# INTO AFRICA

A publication from Capital Markets in Africa

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# DELIVERING VALUE
## VIA AFRICAN CAPITAL MARKETS

**PAN-AFRICAN CAPITAL MARKET INVESTMENTS: GEOPOLITICAL, LEGAL AND OTHER ASPECTS**

**ATTRACTING FOREIGN INVESTMENT INTO AFRICA'S CAPITAL MARKETS**

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Welcome to the August edition of INTO AFRICA, the publication with fresh insight into Africa's emerging markets. This month edition focuses on Capital Markets in Africa and titled: ***Delivering Value via African Capital Markets.***

Capital market is one of the key components of the engine of a modern economy, as it mobilises and pools savings from the public and efficiently channels them into business investments. It also helps firms and individuals to manage risks and provides incentives for companies to improve their performance. Capital markets complement other sectors of the financial system, such as banks and insurance firms; thus expanding the range of funding sources available (such as public equity markets, private equity, and the issuance of debt securities) and creating alternative investible assets for investors.

As African economies and populations continue to grow, it is expected that the continent's demand for infrastructure and consumer goods will generate increasing financing requirements, and that the capital markets will provide a proportion of that funding, allowing investors to participate in the growth prospects.

We start with a discourse from **STUART MATTY** (Partner, White & Case LLP, London), **MICHAL AMIR** (Associate, White & Case LLP, London) and **PAUL GALLUP** (Associate, White & Case LLP, London). They explore the emerging trends, developments, challenges and opportunities as well as provide an overview and the structure of capital markets in Africa in *"Pan-African Capital Markets Investments: Geopolitical, Legal and Other Aspects"*.

**SUDIP CHATTERJEE** (Head of Global Capital Markets, Euroclear) in *"Attracting Foreign Investments into Africa's Capital Markets"* offers insight into how would capital markets development affect the African social climate and the need to strengthen and harmonise regulatory and legal framework to international standards. While **SHAYNE KRIGE** (Director, Werksmans Attorneys, South Africa) provides answers to the question as to how to best structure investment funds in Africa as well as enumerates some criteria to consider in *"Structuring African Investment Funds: Some considerations"*.

**PHILIP BUYSKES** (Chief Executive Officer, Frontclear) and **MARIA-PAI KELLY** (Corporate Communications Officer, Cardano Development) give insight into money markets and opine that the stability and depth of money markets are key for economic growth and poverty alleviation in Africa in *"Clearing the Path to Liquid African Money Markets"*. In similar vein, in *"The risk of trading in Africa: Will the Forex Market Code of Conduct Help?"*, **IAN BESSARABIA** (Market Development Lead, Foreign Exchange & Fixed Income, Africa, Thomson Reuters) looks at the trading risk with emphasis on Forex trading risk in Africa. Whereas, **WILDU DU PIESSIS** (Head of Africa and Partner, Baker McKenzie) provides a review of cross-border IPO in Africa with a global perspective in *"Capitalism: Meeting the Genuine Development Needs of African"*.

**CATIANA GARCIA-KILROY** (Lead Financial Sector Specialist, World Bank), **CAROLINE CERRUTI** (Senior Financial Sector Specialist, World Bank) and **SWEE EE ANG** (Senior Financial Sector Specialist, World Bank) explore options of financing African infrastructure deficits via the capital markets with Kenya as a case study in *"Financing Infrastructure in Africa via Capital Markets: Addressing the Myths and Creating Viable Markets"*.

In the ***Exclusive Interview*** segment, **MARK MOBIUS** (Executive Chairman, Templeton Emerging Markets Group), **ANDY GBOKA** (Co-Portfolio Manager, BB African Opportunities (LUX) Fund) and **ALAIN NKONTCHOU** (Co-Founder and Managing Director, ENKO Capital) conclude that now is a good time to take a risk on African capital markets. While **JAMES DOREE** (Managing Director at Lion's Head Global Partners) speaks about how to tap into opportunities in African local currency bond markets.

**WIKUS FURSTENBERG** (Portfolio manager, Futuregrowth Asset Management) and **OLGA CONSTANTATOS** (Credit & Equity Process Manager, Futuregrowth Asset Management) pose a philosophical question or discourse in *"When lower economic growth becomes Bond Bearish"*. **ALASTAIR CAMPBELL** (Managing Director, Vantage Capital Fund, South Africa) discuss the use of inflation linked structures in South Africa and **NANCY MURULE** (Research Analyst, Cytonn Investments Management Limited) enumerates some of the challenges and opportunities in Kenyan Real Estate Markets.

Also, we bring you selected special features from **ANNE KEPPLER** (Vice President, DEGs Private Equity team), **NICOL MULLINS** (Principal Consultant, Mercer, South Africa), **TANYA KNOWLES** (Managing Executive, Fractal Solutions South Africa) and **JOLETTE ROODT** (Writer/Analyst, Entersekt, South Africa) on a range of topic from small medium-enterprises (SMEs), human capital in Africa, emergence of Africa's Fintech sector and protecting against cyber risk in African Banking sectors.

On final note, **DEVIN FORBES** (Investment Analyst, Citadel Asset Management, South Africa) in *"Hedge Funds: Unveiling the Mystery"* provides an introduction to Hedge Funds and explains the fundamentals as well as some strategies commonly employed.

*Tunde Akodu*
**Editor**

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# PAN-AFRICAN CAPITAL MARKET INVESTMENTS: GEOPOLITICAL, LEGAL AND OTHER ASPECTS

By **Stuart Matty,** Partner, White & Case LLP, London
**Michal Amir,** Associate, White & Case LLP, London
**Paul Gallup,** Associate, White & Case LLP, London

## Economic Growth and a Burgeoning Bond Market

Over the past decade, the African continent and the economies of Sub-Saharan Africa, in particular, have experienced significant growth, spurred by (and, in turn, attracting) large sums of foreign direct investment. Although the impact in recent years of lower oil prices and reduced worldwide demand for commodities has dampened growth in a number of African countries whose economies rely on them, many countries in Africa have nevertheless achieved relative political and macro-economic stability, with strong prospects for sustained growth. As African economies and populations continue to grow, it is expected that the continent's demand for infrastructure and consumer goods will generate increasing financing requirements, and that the capital markets will provide a proportion of that funding, allowing investors to participate in the growth prospects in such countries.

While traditional sources of funding are expected to meet some of this demand, the rising economic growth has created a push for new financing alternatives across a broad range of geographies and industries, prompting sovereign and corporate issuers throughout Africa to turn increasingly to investor-led funding solutions, whether from traditional capital markets or alternative capital providers. As demand increases, this trend is likely to continue as more traditional lenders will struggle to keep up with the demand as they adjust to new capital retention requirements and tighter regulation at home and abroad. Over twenty sovereign issuers across the continent now have ratings from established credit agencies, giving corporate entities in previously untapped markets increased access to international investors with the sovereigns having established a ceiling for ratings in those countries. Put into context, African credits continue to represent a very small percentage of the overall debt exposure in emerging markets, and so many recent bond issuances by African sovereigns and corporate entities have been heavily oversubscribed, indicating strong investor appetite for higher yielding securities from a relatively untapped region.

While Africa offers significant potential for international investors looking to enhance their portfolios, investing in frontier markets such as Africa is inherently riskier than investing in more mature markets, and understanding the geopolitical, economic, legal and regulatory risks in investing in these markets, and the various structuring options available, is therefore key.

## Geopolitical and Economic Considerations

When making investment decisions and structuring transactions, investors must bear in mind that many countries have only relatively recently begun to experience economic and political stability. In addition, allegations of corruption and a lack of transparency are widespread, and many of the continent's legal systems and the rule of law are less developed and more subject to potential abuse than in more developed jurisdictions. Often mired in bureaucratic red tape, Africa's economies are, to varying degrees, characterised by growth that is heavily influenced by commodity prices, significant inflation, weak fiscal and monetary policies, low foreign currency reserves, high external debts and volatile currencies. Investors must also recognise that each country presents its own unique challenges as well as opportunities and that a highly tailored approach should be taken to considering each investment and structuring each transaction.

Given the range in levels of geopolitical and economic development across Africa, access to international capital markets remains higher in some regions than others. Generally, capital markets in Africa have developed along the lines of other emerging regions. Sovereign or sovereign-linked entities were the first to access capital markets, followed by financial institutions with established credit profiles. Today, a diverse range of corporate issuers has successfully raised capital through international debt issuances.

Despite the recent volatility in oil prices and the end of the "commodities super-cycle", African issuers present opportunities for a diverse group of capital markets investors less likely than traditional lenders to be put off by macro-economic uncertainties. As African economies seek to diversify away from extractive industries, issuers across other sectors and in other jurisdictions are taking advantage of the interest shown in the bond markets in Africa. While all sectors seem positioned for varying levels of capital markets growth, the financial, natural resources and communications sectors have, in particular, demonstrated the potential to lead the expansion in the corporate space.

South Africa has historically dominated international bond issuances among African countries. It boasts a broad investor base with a large number of high-quality established issuers. Outside of South Africa, Nigeria leads the African bond issuance market, with a number of banks having raised in excess of US$3 billion through capital markets debt issuances in recent years. In 2014, telecoms operator Helios Towers' Nigerian subsidiary became the first corporate in the country outside of the oil and banking sectors to issue a bond, which was offered on the standard listing segment of the London Stock Exchange.

A number of Sub-Saharan African sovereigns, including Angola, Cote d'Ivoire, Ethiopia, Gabon, Ghana, Kenya, Namibia, Nigeria, Rwanda, Senegal and Zambia have also accessed international capital markets in recent years, in some instances on multiple occasions, collectively raising over US$10 billion in the international capital markets in the past five years. Ghana's 2015 bond issuance benefited from a partial guarantee provided by the World Bank's International Development Association, demonstrating the potential credit enhancement that support from multi-lateral development banks can provide African issuers.

Several countries in Africa also have growing domestic bond markets, with instruments denominated in local currencies. While South Africa's market for Rand-denominated debt is by far the continent's largest, Nigeria and Ghana also have growing debt markets in their respective currencies. Although these markets may become attractive to African issuers should the U.S. dollar continue to strengthen, local currency bonds present certain challenges to international investors, including illiquidity within local markets and greater exposure to fluctuations in the local currency. International investors must also be wary of local tax and exchange control regulations that could impact their investments. One option to monetise such local assets is to look to repackage them into instruments that trade and settle in the international markets. For example, in 2014, Nigeria issued Global Depositary Notes, an alternative product offering investors the option of buying into the local Naira-denominated bond market while still collecting U.S. dollar-denominated interest payments. This was the first such structure utilised in Africa, although there is no reason why investors wary of a direct holding in a locally traded instrument could not look to replicate this in other markets.

*"As African economies seek to diversify away from extractive-industries, issuers across other sectors and in other jurisdictions are taking advantage of the interest shown in the bond markets in Africa."*

### Legal, Tax and Regulatory Considerations

As with most emerging markets transactions where assets are primarily located within the issuing country, investors must consider closely the choice of venue for dispute resolution and related concerns over the enforceability of judgments and the attachment of assets. Certain countries in Africa do not have treaties providing for the reciprocal recognition and enforcement of judgments of courts with the United States, England and many other countries. As a result, recognition and enforcement in these countries of judgments of foreign courts may be difficult. In such circumstances, investors should consider whether arbitration in an internationally recognised court would be preferable to submission to the courts of a particular jurisdiction. Additionally, the legal systems in the various African jurisdictions continue to undergo development and face a number of challenges including delays in the judicial process. Once a judgement or award has been granted, its enforcement is often hampered by inefficiencies in the relevant judicial system and can result in uncertain legal positions. Investors must take into account the potential for delays in obtaining judgments or awards and enforcing them, in particular where enforcing against underlying collateral.

When structuring African investments, consideration should also be given to exchange and capital controls and local tax (withholding or otherwise) regulations that could limit profitability for foreign investors. While African jurisdictions have generally begun to take a more liberal approach to foreign exchange and capital import regulatory oversight, government and monetary authorities may nevertheless impose exchange and capital controls (as Nigeria did in 2016 amid an economic downturn) that could render investing in certain jurisdictions less desirable and/or adversely affect existing investments (due, for example, to a shortage of U.S. dollar liquidity in the local market).

Emerging markets can also be affected by higher levels of corruption by government officials and misuse of public funds than more mature markets. Failure adequately to address actual and perceived risks of corruption adversely affects the investment environment in such countries and their ability to attract foreign direct investment. According to Transparency International's 2016 Corruption Perception Index, the overall majority of African countries (with the exception of Botswana and Cape Verde) scored lower than 55 out of 100 on the scale (where 100 means "very clean" and 0 means "highly corrupt"), with many countries scoring lower than 30. Similarly, African countries rank low in the World Bank's 2016 Doing Business report, with the majority of countries ranking below the 140th place (out of a total of 190 countries).

While many African issuers may not directly fall within the scope or jurisdiction of either the U.S. Foreign Corrupt Practices Act or the U.K. Bribery Act 2010, entities that transact with them often will be, and, in many cases, investors want to be certain that their business partners and the entities in which they invest will uphold a similar standard, effectively meaning that these laws and regulations have created a regime that has arguably become international best practice. With anti-money laundering, anti-bribery and corruption and international economic sanctions becoming increasingly relevant when making sound investment decisions, careful consideration needs to be taken when looking at particular investments. Investors seeking access to African capital markets should look for issuers that have demonstrably implemented suitable internal anti-money laundering and anti-corruption controls, monitored using appropriate technologies and systems. African issuers have been working to promote investor interest in debt offerings by conducting focused and tailored internal due diligence, vetted by underwriters and legal advisers, and providing greater-than-required voluntary disclosure. In addition, investors should focus on intended uses of proceeds, to ensure they are appropriate.

