REPUBLIC OF RWANDA

MEDIUM TERM DEBT STRATEGY

MINISTRY OF FINANCE AND ECONOMIC PLANNING

FY 2018/19 – FY 2020/21

CONTENTS

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ABBREVIATIONS

ADF	African Development Fund
ATM	Average Time to Maturity
ATR	Average Time to Re-fixing
AfDB	African Development Bank
BNR	Banque Nationale du Rwanda
CNY	Chinese Yuan
DSA	Debt Sustainability Analysis
EDPRS	Economic Development and Poverty Reduction Strategy
EAC	East African Community
EUR	European Euro
EU	European Union
FY	Fiscal Year
GoR	Government of Rwanda
GBP	Great Britain Pound
GDP	Gross Domestic Product
GDF	Gross Domestic Financing
GE	Grant Element
GEF	Gross External Financing
KCC	Kigali Convention Center
IDA	International Development Association
IFAD	International Fund for Agricultural Development
IMF	International Monetary Fund
IR	Implied Rate
JPY	Japanese Yen
KWD	Kuwait Dinar
MTDS	Medium Term Debt Strategy
MINECOFIN	Ministry of Finance and Economic Planning
PV	Present Value
TZS	Tanzanian Shillings
OBL	Organic Budget Law
OPEC	Organization of the Petroleum Exporting Countries
PSI	Policy Support Instrument
RSSB	Rwanda Social Security Board
RWF	Rwandan Franc
SAR	Saudi Riyal
SDR	Special Drawing Rights
USD	United States Dollar
XR	Exchange Rate

EXECUTIVE SUMMARY

1. This three-year rolling Medium Term Debt Strategy (MTDS) helps determine how to best meet the Government of Rwanda's financing requirements, while balancing the difficult trade-offs between alternative financing options. In this strategy we assess the current and desired composition of the debt portfolio reflecting the preferred costs and risks trade-offs. Based on this, the preferred borrowing strategy going forward was selected.

2. The MTDS's overall objective is to maintain sustainable debt levels. Based on the Debt Sustainability Analysis (updated April 2018), Rwanda has maintained low risk of debt distress. However, risks are mounting and must be careful mitigated. It is the policy of the Government of Rwanda to maintain a low risk, and it adjust borrowing accordingly. A review of the existing debt portfolio shows that debt levels are increasing, with highly concessional borrowing options increasingly restricted, continued high exposure to foreign exchange risks in the external debt portfolio, while financing needs have soared with the pressing need to implement ambitious programs to fast track development under the *National Strategy for Transformation.*

3. Four alternative financing strategies have been developed and evaluated against costs and risks trade-offs and a strategy meeting GoR's medium-term debt objectives have been selected. strategy selection is based on projected concessional financing needs in the medium-term on one hand and, on the other, the medium-term objectives for the development of the Government's domestic securities market development.

4. The current selected strategy minimizes the costs and risks relative to the existing portfolio. The objective of this strategy is to ensure that government's financing needs and payment obligations are met at the lowest cost and risk levels while maximizing the use of concessional loans and developing the domestic capital market. This strategy lengthens the maturity of short-term domestic instruments while also providing the cheapest and least risky debt portfolio composition alternative. In addition, it is evident, from the assessment of alternative debt strategies, that a strategy that maximizes borrowing from concessional sources is cheaper than semi-concessional bilateral borrowing. The Government plans to continue to maximize wherever possible concessional borrowing in the external portfolio, while undertaking steps to plan for the repayment of Rwanda's Eurobond and deepening of the domestic market.

1. INTRODUCTION

In 2018, with Rwanda emerging from the effects of low global commodity prices and with economic growth rebounding, prudent debt management remains crucial. The implementation of the 2017/18 budget remains committed to fiscal consolidation and a prudent borrowing policy to keep Rwanda's level of debt sustainable.

The primary aim of Rwanda's debt management is to raise the required amount of funding at the lowest possible cost over the medium to long run, consistent with a prudent degree of risk; debt management is and remains critical to macro-financial stability and to financial sector development. Over FY 2015/16 and FY 2016/17, Rwanda's external imbalances widened together with the appreciation of the U.S. dollar. This led the country to the reduction of export receipts and asserted pressure on the exchange rate and official reserves.

In FY 2017/18, the pressures have reduced, however medium-term risks persist. While public investment plan continues to expand with Government as the main investor, Grants and concessional loans are diminishing. To meet the investment spending needs and middle-income growth ambitions articulated in Rwanda's *National Strategy for Transformation 2017-2024 (NST1)* and *Vision 2050*, both public and private investment must increase, and will require increasingly-complex financial transactions and strengthened management of public-private partnerships (PPPs). As Rwanda's economic performance improves (i.e. as measured by the Country Policy Institutional Assessment, CPIA), access to highly concessional borrowing from multilateral development partners will be increasingly restricted.

In the medium-term, careful accrual of new, growth- and export-enhancing debts should be managed against the rising costs of annual debt service. This includes consideration of state-owned liabilities and leases, risks which, if materialized, would erode Rwanda's capacity to invest in economic development. It will be particularly important to ensure a sound macroeconomic framework is in place to set the stage for the 2023 maturity date of Rwanda's USD-denominated $400 million Eurobond.

The Debt Sustainability Analysis (DSA) conducted in April 2018 by MINECOFIN shows that **Rwanda remains at low risk of debt distress**. This is based upon careful management of debt service, accelerating economic growth, and continued improved performance in exports in 2017-2018, which will expand domestic production and implementation of sound macroeconomic policies, including improved revenue mobilization and exchange rate flexibility. Except for a minor and temporary breach associated with Eurobond rollover, baseline indicators remain below thresholds.

For resilience in external shocks, and to deepen the domestic securities market, Rwanda is introducing the Benchmark bond through a series of bond reopenings starting from FY 2018/19, which will reduce the number of outstanding series, enhance liquidity in the market, and complete the previous subscription. This is intended to strengthen the ability to meet future debt obligations while developing a domestic capital market.

It is in this context, that the Medium-Term Debt Strategy for FY 2018/19 has been designed. The overall goal is to ensure that the contracting and payment of borrowed funds is made at a **lowest possible cost and risk level, prioritizing concessional borrowing wherever possible while supporting the development of the domestic capital market**.

2. OBJECTIVES AND SCOPE OF THE MTDS

2.1. OBJECTIVES

The objectives of Debt Management are to ensure that government's financing needs and settling of obligations meet the medium-term objectives and achieve the lowest-possible borrowing costs, while maintaining a Prudent risk exposure, and promoting an active domestic debt market.[1]

2.2. SCOPE AND TIME HORIZON

The time horizon for this MTDS covers a three (3) year rolling period running from July 2018-June 2019 to July 2020-June 2021. Annual update of the strategy is required by the organic budget law on state finances to ensure that the strategy remains aligned and coherent with the medium-term fiscal framework. In addition, it also enables regular monitoring of the debt portfolio costs and risks and assess whether the implementation of the borrowing transactions is in line with strategy under implementation. The scope of the strategy includes both public and publicly-guaranteed domestic and external debt.

3. BACKGROUND AND DEVELOPMENT OF THE DEBT PORTFOLIO

3.1. EXISTING PORTFOLIO AND TRENDS

Total public and publicly guaranteed debt for FY 2017/18 rose to a level of 51.6 percent of GDP (nominal, projected at end-June 2018).

Rwanda's external debt stock remains among the lowest in the region as a result of prudent macroeconomic, and debt management. The risk of debt distress remains low across the EAC, excluding Burundi and South Sudan (IMF-World Bank Debt Sustainability Analysis, 2017). Yet across EAC countries, public debt has been increasing faster since 2012.

The majority of Rwanda's debt is external (institutions (83 percent projected at end FY 2017/18), of which this is predominantly composed of concessional loans provided by multilateral institutions (74 percent of external debt at end FY 2017/18). Domestic debt is mainly composed of government securities especially Treasury bills together with Treasury bonds (more than 75 percent of total public domestic debt at end FY 2017/18).

Although concessional loans still constitute the majority of public debt (61.6 percent of the total portfolio at June 2018), non-concessional loans are showing a significant increase. This includes guarantees provided by the GoR to UCL for the completion of the Kigali Convention Centre (KCC), and loans and leases contracted by Rwandair for the acquisition of new aircrafts in anticipation of new service routes.

