Corporate Bonds Market in Tanzania – what is not but should be working?

Recently, the African Development Bank launched a new bond program for infrastructure development in Sub-Saharan Africa, in its announcement AfDB had indicated that it planned to raise up to US$40 billion for investments in infrastructure projects such as ports and airports, highlighting the growing role for bond markets in financing development. This initiative by the bank underscores the fact that bond markets in Sub-Saharan African countries are at a nascent stage of development and there is a strong need to promote their development.

Tanzania, is one of the countries in Sub-Saharan Africa whose bonds market is underdeveloped; this has been and is still being the case despite our strong need for long term funding to feed into our business enterprises, to finance our infrastructure projects, to finance investments into housing projects and other programs that should be implemented to improve our people's social and economic welfare. Why haven't we being using the bonds market, both domestic and international, to fast-track our development projects and needs?

Before I proceed any further let me support what I am about to say with some data and statistics. As of 2013, the size of the worldwide bond market (total debt outstanding) was estimated to be slightly over $100 trillion, and according to Bank for International Settlements (BIS) and the Securities Industry and Financial Markets Association (SIFMA) as a proportion of the Global GDP, bonds market was about 140% of the Global GDP. In Tanzania, our bonds market is only 7% of the country's GDP.

Despite such a low level of bonds market development, our existing bonds market is also skewed towards Government bonds issued by the Central Government, there are few bonds issued by corporates and there are no bonds issued by municipals and local governments. Currently, bonds worth about Tshs. 3,500 billion listed at the the local exchange, but only 2% are corporate bonds – the remaining 98% are Government bonds and there no single Municipal or Local government bonds. Benchmarking with the U.S.A that dominates the total global bond market (the U.S commands about 40% of the global bonds market) – Government bonds in the U.S makes only about 30% of the total bonds market, Corporate bonds 25%, Mortgage backed bonds 30%, Municipal bonds 25% and other forms of bonds are 15%.

Even though banks, real estate development companies, corporate entities, SMEs and other entities may make use of the corporate bonds market for their growth and development, that has never been the case for us so far. For example, for the past 15 years of existence of the local stock exchange only nine companies have issued 13 corporate bonds worth about TZS 173 billion.

While corporate bond market has become an increasingly important component of the total bond market even in the Sub-Saharan Africa standards, where corporate bonds about 10% of total bonds market, this level is only 2% in Tanzania. Corporate bonds market capitalization to GDP in Sub Saharan Africa is currently at about 2%, for us it is less than one per cent (to be precise it is only 0.9%), while countries like South Africa it is at 15-20% levels.

So we may strongly argue that we have not used the bonds markets to develop our enterprises or even public development projects – why is that and why do we need to develop a vibrant bonds market?

Tanzania, like other most sub-Saharan Africa, has been heavily dependent on external grants and concessional loans for funding capital spending and government deficits and therefore has developed limited capacity to tap in and develop local bonds markets and have limited access to global capital markets for bonds issuance. Now, as western donors are now facing fiscal challenges on their domestic fronts, consequently donor flows to us may continue to be scaled back significantly. And, without access to alternative sources of finance, including bond markets, we could find it difficult to sustainably finance some of our critical needs.

The other reason for us to develop our bonds market is that the well-functioning bond markets will help to sustain our economic stability and the Asian experience supports this point. Since the 1997 Asian financial crisis, many Asian economies have made significant progress in strengthening bond market development. This has in turn helped these economies weather the recent global financial crisis because deeper financial markets generated valuable funding sources for these countries to finance fiscal stimulus packages.

Furthermore, the development of bond markets will definitely improve the intermediation of savings within the economy. As is, we are a bank-based economy with few other financial products or financial intermediations, as a result there is limited investment choices for passive investors. I have heard pension funds, insurance companies, fund managers; even banks complain that they have minimal options for investing their liabilities and obligations within our domestic context. This is mainly because there is a lack of effective intermediate channels to absorb this capital. Bond markets are an effective way to intermediate capital savers with capital users.

Also, in promoting bond market development in our country we will improve the structure of our financial system. As said above, our financial sector is dominated by banks. The non-banking sector and bond markets, both public and private, is still in its infancy and requires a deliberate efforts to push it to the level that we are supposed to be based on the current level of our development and development of the global financial markets. We may wish to note that bond markets and bank finance are complementary rather than incompatible. While banks tend to be more adept at providing short-term (working) capital, bond markets enjoy a comparative advantage in financing government deficits and infrastructure investment, and providing longer-term capital to companies for growth.

Lastly, deeper bond markets will enable our central bank to conduct monetary policy in a more effective manner. At present, our domestic fixed-income instrument is dominated by short term and long-term government debts. In this case a deeper bond markets would provide a wider, more effective range of instruments for monetary policy implementation.

In my next week’s columns I will further explain and expand my arguments in the above.