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The new scramble for Africa

The first scramble for Africa occurred at the end of the 19th century as colonial powers raced to claim dominion over vast tracts of a resource-rich continent. A hundred years later, something of a re-play is occurring, as Caroline Allen reports.

National Geographic magazine, in a headline for a cover feature in 2005, proclaimed: "Africa: whatever you thought before, think again". Just two years on, the global investment management industry is doing just that.

A resource-rich continent of 600 million people that has been largely rejected by investors and asset managers in recent years is right back on their agenda. Michael Power, strategist at Investec investment bank, observes that with Africa's well-known problems, it has simply been easier for investors to make money elsewhere. But with a few enduring exceptions, a region of 54 countries now has "less to hide, and more to celebrate", he says.

The reasons depend on who is investing, why and how. There is no doubt that the inevitable turn in the 30-year commodity cycle has been a galvanising influence, resulting in what has been described as a "giant sucking sound" as China siphons off from the continent all the natural resources it can get to satisfy its rampant economic growth. But there has been real corporate and governance progress as well.

"There is GDP growth evident in 30-40 African markets, less than half of which are exporting commodities, so it is not just a commodity driven boom," notes Hurley Doddy, chief operating officer of Washington-based Emerging Capital Partners (ECP), a private equity group that has raised more than \$1.2 billion for African investments since 2000. So far, it has made 40 investments in 30 countries with 18 realisations via listings or trade sales.

"Africa can see what is happening in Asia, and people accept they can either emulate that or fall further behind. The old ideological battles have been fought and won. Governments want to attract foreign direct investment and grow the private sector," he adds. "There are no more drives to centralisation, there is a recognition that the only way to close the prosperity gap with the rest of the world is to let markets drive growth, bring in capital and allow competition, which means customer care. The most remarkable change has been one of attitude."

ECP's sister company EMP Africa Management took over the West Africa Growth Fund and the Central Africa Growth Fund from Framlington Investment Management last November. ECP's investment goal is to deliver consistently above-market returns to investors that are uncorrelated to the US and other global economies. The firm, initially part of EMP Global before spinning out in 2005, has a stable of six successful funds.

While foreign investors are welcome, they are not alone in the market. This time round, Africa is not depending on foreign interest to drive its nascent economic growth. In fact, notes Dr Ayo Salami of African Business Research, growth is occurring off the back of a thriving domestic investor base.

"Current liquidity pre-dates foreign investor interest. The pension fund industry is being constructed or reconstructed in countries like Nigeria, Kenya and Uganda," he notes. "On top of that, local banks are broadening their product range to draw in savers, and there is a real surge of interest where there are IPOs on local exchanges in the pipeline."

Among foreign investors, there is attention from corporate, commercial and investment banks, to asset managers, private equity and hedge funds, and wealth managers. A key driver for this interest is that, like other emerging markets, Africa has proved largely immune to the fallout from the US sub-prime lending crisis.

"One of the most attractive elements at the moment is the low correlation between African markets and developed markets, although the gap is narrowing," notes Mark Breedon, a global equity fund manager at Investec Asset Management. "It is true many of these markets are not as cheap as they were, but the growth rate is faster than almost anywhere else. And Africa overall is not leveraged, so you don't get the recoil that you do with leveraged bets in developed markets."

Perceptions

"Correlations are low because the foreign investor is not there," adds Breedon. "And the foreign investor is not there because there is a certain perception about Africa, one that is probably very outdated. But there are plenty of local institutions engaged." He points to watermark deals like China's ICBC bank taking a \$6 billion stake in South Africa's Standard Chartered bank, now the biggest injection of capital Africa has ever experienced, and the biggest foreign direct investment out of China. "Some managers say Asian investors seem to see potential where their Western counterparts only see problems," he comments.

The fact is, Africa's macroeconomic backdrop has improved dramatically in the last 10 years. The continent's share of world trade is also picking up, although from a low base. Critically, Africa/China trade is already worth some \$50 billion annually. African governments are beginning to realise that better governance makes economic sense, resulting in higher GDP growth, lower inflation and easing interest rates. Africa, at a rate of 5.8%, has actually outpaced world real GDP growth at 4%, since 2001.

More countries are categorised "at peace" than ever before and various studies point to the rising number with 'functioning democracies'. More markets in Africa and the Middle East made 'at least one positive reform in the last year' than in Latin America or Asia – although that may reflect the opportunity they had to do so.

"The proof of the resilience of Africa's growth story is the impact of the oil price, which has risen four fold in the last six years," comments ABR's Salami. "Two decades ago that would have meant IMF advisors all over the continent handing out structural adjustment programmes. Africa doesn't need them now, the economies are coping well with what is a fairly major shock."

As markets open up, there is strong demand for goods and services, competition among suppliers, pricing power, faster than average profit growth and high return on equity. Sectors that have benefited recently include cement producers, telecom operators and African banks. Also coming up are real estate/infrastructure opportunities, including public/private partnerships, notably in Algeria, South Africa, Angola and Nigeria.

Renaissance Group comprises a number of investment banking, asset management, merchant banking and consumer finance companies, specialising in high-opportunity emerging markets. It began operations in Sub-Saharan Africa last year, branching out from offices in Lagos, in Nigeria and Nairobi, in Kenya.

The group has invested \$500 million in Africa, including a share in ETI, a leading West African banking franchise operating in 16 countries. It also led the \$300 million equity offering by Nigeria's United Bank for Africa in April, and the \$300 million equity offering by Nigeria's Access Bank in July 2007.

"An amazing economic transformation is underway in Sub-Saharan Africa, unlike anything the investor community has seen in the region's 40-year post-colonial history," Renaissance chief executive Stephen Jennings told a two-day investor forum in London. The forum saw some 400 delegates flocking to discussion sessions, as well as one-on-one meetings that followed.