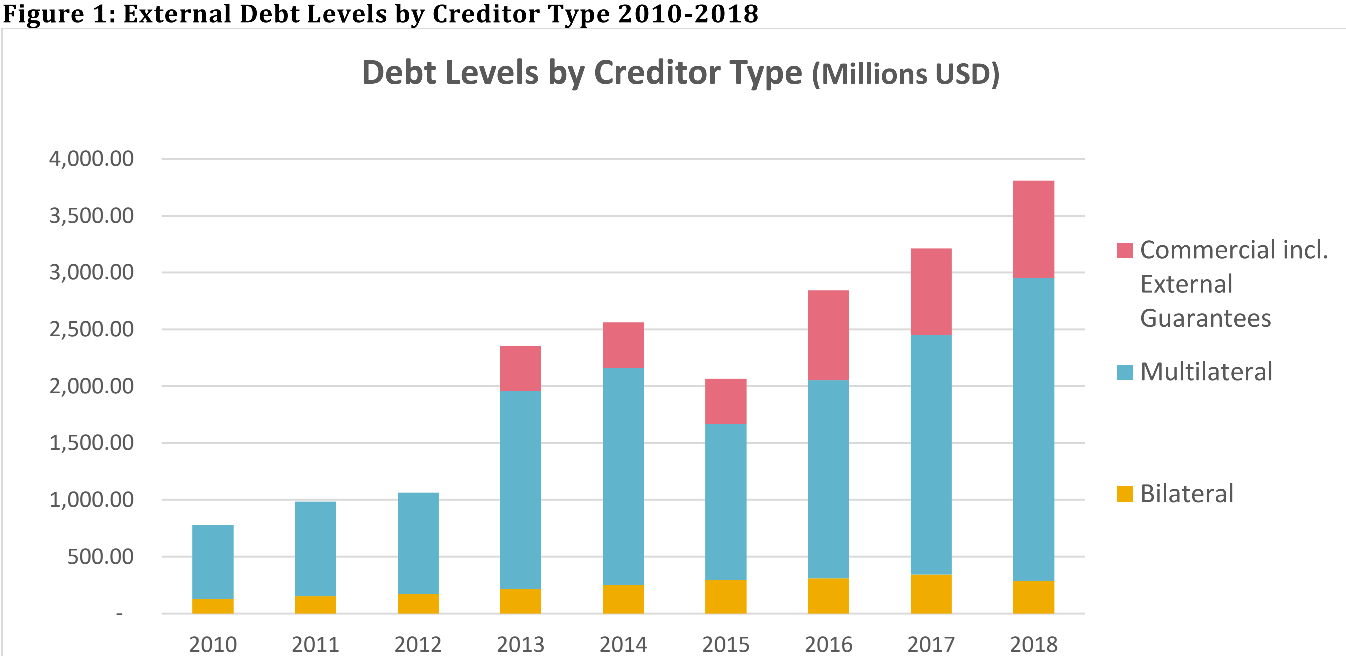
[1] Reference to the Ministerial order establishing revised financial regulations in its article 49 related to the Purpose of and authority for public debt management (January 2016).

Table 1: Rwanda Public Debt Stock 2017-2018

Public and Publicly Guaranteed Debt	June 2017 (End-FY 2016/17)			June 2018 (End-FY 2017/18)		
(Billion RWF, unless specified)	Billion (FRW)	% of GDP	share of total debt (%)	Billion (FRW)	% of GDP	share of total debt (%)
Total public debt	3207.9	45.0	100.0	4120.4	51.6	100.0
External	2540.1	35.7	79.2	3432.9	43.0	83.3
Concessional	1900.8	26.7	59.3	2538.1	31.8	61.6
Multilateral	1628.7	22.9	50.8	2291.4	28.7	55.6
Bilateral	272.1	3.8	8.5	246.7	3.1	6.0
Commercial	639.4	9.0	19.9	894.8	11.2	21.7
o/w Eurobond	332.1	4.7	10.4	344.0	4.3	8.3
o/w State Owned Enterprises	307.3	4.3	9.4	550.8	6.9	13.4
Domestic	667.8	9.4	20.8	687.5	8.6	16.7
Domestic Securities	622.8	-	-	633.4	-	-
Domestic Guarantees	44.9	-	-	54.0	-	-
GDP (current) in billions of Rwf	7,125			7,992		
GDP (current) in millions of USD	8,820			9,427		
Exchange Rate (Period Average)	808			848		
Exchange Rate (end of period)	830			866		

Source: MINECOFIN, June 2018.

Figure 1: External Debt Levels by Creditor Type 2010-2018



Source: MINECOFIN, June 2018.

3.2.COMPOSITION OF DEBT PORTFOLIO

External debt: Concessional loans are mainly provided by the World Bank IDA and African Development Bank AfDB (together, reflecting 60 percent of total external debt). Other key external funders include the Arab Funds, ADB, JICA, EU, China, and India. The funds were used for projects in the areas of transport, construction, energy, poverty reduction and rural development. In terms of currency composition, the SDR has the largest portfolio share.

Domestic debt: Domestic debt is mainly composed of short and long-term debt, while short-term debt constitutes 45 percent of domestic debt with issuance of treasury bills.

4. ANALYSIS OF RISKS IN THE PUBLIC DEBT PORTFOLIO

Rwanda's public debt portfolio poses overall low risk. Table 2 presents standard risks indicators which are normally included in the MTDS framework. This includes sustainability risks, interest rate risks, exchange rate risks, and refinancing risks.

TABLE 2: Cost and Risk Indicators for Existing Debt as at end-2018

Risk Indicators		**External debt**	**Domestic debt**	**Total debt**
Amount (in millions of RWF)		3,432,962,357,085	687,472,284,642	4,120,434,641,727
Amount (in millions of USD)		3,991,816,694.3	799,386,377.5	4,791,203,071.8
Nominal debt as % GDP		43.0	8.6	51.6
PV as % of GDP		29.2	8.6	37.8
Cost of debt	Interest payment as % GDP	1.3	0.7	2.0
	Weighted Av. IR (%)	3.1	7.8	3.9
Refinancing risk	ATM (years)	13.6	2.1	11.7
	Debt maturing in 1yr (% of total)	2.4	51.5	10.4
	Debt maturing in 1yr (% of GDP)	1.0	4.3	5.3
Interest rate risk	ATR (years)	12.8	2.1	11.0
	Debt refixing in 1yr (% of total)	18.2	51.5	23.7
	Fixed rate debt (% of total)	82.6	100.0	85.4
FX risk	FX debt (% of total debt)			83.6
	ST FX debt (% of reserves)			7.4

Source: MINECOFIN, Debt Unit, *Medium-Term Debt Strategy Tool*, June 2018.

In addition, the MINECOFIN Debt Management Unit, have customized other risks indicators with the objective of making the cost and risk analysis of the debt portfolio more relevant to MINECOFIN executive management and aid in prudent policy-making and performance management (*imihigo)*, e.g. debt-to-exports.

4.1.SUSTAINABILITY

Rwanda's risk of debt distress remains low. However, the level of public debt has been growing steadily to fuel public investment projects. The latest Debt Sustainability Analysis (DSA) conducted in April 2018 revealed that the **low risk of debt distress status** will be maintained – but requires careful monitoring and continuing to strengthen export and revenue collection performance.

Rwanda's PV of debt-to-export stood at 120.2 percent in 2017 (compared to the level of 112.7 percent in December 2015). The PV of debt service-to-exports stands at 7.2 percent in 2017, but increases sharply to 17.3 percent in 2023—the year of Rwanda's Eurobond repayment—with the potential for breaches particularly in the event of an exchange rate or other external shock.

The main reason for this deterioration is an increase in the level of non-concessional borrowing (as highly concessional multilateral lending sources are restricted as Rwanda' CPIA performance improves), as well as leases incurred for Rwandair fleet expansion plan, debt service, repayment associated with the Kigali Convention Center in 2019-2020, and the pressure of the Eurobond rollover in 2023.

At the same time, GDP growth is projected to rise; to ensure continued debt sustainability, borrowing must generate an economic rate of return recaptured by the Government, and economic growth must be translated into increased domestic revenues, enhanced export performance, and reserves. Going forward, high return in exports receipts are expected from diversification and strengthened export performance in non-traditional products like horticulture and floriculture, as well as the reduction of the import bill through substitution, including through the ''Made in Rwanda" initiative. But to do so, public investments should themselves be export-enhancing. This, combined with a prudent medium-term debt management strategy and a careful assessment of future projects' financing will remain critical to prevent public debt levels from becoming unsustainable.

TABLE 3: Debt Sustainability Indicators, per April 2018 DSA

Indicators	2018	2019	2020	2021	2022	2023	2024	*Threshold*
PV Debt to GDP	27.7	30.5	29.4	27.7	26.6	25.6	24.7	*50*
PV Debt to exports	120.2	126.3	121.3	116.4	112.7	107.1	102.4	*200*
PV Debt to Revenues	153.8	161.8	151.4	140.7	134.1	129.2	134.6	*300*
PV Debt service to Exports	7.2	7.5	10.8	11.4	8.1	17.3	6.5	*25*
PV Debt service to Revenues	9.2	9.6	13.5	13.8	9.6	20.8	8.5	*22*

Source: MINECOFIN, Debt Unit, April 2018.

