

- Guarantee Example Corporate Bond

The extension of MTN's mobile network in Uganda to 24 rural municipalities was enabled by a guarantee from Sida. This kind of intervention plays an important role in supporting the development of financial sectors. Research studies also show that cash strapped women in Uganda found new income possibilities, as they started to sell airtime in villages.

The problem and the opportunity

The African telecom company MTN won a license in Uganda in 1999 to build a second nation wide GSM network. Since the company had achieved a great demand for the mobile services among all customer types, they believed that it would be possible to build out the network beyond the original investment plan, thus completing the national coverage and doubling the number of subscriptions. 24 rural villages had been identified as part of this extended plan, which were located in less densely populated and poorer areas.

Additional funding of another USD 40 million was needed, of which coverage of the 24 villages would cost USD 7 million. Sida was asked for its traditional aid financing to support this additional expansion, but wanted to try another approach. Therefore, Sida proposed MTN to issue a bond in local currency, backed by a guarantee from Sida; i.e. Sida would secure MTN's obligations against the bond investors. This meant that Ugandan pension funds and other potential local investors with excess cash on deposits could fund MTN in local currency with no currency risk and higher return than on US treasury bills.

The most important development aspect of improved telecom infrastructure is increased economic activity and productivity. It is saving time and money when a

phone call can replace a trip to a distant market in order to search for a product, and can allow for more regular updates of information than the traditional weekly radio broadcasts, newspapers or letters. There are numerous research studies that confirm the links between increased and improved access to ICT and the economic uplift of developing economies.

Telecom in Uganda – before

In 1999 about two households in one hundred had a telephone in Uganda, which was even lower than the African average at the time. The first mobile phone users were primarily male, educated and urban populations¹. After two years in operation, MTN had captured a 56% market share. The government started a reform of the sector and issued two mobile licenses. The conditions of the operator's license demanded that the 37 regional capitals of Uganda were to be covered and that every county headquarter have a public telephone. MTN wanted to go beyond the requirements and include more rural areas and 2,000 public phones (instead of the required 165) to allow access to telephone for those who could not afford to buy a handset.

The investment plan – and the proposed extension

MTN's original investment plan was about USD 60 million over five years. This was financed with the company's own funds of USD 32.5 million and USD 27 million with loans. Several international institutions, including Swedfund, agreed to contribute to loans and mezzanine funding.

MTN issued bonds, a financial instrument that contains a written promise by the company to pay the buyer an agreed sum of money at a specific date, via

¹ Aker, Mbiti (2011), *Mobile Phones and Economic Development in Africa*, Center for Global Development, Washington.

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Standard Bank and its local affiliate Stanbic Bank Uganda. Sida's guarantee covered the commercial risk, in case MTN would be unable for liquidity reasons to pay back investors, up to SEK 80 million over five years. For this MTN paid Sida an annual fee, set in relation to the risk of the project, of 3% of the value of the guarantee.

In the end, bonds of an equivalent value to only SEK 60 million were issued. Reason for this was that over time the cost of borrowing from the local capital market without a guarantee became lower than the cost including the guarantee premium charged by Sida, i.e. the guarantee not only fulfilled the intention to utilize local capital, but also to crowded in the local capital market.

How Sida's key principles and conditions apply

Additionality: In this case no commercial actor was able to provide a guarantee and the local issuance of securities at this scale had not been done before.

Market Distortion: Since no other actor would offer the guarantee, it also meant that the operation was non-distortionary i.e. not interfering with market conditions.

Risk-Sharing Partnership: Sida cannot take on the full risk in an investment. In this case Sida assumed the full commercial risk of the nominal principal (i.e. the value of the bond) but not the bond coupon (i.e. the interest rate). Finally, the political risk was not covered by the guarantee or the issuer, thus the buyers of the bond carried that risk, in addition to the credit risk on the coupon.

Sustainability: The guarantee helped to create a market in Uganda for longer-term financial instruments as it provided a 'safety net' while investors and banks could try a new type of funding to a borrower with a strong balance sheet.

Eligibility: Sida contributions must be supported by a country and/or sector strategy. In this case, the build-out of the telecom network was in line with the country strategy to stimulate the private sector in areas that would have great impact on economic activity.

Outcomes and impact

The funding of the network and payback of the bond to investors progressed as planned, and the Sida guarantee served its purpose without being called. Sida's guarantee obligations ended in 2009. MTN doubled its capacity compared to the original plan and mobile phone penetration increased from only 1-2% to approximately 25%. Since then, more telecom operators have entered Uganda.

There has not yet been a study of the specific impact of the Sida guarantee. Several independent studies of ICT do however show some results of the improved infrastructure:

- Mobile phone coverage is associated with a 10% increase in Ugandan farmers' probability of market participation for bananas, although not maize, which suggests that mobile phones are most useful for perishable crops. This effect is greater for farmers located in communities furthest away from district centres.²
- In many villages mobile payphone businesses have been established. These are mostly operated by women, who were previously poor and cash-strapped. A study in Hoima, a rural village 225 kilometres northwest of Kampala, showed that all the women reported not only making substantial contributions to meeting domestic, personal and other expenditures, but also saving and reinvesting the profits in the business. Apart from the direct monetary benefits, it also provided the women operators with a physical and digital address, which had the effect of reducing their social and physical isolation.³
- In other countries the effect of instant access to market information has also meant increased supply of food in markets and reduced waste, when for example fishermen

² ibid

³ Khymouhendo (2010), *The mobile payphone business: a vehicle for rural women's empowerment in Uganda*. In: Africa and ICT development. IDRC.

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have been able to sell their fish where demand is greatest.

- Researchers have found significant impacts of increased mobile penetration on the rate of economic growth for the average developing country (1980–2005). ICT is not necessarily a panacea for development challenges, but it may be part of a package, together with investment in basic infrastructure, reform processes, and skills development in bringing about change.⁴

There has been no impact study in Uganda regarding supporting interventions to the financial markets. Studies elsewhere however show that guarantees contribute to financial deepening by increasing the array of financial instruments available and improving the market's ability to price and settle transactions in a country. An important factor for successful guarantees in the financial sector is that the recipient, or an intermediary, has a long operating experience in the country or globally.⁵

⁴ IEG World Bank (2011), *Capturing Technology for Development*.

⁵ Evaluations of 41 IFC guarantee projects 1996–2008, of which 10 were in the financial sector.
IEG World Bank (2012), *MIGA's Financial Sector Guarantees in a Strategic Context*

Summary

Country:	Uganda
Implementing Partner:	MTN Uganda
Guarantee recipient:	Stanbic Bank Uganda on behalf of bond investors
Direct Beneficiaries:	Uganda buyers of the promissory notes
Indirect Beneficiaries:	Poor and low income people in 24 villages
Value of guarantee:	Agreement of SEK 80 million Stanbic issued bonds to a value of SEK 60 million, with a 100% guarantee on principal. Nothing was paid out under the guarantee.
Amounts called under the guarantee:	Zero – MTN paid back the investors in full
Duration:	2001–2009
