021	▼	Affirmation
Mozambique	CCC	09-Dec-2020	-	Affirmation
Namibia	BB	07-Dec-2020	▼	Affirmation
Nigeria	B	19-Mar-2021	►	Affirmation
Tunisia	B-	08-Jul-2021	▼	Downgrade
Zambia	RD	12-Apr-2021	-	Affirmation
Latin America & The Caribbean				
Bolivia	B	30-Sep-2020	►	Downgrade
Costa Rica	B	16-Mar-2021	▼	Affirmation
El Salvador	B-	27-Apr-2021	▼	Affirmation
Guatemala	BB-	04-May-2021	►	Affirmation
Jamaica	B+	18-Mar-2020	►	Affirmation
Paraguay	BB+	02-Dec-2020	►	Affirmation
Suriname	RD	01-Apr-2021	-	Downgrade
Asia				
Mongolia	B	25-May-2021	►	Affirmation
Pakistan	B-	27-May-2021	►	Affirmation
Sri Lanka	CCC	14-Jun-2021	-	Affirmation
Vietnam	BB	01-Apr-2021	▲	Affirmation
Europe				
Armenia	B+	26-Mar-2021	►	Affirmation
Azerbaijan	BB+	14-May-2021	►	Affirmation
Belarus	B	07-May-2021	▼	Affirmation
Georgia	BB	12-Feb-2021	▼	Affirmation
Uzbekistan	BB-	09-Apr-2021	►	Affirmation

Legend

▲ (positive), ► (stable), or ▼ (negative)

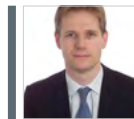
Source: Fitch Ratings

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