To date, while investors have not gone so far as to require ongoing testing and compliance as regards the use of proceeds (as would be expected of traditional lenders), there has been in certain instances, including Angola's and Rwanda's debut offerings, a push for greater analysis of and heightened due diligence on the specific projects to be financed. One need not look much further afield to observe what can happen when these do not tie up, as was seen in the case of Mozambique's so-called "tuna bonds". This example underscores the importance of "asking the right questions" when conducting due diligence. The bonds, which were defaulted on in 2017, coupled with the later disclosure of more than US$1 billion of undisclosed debt linked to state-affiliated companies, led to the ongoing restructuring of Mozambique's international debt, the decision by the International Monetary Fund and other donors to suspend aid programmes to the country and international regulatory scrutiny of the transaction.

## Looking Forward

The developing nature of capital markets across Africa affords issuers a degree of flexibility in structuring bond instruments, and investors must fully assess the accompanying geopolitical, economic, legal and regulatory risks involved. Although capital markets issuances across emerging regions have been particularly impacted by external and internal factors in recent years, in line with the historical cyclicality of international capital markets, signs for future growth in this segment look favourable. Continued openness to international investment, more robust governance and the successful combat of corruption combined with the introduction of innovative, versatile and attractive investment products will be an important component for African nations' growth and resilience.

*"As African economies and populations continue to grow, it is expected that the continent's demand for infrastructure and consumer goods will generate increasing financing requirements, and that the capital markets will provide a proportion of that funding, allowing investors to participate in the growth prospects in such countries."*

## Contributors' Profiles

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Stuart is recognized as a leading capital markets practitioner in numerous guides to the profession. He is ranked Band 1 by Chambers UK 2016 and is listed as a Leading Individual in Legal 500 UK (2015) for Debt Capital Markets

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**Paul Gallup**, Associate, Capital Markets, White & Case LLP (London). Paul Gallup is an Associate in the Firm's Capital Markets Group in London. He has experience representing sovereign, public and private issuers and underwriters in a range of debt and equity capital markets transactions, with a primary focus on emerging and developing markets. Paul previously worked with another leading American law firm out of its São Paulo, Brazil and Paris, France offices, where his focus ranged from capital markets (debt and equity) to mergers & acquisitions transactions.

# ATTRACTING FOREIGN INVESTMENT INTO AFRICA'S CAPITAL MARKETS

By **Sudip Chatterjee,** Head of Global Capital Markets, Euroclear

Africa is a continent of contrasts. Different parts of Africa are making rapid advancements, using mobile technology to leapfrog the rest of the world. Innovations driving African markets forward are M-Pesa which allows mobile-based payments; M-Akiba which allows bidding for government bonds similarly and mHealth which provides basic health information on mobile phones.

Africa is a vast continent with substantial natural resources, however it continues to struggle with inadequate infrastructure, healthcare and has recurrent social disruption, poverty and corruption. These social challenges have stalled the industrial development for decades. Growth in sub-Saharan Africa is currently less than 1.5% per annum. So what then can the African community do to overcome its social and economic challenges?

### Pull vs. Push

The recent G20 summit in June, attended by the African leaders of seven countries, agreed that there was a need to additionally invest more than $45 billion in infrastructure development in Africa. At present, Africa does not have this amount of capital for investing, and if African leaders want to raise this money domestically, this would come at the price of reducing the social standards of the people as a result of higher taxes and duties.

This investment will only be possible when international investors can channel their capital into the continent. Today, this is not happening due to a lack of development of the capital markets within some of the African countries. This needs to change. So how would capital markets development affect the African social climate?

To put this into context, India in the early 1990s had roughly the same population as Africa. At that time, the Indian government decided to boost an untapped segment of the market – software development. They introduced the concept of software technology parks (STP). Regulations for setting-up software companies in these parks were eased and tax-exemptions were granted if a certain part of their business was export oriented. Soon, companies opened offices in these parks and started receiving overseas contracts.

However, these companies needed the software engineers to execute the contracts. Software education was limited and the good software engineers had to be hired from all across the country. When they arrived, they needed basic amenities like accommodation, food, healthcare and schooling for themselves and their families. This demand created a complete social ecosystem with new apartments, restaurants, hospital and schools centred around the STPs - creating various types of jobs. The diversity of the jobs and work force ensured there was work for women and men, for the skilled and the unskilled and for the young and the old alike. This created a certain purchasing power, resulting in a fast growing middle class – which is currently 20% of the Indian population and estimated to double in the next 10 years.

Creating healthy capital markets in parts of Africa could generate the same virtuous cycle as the STPs did in India. The improved capital markets would provide direct jobs for the young professionals, which would result in a pull effect to create a social ecosystem that would provide various ancillary jobs in information technology, healthcare, education and real estate. In addition, small and medium enterprises (SMEs) borrowing from the capital market would create their own opportunity, generating further jobs and social development. This new ecosystem could therefore break the vicious cycle of social infrastructure underdevelopment and low growth potential and lead to a virtuous cycle of growth-propelled social development and inclusion.

### Building an effective capital market

International investors will invest in capital markets only when the market is easy to access, safe to invest and attractive. To achieve this, there are essentially two steps that need to be taken:

- creating the right conditions
- creating a connection with international investors

### Creating the right conditions

International investors look for an efficient capital market structure backed by a robust and reliable legal and regulatory framework – in other words, exchanges, central counterparties (CCPs) and central securities depositary (CSD) to ensure transparency, settlement finality and asset protection. Additionally, they need to have a range of securities financing options like repos, swaps, securities lending and borrowing, in order to ensure liquidity in the market.

To achieve this, market authorities need to transform their markets by adopting a legal and regulatory framework that effectively combines the best practices in the international markets with the local market realities.

### Examples of market successes

In 2008-09, Russia's GDP contracted by 8% on the collapse of oil prices, prompting capital outflows and rising bond yields. The market saw various protests by people fearing job losses or lowering of wages. International investors formed just 3% of the Russian capital market.

Over the next four years, the authorities merged the two exchanges, created a single CSD, changed the pension fund regulations, introduced the nominee concept in law and introduced T+2 settlement. They also changed the rules to allow OFZ's (Russian government bond) to be traded off-exchange, exempted foreign investors from taxes on OFZ and allowed International CSDs (e.g. Euroclear) to link to the market to represent foreign investors.

Foreign holdings of OFZ climbed from 3% of the market to 25% within three months of these changes. Liquidity increased by 200% and yields fell by 150 basis points, allowing the sovereign to save on the borrowing cost and pass on the benefits to the people.

In another example, Chile faced challenges around market liquidity while international investor participation in their government bonds was approximately 5%. The Chilean authorities moved to a record based tax system in 2016 and paved the way for omnibus accounts, an important step in facilitating foreign access. These changes resulted in an international investor participation of 20% in the first Euroclearable issuance in 2017. J.P. Morgan raised Chile's weighting in its Emerging Markets Bond Index from 0.1% to 1.34% resulting in a greater foreign investor participation in existing Chilean bonds.

### Establishing the connection

In order to maintain maximum liquidity with their investments and utilise them for collateral management, international investors prefer to have a single global account in a financial market infrastructure (FMI) like Euroclear, to access the securities in different markets through that single account. This is why Euroclear has established links in 44 markets around the world and international investors hold $30 trillion of their investments through their accounts in Euroclear.

Creating a link between an FMI and a local capital market acts like a highway that connects international investors to the local market investors and issuers. If the local market has created the right conditions, the international investors would use this highway to invest in that local capital market, thus bringing substantial macroeconomic benefits for these markets. Creating the right conditions and establishing the connection to international investors could create a robust capital market for African countries, which, as discussed earlier, could start the virtuous cycle of growth-propelled social development and inclusion.

### A pan-African marketplace?

Unfortunately not all countries within Africa have the level of resources or adequate size of capital market to undergo such a transformation. So how can they therefore attract foreign investment to start the above mentioned virtuous cycle?

Countries that cannot directly connect their local capital market to international investors have the option to connect to another African country that has established such connection, in order to indirectly access the international investors and get the necessary capital. If we extend the analogy to the entire continent, this would result in a pan-African marketplace, where all the countries are connected in one big capital market.

Europe has tried to achieve similar results through centralisation with Target 2, which has proven to be a lengthy process involving negotiations and harmonization. However, in Africa, a less decentralized approach to achieve the same results could work, since parts of Africa have already leap-frogged Europe in the use of technology.

If the continent's markets were to take advantage of digital advances, such as distributed ledger or other financial technology initiatives, to design a uniform capital market architecture, they could achieve a degree of seamless integration between markets even without a centralised marketplace. Though countries would still keep their sovereignty and apply their own regulations to local transactions, the uniform architecture would facilitate cross-border transactions necessary to access foreign investors - a vision of the future that is promising and worth exploring.

*"African market authorities need to transform their markets by adopting a legal and regulatory framework that effectively combines the best practices in the international markets with the local market realities"*

**Contributor's Profile**

Sudip Chatterjee is Head of Global Capital Markets business at Euroclear. Mr. Chatterjee is responsible for defining and designing the vision and strategy, along with aligning all business initiatives across the global capital markets business line of Euroclear. In this capacity, Mr. Chatterjee leads the discussions with market authorities and regulators in local and international markets across the world, with the objective of implementing solutions that help market liquidity resulting in a stronger macroeconomic climate.

Prior to his current role, Mr Chatterjee held a number of senior positions within Euroclear, including Product development, Network Management and Change Management. Prior to joining Euroclear, Mr. Chatterjee was a management consultant, advising various organisations, such as Bank of America, Axa and Eurocontrol.

Mr. Chatterjee has a bachelor degree in Civil Engineering and a post-graduation in Management from India.

# THE RISK OF TRADING IN AFRICA: WILL THE FOREX MARKET CODE OF CONDUCT HELP?

By **Ian Bessarabia,** Market Development Lead - Foreign Exchange & Fixed Income, Africa, Thomson Reuters.

In the world of investments and forex trading, timing is everything. It can be the difference between making a profit or a loss. However, do you trust the counterparty you are dealing with?

Africa is an increasingly popular investment destination for foreigners, with interest in infrastructure development, energy generation and innovation.

However, it helps to be well informed before diving head-first into markets that are not well known or understood.

The World Bank Ease of Doing Business Index measures the complexity in each country's regulatory environment based on many key parameters. In the 2017 report, which ranks 190 countries, the first sub-Saharan African country on the list was Mauritius at 49, followed by Rwanda at 56. Only eight countries in SSA made the top 100. Highlighted indicators identified are weak economic policies and regulation.

Foreign companies that act responsibly by pursuing domestic economic participation, long-term and sustainable development strategies that should contribute to the respective country's economy have a better chance of succeeding.

What is encouraging is witnessing how economic policies and government regulations are undergoing significant reforms to improve market access. For the countries, there is an obvious upside – they need foreign skills, relationships and capital to build infrastructure and modernise and diversify their economies.

So, what does the global forex market code of conduct have to do with foreign investment in and across Africa?
To understand the full picture let's go back a few years.

In the wake of scandals concerning the wholesale FX market between 2013 and 2014, the Bank of International Settlements (BIS) set up the Foreign Exchange Working Group (FXWG).

Clamping down on misconduct may have been partially successful, through the issuance of multi-billion-dollar fines, and remediation processes handed out by regulators. However, this failed to restore trust in what is estimated to be a $5.1 trillion daily trading market.

The FXWG was set up with the mandate to establish a single set of global principles of good practice for foreign exchange markets.

A unique differentiator of the code is its global nature, and its aim to be adopted consistently and in its entirety, unlike other forms of regulation which have been open to interpretation and implementation by local regulators.
The group's membership covers major financial centres in both advanced and emerging market economies.

Its focus was to create a single set of standards and principles for jurisdictions globally, and to enhance principles-based approaches to best practice.

Putting the code together was by no means easy, with the need to cover the wholesale foreign exchange market and a broad range of market participants and infrastructures, with appropriate consideration to local circumstances.

After two years of work by central bankers and market participants, the BIS issued the code at the end of May.

The code consists of principles rather than rules to minimise loopholes.

The code contains 55 principles covering six categories:
- Ethics
- Governance
- Execution
- Information sharing
- Risk management and compliance
- Confirmation and settlement processes

Africa faces the challenge of fragmented financial market trading, coupled with greater regulatory oversight and the need for operational efficiency. The focus on confirmation and settlement processes in the code will go a long way to building investor confidence and reducing risk

At a minimum, Market Participants will be expected to have sufficient technical and operational capability to support end-to-end FX processing in both normal and peak market conditions without undue impact on the processing timeline.

This will put a clear focus back on the need for enhanced automation and straight-through processing.

Workflow solutions will need to be adopted to help improve clients' efficiency in order to meet the above expectations. Transactions will need to be automatically captured, tracked and reported to Central Banks in the respective jurisdictions. The ability to monitor transactions in their domestic FX markets in real-time will provide them with faster, more actionable insight in the markets they oversee.

Effective risk management starts with the identification and understanding by Market Participants of the various types of risks to which they are exposed and typically involves the establishment of risk limits and monitoring mechanisms, as well as the adoption of risk-mitigating and other prudent practices. An effective risk management framework could comprise of an appropriate and well-documented approval process for the setting of risk limits. Not many financial institutions across Africa have robust risk management processes in place.