4.2.RISKS

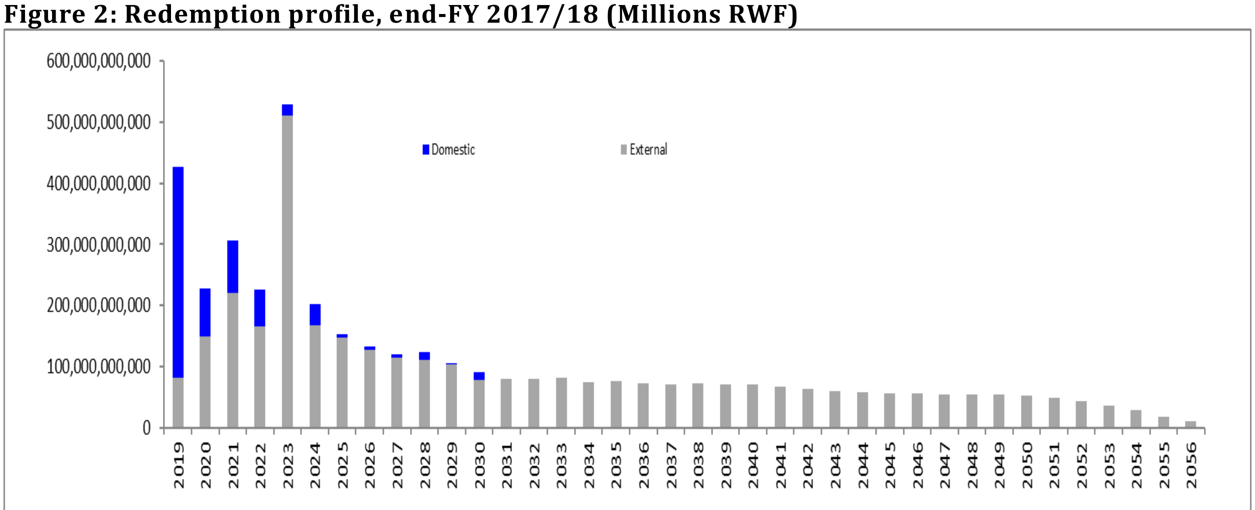
The main medium-term risk to Rwanda's debt sustainability derives from the US $400 million Eurobond, which matures in 2023. This refinancing risk is discussed in more detail below. While global exchange rate and interest rate risks are mounting, for the time being Rwanda is fairly insulated from these risks by its stock of highly concessional loans from development partners. As Rwanda's income level rises, it is taking on more sophisticated, variable rate debt instruments; as these grow in the portfolio, this will heighten interest rate and refinancing risks.

4.2.1. REFINANCING RISK

The average time to maturity (ATM) of the entire portfolio stands at a comfortable level of 11.7 (projected as at end-June 2018). This is explained by the predominance of concessional loans in the portfolio (ATM of 13.6 years for external debt) while the domestic debt shows a high refinancing risk within the next two years (ATM of 2.1 years); this shows a market improvement compared to the level of ATM 3 years ago which stood at approximately 1 year, thanks to the government policy to implement the Bond issuance plan while reducing Treasury bills.

The redemption profile is another measure of refinancing risks exposure of the debt portfolio. This sharp repayment profile indicates the severe liquidity risk presented in 2021 and 2023: in these years, the Treasury will have to service or roll over the existing Eurobond as well as its more traditional multilateral and bilateral debt service commitments. This risk is exacerbated if there were to be poor performance with respect to either revenues or exports, which would severely restrict the Treasury's capacity to service commercial or semi-commercial debts while addressing demand for forex; this could, in turn, have implications for the exchange rate (greater depreciation of the local currency) and would contribute to increased forex risk associated pressures. As such, diversifying the export base and building up exports, strengthening domestic revenue mobilization, and an overall sound macroeconomic framework will be essential leading up to the rollover or refinancing of the Eurobond and is the core of Rwanda's medium-term debt strategy.

Figure 2: Redemption profile, end-FY 2017/18 (Millions RWF)



Source: MINECOFIN, Debt Unit, *Medium-Term Debt Strategy Tool*, June 2018.

4.2.2. INTEREST RATE RISK

The total debt portfolio is entirely constituted of loans with fixed interest rates except ADB/IBRD. This means that the portfolio is insulated to risks related to variable interest rates. However, as Rwanda graduates from highly concessional lending sources, it is likely to be subject to variable interest rates, which will increase the risk and complexity of the portfolio.

4.2.3. EXCHANGE RATE RISK

Since end 2014, the foreign exchange (forex) market in Rwanda deteriorated, reflecting a narrow export base, high imports, and trends in donor support which moved away from budget support grants to more project lending. In addition, the continued strengthening of the US dollar has put pressure on the value of the Rwandan franc. These developments have increased the forex risk exposure of the debt portfolio which stands at nearly 83.6 percent in FY 2017/18 compared to 77 percent in FY 2014/15.

5. EXTERNAL SOURCES OF FINANCING FOR FUTURE NEEDS

The overall fiscal deficit (cash basis including grants) is projected to grow from 4.5% of GDP in FY 2017/18 (revised budget) to 4.8% of GDP in FY 2018/19. The overall fiscal deficit is projected at 4.6% and 4.4% for FY 2019/20 and FY 2020/21, respectively. The fiscal deficit financed through the contracting of external debt and issuance of Treasury-bills and Treasury-Bonds. In addition to that, guarantees were provided.

Debt owed to the banking system increased due to the new issued treasury bonds and treasury bills sold to commercial banks for domestic market development. The external debt stock as well increased due to additional new disbursements of more concessional loans (Bilateral and Multilateral) as well as non-concessional loans (commercial loans).

The low risk status is important to keep the financing windows which are currently available to Rwanda (i.e. AfDB window, IBRD, and also bilateral creditors like Japan, Exim Korea and others). Rwanda has traditionally sourced a significant portion of funding from multilateral creditors with highly concessional windows; however, with Rwanda's graduating income status, funding is likely to be increasingly sourced from bilateral creditors which may impose additional conditions and require low risk of debt distress before lending decisions.

Available funding sources for external borrowing in the near-term are assumed to be broadly similar to those already in place. These would be restricted to only borrowing on concessional terms, from multilateral sources (at fixed rates with maturity above 25 years) and bilateral sources (at fixed rates with maturity above 15 years). Borrowing domestically increasingly assumes longer maturity instruments to both local and foreign investors in order to increase net domestic financing and grow the local market over time. Over the longer-term, as Rwanda achieves higher levels of income and market sophistication, additional financing instruments may be accessed. However, to the extent possible, non-concessional borrowing will be on an exceptional basis, cognizant of any limits prescribed by IMF programs and based on careful consideration of the economic rate of return on the proposed projects.

6. MACRO-MARKET ENVIRONMENT FOR DEBT MANAGEMENT IN RWANDA

6.1.POLICY AND BUDGET ENVIRONMENT

The FY 2018/19 budget and MTDS were developed in the context of Rwanda's emerging economic recovery. In FY 2016/17, Rwanda's growth rebounded from the slowdown in first half of 2017 and the medium-term outlook is strong. Yet overall in FY 2016/17 the Rwandan economy grew by 3.4%, one of the lowest growth rates of the last five years. However, over the second half of 2017 growth rebounded, and early into 2018 there are positive signals about agriculture, exports, and overall growth over the period of this MTDS.

Export performance strengthened significantly in 2017. During FY 2016/17, the overall balance of payments is in deficit of US$ 5 million from a deficit of US$19.3 million at the end of previous FY 2015/16. The 74.1% increase was due to the strong performance seen in the trade balance, driven by an uptick in Rwanda's core commodity prices and enhanced performance in non-traditional exports. The current account balance improved by 14% in FY 2016/17. The trade balance is expected to improve by 21.8% in FY 2017/18, to US$ -1,063.7 million from US$ -1,359.9 million, driven by strengthened export performance (coffee, tea, minerals, non-traditional exports) bolstered by a more competitive exchange rate. Positive export trends and more modest import growth are expected to support the continued narrowing of the current account deficit to around 7.8 percent of GDP by 2019. Rwanda's performance at end-2017 confirms the projected rebound and establishes a solid foundation for further upward trends in FY 2018/19.

Fiscal performance during FY 2016/17 was affected by general economic performance and donor disbursements which affected the flow of resources on one hand and periodic fluctuations in expenditure commitments on the other hand which impacted on spending. Tax revenues registered solid performance under direct taxes and offset the shortfall from both tax on goods and services and tax on international trade.

Rwanda's fiscal consolidation in FY 2018/19 is an ongoing policy response to: the lingering effects of lower commodity, expansionary fiscal and monetary policies, and increased imports (on account of large public and private investment projects), which caused an increase in the current account deficit and loss of reserves. In response, the government adopted fiscal consolidation and a prudent borrowing policy to external balances sustainable.