African markets are generally locally owned but growing, from minnows like Swaziland, Namibia and Tanzania, to bigger fish like South Africa, Morocco, Egypt and Mauritius. In Sub-Saharan Africa, there are now 16 fully operational bourses with a combined market capitalisation of \$100 billion. There have been plans for years to create regional stock exchanges, but these are being revived, notably in East Africa among the Nairobi, Dar es Salaam and Uganda exchanges.

The three bourses aim to use a single Depository System Corporation and an Automated Trading System (from Millennium Information Technologies of Colombo, Sri Lanka) linked to the electronic Central Depository System launched in 2005.

Among the sectors attracting attention are telecoms, financials and mining. "Telecoms reform has touched virtually every country, having a tremendous impact on business and on each society," says Thomas R Gibian, chief executive of Emerging Capital Partners. "In 2000 there were only fixed line telecoms companies but now next generation licences are being sold and the growth potential is fantastic. In 2000 there was just 2% penetration of phone lines on the continent, and it is still less than 20%."

Many countries – Nigeria, Egypt and Kenya among them - have tightened up capital requirements for banks, slimming their sectors from dozens of players to far fewer, but

more competitive firms. Many have been surprised at the rapid up-take of services among populations who want to save, invest and profit. In Kenya, Standard Bank recently found demand for mortgage products six or seven times higher than they had anticipated.

"Nigeria took some tough decisions," notes ECP's Gibian. "It cut 80-90 banks down to 25, but they now have a market capitalisation of \$1 billion-plus, and are becoming increasingly international."

Mining has always been a critical industry for the continent, which has about 30% of the planet's mineral reserves, but still produces less than 7% of the world's major metals. In a recent deal with Truffle Capital, ECP jointly acquired 100% of Compagnie Minière de Touissit (CMT). The \$53 million investment represents ECP's third in the mining sector, following positions in Anvil Mining (Democratic Republic of Congo) and Mineral Deposits Limited (Senegal).

As domestic markets have developed, support services are evolving alongside them. Sectech was established in 1998 in the UK but now provides custody, settlement, corporate actions, SWIFT and other electronic messaging systems to financial services firms across Africa.

The principals, Khalid Muktar, Anurag Gupta and Govind Gupta, have all had years of experience in major Western firms before setting up and designing the Custody 2000 system that is used by Barclays Bank in Botswana, Egypt, Ghana, Kenya, Mauritius, Uganda, Zambia and Zimbabwe. Other clients include Nigeria's Diamond pension fund, the UBA pension fund and UBA Global investor services.

In Nigeria, where Stanbic and Barclays Bank have been rivals in the sub-custody business for years, First Bank of Nigeria has emerged as a real contender, leveraging its local branch network and its relationships with local pension institutions.

Investors unfamiliar with the continent still find it difficult to put together portfolios without the information flows they are used to. That is why ABR's Salami, in conjunction with London-based Duet Asset Management, has just launched an Africa index fund, aimed at giving institutional investors the low-cost exposure to the markets they want.

There are maybe 10,000 publicly listed companies in Africa but only 20% of those are truly investible, and especially in smaller markets, there is a negative correlation between the visibility of a stock and alpha returns. The index constructed by Salami has been back-tested to 1999, when just three companies were eligible to participate in it. Now there are 68.

Many of the investment players engaged in Africa are actively working alongside public and private sector influencers to create and develop local financial institutions and infrastructure. The bond market, particularly, has lagged behind.

A research note from Ashmore, an emerging market debt specialist, believes a serious impediment to Africa's private sector development is the lack of medium term corporate lending. Few banks lend beyond 90 days, except to governments, because the banks

themselves have no access to term finance. That in turn denies financing to the non-bank corporate sector, and depresses growth potential.

"The lack of a corporate bond market also makes it impossible to trade interest rates, and hence renders monetary policy largely ineffective," notes Ashmore's Jan Dehn. "Clearly, the development of term finance, especially for African banks, would not only stimulate the supply-side and boost growth, but also aid central banks in controlling inflation."

Sub-Saharan Africa is inevitably dominated by South Africa, but local fund managers freely admit that it is likely to be overtaken within 10 years by Nigeria – Africa's answer to China, India or Brazil – and perhaps even by the North Africa region, which is being strongly supported by European and Middle Eastern investors.

North Africa

The charge into North Africa is being led by French banks, exploiting their historic and linguistic connections there. The main players are BNP Paribas, Société Générale and Crédit Agricole, targeting acquisitions in Algeria, Libya, Tunisia and Egypt. The area's banking system is prospering with robust demand from a young population and from foreign investors seeking strategic diversification from their home markets.

Powerful Middle East names are already bidding for second tier banks. Bahrain's Arab Banking Corp, Jordan's Arab Bank and Morocco's Attijariwafa Bank are all chasing Libya's Al-Wahda. In Egypt, JP Morgan has been brought in to sell off an 80% stake in Banque du Caire.

The Anglophone response is evident in the strategic plans of banks like HSBC and Standard Chartered, both long-time players on the continent. The entry point to these markets may be through brand-rich commercial banks, but the asset, wealth and real estate units are not far behind.

Some states are retaining elements of control as their banking sectors open up, notably in Algeria, where the government, advised by Rothschild, is holding a beauty parade for the imminent privatisation of Crédit Populaire d'Algerie. One of the heavyweight contenders is Citigroup. BNP Paribas meanwhile has won control of Libya's Sahara bank, when it paid the government €145 million for a 19% stake, fighting off SocGen for the prize.

Risks remain in engaging with truly emerging markets such as those across Africa. But global investors are indicating they are interested in the challenge, supported by a political dynamic that wants to draw the continent into the global financial system, and a far firmer economic base than has been the case for some time.