

Angola's Interest Rate Fixings Generate USD 270 Million in Potential Savings

The World Bank Treasury supported Angola to reduce interest rate risks on 98 percent of their IBRD outstanding debt amount and helped create up to USD 270 million in potential savings on the estimated interest repayment.¹

Background

As the interest rates started to increase globally in 2021, the Angolan government was concerned about financial risks associated with variable reference rates. Angola had 80% of its external debt portfolio tied to variable reference rates. The mitigation of interest rate risks became even more urgent with the impending transition of the London Interbank Offered Rate (LIBOR) to new reference rates by the end of 2021, and the uncertainty surrounding the transition. The government wanted to build its capacity on how to manage financial risks and requested training from the World Bank on IBRD's financial solutions, as well as analyses of market trends.

Financial Objectives

- Reduce the interest-rate risk of Angola's debt portfolio
- Eliminate uncertainty around LIBOR transition
- Benefit from lower interest rates in 2021

Financial Solution and Outcomes

The IBRD Flexible Loan (IFL) includes options to manage interest rate risks over the life of the loan. These options are embedded into the loan agreement and can be executed at any time at the borrower's request.

Borrowers of IFL can fix the reference rate for all or part of the disbursed amount for the whole or partial maturity of the loan. They can also unfix or refix the reference rate at any time during the life of the loan¹.



Luanda's waterfront Photo Credit Adobe Stock- JPMatias

In December 2021, after receiving training from the World Bank on financial risk management, and shortly before the LIBOR secession date², Angola requested interest rate conversions for the majority of its disbursed IBRD loans, benefitting from the embedded conversion option of the IFL. The World Bank Treasury converted to fixed rate Angola's variable reference rates for 11 loans, for a total amount of USD eq. 2 billion and a remaining average repayment maturity of 13 years, before December 31, 2021 (Figure 1).

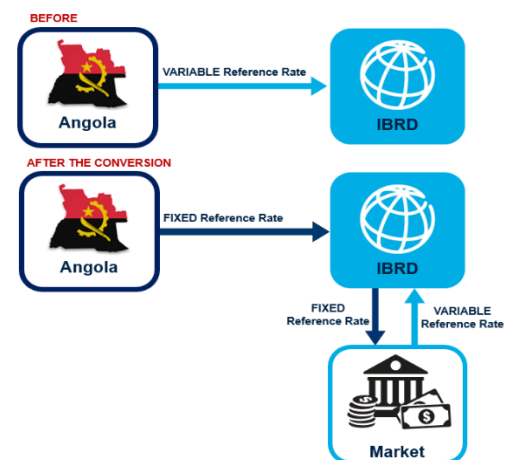


Figure 1. Transaction structure for interest rate conversion by IBRD

¹ There is a charge on interest rate conversions such as this one, and can be found under the [IBRD Flexible Loan Conversion Options](#).

² In March 2021, LIBOR's regulator confirmed the LIBOR cessation date by announcing that all settings for the Swiss franc, euro, Pound sterling, and

Japanese yen, and two settings for U.S. dollar will either cease to be provided by any administrator or no longer be representative after December 2021, and the remaining LIBOR settings for U.S. dollar will cease after June 2023.

After the conversions, in line with market projections, interest rates continued to increase. By July 2022, USD (variable-to-fixed) swap rates were up 155 basis points for LIBOR and 140 basis points for the Secured Overnight Financing Rate (SOFR) for a 12-year maturity loan (vs. December 20, 2021) (Figure 2).

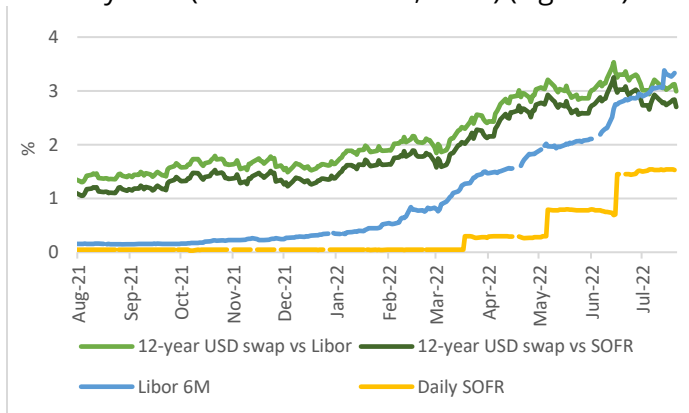


Figure 2. Interest rate developments in 2022

As a result, the government of Angola had a potential saving of USD 270 million on the estimated interest to be paid over the life of the loan (equivalent to 13.5 percent of the total amount converted - data based on Bloomberg as of July 2022). The actual savings at the end of the loans may be higher or lower depending on the path of SOFR rate trajectory.

The interest rate conversions of the 11 loans, accounting for 98 percent of Angola's outstanding debt amount to IBRD, made their debt service predictable and contributed to protecting the country from increases in interest rates.

World Bank Treasury's Role

The World Bank Treasury team worked with the Angolan government to:

- **Built capacity of the client** on the use of financial risk management instruments, by delivering training sessions to the Ministry of Finance officials from September to December 2021.
- **Analyze market trends** for inflation and other factors and shared the market consensus on projected interest rates with Angola to support them in their internal discussions.
- **Provide alternative risk management tools** such as (i) full interest rate conversion; partial interest rate conversion, short vs. long term maturity, (cap and collar options to limit interest rate variability).³
- **Convert 11 loans** with a total of USD 2 billion from variable reference rates to fixed reference rates at competitive financing terms, leveraging the World Bank's triple-A credit rating.
- **Make the conversion administratively cost-effective** and straightforward for Angola as an embedded feature of the IFL agreement.
- **Execute an interest rate swap** with market counterparties to match the fixing of the reference rate with Angola and hedge IBRD's interest rate risk exposure (Figure 1).

The World Bank Treasury helps clients manage interest rate and currency risks in their debt portfolios by sharing over 70 years of capital markets experience, using the flexibility of the IBRD loans, and executing hedges on non-IBRD exposures.

³ Caps set an upper limit on the variable interest rate of the loan. Collars set an upper limit (a cap) and a lower limit (a floor) on the interest rate of the loan, so

that the borrower have the IBRD fix the loan, if the interest rates exceed the cap and unfix the loan if the interest rates drop below the floor amounts.