Across Africa, companies and banks alike are focusing on the adoption of a good risk appetite framework, grounded in the particular issues an organization and industry are facing. The forex market code is a good springboard to start, but making the risk appetite come to life is a much bigger challenge. Organizations need the right people, resources, and solutions in place to ensure that their risk appetite program doesn't get derailed by the process of delivering risk analysis.

In a time when we are faced with too little or too much risk data, manual processes can put the focus on processing the risk information rather than adding value through analysis and management. Technology solutions have a key role to play in ensuring valuable insights are provided about an organisation's risk profile. Implementation of the risk appetite should be focused on delivering the right intelligence to the right people - business line leaders, senior management, and the Board. It is with this information that a true risk culture can be created.

Of course, adherence is the key aim of the new code and in order for it to be as broadly applicable as possible. By demonstrating their own adherence to the code participants have the opportunity to raise awareness about, and increase the profile of the code, and can provide other market participants with an accessible means for comparing potential counterparties and service providers.

Market players who do not support or adopt the code run the risk of commercial pressure from central banks and corporate clients to adhere to the code. Clients could refuse to face counterparties that have not adhered to the code.

There is also the possibility that some clients could say they don't want to see prices from liquidity providers that have not adhered.

Since the code has received endorsements from central banks, which have oversight over bank dealers, it's hard to see how they could ignore the code.

Central banks, when acting as counterparties, will in all likelihood require their trading counterparties to adhere to the code. When there is endorsement from central banks, it will be hard for market participants they have oversight over to ignore the code. The benefit for Africa would be to have more central banks endorse the code. The South Africa - Financial Markets Liaison Group's Foreign Exchange Sub-committee is the only representative from Africa on the Global Foreign Exchange Committee. [1]

Adherence to the code entails more than just sending out a statement. Market participants in the wholesale FX market will need to align their business activities with the principles of the code and be able to demonstrate this.

It is more likely that the consequences will result in greater transparency for liquidity, the smooth functioning of the currency markets and the eventual price of transactions. This bodes well for markets in Africa to align the adoption of the code, with the ongoing domestic reforms which will increase the trust factor investors are seeking.

The code should promote a robust, fair, liquid, open and transparent market, which will alleviate the challenges many African investors experience today, where hard currency is difficult to come by and the market is limited to a few players.

The publication of the Code is a seminal moment in the long history of the foreign exchange industry. The architects of the Global Code have done an exemplary job of drawing input from a wide range of institutions across buy and sell-side institutions and market infrastructure providers. Thomson Reuters publicly supports the code and we will continue to uphold fair and efficient markets. We will be promoting it, and encouraging customers to sign up to ensure widespread market adoption. Our FX Trading platform already has key capabilities that will facilitate and encourage our customers' adherence to the Code.

For the first time, a single set of principles will give market participants around the world a clear and powerful blueprint for sound market practice. No more conflicting rules in different regions, and no more excuses for failing to enforce good conduct.

Doing business across national borders involves many complexities but the peculiarities of each market differ. Africa remains one of the most exciting emerging markets in the world. However, the business environment still presents challenges to trade and foreign direct investment. Over the coming months it will be interesting to see which markets adopt the global forex market code of conduct and what the impact is.

The code, however, will only succeed if all participants take a much more proactive approach to conduct, as both buy-side and sell-side participants play their part.

**Contributor's Profile**

Ian Bessarabia is the Market Development Lead for Foreign Exchange & Fixed Income at Thomson Reuters – a position he acquired in August 2016.

Ian has spent the past 10 years working closely with financial market players, central banks and regional bodies in sub-Sahara Africa, supporting these organisations to improve their business processes. Prior to joining Thomson Reuters, Ian was the Business Development Manager at SWIFT.

Ian has held senior positions in various industry initiatives, including holding the position of chairperson of SUSA (SWIFT Users of South Africa), as well as the South African representative on the Maintenance Working group for Trade Initiation and Confirmation messages. Ian has a Bachelor of Commerce in Business Management and Economics from the University of South Africa.

1. Members of the GFXC include central bank-sponsored Foreign Exchange Committees and similar structures in various regions. Each member Foreign Exchange Committee designates a central bank and private sector representative for the GFXC.

# STRUCTURING AFRICAN INVESTMENT FUNDS: SOME CONSIDERATIONS

By **Shayne Krige,** Director, Werksmans Attorneys, South Africa

As African investments become more attractive to investors, the question as to how to best structure these investments is one we are asked frequently.

The range of structuring options and jurisdictions can be overwhelming. Traditional offshore centres like the Cayman Islands and British Virgin Islands remain compelling low tax, low regulation options. Onshore centres like Luxembourg and Ireland have extensive double tax treaty networks and the advantage of being members of the European Union. A number of jurisdictions have attempted to position themselves between these two poles combining elements of both offerings. These include the Channel Islands jurisdictions and, of particular relevance to African investments, Mauritius.

The choice of jurisdiction is resolved principally through the interplay of two factors – the location of the investment management team and the requirements of the investors.

**The Location of the Investment Manager**

Think of an investment fund as a bucket into which investments are poured. The success of a fund business depends less on the type of bucket used than it does on deciding what to put in and what to take out of the bucket. That is the task of the investment manager.

Investment managers have lifestyle demands that dictate the options for locating the investment management business. They have children who need to go to good schools and they want those schools close by. They look for safe environments, decent infrastructure, travel options, access to entertainment and they want to be close to their peers. Naturally, the more skilled managers can afford to be less flexible about comprising on lifestyle.

It is important to understand the possibilities for locating the manager at the outset because in many jurisdictions a fund is taxed in the jurisdiction where investment decisions are taken, i.e. the investment manager will draw the fund into the tax net of the jurisdiction he calls home.

*"Access to treaty networks is one that is frequently cited in the context of African investment funds with the result that Mauritius and South Africa are seen as optimal jurisdictions"*

**The Requirements of the Investors**

It makes little sense establishing a fund in a jurisdiction that none of the target investors can invest into. Many German and French investors cannot invest in Caribbean funds or will not invest in such funds given the likelihood that the investment will attract audits by the tax authorities. Many pension funds and development finance institutions have specific allocations to specific types of funds or funds located in specific regions.

Some investors may not be prohibited from investing in a particular jurisdiction but their experience with that jurisdiction may be limited and the due diligence burden they may have to bear to invest in a fund in an "exotic" jurisdiction may be more than they are willing to bear. American investors are used to investing in Cayman Islands funds and although a Maltese fund may also meet their requirements, it will often be simpler to sell the Cayman solution to them.

It is therefore important, at the outset, to understand the investors' requirements when it comes to choice of jurisdiction and this means identifying likely investors and having a chat with them about their tolerance for particular jurisdictions.

At the same time, the investors' preference and stated requirements should sometimes be questioned. The fact that an investor already holds an investment in a fund located in jurisdiction X or has heard that jurisdiction Y is the most popular does not necessarily mean that this is the best option for them.

Inevitably there will be some tension between the requirements of the investors and the preferences of the management team. These differences need to be negotiated, preferably before expensive decisions have been taken.

There are certain issues that are often assumed to be important to structuring a fund but are in fact not all that significant in the final analysis. Access to treaty networks is one that is frequently cited in the context of African investment funds with the result that Mauritius and South Africa are seen as optimal jurisdictions. It should be borne in mind that the tax treaty network can be accessed without incorporating the fund in one of these jurisdictions. A Luxembourg-based fund can access the Mauritius treaty network through a Mauritian subsidiary. Given that Mauritius is unlikely to have treaties with all of the African countries that a pan-African fund will invest in, structuring through the use of underlying special purpose vehicles is, in any event, a likely scenario. Location issues can also sometimes be misunderstood. Malta is, for example, closer to North African jurisdictions than either South Africa or Mauritius and given route networks and the frequency of airline flights, London is often closer to many investments than Johannesburg or Port Louis. On the other hand, some investors, notably certain development finance institutions and pension funds, have an investment allocation to "African" investments which requires that the entity they invest in is established in Africa. This is of course, an important reason to consider Mauritius or South Africa, but in other circumstances, the world is the investment manager's oyster.

*“It is therefore important, at the outset, to understand the investors' requirements when it comes to choice of jurisdiction and this means identifying likely investors and having a chat with them about their tolerance for particular jurisdictions”*

As if the regulatory burden on funds and their managers wasn't already onerous enough, the quantity and complexity of regulation continues to increase in all jurisdictions. This poses evident challenges for funds and their managers, but it also poses significant challenges for regulators. Once candidate jurisdictions have been identified, the regulatory regime for both the fund and the management company in the chosen jurisdiction is a key issue. This is not a race to the bottom. One must consider that when things go wrong, the costs of dealing with a regulator whose resources are limited may outweigh the annual costs in a more established, better resourced jurisdiction. The impact on a fund and its investors of regulatory action (such as the freezing of accounts) can be devastating and one would want to be sure that a decision of this nature is taken by an experienced regulator with a deep understanding of the issues. Unfortunately, the increase in the number of new laws in many of these jurisdictions has not always been matched by an increase in regulatory capacity.

Africa remains a hot topic for investors and an opportunity for African-based fund managers. It is, however, still seen as a risky destination for foreign capital and a "plain vanilla" fund structure, one that the investor is used to investing in, will often ease the due diligence burden and facilitate investment in the fund. Investors are increasingly wary of being seen to be minimising their tax exposure and as a result there is a clear trend towards the established onshore centres like Luxembourg and Ireland as fund jurisdictions. When it comes to the location for the managers of African funds, South Africa offers a compelling lifestyle in comparison to other African locations combining good infrastructure and an advanced financial system but depending on the focus of the fund and the location of the assets, other jurisdictions such as Kenya and Morocco are also options. The legal and structuring challenges that need to be overcome should not be understated and it is important to get advice from a neutral party that has experience with a variety of jurisdictions. Very often, however, practical matters and lifestyle choices will be the determining factors in deciding where to establish a fund.

*“It is important to understand the possibilities for locating the manager at the outset because in many jurisdictions a fund is taxed in the jurisdiction where investment decisions are taken, i.e. the investment manager will draw the fund into the tax net of the jurisdiction he calls home”*

**Contributor’s Profile**
**Shayne Krige** is an English solicitor, South African attorney and Eastern Caribbean solicitor. He heads up Werksmans' Attorneys investment funds practice group which offers a one-stop shop to funds of all types, their fund managers and to investors. Shayne has more than 18 years' experience with investment structuring and has practised in the UK, France and South Africa.

# CLEARING THE PATH TO LIQUID AFRICAN MONEY MARKETS

By **Philip Buyskes,** Chief Executive Officer, Frontclear
**Maria-Pia Kelly,** Corporate Communications Officer, Cardano Development

In recent years, the instability of money markets have come to the forefront of international banking policy. Whilst the origin of the 2008 financial crisis was the collapse of the sub-prime mortgage market of the US, it very quickly became a global crisis as fear spread through money markets. This “run on the repo” crisis triggered a global recession that saw an estimated USD 50-100 million people drop below the poverty line across the world. The lessons from the crisis has led to the largest regulatory shake up of global money markets in recent history, having resulted in mandatory margining and clearing rules, new liquidity requirements and minimal capital requirements for swap, repo and other key money market instruments.

African markets have also had their fair share of money market related crises in recent months. In Kenya, following the collapse of two medium sized banks in 2016, money markets came to a complete standstill after larger banks cut credit limits on smaller banks and depositors rushed funds to large institutions deemed more creditworthy. The result was excess liquidity among large institutions, whilst even medium sized institutions became critically dependent on the central bank for liquidity support. Without liquid money market instruments available to all market participants, funding has been unable to flow and the result is less lending and slower economic growth.

In Nigeria, following the sharp drop in oil prices and the maintenance of an unsustainable currency peg, US dollar liquidity to the Nigerian money market all but disappeared as international banks cut credit lines to all but the largest local financial institutions. For an economy which is about 50% dollarized, this dealt a crippling blow to the real economy, triggering Nigeria’s first recession in 29 years.

Money markets in Africa are mostly chronically under-developed and have not been given sufficient attention. The stability and depth of money markets matter for economic growth and poverty alleviation: there is a strong correlation between a bank actively trading in interbank markets and its capacity to extend appropriate financing to its clients. Without extended financing, the economy struggles to develop and prosper.

Unfortunately, many commercial banks in Africa have limited access to both local and global money markets, due to a variety of factors. This forces banks to retain artificially high liquidity and increases systemic risk for the system. Perceived high counterparty credit risk, a wide lack of knowledge and inefficient financial infrastructure are some of the issues relating to a lack of trading depth in the market.

In 2015, Frontclear, a novel financial markets development company set out to begin addressing these issues. Frontclear catalyzes more stable and inclusive money markets through the provision of credit guarantees, thereby facilitating access for smaller financial institutions. Frontclear also maintains a large technical assistance program, focused on capacity building and advisory services. The guarantees cover a transacting institutions’ counterparty credit risk and are provided on the condition that local currency cash and government securities can be utilized for collateral management purposes. Use of local assets as collateral reduces transaction costs as well as default risk, thereby making market access more stable in times of crisis. Frontclear’s guarantees are Basel III compliant and cover the due payment of the Early Termination Amount (ETA) under ISDA contracts and Net Exposure under GMRA. All guarantees are in turn, counter-guaranteed by the German government-owned bank KfW, a AAA-rated development finance institution. Frontclear is funded by a number of European governments and development banks, including the European Bank for Reconstruction and Development, Financial Sector Deeping Africa, FMO, Proparco and The Currency Exchange Fund.