A key source of growth in the medium-term will be regional integration, notably within the northern corridor of the EAC (Uganda, Kenya and Rwanda). In addition, tripartite negotiations are also pending between COMESA, EAC and SADC, as well as across the continent on the African Continental Free Trade Agreement. It is in that context that the government of Rwanda plans to implement its substantial infrastructure investment in order to achieve the targets outlined in the *National Strategy for Transformation for 2017-2024.*

TABLE 4: Medium-Term Fiscal Projections

	FY 2017/18	FY 2018/19	FY 2019/20	FY 2020/21
Revenues and Grants (Billion RWF)	1,766.5	1,997.5	2,241.6	2,589.7
Total Expenditures and Net Lending (Billion RWF)	2,105	2,398	2,677	3,070
Overall deficit (cash basis, including grants, % GDP)	-4.5	-4.8	-4.6	-4.4

Source: MINECOFIN, June 2018.

6.2. MARKET ENVIRONMENT

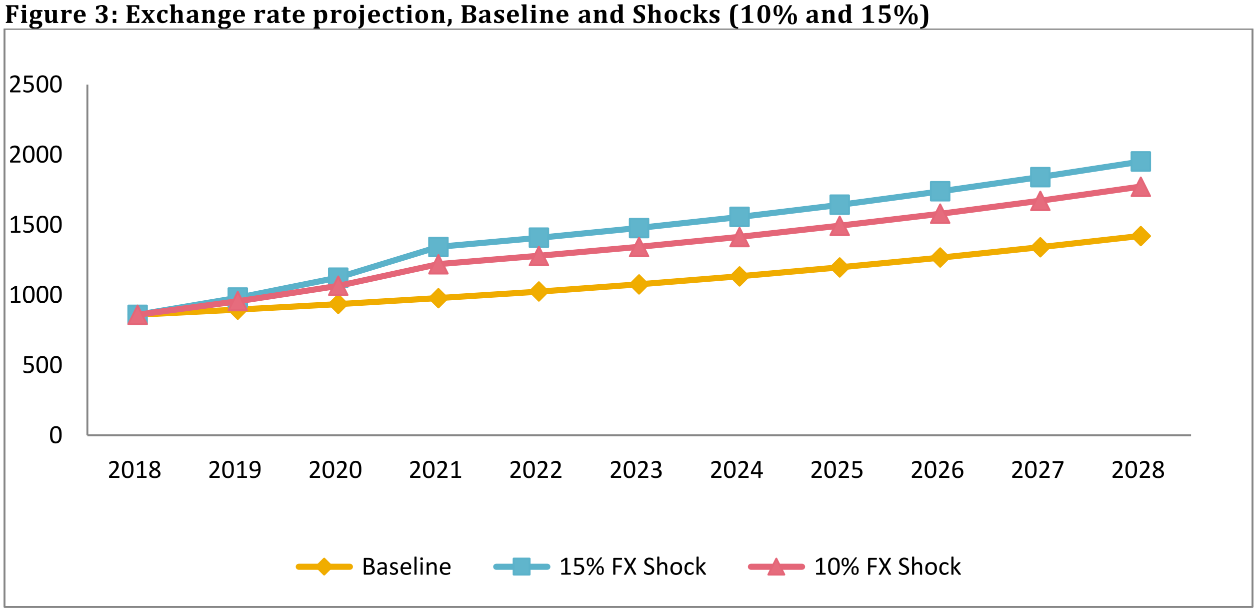
6.2.1. EXCHANGE RATE DEVELOPMENTS

During FY2016/17, the RWF continued the trend of depreciation, albeit at a slower rate overall when compared with the previous fiscal year. For the first half of the fiscal year, a combination of declining international commodity prices and high demand for forex from large Public-Private Partnership projects placed a lot of pressure on the exchange rate. This trend reversed towards the second half of the fiscal year due to a recovery in international commodity prices and improved external sector performance, lowering the pressure on the currency.

The Rwandan Franc (RWF) depreciated by 6.0% against the US Dollar (USD) in the FY2016/17 whereas this was 8.9% in the previous fiscal year. In the medium-term, the target is to maintain depreciation below 3-4% annually.

Based on the recent stabilizing of currency depreciation of the currency, Rwanda's exports performance, and the overall world economic outlook, the strategy assumed depreciation against USD of 4.2%, 4.5%, and 4.5%, respectively, in the next consecutive three years. The strategy models the impact of two possible depreciation shock scenarios: first, an additional 10% and second, an additional 15% against the baseline over the MTDS period. In particular, we consider the potential for a shock arising in 2021 reflecting pressures arising from the Kigali Convention Centre repayment date.[2]

Figure 3: Exchange rate projection, Baseline and Shocks (10% and 15%)



Source: BNR, June 2018. MINECOFIN, Debt Unit, *Medium-Term Debt Strategy Tool*, June 2018.

[2] Additional indicators are shown in Appendix A. *The MTDS was updated following the macroeconomic framework agreed under the 9th review of the PSI arrangement with the IMF (March 2018).*

6.2.2. INTEREST RATE DEVELOPMENTS

Through FY2016/2017, the money market interest rates decreased in response to liquidity conditions and the accommodative stance on monetary policy by the BNR with the key repo rate falling from 6.5% to 6.0%. The weighted normal rate of T-Bills increased from 7.30% to 8.78% by the end of FY2016/17. For the commercial banks' interest rates, deposit and lending interest rates initially increased during the first half of the fiscal year before declining by the end of the fiscal year. The reduction in the lending rate was in response to the drop in the rate charged to individual borrowers.

The first half of FY 2017/18 saw a further reduction in the key repo rate to 5.5%. The BNR has continued regular discussions initiated in 2017 with commercial bank treasurers about market developments and analysis. As result, the interbank market activity has continued to grow in both depth and width, and BNR has succeeded in keeping the interbank market rate close to the Key Repo Rate for almost two consecutive years.

To date, the interest rates of Rwanda’s debt portfolio are fixed to all instruments except to ADB/IBRD.

TABLE 5: Inflation and Interest rate 2014-2017

	Jun-14	Jun-15	Jun-16	Dec-16	Jun-17	Dec-17	Apr-18
Key Repo Rate (%)	6.5	6.5	6.5	6.24	6.0	5.5	5.5
T-Bills Rate (Weighted avg %)	5.6	4.1	7.3	9.0	8.8	7.1	5.8
Deposit Rate (%)	8.6	8.8	7.9	8.0	7.9	8.7	8.2*
Lending Rate (%)	17.5	17.3	17.0	17.2	16.8	17.2	16.8

Source: BNR, June 2018. *Available from March 2018.

6.3.VULNERABILITIES, RISKS AND STRUCTURAL CONSTRAINTS

Rwanda's economy remains vulnerable to internal and external imbalances, exacerbated by savings and investment imbalances. Increasing domestic savings and both public and private investment going forward are foundational to the macroeconomic goals laid out by Rwanda. The external debt portfolio has a large component of foreign currency denominated debt which also makes it vulnerable to exchange rate risks. On the domestic debt side, the high level of short-term notes increases rollover and liquidity risks.

Despite a robust macroeconomic environment and the efforts of the Government to sustain its stability, some associated vulnerabilities were identified as indicated below. They are taken into careful consideration in the selection of debt management strategies.

1. Constraints on domestic financing may be unfavorable to further develop the domestic market for Government securities. In response, in 2018 efforts are underway to deepen Rwanda's financial market through bond reopenings intended to establish benchmark bonds and promote depth and liquidity in the government bond market. BNR is taking steps to deepen the government securities market, enhance the yield curve, and improve price discovery.
2. Higher inflation on the domestic market, leading to monetary policy interventions, could raise the cost of issuing financing instruments. That is, investors might only be willing to hold instruments at higher nominal interest rates to protect themselves from yield losses resulting from high inflation.
3. Higher external current account deficits, mainly through increasing trade deficits and a larger current account deficit (resulting from lower official transfers) could adversely impact on the financing needs and contribute to a depletion of existing reserves buffers.
4. A greater than expected depreciation of the Rwf against major currencies (US dollar primarily), although potentially beneficial for export competitiveness, could raise the cost of servicing the existing and forthcoming external debt stock.
5. Exchange rate policies to smoothen currency volatility could weigh on available international reserves and increase the foreign exchange risk indicator of short-term debt to reserves.
6. Higher than envisaged domestic financing resulting from higher financing needs could crowd out private sector credit and adversely impact on growth.
7. Adverse climate or other emergencies (as have already been seen in 2018 with higher rainfall and flooding) could pose higher costs requiring borrowing, while undermining GDP growth and exports projections, further restricting sustainable borrowing limits.

