



Ayo Salami

Equity markets hold bugs but no bears

For most equity investors, 2008 was a year to forget and 2009 has begun in the same vein. Sub-Saharan African equity markets delivered some of the worst returns in living memory, but there were also pockets of good news as the region provided the two best performing stock markets in the world: Malawi and Ghana.

The performance of SSA equity markets in 2008 was largely in line with the rest of the world. However, 2008 has to be viewed as an anomaly given the unprecedented nature of the events that unfolded during the course of the year. In a period of uncertainty and extreme volatility, it is understandable that investors become risk-averse and African equity markets and currencies have been caught in the subsequent flight to safety, as emerging market funds sold indiscriminately to meet rising redemptions from their investors. Neither the fundamental performance of economies nor companies was sufficient to act as protection in the ensuing tsunami.

In these volatile times it is difficult to be positive about any investment proposition or to argue that we are at the bottom of the current nosedive. However, reviewing the performance of Africa's equity markets, I see bugs, but no bears.

There is no evidence in Africa of the 'demand destruction' that has now taken hold in Western economies. While they face structural imbalances, manifested in a weak housing market and a freeze in the credit markets, Africa's domestic demand outlook remains robust. The latest IMF forecast projects GDP growth in SSA of 3.25 percent for 2009. In comparison the forecasts are 0.5 percent and -2 percent for global growth and advanced economies respectively. It is increasingly likely that SSA will avoid a recession in 2009.

The negative performance of SSA's equity markets has undermined the idea that the region is not correlated to developed equity markets. However, while returns have been negative, SSA has not been as volatile as other global markets. In 2008, volatility was 18 percent compared to 33 percent and 41 percent in developed markets and emerging markets, respec-

Equity returns to regional markets in US dollars

	Year to Dec 08	2 Mths to 28 Feb 08
Sub-Saharan Africa	-54%	-27%
North Africa	-38%	-11%
South Africa	-46%	-18%
Emerging Markets	-54%	-12%
Frontier Markets	-55%	-24%
Eastern Europe	-70%	-21%
Latin America	-53%	-6%
Asia	-54%	-13%
G7 Countries	-41%	-18%
World Index	-42%	-18%

Equity returns to sub-Saharan Africa by country

	Year to Dec 08	2 Mths to 28 Feb 08	Market capitalisation Feb 08 (US\$ Bn)
Sub-Saharan Africa			
Botswana	-32%	-32%	3.2
Cote D'Ivoire	-16%	-16%	4.5
Ghana	21%	21%	1.9
Kenya	-51%	-51%	6.7
Malawi	24%	24%	1.6
Mauritius	-46%	-46%	2.6
Namibia	-16%	-16%	0.5
Nigeria	-53%	-53%	33.3
Tanzania	4%	4%	0.8
Uganda	-31%	-31%	0.6
Zambia	-45%	-45%	1.8
North Africa			
Egypt	-57%	-57%	64.7
Morocco	-16%	-16%	55.3
Tunisia	-5%	-5%	4.6

Volatility in regional markets

	Year to Dec 08	2 Mths to 28 Feb 08
Sub-Saharan Africa	18%	21%
North Africa	27%	25%
South Africa	43%	38%
Emerging Markets	41%	32%
Frontier Markets	23%	26%
Eastern Europe	64%	58%
Latin America	59%	47%
Asia	42%	34%
G7 Countries	33%	29%
World Index	33%	28%

tively, SSA did not see trendless big swings both ways over short periods of time. The negative returns in SSA can be attributed largely to selling by emerging market funds struggling with redemptions, apparently resulting in undershoot.

The paradox for investors is that the performance of the equity markets does not reflect the strength of the macro-economy or the positive earnings performance of the corporate sector. The earnings numbers seen so far for 2008 indicate EPS growth above 30 percent. Given the institutional reforms that have taken place in SSA, the growing economic power of the emerging middle class and rehabilitation of the infrastructure in the region, the prospects for African equities are better than those of developed markets and SSA equities should, on balance, outperform other regions of the world over the medium term.

For investors, it is necessary to delimitate between a short-term, medium-term and long-term investment outlook for SSA. The short-term outlook is hard to predict as it is being driven by investor sentiment and extreme risk aversion. The longer-term outlook for SSA remains compelling, despite the current pessimism. The challenge for investors is how to bridge these short-term uncertainties and the more encouraging longer-term fundamentals. It is difficult to predict where the bottom lies for the current sell-off, but we can be sure there will be a bottom.

Long-term value investors can take some comfort from the words of Sir John Templeton in 1994: "Bull markets are born on pessimism, grow on scepticism, mature on optimism and die on euphoria. The time of maximum pessimism is the time to buy and the time of maximum optimism is the best time to sell". Encouragingly the financial markets in Sub-Saharan Africa have functioned reasonably well during this period of unprecedented turbulence, which augers well for their likely future recovery.

Dr Ayo Salami is CIO of the Duet Victoire Africa Index.