Frontclear’s inaugural transaction was executed in March 2016 in Kenya. Commercial Bank of Africa (CBA) and Standard Bank of South Africa (SBSA) executed a 25 million cross-currency repo transaction, which was 100% guaranteed by Frontclear. CBA received USD 25 million in 1-year funding from SBSA and offered Government of Kenya Infrastructure Bonds as collateral. This is the first example of a Frontclear transaction leading to the deepening of markets in emerging and frontier countries, being the first true repo based on full title transfer and traded under international standard documentation in the market. The transaction was nominated for the African Banker Debt Deal of the Year Award for 2016, due to its replicability and potential market wide influence. Further to this deal, Frontclear is involved in several development projects in support of the Kenyan market. For instance, the company is working with the Capital Markets Authority and has funded a full review of relevant Kenyan legislation with the goal of assisting Kenya to become only the third country after South Africa and Mauritius on the continent to obtain clean ISDA and GMRA netting opinions.

Beyond Kenya, Frontclear has facilitated more than USD 100m in trades since its launch in 2015. The company has partnered with the Ghana Stock Exchange, ACI Uganda, ACI Zambia, the National Bank of Rwanda and FMDQ in Nigeria to jointly work on the development of money markets in Africa. During 2016 the company provided training to more than 350 participants from local banks and regulators on fixed income, derivatives, ISDA, GMRA in 13 training events in 5 countries.

Frontclear's focus on money markets and swap markets is an important component of the wider need to accelerate the develop Africa's capital markets. Without a liquid repo market for instance, primary bond market dealers cannot repo existing inventory to fund the purchase of new issuances, whilst secondary market makers have no ability of hedge price risk and must maintain high inventory levels to ensure adequate supply.

Frontclear is committed to supporting the establishment of financial market infrastructure to support liquid money markets on the continent and has achieved strong initial results since its launch just 2 years ago. Through the provision of interbank guarantees, combined with the appropriate technical assistance, Frontclear is confident that it can play a key role in creating stable and inclusive markets, which will eventually grow to be independent of Frontclear's credit support.

### Contributors Profiles

Philip Buyskes is the CEO and co-founder of Frontclear. From 2008 to 2015, Philip worked at The Currency Exchange Fund as Vice President. Prior to TCX, Philip was an Investment Officer at the Development Bank of Southern Africa for 4 years. Prior to DBSA, Philip worked at the European Institute of Public Administration in Maastricht, The Netherlands. He holds a Master in International Business from Maastricht University and is FRM certified. In 2014 Philip completed Harvard Business School's comprehensive leadership program, the Program for Leadership Development.

Maria-Pia is currently seconded to Frontclear from Cardano Development, a Netherlands based financial and risk Management Company. Maria-Pia is also the Communications Officer for GuarantCo, a local currency guarantee provider. Previously, Maria-Pia worked as an Analyst at Mantis, a macro research company in the Netherlands. Maria-Pia holds an Undergraduate Degree in Economics and Social Studies from Trinity College Dublin and a Master in European Studies from CCBI and Université Catholique de Louvain.

## WHY SOUTH AFRICA'S RESERVE BANK IS UNDER FIRE?

South Africa's central bank is under fire by the nation's ruling party. The anti-graft ombudsman told parliament to start the process of changing the constitution to force the Reserve Bank to focus on the "socioeconomic well-being of the citizens" rather than on inflation. Many investors took this as a threat to the bank's independence. Two weeks later the ruling African National Congress proposed that the bank, which has been owned by private shareholders since its founding in 1921, should become state-owned. With South Africa suffering through a second recession in almost a decade, the 96-year-old central bank has become a scapegoat for many economic woes.

### 1 Why is the bank being targeted now?

As the ANC prepares for a December leadership contest, many are losing faith in the party's ability to raise living standards and reduce inequality. President Jacob Zuma has vowed "radical economic transformation" to accelerate spreading wealth to the black majority. Some of his supporters say the central bank is reluctant to issue new banking licenses to black-owned lenders.

### 2 What do the bank's defenders say?

That removing private shareholders would be a blow to transparency, since they are permitted to ask questions at the bank's annual general meeting. More broadly, that the bank is a last bastion of institutional strength in an economy that's in need of stability.

### 3 How so?

Look what happened earlier this year. South Africa's former finance minister, Pravin Gordhan, clashed with Zuma over expanding nuclear power and managing state companies as part of his efforts to maintain the nation's investment-grade rating. Zuma fired him on March 31. This prompted two companies to cut the country's debt to junk within a week. One of those companies, S&P Global Ratings, cited the Reserve Bank's independence and transparency as "important credit strengths."

### 4 Who owns the bank?

Along with Switzerland and Japan, South Africa is one of the few nations that still hasn't nationalized its central bank. Its Reserve Bank has about 650 shareholders, who can hold up to 10,000 shares each. If the bank ends the year with a profit, it pays a dividend of 10 cents per share, or a maximum of 200,000 rand ($15,000) in total. These modest returns, the illiquid nature of the stocks and the fact that shareholders have no say over policy decisions or who the governor is means holding Reserve Bank shares is more about sentiment and symbolism than about chasing yields.

### 5 What are the complaints about the bank?

Some critics say interest rates have moved in the wrong direction. From 2014 until 2016, the bank raised its benchmark repurchase rate by 2 percentage points, drawing criticism from labor unions who say the bank should be promoting employment rather than fighting inflation. (In July, the bank made its first rate cut in five years.) Also, the bank's licensing and oversight authority came under fire from some ministers last year after four large lenders closed the accounts of companies tied to a prominent family that is friendly with Zuma and in business with his son.

### 6 Does the ANC have the power to reshape the bank?

Maybe, but it will take some doing. South Africa's constitution guarantees the bank's independence and prescribes its primary objective, which is to protect the value of the currency. South Africa's anti-graft ombudsman, known as the Public Protector, wants to start by scrapping that objective, effectively removing the bank's mandate to target inflation. Separately, the ANC would adopt the state-ownership proposal as policy at its national conference in December, then it would ask parliament to change the South African Reserve Bank Act. While the party may be able to drive the change in the act because it holds 62 percent of the seats in parliament, amending the constitution would be a more difficult hurdle because it would require the votes of two thirds of lawmakers.

### 7 What would these changes do to the economy?

It's unclear whether nationalizing the central bank would change much. Currently, the owners have no say over policy or the appointment of the bank's executives. The government determines the inflation target in consultation with the central bank, without any input from the shareholders. Any move towards nationalization would be largely symbolic and won't affect its mandate, the central bank says. If the mandate is changed, the rand could weaken and inflation accelerate, something the Reserve Bank says would exacerbate poverty and inequality.

# IS NOW A GOOD TIME TO TAKE A RISK ON AFRICAN CAPITAL MARKETS?

***MARK MOBIUS*** *is an Executive Chairman, Templeton Emerging Markets Group. Mark has spent more than 40 years working in emerging markets all over the world. He joined Franklin Templeton in 1987 as president of the Templeton Emerging Markets Fund, Inc. He is the author of the following books: Trading with China; The Investor's Guide to Emerging Markets; Mobius on Emerging Markets; Passport to Profits; Equities: An Introduction to the Core Concepts; Mutual Funds: An Introduction to the Core Concepts; Foreign Exchange: An Introduction to the Core Concepts; Bonds: An Introduction to the Core Concepts.*

***ANDY GBOKA*** *has been covering the African investment space since 2011, first as a research analyst generating investment ideas for GEM, Frontier and Africa-dedicated funds then as a co-Portfolio Manager with the BB African Opportunities (LUX) Fund. The fund was launched in 2009 and invests mostly in African Equities following a reform-driven approach. Prior to that, Andy was a sell-side analyst covering European utilities. He holds a Master degree specialized in Finance and has been a speaker at several events related to investment in Africa.*

***ALAIN NKONTCHOU*** *is the Co-Founder and Managing Director of ENKO Capital and based at the London office. His responsibilities include overseeing the firm, managing Enko's client relationships, and investment decision-making. Alain was previously a Managing Director for Global Macro Trading within the Proprietary Trading Group of Credit-Suisse in London and JP Morgan in London. He has traded fixed income, currencies, commodities and stock indices over his 20+ years of experience. He holds an MSc in Electrical Engineering from Ecole Supérieure d'Electricité in Paris and an MSc from Ecole Supérieure de Commerce in Paris.*

***CAPMARKETSINAFRICA:*** *Is now a good time to take a risk on African markets?*

**MARK MOBIUS:** Yes, Africa has some of the fastest growing countries in the world. The increase in internet users combined with the rapid increase in smart phone sales is resulting in innovation that is accelerating productivity.

**ANDY GBOKA:** The overall situation for African markets has improved since commodities prices bounced back from their lows in early 2016. The net exporters of commodities benefited from a temporary relief after two difficult years whilst some of the net importers are progressing on their reform agenda to restore their macro imbalances. However, we are still in an adjustment phase in which investors should choose their risk exposure carefully. Indeed, the better macro picture or strong returns (ytd) in certain equity markets can prove only cyclical and short-lived if not coming along with credible fiscal and monetary policies to address structural weaknesses. Thus, yes this is a good time to take a risk on African markets but we would consider only those where authorities have shown a strong commitment to reform and drive a sustainable growth.

***CAPMARKETSINAFRICA:*** *What are some of the fundamentals that you consider when looking at African markets?*

**MARK MOBIUS:** The key is political stability – the rule of law – foreign exchange policies that allow the free flow of funds and, of course the quality of management.

**ANDY GBOKA:** Investing in Africa can be a bumpy ride when taking a short-term view, reason why we tend to look at a 3-to-5 year horizon in our investment decisions. From a top-down perspective, we carefully assess that fiscal and current account deficits remain manageable and do not constitute an impediment to returns in USD terms. Once comfortable with the macro dynamics, identifying key reforms or major competitive moves in specific sectors sets the stage for a bottom-up analysis from which opportunities in the equity space could emerge. Political developments, particularly before and after a major election, are also important because of the consequences they could have on the private sector (e.g. change in regulation or taxes). The last fundamental factors worth mentioning are commodities prices and global monetary conditions as they both have an important impact on the balance of payments of big economies on the continent.

***CAPMARKETSINAFRICA:*** *In your opinion, how would you describe the current African capital markets setting?*

**ALAIN NKONTCHOU:** We believe the scene is still in its infancy as there is still much less credit (when measured by credit/GDP) in Africa when compared to other markets. Similarly, there are fewer asset managers that are solely dedicated to the continent. Hence we believe that as local economies grow, there is significant potential for growth of the African capital markets sector. Although it has grown strongly in recent years, particularly in the private equity space, there is still space for future growth. The market continues to get increasing attention as some countries realise the benefits of financing locally instead of going to the international capital markets. However the local markets, in general, are relatively shallow although there have been improvements over recent years.

**CAPMARKETSINAFRICA:** *What are some of the challenges you see in African Markets at the moment, and how does that influence your investment decisions?*

**ANDY GBOKA:** Since the drop in commodities prices have brought serious strains to the current account positions of economies relying the most on commodities exports, the main challenges we see are related to the FX controls introduced over the past two years. The latter not only strangled capital repatriation for foreign investors but also weighed negatively on corporates' access to FX to operate normally, fund their capex needs or face their debt / payables obligations. These problems are not always visible at first glance, especially when looking at markets such as Nigeria or Zimbabwe that are among Africa's top performers ytd in USD terms. Nonetheless, digging into the financials of domestic corporates shows how difficult the situation is: the subsidiaries of Lafarge, Diageo and Unilever in Nigeria have come to the market to raise additional capital to plug the gap whilst Etisalat Nigeria terminated talks to renegotiate its USD1.2bn syndicated debt and left the country. These recent examples are only factual elements that do not illustrate the whole complexity and lack of transparency embedded in some of the FX systems currently in place. As an Africa-dedicated fund, we avoid places where there is no clear and sustainable FX repatriation mechanism despite the potential for high returns. We think it the best way to access the reform-driven growth story of Africa while fulfilling our duty to protect investors' capital.

**MARK MOBIUS:** The challenges are related to the above. Too many countries in Africa have governments that are corrupt, violate the rule of law and appeal to populist sentiments with the result that the countries' spending go beyond their ability to pay. This creates an unstable environment.

**CAPMARKETSINAFRICA:** *Domestic bond markets are essential to provide long-term local currency financing for key economic sectors – government, corporate and sub-national. They also offer investors much needed long-term investment opportunities. What are opportunities, key constraints and potential solutions to domestic bond markets development in Africa?*

**ALAIN NKONTCHOU:** We believe the opportunity is significant given that the savings ratio is still lower than in other regions hence is expected to rise over time. Strong economic growth will lead to a natural demand for financial products and will need to be financed hence creating additional opportunities for the industry. The key things to monitor include political stability, macroeconomic imbalances, and savings ratios. Key constraints are regulatory uncertainties and macroeconomic imbalances which may make it more difficult to embark on longer term financing projects. Potential solutions include discussions with key stakeholders including Central Bankers, Ministers of Finance and policymakers etc.

**CAPMARKETSINAFRICA:** *How do you see the sea-change in global politics effecting African market equity investment? What are the downsides and upsides?*

**MARK MOBIUS:** Global politics is not impacting African market equity investment since the major impact is not from political sources but individual and institutional investors in search of investment opportunities. The downsides are the inability to remit funds out of countries and the possibility of changing rules. The upside is rapid growth.