Vulnerabilities and constraints

- Savings and investment imbalances
- Aid predictability, reduced availability of grants or highly concessional loans
- Underdeveloped financial sector
- Large exposure to foreign currency
- Weaker-than-expected export performance
- Higher-than-expected depreciation and/or inflation

Implications for the debt strategy

- Reduced concessional financing scope going forward
- Constrained domestic financing
- Domestic bond reopening to deepen securities market
- Ensure borrowing is restricted to high-return, export-enhancing investment projects
- Conservative debt management to manage liquidity constraints
- Monitor GDP and exports trends to moderate borrowing plan accordingly

7. ANALYSIS AND STRATEGY SELECTION

7.1. ANALYSIS, ASSUMPTIONS, AND FORECASTS

Potential sources of financing from abroad were identified, and strategies were designed in order to **ensure that funding plans are achieved while minimizing the possible impact on the costs and risks of the debt portfolio**. The expected costs (interests and exchange rates) and the risks have been calculated for each of the borrowing strategies. Further detail is provided in the annexes.

Borrowing strategies evaluated as part of the MTDS modelling include:

- **Strategy 1 (S1):** Status quo: predominantly concessional financing (85% external debt today, 70% of new debt over the FY 2018/19-2020/21 period).
- **Strategy 2 (S2):** Primarily external concessional borrowing (approximately 92% of outstanding debt, 73-75% of new debt over the period), with active efforts to deepen the domestic market in longer-term securities.
- **Strategy (S3):** Greater share of domestic debt relative to S2, to deepen the domestic debt market.
- **Strategy (S4):** Greater share of external commercial borrowing relative to S2.

TABLE 6: Summary of Strategies

Strategy	Rationale	Risks
S1	Status quo. Prioritizes concessional external borrowing, implying that there is preference for multilateral and bilateral debts with longer maturity and grace periods and fixed interest rates	• High forex exposure • High share of Treasury bills with short or one-year maturity • Exposure to exchange rate fluctuations
S2	Maximizes external concessional borrowing + development of domestic debt market for longer-term instruments	• Highly exposed to forex risk • Lower refinancing risk for debt maturing in one year, but higher exposure to exchange rate fluctuations
S3	Growing share of domestic debt, with more long-term domestic debt instruments combined with a reduction of short-term debt	• Reduces exposure to forex risk, but more costly + higher interest rates
S4	External commercial & non-concessional borrowing	• Highest cost, high interest rates, shorter time to maturity

Modelling results indicate **Strategy 2** being the best approach and evaluated according to criteria including lowest cost of borrowing, minimising foreign exchange (forex) currency risk, minimizing interest rate risk, and minimizing refinancing risks.

Going forward, the government's large investment agenda will require funding that remains within sustainable limits. All four strategies achieve this outcome; however, some strategies may have conditions attached to it, take longer to materialize, or are costlier.

TABLE 7: Objectives and Risk Mitigation Strategies Considered

Objective	Strategy
Lowest Cost	• Preference for all external borrowing to be concessional • Non-concessional borrowing on a case by case basis and subject to approval for exceptional high-return projects • Maximize cost-effective multilateral and bilateral borrowing • Restrict commercial borrowing to finance or refinance existing priority development projects
Mitigate Currency Risk	• Manage portfolio exposure to forex risk • Monitor USD- and SDR-denominated debt
Mitigate Interest Rate Risk	• Preference for fixed interest rate debt
Mitigate Refinancing Risk	• Gradually lengthen maturities of domestic borrowing. • Preference for multilateral and bilateral external borrowing with longer maturities and grace periods

TABLE 8: Risks Indicators of Proposed Strategies

Risk Indicators		2018	As at end 2021			
		Current	S1	S2	S3	S4
Nominal debt as % of GDP		51.6	48.9	48.9	48.9	49.0
Present value debt as % of GDP		37.8	33.7	33.3	34.2	35.3
Interest payment as % of GDP		2.0	1.6	1.6	1.7	1.7
Implied interest rate (%)		3.9	3.7	3.7	3.8	3.8
Refinancing risk	Debt maturing in 1yr (% of total)	10.4	5.9	5.0	4.9	5.1
	Debt maturing in 1yr (% of GDP)	5.3	2.9	2.4	2.4	2.5
	ATM External Portfolio (years)	13.6	14.6	14.8	14.6	13.5
	ATM Domestic Portfolio (years)	2.1	2.7	3.0	3.8	2.8
	ATM Total Portfolio (years)	11.7	13.9	14.2	13.7	13.0
Interest rate risk	ATR (years)	11.0	13.1	13.4	13.0	12.1
	Debt refixing in 1yr (% of total)	23.7	21.6	20.0	18.7	22.5
	Fixed rate debt (% of total)	85.4	82.4	83.0	84.2	80.7
FX risk	FX debt as % of total	83.6	91.0	91.7	87.5	92.5
	ST FX debt as % of reserves	7.4	11.5	11.5	11.5	11.5

Source: MINECOFIN, Debt Unit, *Medium-Term Debt Strategy Tool*, June 2018.

7.2.STRATEGIES

Strategy 1: Status Quo

This strategy essentially continues with the current debt portfolio, predominantly characterized by external, concessional debt. The ATM is the second highest risk (14.6 years), which is explained by the fact that limitations on commercial borrowings. The exposure to exchange rate risk in this strategy is high (91.0 percent) – as is true across all of the strategies available to Rwanda – due to a high level of foreign currency-denominated debt. However, the cost implied by this strategy is the second lowest because it is characterized by more concessional funding.

With regards to the short-term performance, the high share of treasury bills assumed in this strategy implies a higher refinancing risk, more than other strategies, for debt maturing in one year (2.9 percent of GDP). The interest rate of the strategy will not be affected in the near-term (13.1 years average time to refixing, ATR) due to small share of short-term domestic debt in the portfolio.

Strategy 2: External Concessional Maximization and Domestic Market Development

The chosen strategy focuses on concessional external debt, while domestic financing continues with the issuance of more treasury bonds. This strategy is the most sustainable and least costly: the ATM is 14.2 years, but highly exposed to exchange rate fluctuations (91.7 percent). Rwanda will continue to pursue concessional funding as the majority source, to mitigate risks in terms of interest, maturity and grace period. Non-concessional borrowing will be restricted to select, high-return projects.

This strategy also focuses on the development of the domestic capital market as it suggests more long-term domestic debt, in replacement of short-term notes. This strategy indicates that major developments are required in the structure of the domestic debt instruments in order to improve the existing indicators of risks related to refinancing of debt maturing in one year (2.4 percent).

This strategy ensures the lowering of the refinancing risk for debt maturing in one year, while the exposure to exchange rate fluctuations remains high. Nevertheless, it is the least costly strategy. The implied interest rate remains low (3.7 percent). In present value terms, this strategy minimizes the cost (33.3 percent of GDP).

Strategy 3: Domestic Debt Market Development

One alternative aims at more long-term domestic debt instruments combined with a reduction of short-term debt in order to contribute to domestic capital market development. A higher share of domestic debt would lower the exposure to exchange rate risk which is the lowest among all strategies (87.5 percent). However, this strategy is the highest cost (3.8 percent implied interest rate) and its interest rate would be affected sooner compared to other strategies (13.4 years) due to the big share of domestic denominated currency.

Strategy 4: External Commercial

New borrowing demand could be met through external non-concessional borrowing complemented with other external debt and some issuance of bills and bonds. The key point of this strategy is the foreign commercial borrowing, mainly through the financing of high-return projects. The risk indicators associated with this strategy are relatively accentuated: the ATM (13.0 years) is lower than other strategies, as the share of non-concessional borrowing is lower; the cost implied by the interest payments increases (3.8 percent); and the PV substantially higher (35.3 percent of GDP).

8. RECOMMENDATION

The borrowing option indicating at the **lowest-risk strategy is S2, characterized by a high share of concessional instruments. Strategy 2 remains Rwanda's most appropriate and feasible financing option, given the fact that it is less costly, balances risks, while allowing room to grow the domestic and foreign instruments available to Rwanda over time.**

The proposed strategy includes:

- **Mitigate cost of borrowing:** High concessionality requirement for all external borrowing; maximize multilateral borrowing and bilateral borrowing if concessional; non-concessional borrowing shall be limited to cases where grants or concessional resources are unavailable, where the project generates a high economic rate of return (ERR), and where the borrowing would not result in a significant and persistent increase in debt vulnerabilities.
- **Mitigate interest rate risk:** Preference for fixed interest rate debt; and
- **Mitigate refinancing risk:** Gradually lengthen maturities of domestic borrowing; a preference for multilateral and some bilateral debt with longer matruities.
- **Develop domestic market:** These are achieved while over time deepening Rwanda's domestic market.

Strategy	Cost of borrowing	Foreign exchange	Interest rate risk	Refinancing
S1	✓	⊜	✓	✗
S2	✓	⊜	✓	✓
S3	✗	✓	✗	✗
S4	✗	✗	✗	✗

9. PORTFOLIO BENCHMARKS

TABLE 9: Benchmarks for Desired Portfolio (at end of period)

Risk Indicators				**Benchmark**
		2018	**S2**	**End Period**
Nominal debt as % of GDP		51.6	**48.9**	Max.55
Present value debt as % of GDP		37.8	**33.3**	Less than 40
Interest payment as % of GDP		2.0	**1.6**	Max.4.5
Refinancing risk	Debt maturing in 1yr (% of total)	10.4	5.0	Max. 13.3
	ATM External Portfolio (years)	13.6	14.8	Min. 12
	ATM Domestic Portfolio (years)	2.4	3.0	Min. 2.5
	ATM Total Portfolio (years)	11.7	14.2	Min. 12
Interest rate risk	ATR (years)	11.0	13.4	Min. 11
	Debt refixing in 1yr (% of total)	23.7	20.0	Max. 20
	Fixed rate debt (% of total)	85.4	83.0	Min. 85
FX risk	FX debt as % of total	83.6	91.7	Max. 90
	ST FX debt as % of reserves	7.4	11.6	Max. 10

Source: MINECOFIN, June 2018.

TABLE 10: SELECTED MACRO-MARKET INDICATORS, FY 2018/19-2020/21

	FY 2018/2019	FY 2019/2020	FY 2020/2021
RWF UNITS			
Revenues and grants	1,997,483,310,162	2,241,605,843,441	2,589,729,879,906
Total primary expenditures	2,206,985,425,265	2,485,302,461,785	2,852,455,477,259
Total expenditures	2,301,706,403,875	2,579,713,254,826	2,950,035,248,414
Total interest expenditure	94,720,978,610	94,410,793,041	97,579,771,155
International reserves (USD million)	1,389,388,619	1,602,032,296	1,838,569,077
GDP	8,936,475,855,975	10,162,860,927,920	11,702,193,792,499
Baseline exchange rate, RWF per USD	881.53	921.20	962.65
Primary Deficit	209,502,115,103	243,696,618,343	262,725,597,353
Interest Payments	163,468,592,158	132,011,881,110	124,097,142,812
Interest on Existing Debt	163,468,592,158	132,011,881,110	124,097,142,812
Interest on New Debt	0	0	0
Amortization	414,947,896,309	158,791,200,064	207,774,087,882
Amortization on Existing Debt	414,947,896,309	158,791,200,064	207,774,087,882
Amortization on New Debt	0	0	0
Gross Financing Need	787,918,603,570	534,499,699,517	594,596,828,047
Gross Financing Need in USD millions	893,806,014.5	580,220,532.0	617,663,481.7
Gross Financing Need to GDP (%)	8.8	5.3	5.1
Primary Deficit (in % of GDP)	2.3	2.4	2.2
Fiscal Deficit (in % of GDP)	4.2	3.7	3.3

ANNEX B: POTENTIAL SOURCES OF FUNDING AND FINANCING STRATEGIES

TABLE 11: KEY INSTRUMENTS

Instrument Nr.	Instrument Type / Name	Fix / Var	Concessional or Market Instrument?	Maturity (y)	Grace (y)	Currency Type	Currency (3-letter code)
USD_1	EXISTING AND NEW IDA	Fix	Concessional	38	6	FX	USD
USD_2	ADF	Fix	Concessional	40.0	10.0	FX	USD
USD_3	ARAB FUNDS	Fix	Concessional	28.0	8.0	FX	USD
USD_4	EURO BOND	Fix	Market	10.0	9.0	FX	USD
USD_5	ADB_IBRD	Var	Concessional	20.0	5.0	FX	USD
USD_6	CHINA_INDIA	Fix	Bilateral	20.0	6.0	FX	USD
RWF_7	TBILLS-6MONTHS	Fix	Market	1.0	0.0	DX	RWF
RWF_8	TBILLS-1 YEAR	Fix	Market	1.0	0.0	DX	RWF
RWF_9	RSSB_CSR	Fix	Market	9.0	4.0	DX	RWF
RWF_10	BNR	Fix	Market	15.0	3.0	DX	RWF
RWF_11	TBONDS 7-10YRS	Fix	Market	9.0	8.0	DX	RWF
RWF_12	TBONDS 15YRS PLUS	Fix	Market	15.0	14.0	DX	RWF
RWF_13	TBONDS 3-5YRS	Fix	Market	4.0	3.0	DX	RWF
USD_14	EXT GUARANTEES	Var	Market	8.0	2.0	FX	USD
RWF_15	DOM GUARANTEES	Var	Market	8.2	2	DX	RWF

TABLE 12: NEW AND OUTSTANDING DEBT BY INSTRMENT, AS OF END 2021 (% AND USD MILLIONS)

% of gross borrowing - Over Projection Period					
New debt		S1	S2	S3	S4
EXISTING AND NEW IDA	FX	29%	33%	30%	22%
ADF	FX	11%	13%	8%	6%
ARAB FUNDS	FX	5%	4%	6%	3%
EURO BOND	FX	0%	0%	0%	13%
ADB_IBRD	FX	7%	8%	7%	8%
CHINA_INDIA	FX	6%	6%	6%	7%
TBILLS-6MONTHS	DX	17%	13%	12%	14%
TBILLS-1 YEAR	DX	2%	2%	2%	2%
RSSB_CSR	DX	0%	0%	0%	0%
BNR	DX	0%	0%	0%	0%
TBONDS 7-10YRS	DX	2%	2%	6%	2%
TBONDS 15YRS PLUS	DX	0%	0%	0%	0%
TBONDS 3-5YRS	DX	6%	7%	12%	5%
EXT GUARANTEES	FX	12%	10%	8%	15%
DOM GUARANTEES	DX	3%	2%	4%	3%
External		70%	73%	64%	75%
Domestic		30%	27%	36%	25%
		100%	**100%**	**100%**	**100%**

In % of Total	FY2018	As at end FY2021			
Outstanding by instrument	Current	S1	S2	S3	S4
EXISTING AND NEW IDA	37%	41%	42%	41%	38%
ADF	13%	15%	15%	13%	12%
ARAB FUNDS	6%	6%	6%	7%	5%
EURO BOND	9%	7%	7%	7%	12%
ADB_IBRD	1%	4%	4%	4%	4%
CHINA_INDIA	6%	7%	7%	7%	7%
TBILLS-6MONTHS	0%	1%	0%	0%	1%
TBILLS-1 YEAR	8%	0%	0%	0%	0%
RSSB_CSR	0%	0%	0%	0%	0%
BNR	1%	1%	1%	1%	1%
TBONDS 7-10YRS	1%	2%	2%	4%	2%
TBONDS 15YRS PLUS	0%	0%	0%	0%	0%
TBONDS 3-5YRS	3%	3%	4%	6%	3%
EXT GUARANTEES	14%	12%	11%	10%	14%
DOM GUARANTEES	1%	2%	1%	2%	1%
External	85%	91%	92%	87%	92%
Domestic	15%	9%	8%	13%	8%
Total	100%	100%	100%	100%	100%

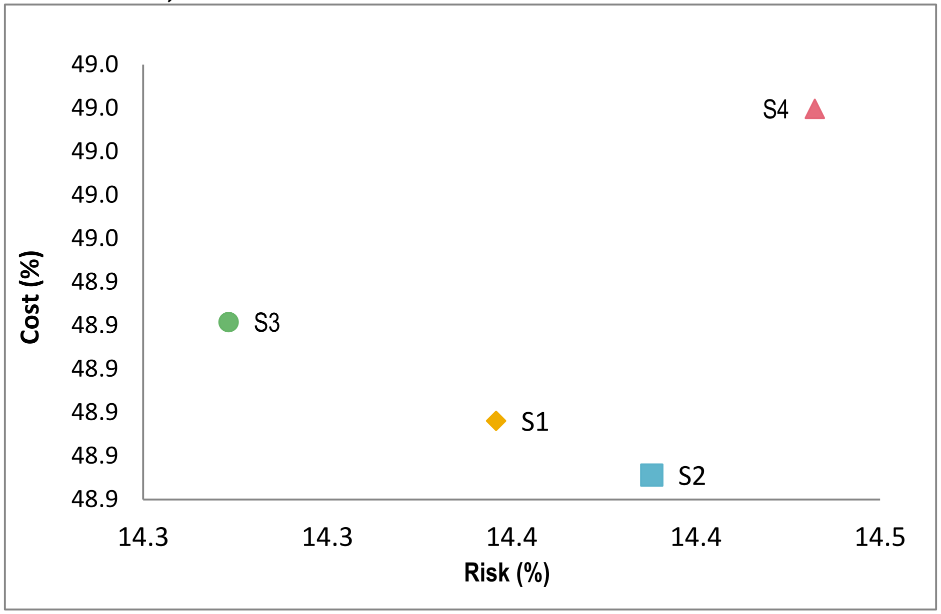
In millions of USD	FY2018	As at end FY2021			
Outstanding by instrument	Current	S1	S2	S3	S4
EXISTING AND NEW IDA	1,724,887,971	2,420,482,050	2,483,582,136	2,416,195,119	2,233,500,865
ADF	599,589,411	864,250,103	898,076,699	777,984,415	741,024,805
ARAB FUNDS	286,655,491	373,878,217	348,614,641	395,953,543	321,852,571
EURO BOND	400,000,000	400,000,000	400,000,000	400,000,000	719,563,403
ADB_IBRD	53,328,453	224,687,854	255,982,304	211,792,852	256,153,884
CHINA_INDIA	286,832,338	401,887,289	391,637,039	394,467,028	426,311,788
TBILLS-6MONTHS	0	76,818,967	27,358,007	13,875,285	38,543,391
TBILLS-1 YEAR	352,684,437	15,305,242	12,046,919	21,094,320	11,276,234
RSSB_CSR	2,759,169	56,477	56,477	56,477	56,477
BNR	43,583,906	33,824,584	33,824,584	33,824,584	33,824,584
TBONDS 7-10YRS	65,040,650	108,800,949	117,382,480	210,131,568	100,493,016
TBONDS 15YRS PLUS	11,614,402	10,206,963	10,206,963	10,206,963	10,206,963
TBONDS 3-5YRS	162,601,626	190,837,386	212,638,877	335,505,846	167,100,434
EXT GUARANTEES	640,523,031	725,275,115	669,654,488	608,198,896	806,996,915
DOM GUARANTEES	52,373,013	99,036,028	82,771,578	118,823,562	87,167,552
External	3,991,816,694	5,410,460,628	5,447,547,306	5,204,591,853	5,505,404,231
Domestic	690,657,204	534,886,597	496,285,885	743,518,605	448,668,652
Total	**4,682,473,898**	**5,945,347,225**	**5,943,833,191**	**5,948,110,459**	**5,954,072,883**