**ANDY GBOKA:** At this stage, we believe that global monetary conditions have had more impact on African equity markets than global politics. Indeed, the global liquidity and appetite for risk assets subsequent to global central banks' monetary cycles have driven portfolio flows in and out of equity markets. This has, to a certain extent, been visible in the performance and valuation of listed equities. The impact of global politics on the other hand is less easy to assess, particularly because it mostly goes through private channels for which information is less available. Even looking at the Foreign Direct Investments in countries we cover does not allow us to have a clear view on the impact from global politics. However, in the context of the current migrant crisis and the last G20 summit held in Hamburg, there has been a pickup in interest towards Africa, which is a first step in the direction of a pick-up in investments towards the region. Further, the continent has been strengthening its ties with the "new super-powers" such as China or India; a move initiated more than a decade ago that bodes well for foreign direct investments.

**CAPMARKETSINAFRICA:** *Please tell us about the Enko Capital Debt Fund (EADF) and what is the rationale behind it as well as where will the fund be investing (countries or sectors that will be targeted)?*

**ALAIN NKONTCHOU:** The aim is to provide a vehicle for investors to gain exposure to the African debt market. The fund is predicated on the pillars of debt sustainability, value investing and active risk management. It is one of the few funds that exist globally which provides direct access to the African debt market, including both hard and local currency opportunities. It is one of the largest of its size at the moment and has the ability to invest in both the public and private debt markets. We expect the African debt market to continue to increase over time and believe that our expertise and knowledge of the market will lead to creating alpha for our investors. We tend to look for opportunities where we find attractive opportunities either due to policy mistakes, improving credit stories, macroeconomic imbalances, or market dislocations. We believe there is capacity to scale up the fund up to US$1 billion. Key markets to monitor include Egypt, Ghana, Ivory Coast, Kenya, Uganda, Nigeria, and Zambia."

**CAPMARKETSINAFRICA:** *Thank you very much for granting this interview!*

# CAPITALISM - MEETING THE GENUINE DEVELOPMENT NEEDS OF AFRICANS

By **Wildu du Plessis,** Head of Africa and Partner, Baker McKenzie

There were no cross-border Initial Public Offerings (IPOs) from African companies in the first six months of 2017, the first time in five years this has happened.

The Index also shows that five companies in Africa have raised a total of USD 512 million so far in 2017 from domestic listings, up from the eight companies that raised USD 492 million in H1 2016, but down from the USD 596 million raised from seven domestic deals in H1 2015. Three of five the companies that went public in H1 2017 are South African, while the remaining two are Egyptian and Tanzanian.

The fact that there were no cross-border IPOs in Africa in H1 2017 clearly shows that political and economic instability in Africa has affected the volume of cross-border IPOs on the continent. Businesses simply do not carry out IPOs if they are unsure of the investment environment.

In 2016 there was one cross-border IPO in Africa valued at USD 130 million, and in 2015 there were four IPOs, which raised a total of USD 825 million.

Globally, IPO activity rebounded in H1 2017 compared to the same period last year as economic fundamentals in major developed markets such as the EU and US stabilized and some political uncertainties settled.

The value of issuance rose by 76% to USD 89 billion and volume increased to 728 deals, up 53% from the first half of last year. As Baker McKenzie predicted last June, domestic deals outpaced cross-border IPOs in H1 this year, rising 93% in value compared to a 41% increase in cross-border deal values. The greater popularity of domestic issuance was largely driven by the comfort of home markets and the protection against currency volatility provided by listing in companies' functional currencies.

Although political uncertainty remains a key concern for potential issuers, the absence of blockbuster votes of the magnitude of the Brexit referendum and the US elections have made the timing of IPOs in 2017 much easier than in 2016. Meanwhile, business imperatives are driving companies to proceed with listing plans for deals that have

There is a correlation between global IPO predictions and African IPOs, and so the current global recovery is expected to influence a recovery in Africa as well. However, Africa tends to lag behind the rest of the world so it might be some time before we an improvement the volume and value of IPOs on the continent.

In the meantime, how do we address Africa’s capital raising challenges? One idea is that governments and legislators in African nations should act as enablers of the basic principles of capitalism as an economic system, such as free market competition, private ownership and investment of capital to make a return. Capitalism, notwithstanding its imperfections, had lifted billions of people out of subsistence poverty in the past three decades alone. It delivers good things when allowed to function as it should.

Treat capitalism as an economic system that has been empirically proven to work and everyone will benefit through the emergence of a large and more affluent middle class. However, if it is twisted it into so-called "crony capitalism”, only the elite will benefit and the very concept of capitalism becomes misunderstood and vilified.

Colonialists had set the tone for this in Africa. While Britain and others were embracing free trade, industrialisation, liberalism, competition and the development of a market economy, the story in Africa was of conquest by European nations and the handing of de facto monopolies to powerful individuals to extract valuable natural resources. This benefited small elites rather than the collective interest, creating an inaccurate view among many governments of what capitalism is and the vast benefits it can deliver to the many, not just the few.

More recently, the combination of Africa's fertile land, abundance of natural resources, and governments that hope to benefit from foreigners' investment but without the technical expertise to retain and direct the benefits of such investment, have made the continent an easy target for exploitation by unscrupulous investors and politicians.

This leaves the continent in a strange hinterland between development opportunity and crisis. This is, of course, a gross generalisation - many countries have made enormous progress.

The majority of today's African leaders want the best for their people. Investors want to invest but needed legal certainty to take commercial risks. Potential investors are not looking for guaranteed profits, but legal certainty simply allows them to assess opportunities and risks on a commercial basis. This is essential for drawing in the capital Africa desperately needs to develop the infrastructure necessary to deliver on its growth potential. The question is how to do this.

To address these issues, growth and capitalism needs to be facilitated by many things, the three essentials are:

- Strengthening the rule of law. Foreign investors will only ramp up their investments if they are confident no government can simply take away their assets on a whim.
- Cooperation. The emergence of nascent trading blocs such as the East African Union for example. As parts of the world seem to be fragmenting (for example, Brexit and the EU) or turning inward (the US), there is an opportunity for African nations to collaborate. Speaking with one voice means a strong hand in trade negotiations.
- Energy and Infrastructure in Africa and for Africa. It is the same old issue but it is an unavoidable fact that Africa cannot reach its potential without more and better energy and infrastructure.

To fully leverage the continent's wealth potential, legal structures need to be put in place to guide Africa's development agenda from within by enabling entrepreneurship, cutting red tape and bureaucracy, supporting success and selling opportunities to the wider world of foreign investors.

The world is moving increasingly towards mixed models of capitalism and what is certain is that Africa needs a model that both caters for its unique advantages and addresses its equally unique challenges. As Africans, we must be open to new ideas and redirect the positive energy of capitalism to meet the genuine development needs of Africans, while understanding we cannot do this alone. Foreign expertise and capital will be a necessity whatever the approach. Local and foreign investors in Africa must work together to ensure that raising capital in Africa works for every African. Hopefully, future IPO Index's will reflect a move towards this approach.

**Contributor's Profile**

**Wildu du Plessis** is a partner and head of Baker McKenzie's Banking & Finance Practice Group in Johannesburg. He also acts as the office's Africa Head. Mr du Plessis is regularly ranked as one of South Africa's leading banking and finance and capital markets lawyers and is recognized by Chambers Global 2016 and the Legal 500 2016. He represents and advises leading domestic and international financial institutions, private equity groups and corporates in connection with a wide range of financing transactions, acquisitions, restructurings, regulatory and general finance matters.

## BAKER MCKENZIE CROSS-BORDER M&A INDEX Q2 2017

As dealmakers adjust to a challenging M&A climate, they have reason to be positive, with cross-border deal value jumping 49% year on year while the Index is up 30 points on Q2 2016.

Global dealmakers faced a range of political challenges in Q2. The nature of the UK's exit from the EU is still unclear following a snap election which delivered more uncertainty. A cloud of doubt hangs over President Trump's ability to pass his pro-business agenda through Congress. In spite of this political volatility, M&A has remained stable.

There were a total of 1,368 cross-border deals valued at US$345.8bn announced during Q2, down a mere 1% by value compared to the previous quarter but up 15% year on year. The EU proved a draw for cross-border dealmaking despite political volatility. The largest cross-border deal of the quarter saw US-based Praxair purchase Germany's industrial gas firm Linde for US$45.5bn.

The deal pushed chemicals and materials into the top value slot for the quarter with US$60.4bn. Industrials led the way in terms of volume with 209 announced deals. This was despite the sector taking seventh place on the value table with US$25.4bn, highlighting a flurry of midmarket activity.

However, there was a quarter-on-quarter drop of 10% in volume and, as a consequence, Baker McKenzie's Cross-Border M&A Index, which tracks quarterly deal activity using a baseline score of 100, slipped to 233 in the first quarter of the year. This marks a 4% decrease on the previous quarter. As a result of the drop in volume but considerable rise in value, the cross-border deal average rose to US$477m in Q2—up 63% year on year. For this quarter, it would appear that the increased risk and uncertainty facing cross-border transactions has led dealmakers to choose to invest more money in a smaller number of handpicked deals.

# THE POTENTIAL OF SMES IN AFRICA: A PERSPECTIVE FROM DFI

By **Anne Keppler,** Vice President, DEGs Private Equity team

Small to medium-sized enterprises (SMEs) have certainly developed into a buzz word for impact in Africa over the last decade – and rightly so. While SMEs attract a lot of interest, there seems to be unmet funding demand in many countries. Why are SMEs seen as so beneficial to economies but only selected players manage to finance this segment? What barriers exist to this funding?

As German development finance institution, DEG (Deutsche Investitions- und Entwicklungsgesellschaft) can certainly attest to the relevance of SMEs in our home market. The often quoted German Mittelstand is very validly seen as an engine of the German economy, not only because especially German automotive companies have perfected the integration of SMEs into their own operations. DEG's holding company, KfW Bankengruppe has published a fact sheet in 2015 which proofs the relevance of SME in Germany[1]:

With an annual turnover of up to EUR 500 million, the 3.67 million small and medium-sized enterprises form the backbone of the German economy representing 99.95% of all companies. They employ 29.1 million people, or 68 per cent of the working population. Micro enterprises with less than 10 employees provide a good third (34 %) of workplaces in the German SME sector.

Although SMEs are defined differently by different criteria for each market, a common classifications sees revenues below USD 15m p.a. and up to 300 employees to qualify a business to be a SME.[2] These number driven definitions often fall short in an African context to grasp the size of a business as revenues or the number of employees are not seen in relation to the operating environment.

But a clear common denominator is the high contribution to employment. Creating employment is one of DEG's main impact targets and hence promoting SMEs across Africa is an important aspect of DEG's mandate – and DEG certainly subscribes to the relevance of SMEs outlined above. But why is access to finance still a shortfall in Africa? What are requirement for SMEs to unleash their impact and contribution to employment and economies?

The challenge seems to have two main aspects in many different variances: operational and financial. Growing a business requires a supportive business environment, frequently measured by the WorldBank and rated as "doing business indicator". Many African countries retain bureaucratic hurdles, not only in formalising and establishing a business but also on land ownership, labour laws and taxes. Another aspect is the formalisation and developing an owner managed business into corporate entity, reducing key person risk and preparing for growth and succession (a key challenge currently discussed for SMEs in Germany).

Access to funding as second main area is certainly defined by the operational performance of the business. Establishing and the ability to enforce collateral as well as financial management and accounts are common restrictions to access debt for SME. Both aspects are closely linked to the operating environment and require more hands on support than most banks can realistically provide. PE funds focussing on SME tap into this niche offering capital but also the operational support to bridge such shortfalls. However, an equity injection dilutes ownership and control which is more often than not a high (emotional) barrier for entrepreneurs.

A worrisome statistic is however the failure (or inverted success rate) of young SMEs. Varying statistics for start-up businesses quote numbers of 50% even up to as high as 80% of businesses that do not survive. From an investor's perspective, this certainly raises a concern and has to be considered.

Seeing restrictions and shortfalls in SME growth, how does DEG approach the SME sector in Africa and are there additional measures to change potential into actual growth?

1) As DFI, DEG's first focus is certainly on providing access to funding. DEG approaches SME through different channels: Indirectly through Banks: DEG has financed financial institutions across Africa with 450m EUR. Globally, our clients and partners have been able to fund 1.7million SMEs with EUR 41 billion.

*"With an annual turnover of up to EUR 500 million, the 3.67 million small and medium-sized enterprises form the backbone of the German economy representing 99.95% of all companies."*

1 https://www.kfw.de/migration/Weiterleitung-zur-Startseite/Homepage/KfW-Group/Research/PDF-Files/The-SME-sector-in-Germany.pdf
2 https://www.ifc.org/wps/wcm/connect/de7d92804a29ffe9ae04af8969adcc27/InterpretationNote_SME_2012.pdf?MOD=AJPERESA

| Indicator | Micro Enterprise | Small Enterprise | Medium Enterprise |
|---|---|---|---|
| Employees | <10 | 10<50 | 50<300 |
| Total Assets | <$100,000 | $100,000<$3 million | $3 million < $15 million |
| Total Annual Sales | <$100 000 | $100,000<$3 million | $3 million < $15 million |

2) Indirectly through SME fund: DEG has committed EUR 67.5 million to SME dedicated private equity funds in Africa. These funds can support approx. 60 businesses. In selecting the teams, DEG has focussed on the financial but also the operational value-add capacity the fund managers can offer their investees. In addition, also private equity funds rather classified as mid-market, i.e. investing in businesses exceeding the IFC classification criteria for SME, often support SME. High growth businesses may be lifted to very productive, formal medium-sized companies outgrowing the SME segment in a few years.