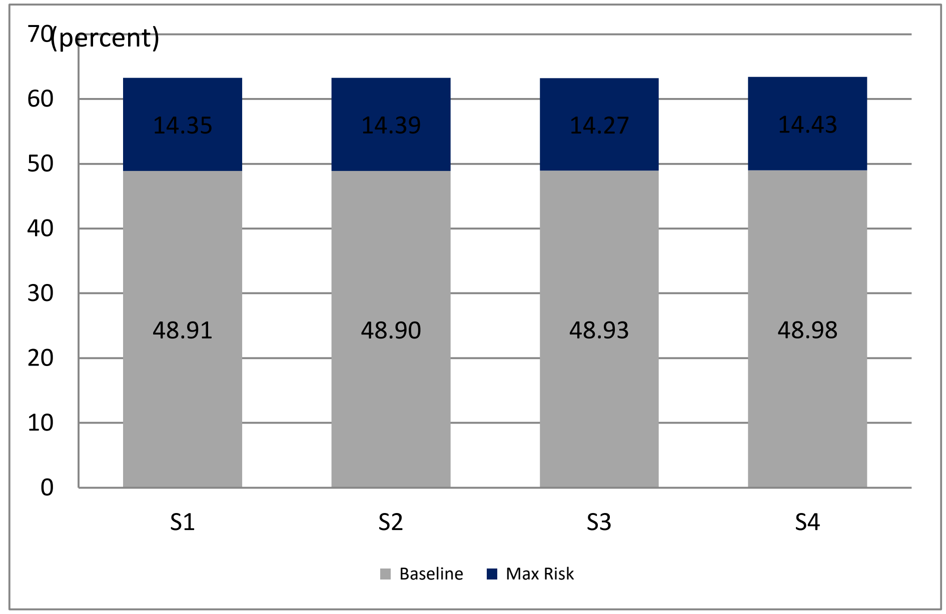
TABLE 13: BORROWING STRATEGY PERFORMANCE FOR EACH RISK INDICATOR

Risk Indicator	**Best Performing Scenario as at 2021**	**Graph Reference (Refer *Appendix B*)**
Debt to GDP	Scenarios on par	*Figure 1*
PV of Debt to GDP	S2	*Figure 2*
External Debt to GDP	S3	*Figure 3*
Total Debt Service to GDP	S2	*Figure 6*
Interest Rate to GDP	S2	*Figure 4*
Interest to Revenues	S2	*Figure 5*
External Debt Service to International Reserves	S3	*Figure 7*

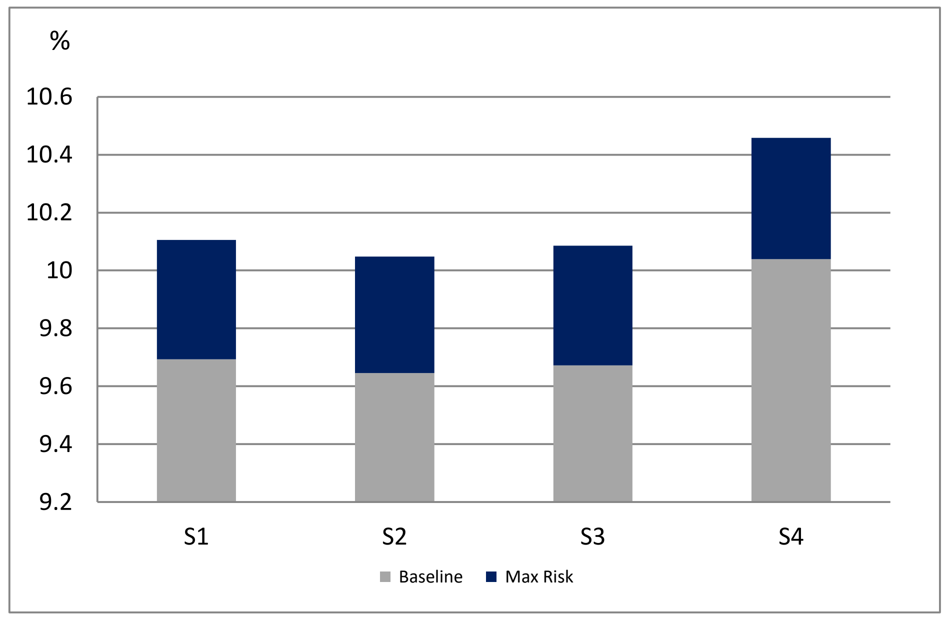
FIGURE 4: KEY COST AND RISK INDICATORS BY STRATEGY (AS OF END-2021, %)