3) For the larger business in the SME segment, DEG has also engaged directly with debt or equity. For example DEG has provided the Kenyan fruit juice producer Kevian with a long-term loan to the amount of USD 7.5 million for expansion investments. The company increased its production capacity of fruit juices and improved its packaging systems.

Secondly, DEG addresses operational challenges with our Business Support Services offering ("BSS"). The BSS programme aims at enhancing our customers' sustainability - with respect to commercial as well as social and environmental best practices. Possible areas for BSS support are for example corporate governance, risk management, strategy, environmental and social management, resource and energy efficiency as well as training of staff or suppliers. DEG connects companies with external experts to realize tailor-made advisory solutions and help customers to design coherent development projects. An example for these efforts is the investment into the Kenyan company Meru Greens Horticulture under DEG's Up-Scaling Programme. Meru Greens Horticulture mainly grows fruit for the local market and exports green beans to Europe. With growing demand, the company has set up the company's own canning facility in order to meet demand in Europe. As a result, the company is able to guarantee continuous production and consistently good quality.

Furthermore, as DEG is planning to open a dedicated "German Desk" , a centre of competence for funding German businesses in Africa in cooperation with commercial banks on the continent later in 2017. This service will be available for German SME's and their local trading partners in Africa. The range of services extends from setting up accounts through services for financing trade and transaction banking, to credit lines or investment financing for local companies wishing to acquire German equipment, for example.

Successful SME promotion requires tailored finance, close contact with the clients and advice based on their individual business needs. While such measures address not only financial challenges but operational and structural measures, certainly more support is needed to improve the operating environment for all business. So overall, there does not seem to be one response or action item to promote SMEs in Africa. As always, challenges are multi-dimensional and have different facets. However, focussing only on providing finance might not be enough to tap into the potential of SMEs in Africa. Considering the relevance SMEs traditionally have for every economy, reducing barriers and enabling access to finance through operational improvement will stay in focus for many development financiers and stakeholders.

*"Many African countries retain bureaucratic hurdles, not only in formalising and establishing a business but also on land ownership, labour laws and taxes. Another aspect is the formalisation and developing an owner managed business into corporate entity, reducing key person risk and preparing for growth and succession"*

**Contributor's Profile**
Anne Keppler has been working as Vice President for DEGs Private Equity team since June 2010 and is based in Johannesburg since 2011. Her responsibilities within the team include the assessment, structuring and management of equity and mezzanine investments for corporates in Sub-Sahara Africa as well as the PE fund portfolio. DEG has grown its African PE portfolio significantly over the last five years, with equity commitments across all sectors of almost USD 1bn and more than 30 fund investments on the continent. Before joining the PE team Anne has been part of DEGs Financial Services team working on debt and equity transactions since 2005 and worked as credit analyst for financial institutions at WestLB in Germany.

# FINANCING INFRASTRUCTURE IN AFRICA VIA CAPITAL MARKETS: ADDRESSING MYTHS AND CREATING VIABLE MARKETS

By **Catiana Garcia-Kilroy,** Lead Financial Sector Specialist, World Bank
**Caroline Cerruti,** Senior Financial Sector Specialist, World Bank
**Swee Ee Ang,** Senior Financial Sector Specialist, World Bank

## Why capital markets for infrastructure finance?

Bridging Africa's infrastructure gap can help address its development challenges by supporting social programs in education and health; providing opportunities for developing businesses and access to markets; de-fragmenting Africa's regional markets; and integrating the continent into global value chains.

The quantity and quality of infrastructure in Africa lag considerably behind those in other regions, with the gaps particularly large in power, transport and social services. Infrastructure needs of the region are expected to be more then USD 93 billion per year over the next decade, equivalent to about 15 percent of the region's GDP. The impact of improving Sub-Saharan Africa's infrastructure gap is potentially large. For example, growth of GDP per capita for the region would increase by an estimated 1.7 percentage points per year if it were to close the gap with the median of the rest of the developing world[1].To date, less than half of the needs, around USD 45 billion, is funded and mainly from the public sector.

Governments do not have the fiscal capacity to bridge the infrastructure gap by themselves. Other traditional financiers such as commercial banks have, substantially low risk appetite, especially after the financial crisis and are only willing to finance projects in shorter tenors. Development Financial Institutions (DFIs) can still provide financing to certain projects and countries, but they do not have the capital to fill in the gap by themselves. Therefore, creating the conditions to attract new private sector investors into infrastructure under fiscally sustainable conditions, with limited exposure to foreign exchange risk, is a necessity. In this context, long-term capital in local currency, as can be provided by domestic institutional investors, and some international investors, should be considered a priority.

## Pre-requisites for financing infrastructure with capital markets

Following developments in other continents, such as Latin America, and some incipient examples in Africa, the commitment of Governments and DFIs to a programmatic approach can trigger a virtuous circle supporting infrastructure finance. Four pre-conditions are critical for any successful mobilization of capital markets for infrastructure finance in Africa. First, a program of bankable projects reaching a certain critical mass under standardized structures, contracts and procurement rules. This is achieved with a solid Public Private Partnerships (PPP) framework that is credible and fiscally sustainable.

Second, the existence of a minimum size of assets under management by domestic long-term institutional investors (pension funds and insurance companies). This needs to be coupled with some familiarity of investors with infrastructure assets; the existence of the appropriate investment vehicles and credit enhancement products; and by the commitment of the financial regulators to support flexibility in investment rules within prudent limits.

Third, counting with a minimum level of development of the domestic capital markets. The threshold may vary depending on the country. However, in all cases it needs a strong commitment from the financial authorities to support a relatively well-functioning government debt market with a credible yield curve for pricing long term assets; the framework for developing investment instruments and vehicles for structured finance (e.g. special purpose vehicles, infrastructure funds); and the existence of committed and capable financial sector regulators for capital markets and institutional investors.

Fourth, the availability of DFIs prepared to use their balance sheet to de-risk infrastructure projects to crowd-in private sector investment as trust builds into the new frameworks.

*"Infrastructure debt funds instead of project bonds seem to be more appropriate vehicles in Africa to engage institutional investors into infrastructure, at least in the initial stages"*

## Where can this approach work in Africa?

The World Bank Group (WBG) is committed to supporting countries adopt this approach in Africa. Kenya and South Africa, for example, are working with the World Bank on comprehensive programs along these lines described above. In Kenya, the WBG is working with the Government in four critical lines of work:

1. A comprehensive project to support the development of a PPP program with sufficient critical mass of bankable projects. This process was initiated in 2012 and is now

1 World Bank, Africa's Pulse 2017

starting to bear its fruits with a pipeline of around 60 projects of which five toll roads are being tendered.

2. A medium-term engagement to facilitate the dialogue between the PPP authorities, financial regulators and domestic asset managers so they are prepared to take investment decisions when projects are tendered. This includes hands-on-training of domestic asset managers and trustees on infrastructure financing and a continuous dialogue to find solutions to regulatory and policy bottle-necks. The engagement includes a close collaboration with the National Association of Securities Professionals (NASP) from the United States representing the interests and views of international investors that could potentially partner with domestic investors in these projects.

3. Facilitating the creation of a new vehicle in Kenya to mobilize domestic institutional investors into infrastructure. This would be an infrastructure debt fund following a successful experience in Latin America in a comparable context. This vehicle will allow domestic investors to invest along with banks in the debt of projects but in longer maturities.

4. Developing a credit-enhancement product for the first projects to be tendered in the pipeline. This will help build credibility of a PPP program that is already solid but still needs to build a track record. The credit enhancement product will benefit all lenders: including banks, domestic and international investors.

*"Governments do not have the fiscal capacity to bridge the infrastructure gap by themselves. Other traditional financiers such as commercial banks have, substantially low risk appetite, especially after the financial crisis and are only willing to finance projects in shorter tenors"*

**Lessons learned so far on the role of institutional investors in infrastructure finance in Africa**

The program in Kenya is already underway and it is also providing important inputs, along with the WBG experience in other countries, to reassess how to address some of the challenges and myths regarding the role of institutional investors in financing infrastructure. These findings will allow a more flexible approach when trying to mobilize institutional investors, including developing strong partnerships with commercial banks to create win-win financing structures. Findings so far can be grouped in three categories.

*1. What matters for institutional investors?*

Some institutional investors are open to invest in greenfield projects, with construction risk, provided there is a solid project sponsor and PPP contract. They can invest along with experienced banks that take the burden of project due diligence; and they can outsource project finance expertise to a third party such as an infrastructure fund. Institutional investors in Africa tend to invest in real estate in their alternative assets allocation. Well-structured infrastructure projects are better aligned with their investment objectives than real estate assets.

Lack of liquidity of infrastructure assets is not a problem for most long-term investors. They generally do not need liquidity because of their long-term investment horizon and they have relatively large portfolios of government debt for liquidity purposes. Infrastructure investments offer them a yield pick-up to compensate them for the higher risk and lower liquidity.

For institutional investors, listing is not as important as having the right vehicle and the right asset manager. Private placement markets through infrastructure funds seem to be, at least in Africa, the source of financing with most potential. This is important in Africa as only very few countries have well-functioning formal securities markets. However, the World Bank continues to support the development of domestic securities markets, starting with government bond markets.

*2. What are effective investment structures?*

Institutional investors, for now, are not going to be providing the bulk of the financing. This will continue to be provided by banks. But institutional investors can play a critical role in lengthening financing tenors and complementing financing needed. Hybrid financing between banks and institutional investors seems to be the solution for newly tendered projects, whether greenfield or brownfield. Banks contribute with their expertise in project finance and institutional investors contribute with longer tenors that banks are not able to offer.

Infrastructure debt funds instead of project bonds seem to be more appropriate vehicles in Africa to engage institutional investors into infrastructure, at least in the initial stages. Debt funds have several advantages over project bonds in Africa. They allow institutional investors to invest in project loans along with banks. This simplifies the project's financial structure and is less costly to the project sponsor as funds are disbursed in line with the drawdown needs of the project. Additionally, through an infrastructure debt fund, institutional investors can outsource project finance skills to a third party. It is important, though, that the infrastructure debt fund is aligned with the interest of long term institutional investors in terms of fees and tenors. This currently and important area of work for the World Bank in Kenya.

There are enormous virtues in co-mingling international and domestic institutional investors if this is conducted through the appropriate vehicles. In addition to mobilizing larger volumes, there are complementary skills from which both parties can benefit. There are very good examples of foreign and domestic partnerships in Latin America, e.g. Mexico's partnership between Caisse de dépôt et placement du Québec (CDPQ) and the domestic pension funds, that can serve as an example for Africa.

*3. Pending hurdles for institutional investors*

Forex exchange risk is one of the main hurdles to bring international institutional investors. In addition to macro-economic and political stability, more sophisticated and deeper domestic markets are needed to develop affordable hedging instruments. Other potential options are the development of a foreign exchange liquidity facility as implemented in other continents.

Even if PPP programs are of good quality, generally, being first to market comes with a penalization in pricing or in tenors. In these cases, credit enhancement products, such as the ones offered by multilateral development banks, could have an important role to play.

This approach is not exempt from risks and important challenges that still need to be thought through. However, there are some initial positive results in select African countries, as well as other regions, which contribute to making Africa, a credible infrastructure investment opportunity for both domestic and international investors. This approach is in line with the World Bank Group so called "cascade" approach that focuses on prioritizing strategies to "crowd in" private investment and limiting, to the extent possible, the use of public resources to de-risking private projects.

*"Bridging Africa's infrastructure gap can help address its development challenges by supporting social programs in education and health; providing opportunities for developing businesses and access to markets; de-fragmenting Africa's regional markets; and integrating the continent into global value chains."*

## Contributors Profiles

**Catiana Garcia-Kilroy** is a Lead Financial Sector Specialist in the Finance & Markets Global Practice at the World Bank. She coordinates a global program on capital markets with a focus on infrastructure finance.

Before joining the World Bank in 2010, Catiana worked for fifteen years as international consultant for Development Financial Institutions, Ministries of Finance and Central Banks on capital markets policies and regulations, and developing fixed income markets and financial infrastructure projects. Previously she worked for four years as a stock broker in Madrid and London.

Catiana has an Economics degree from the Catholic University of Louvain in Belgium and a Geography and History degree from the Complutense University in Madrid, Spain.

**Caroline Cerruti** is a Senior Financial Sector Specialist in the Africa region of the World Bank. She works primarily on housing and infrastructure finance, financial sector restructuring issues, and financial inclusion. She has been involved in various financial sector assessments jointly with the IMF.

Before joining the World Bank, Caroline worked for the French Treasury on trade and financial regulation issues, and for three years as a banker in the European Bank for Reconstruction and Development. Caroline was educated at the Institute of Political Science in Paris (Sciences-Po), the Ecole Nationale d'Adminis-tration (ENA) in Paris, and is a CFA Charter holder.

**ANG Swee Ee** is a Senior Financial Sector Specialist in the Long Term (LT) Finance and Risk Management (F&M) Global Practice of the World Bank. Her work programs include Kenya, Indonesia and Ghana supporting the mobilization of LT-financing for infrastructure thorough capital markets. She spent 9 years as a credit analyst in RAM Ratings, a credit-rating agency domiciled in Malaysia and the largest in ASEAN – covering project and infrastructure finance and ABS transactions. In 2011, Swee Ee joined BNP Paribas Malaysia Berhad as the 'Head of Credit Analysts' but returned to RAM Ratings to head the Business Development team in 2013.

# TAPPING INTO OPPORTUNITIES IN AFRICAN LOCAL CURRENCY BOND MARKETS

***An Interview with Mr. James Doree, Managing Director, Lion's Head Global Partners, London***

***JAMES DOREE***

*is Managing Director at Lion's Head Global Partners and he joined Lion's Head in 2011 as a Director. He provides financial and strategic advice to governments, institutional investors and companies in Frontier Markets across infrastructure, financial services and other high impact sectors.*

*As part of Lion's Head's work in African capital markets, James has responsibility for managing the African Local Currency Bond Fund (www.alcbfund.com). Through this and other initiatives, he originates and executes transactions across the Continent.*

*James was previously a Senior Consultant at Cambridge Economic Policy Associates and, prior to that, worked for Pricewaterhouse Coopers in Nairobi. He has a Masters in Development Economics and a first class MA in History and Economics from Balliol College, Oxford.*

***CAPMARKETSINAFRICA:*** *Most international investors want to buy the most liquid instruments to get exposure to local currency African assets. This usually means government paper. The ALCB Fund focuses solely on non-Sovereign credit. Why?*

**JAMES DOREE:** The Fund's sponsor, KfW, has given the ALCB Fund a broader mandate to help the development of African capital markets. At their core, capital markets provide a set of institutions and processes for recirculating savings – pensions, unit trusts, bank deposits, etc. – back into the real economy. These pools of savings have grown substantially over the past 15 years and there is a historic opportunity to mobilize local resources for economic development. However, as things stand, local capital markets are under developed in a number of ways, while issues vary significantly by country and region. The problem the ALCB Fund has chosen to address is the lack of primary bond issuance among non-Sovereign entities, i.e. companies, financial institutions and projects. While there has been great progress in the development of Sovereign bond markets in many countries, non-Sovereign bond issuance remains rare. Larger, established companies can access longer-term finance from local banks and bilateral loans from Development Finance Institutions, usually in foreign currency. Awareness of local bond markets and local institutional investors is limited among the vast majority of private-sector companies, even those with track-record and strong performance.

***CAPMARKETSINAFRICA:*** *What makes you different from DFIs or other African credit funds?*

**JAMES DOREE:** The Fund does three things. Firstly, we engage with companies and institutions unfamiliar with bond issuance, providing insight into the processes and requirements, and connecting them with local intermediaries. The role of these intermediaries (advisers, brokers, lawyers, etc.) is crucial, not only to successful issuance but to the accumulation of greater transaction experience and momentum in the local market. We do not act as an adviser to the issuer, but assist throughout the process in a "hand-holding" role. A successful issuance is one which maximises the participation of local investors.

Secondly, we are able to fund specific deal costs through our technical assistance facility. This usually involves contributing towards the expenses of credit ratings, legal support, reporting accountants and other service providers. This is designed to reduce some of the perceived transaction costs and barriers to coming to market.

Thirdly, and most visibly, we act as an anchor investor in the bond issuance. This provides confidence to the issuer that they will be able to meet a minimum amount of their funding need if they come to market. It also gives comfort to local investors that a sophisticated international investor has completed due diligence and has appetite to invest.

Our key requirement is that there is local participation in the bond. We generally aim to be less than 30% of a bond program, so we can anchor a first-time issuance to the tune of 50% or 60%, so long as we have confidence that the company will come back to market and issue further tranches. We have proven this in a number of cases. Overall, for every $1 we have deployed in private and listed bonds, there has been more than $10 invested by other institutions, usually pension funds, insurance companies, banks and asset managers. Ultimately we are successful when an issuer no longer requires our support as an anchor investor!

As local currency investors, we are assisting companies to reduce their foreign exchange risk and other balance sheet risk. Some of our clients have been able to reduce the FX liabilities from 80% to 0% through local bond issuance. Crucially, we "price to market" – i.e. local investors set the price. Since local investors do not price risk in the same way as offshore investors (particularly country and political related risks), local funding is generally cheaper on a like-for-like currency basis. Companies do not have to exclusively fund themselves through bonds, but building relationships in their own markets with local investors should be more sustainable long-term and allow them to diversify their funding sources.

***CAPMARKETSINAFRICA:*** *What sectors do you have appetite for? What opportunities do you see?*

**JAMES DOREE:** Our mandate covers microfinance and SME lending, housing, renewable energy, agriculture, healthcare and education. In reality, most of our deals to date have been financial institutions, including micro-lenders, leasing companies and mortgage providers. However, we are actively working on opportunities across these sectors.

*"As local currency investors, we are assisting companies to reduce their foreign exchange risk and other balance sheet risk. Some of our clients have been able to reduce the FX liabilities from 80% to 0% through local bond issuance."*

There is great potential in affordable housing, which inherently needs long-term local currency funding and is hugely reliant on functioning financial markets to ensure affordability. Traditional mortgage lending models are being tailored to local conditions, through micro-mortgages and home-building mortgage products. Microfinance institutions are increasingly offering incremental finance for housing. Rent-to-own mortgage finance is particularly tailored towards lower income groups seeking to build wealth through their home, but without the resources required for a traditional mortgage. The capital markets can play a vital role in channelling liquidity and long-term funding into these sectors.

The ALCB Fund anchored the first bond issued by CRRH, the regional mortgage refinancing company for the UEMOA region. We have invested in the MTN Program of innovative mortgage lenders such are Zambian Home-loans. Going forward, we are considering an anchor investment in a new mortgage liquidity warehousing facility in Nigeria, to complement the role of NMRC in that market. We're also considering corporate bonds for successful housing developers.

Furthermore, there are various innovative models emerging to provide renewable energy to African households and companies. While utility-scale renewables projects are financed by DFIs in hard currency in most markets, the other approaches to energy access have a clear need for local currency. Household-level off-grid solar, often on pay-as-you-go models, has a significant need for local currency funding and has many parallels with the microfinance, SME and leasing sectors in the past. Similarly, commercial and industrial solar can mobilize local funding through securitization structures. Also, eventually, there will be opportunities to refinance larger projects through capital markets instruments (project bonds, portfolio securitizations, credit linked notes), an opportunity we are already exploring in South Africa.

***CAPMARKETSINAFRICA:*** *What challenges do you face in pursuing this mandate, and how do you go about overcoming these?*

**JAMES DOREE:** Firstly, intermediation – that is the promotion of the capital markets and deal-flow by investment banks, corporate finance advisers and brokers – needs to become much more proactive. Hopefully we can assist such intermediaries by acting as a trusted partner and anchor investor. Secondly, standards of documentation need to improve greatly, particularly for deals involving security. We provide input from international lawyers to bond documentation to ensure that local investors benefit from international best practice. Thirdly, the capacity and experience of regulators needs to focus much more on the needs of the market and offering transparency to stakeholders.

Currently, regulators see their role as a sort-of "credit committee" for the market, rather than as overseeing compliance and disclosure procedures. We hope to be able to use technical assistance to assist regulators with streamlining their listing requirements. Fourthly, credit capacity and analysis among investors varies significantly. In many countries, there is no "credit culture" whatsoever, with investment decisions based on name recognition and familiarity. By increasing deal-flow, promoting credit ratings and undertaking detailed and robust due diligence, we hope to improve standards and create a virtuous circle in the capital markets.

*"CRRH is a specialist financing facility set up to channel long-term funding into regional mortgage markets by refinancing the mortgage portfolios of member/ shareholder banks of the West African Monetary Union. It provides valuable liquidity to multiple mid- to small-sized commercial banks providing property and housing loans across francophone West Africa."*

***CAPMARKETSINAFRICA:*** *Thank you very much for granting this interview!*

# PROVIDING CERTAINTY AND SAFETY TO OUR HUMAN CAPITAL IN AFRICA

By **Nicol Mullins,** Principal Consultant, Mercer, South Africa

*The eyes of the world are on Africa and more so the Capital Markets of Africa. Like much of Latin America, Africa has faced its fair share of problems when it comes to stubbornly high inflation and currency volatility. Rapidly rising inflation and the subsequent depreciation of currency cause uncertainty, which in turn affects productivity and brings risk to the business. This poses a risk to our human capital. This article summarizes survey findings of the responses of affected employers in Africa, and gives recommendations to employers across emerging markets who are contending with similar macroeconomic conditions.*

Milton Friedman, a Nobel Prize-winning economist, famously wrote, "Inflation is always and everywhere a monetary phenomenon." Based on this premise, the knee-jerk reactions of many employers in the face of inflation— what increase should we provide to our employees? How is the market reacting? What are our peers doing?—will only compound the problem. As inflation is often triggered by currency volatility, which is hard to predict and contain, our surveys indicate that a more measured response is more appropriate.

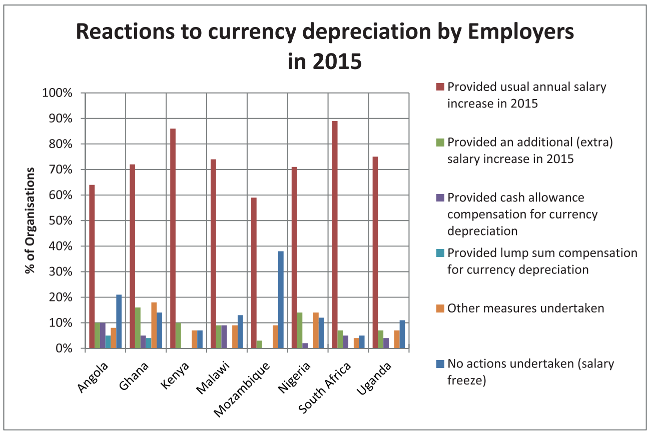
We have closely studied how employers in Africa have reacted to these conditions, collecting market data during our 2016 Africa Depreciation Surveys as well as spot polls conducted in several African countries in 2015. The participants consisted of multinationals and leading large local national employers in several African countries, with a focus on countries experiencing currency volatility and high inflation. We assessed a range of reactions to these conditions, including keeping salary increases the same, providing extra salary, giving cash allowances, giving lump sum compensation and doing nothing (freezing salaries).

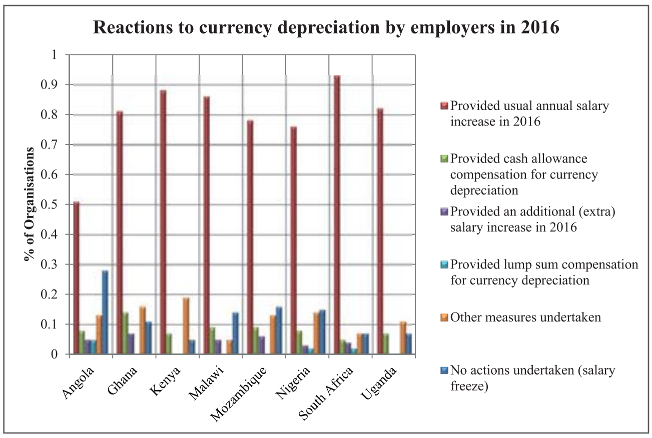
### Employer responses to inflation in Africa, 2015-2016

Most employers did not respond to inflation and the subsequent effect on local cost of living by providing out-of-cycle increases or by increasing cash allowances and benefits; the most prevalent response by employers in 2015 was to increase salaries as normal.

According to Mercer Africa Total Remuneration Survey 2017, most employers provide salary increases in the first part of the year. Therefore, for most employers, the salary increases which were given in 2015 did not take into consideration the major depreciation of the various currencies in 2015. Ghana stood out from the crowd, with 10% of employers—the highest figure among the countries surveyed—providing cash compensation for currency depreciation.

To put this data into context, consider the same companies' responses in 2016. The assumption is that the previous year's inflation would have had time to significantly impact local purchasing power, prompting more extreme employer responses. However, we see that most countries continued to provide the usual salary increases.

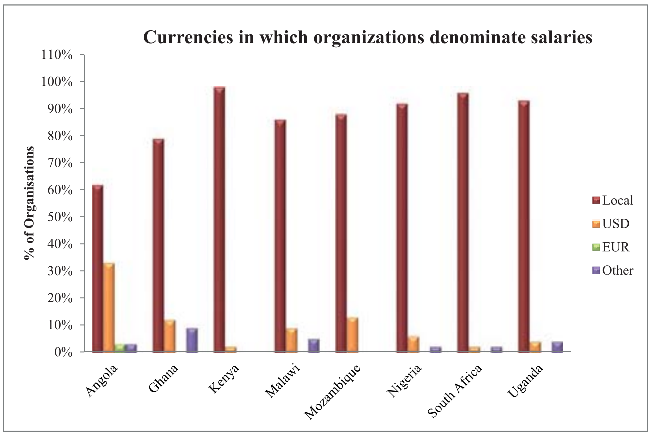



It is clear that not all countries' inflation is equally affected by the depreciation of its currency. An example is the South Africa. The South African Rand depreciated almost 40% within 12 months by January 2016 had, yet its inflation has stayed fairly consistent. In contrast, the Mozambique Metical had depreciated over 40% and inflation has increased by almost 15% in 12 months, from 8% in January 2015. Thus employers are responding more to inflation, or increased cost of living, than depreciation of the local currency.

When considering how companies planned to respond in 2016, the major vehicle used to tackle the depreciation of the local currency (and the possible impact on the local cost of living) is once again the annual salary increase. In most cases, employers are very hesitant to increase any existing cash allowances and even more hesitant to provide new cash allowances. Ghana stands out again, with 14% of employers planning a cash allowance to compensate for the currency depreciation in 2016.