Debt to GDP,

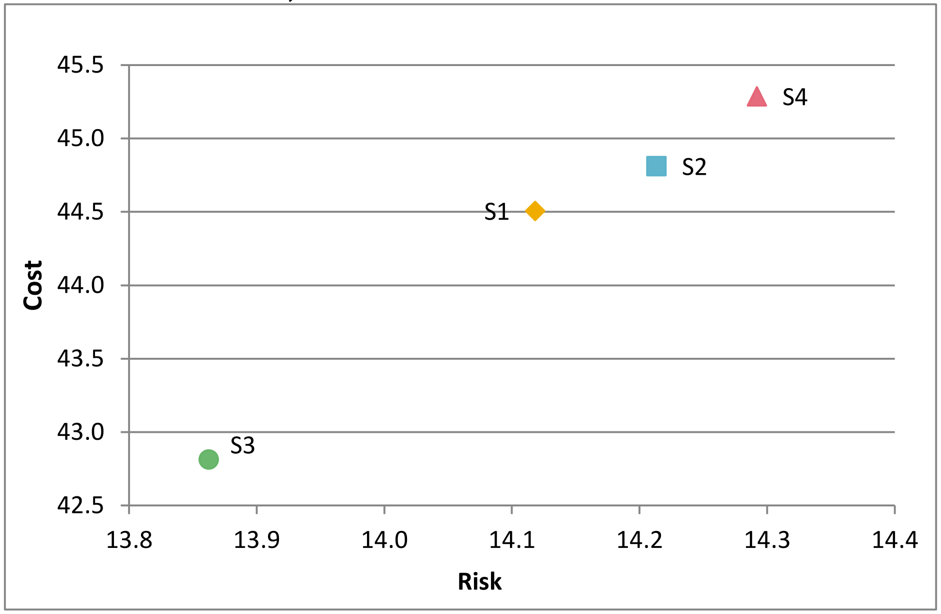


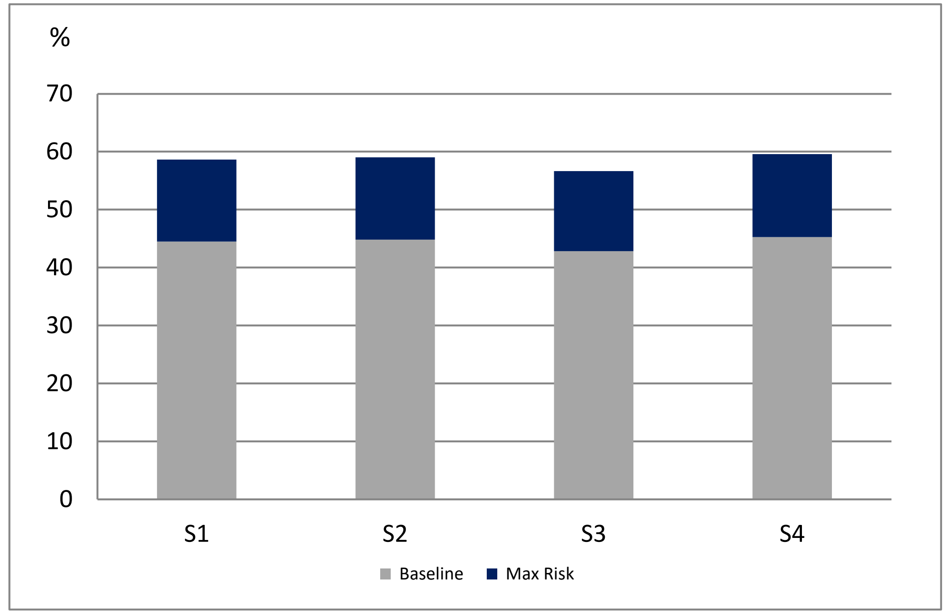


PV of Debt to GDP, as of end 2021

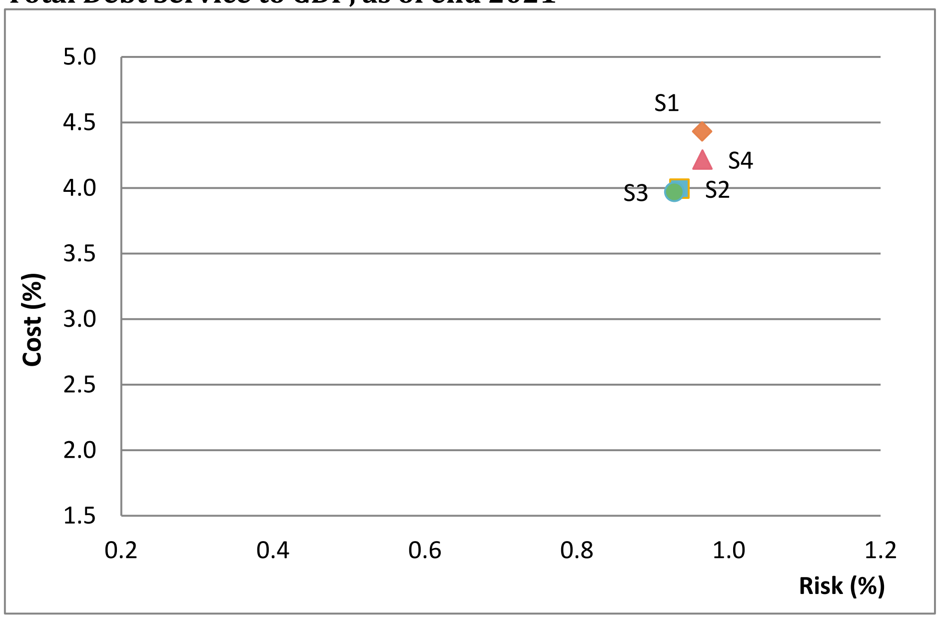


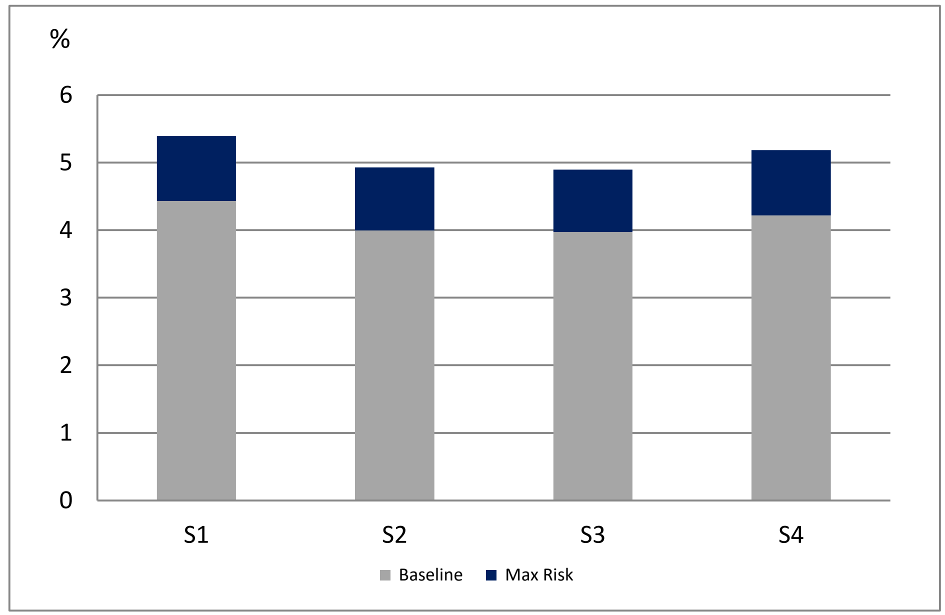
External Debt to GDP, as at end 2021



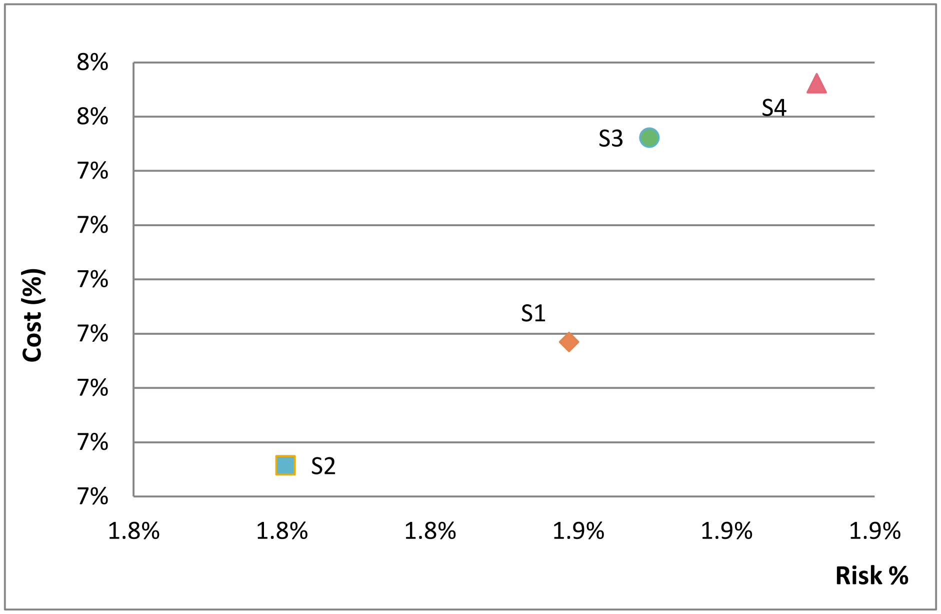


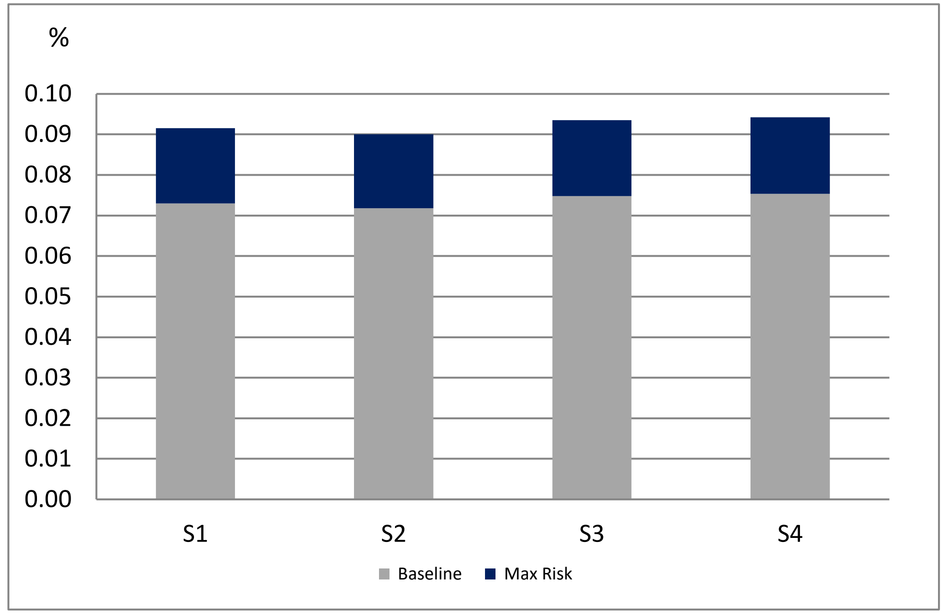
Total Debt Service to GDP, as of end 2021





Interest to Revenues





External Debt Service to International Reserves