Another possible approach for employers is to change the currency used to calculate salaries from the local currency to a foreign one, typically the US dollar (USD).




Most employers calculate and state their employees' salaries in the local currency. With local currency depreciation has come renewed pressure from employees to have their salaries denominated in a foreign currency, specifically USD. However, not many employers planned to make this change in 2016. In fact, some companies that had calculated salaries in a foreign currency planned to change it to their local currency. An exception is Angola, which has a relatively high number of companies (33%) calculating salaries in a USD, compared to South Africa and Kenya (2%).

## Recommendations for employers

*Respond to labor markets, not currency markets, when deciding salary*

Globally, many countries have dealt with high inflation and depreciating currency by setting budgets based on "inflation plus a bit." If you typically follow this practice, what will your organization's response be when inflation hits 30%, 40% or 50%? Will you still align to the local inflation rate? In economic terms, we need to look at the supply and demand of skills in a particular market. This is what determines the market value of jobs, rather than inflation, depreciation, devaluation or the cost of living.

*Respond, don't react, to inflationary and currency risk*

For all companies, inflationary and currency risk can be dealt with in various ways. For starters, there is a difference between reacting and responding to risks. A reaction is typically a quick decision driven by emotions in response to a tense situation. Responding, on the other hand, is a well-thought-through decision based on evidence.

Designing a framework for decision-making when there is certainty, clarity and, most importantly, time, makes this response possible in times of crisis. A pro-active approach also provides sufficient time for stakeholder buy-in and sign-off so that the response is clear, concise and considered. Risks will always be present, but how well an organization is prepared for them makes the difference. Planning a response in advance can help to proactively mitigate uncertainty, whatever form it takes.

*Adopt a "wait and see" approach*

Currency depreciation and high inflation is a macro-economic phenomenon over which the employer and employee have little to no control. Most employers have adopted a "wait and see" approach, using the annual salary increase as their primary tool to address increases in the cost of living, while calculating salaries in the local currency. We believe that an organization's line of sight should always be on future sustainability, rather than short-term fixes.

*Implement a framework*

We recommend that companies with multiple offices in Africa and around the world deal with currency depreciation by designing a proper framework. This framework guides the employer's reaction in various depreciation severity scenarios. A systematic approach helps to ensure that the response is objective, rather than emotional, as well as that it is based in correct metrics and applied equitably across various offices.

With careful planning, an eye on the labor market, and a solid framework, organizations in Africa and across emerging markets can prepare themselves to respond to any change in the economic climate.

**Contributor's Profile**

Nicol Mullins has a passion for people and numbers. As a Principal Consultant in Mercer's Career line of business his role encompasses project management, delivery and implementation across industry segments in 39 sub-Sahara Africa countries. He has extensive knowledge and insight to compensation & benefits trends on the African Continent and has written articles on this for the Africa Reward Association. He has guided and supported clients in the implementation of agreed pay structures and policies by analyzing their remuneration philosophy, guiding where none is in place, and implementing changes.

# THE USE OF INFLATION LINKED STRUCTURES IN SOUTH AFRICA

By **Alastair Campbell,** Managing Director, Vantage Capital Fund

## Introduction

The structuring of financing packages that make increasing use of inflation linked debt, also known as CPI-plus debt, is a relatively new trend in South Africa. It has in many respects derived from the highly competitive nature of South Africa's Renewable Energy IPP procurement program (REIPPPP) which has forced the developer market to rethink their funding strategies to come up with ways to make their bids into REIPPPP more competitive.

To put the level of competition into perspective, REIPPPP has been through six bidding windows over the last five years. 460 bids have been received in total, comprising 27.6GW of capacity or approximately R800bn ($60bn) of foreign direct investment into South Africa. 102 of these bids, comprising 6.376GW of power were awarded preferred bidder status. The total investment comprises R194bn ($15bn) of foreign direct investment. From an electricity tariff perspective, the average tariff in the first bidding window was R3.65/kWh for solar photovoltaic and R1.51/kWh for wind. This has come down to R0.62/kWh for both solar photovoltaic and wind respectively in the most recent bid window.

Part of this precipitous drop in tariffs can be attributed to the drop in both the cost of equipment and construction contractor costs. The majority of the drop is however due to the increasingly competitive nature of the process. To achieve these low tariffs bidders have had to make a number of innovative changes to what has traditionally been a fully wrapped construction contract which is banked against a conservative debt and equity package with gearing levels of about 70%.

The current trend is that construction contracts are now structured as split contracts (i.e. they are not fully wrapped), gearing levels have increased to about 80% and some of the debt service covenants have been relaxed. In addition, in the last three bid windows, a number of bidders have recognised the benefit of using CPI-plus debt. The main attraction being that it has a back-ended repayment profile.

### CPI-plus debt in South Africa

CPI-plus debt first made an appearance on the South African scene when the first toll-road public private partnerships ('PPP's") came to market in the mid 1990's. CPI-plus debt wasn't a nice-to-have, it was necessary because the toll-roads were unable to generate sufficient revenue in the early years of operation to cover their debt service obligations.

CPI-plus debt is usually provided by both commercial banks and debt funds who's typical investor base comprises pension and provident funds. Prior to the commencement of the REIPP procurement process there were very few pension and provident funds that were prepared to lend to projects that were structured as project financings. This was primarily due to the long construction times and an unwillingness on the part of these organisations to take construction risk. Their preference was to acquire debt in the secondary market once a project had been de-risked – i.e. after construction was complete and the plant was fully operational.

One of the things that will impact the growth of the availability of CPI-plus debt is a regulatory constraint – specifically Basel III. Should Basel III eventually get promulgated in a form that is similar to that currently being contemplated, then it is likely that the universe of CPI-plus debt providers will shrink as Commercial banks will find it difficult to provide the product. It will be left to debt funds as the sole providers of this product. There are two reasons for this.

The first is that the commercial banks typically fund themselves off Jibar and then swap that JIBAR debt into CPI debt using a derivative product. Under Basel III, the capital requirements for long-dated derivatives are punitive and so it will force the pricing of commercial bank CPI-plus debt upwards.

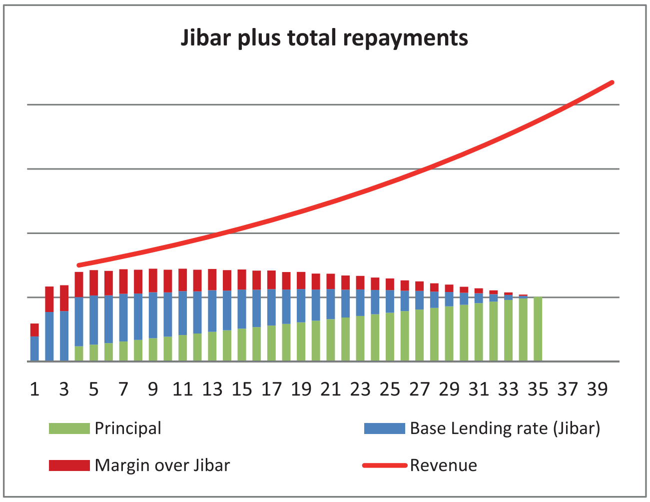
The Second is that under Basel III, commercial banks will find it difficult to provide long-dated debt to borrowers as the match-funding requirement under Basel III will also force the banks to set aside a considerably larger amount of capital to provide the loan. This factor will also force the price of commercial bank CPI-plus debt upwards
Pension and provident funds on the other hand are not governed by Basel III and so going forward, it is likely that commercial banks will only provide CPI-plus debt to the market if (i) there is a pre-agreed take-out from a debt provider that isn't caught by Basel III legislation (such as a debt fund), or (ii) the commercial bank has a pre-ordained distribution vehicle set up to take on the debt once the projects have been de-risked and are operating successfully.

Both of these market developments have already started to take place in the South African market.

### Reasons why CPI-plus debt is attractive

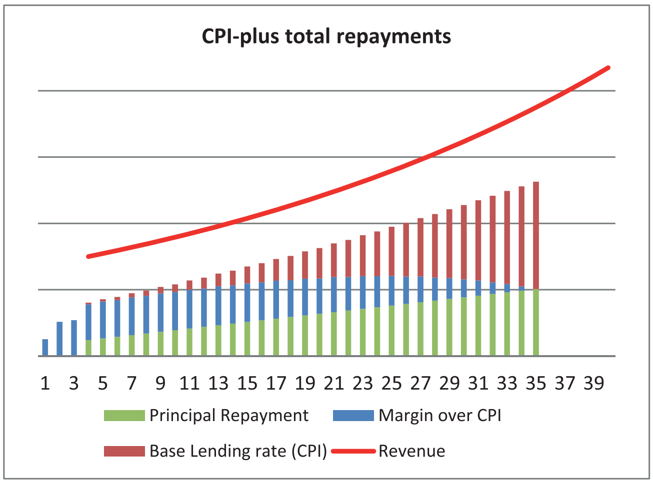
The typically back-ended CPI-plus loan repayment profile is attractive for two reasons. The first is that it front-ends the equity returns earned by the shareholders and the second is that the debt repayment profile more closely resembles the revenue profile of the projects in question. This is because REIPPPP projects earn income through a tariff that is increased each year by inflation (In this case the index used is the annual Consumer Price Index ("CPI") adjustment). Expressed graphically the revenue profile vs the debt repayment profile on a typical REIPPPP project will look something like the following:

**Jibar plus loan**




This loan repayment profile assumes that the real principle repayments are sculpted to achieve an annuity style instalment profile. The total interest paid comprises the Base Lending Rate (Jibar) plus the Margin over Jibar. What the graph illustrates is how, with a traditional Jibar-plus profile, debt service covenants come under pressure in the earlier years.

The following **CPI-plus** graph has an identical real principle repayment profile to the Jibar-plus loan.




The difference between the two profiles can be seen quite clearly; the inflation component (in red) is accrued over the life of the loan in the same way as the Jibar-plus loan, but it is only paid later - on a pro-rata basis across the remaining principle repayments.

When expressed graphically, it becomes clear why CPI-plus debt is attractive to the developers of REIPPPP deals, particularly when they are involved in a competitive tender process. Not only is the debt service amount lower in the earlier years, but the CPI-plus debt also provides a natural hedge to the developer as revenue and debt service will go up or down in line with each other as the official CPI level goes up or down.

### Conclusion

The REIPP procurement program in South Africa has been an unambiguous success. Unlike traditional feed-in tariff processes where bidders simply compete against each other for a MW allocation at a pre-agreed tariff, REIPPPP effectively changed the global game in the renewable energy sector. Its success has won many plaudits around the world and many other countries have started to replicate the process at home.

In addition to the procurement of cost effective electricity for South Africa, one of the unexpected benefits to come out of the REIPP procurement process has been the emergence of CPI-plus debt as an important part of the financing structures being bid in the process. If anything, the REIPP procurement process has accelerated the establishment of an alternative lending product in the local market.

Further, the fact that pension and provident funds are now prepared to invest in debt funds that come into transactions at financial close provides further evidence of the rapid maturation of the pension and provident fund investor base which now has appetite for both construction risk and primary lending risk. From a South African debt perspective, this is all very positive news.

### Contributor's Profile

Alastair Campbell is the Managing Director of the R2.1bn Vantage GreenX sustainable energy debt fund. He joined Vantage GreenX in January 2014. Note I is now fully invested and the R2.9bn Vantage GreenX Note II closed at the end of 2016.Prior to joining Vantage GreenX, Alastair headed up the Power Finance team within Standard Bank, where he successfully oversaw the funding of more than R15bn of debt to 15 wind and solar projects in bid dates 1 and 2 of the REIPP procurement program. Over the last 20 years he has worked on projects in various sectors and countries on the African continent in both an advisory and arranging capacity.

Alastair is a chartered accountant and graduated with a B.Comm from the University of Cape Town. He completed his articles at Deloitte and Touche in Johannesburg and moved to London where he worked for NatWest Markets before joining the Standard Bank London in February 1997. After a number of years working on projects in Africa, Eastern Europe and Latin America, he moved to Johannesburg in 2003 to join the Mining Energy & Infrastructure team within the Corporate and Investment Banking division of Standard Bank, and most recently moved to Vantage GreenX to run their renewable energy debt fund.

# REALITIES AND OPPORTUNITIES IN KENYAN REAL ESTATE

By **Nancy Murule,** Research Analyst, Cytonn Investments Management Limited

Kenya's economy has recorded strong growth over the last decade with the country recording an average GDP growth rate of 5.4% over the last five years, faster than Sub Saharan Africa average of 4.2%. Underpinning this growth has been a robust real estate and construction sector whose contribution to GDP has increased from 10.5% in 2000 to 13.8% in 2016. The volumes have even been larger with approvals increasing at a 5 year Compounded Annual Growth Rate (CAGR) of 22.9% to Kshs 308.0 bn in 2016 from Kshs 135.0 bn 2012. In this article we take a closer look at the real estate environment in Kenya. We start by exploring the factors driving this growth, the challenges facing the sector, the performance of various real estate sector themes in 2016, and identify the opportunities, then conclude by giving an outlook for the real estate sector.

## Factors Driving Real Estate in Kenya

Demographic Trends: Demographic trends such as rapid population growth at 2.6% p.a., urbanization rate of 4.4% p.a., the growing middle class, increasing disposable income and the youth bulge (21-35 years) has created demand for real estate products, with developers and investors working towards fulfilling their housing and lifestyle needs thus boosting the performance of residential and retail real estate themes.

*High Returns:* Over the last five years, real estate has consistently outperformed other asset classes generating average total returns of above 25.0% against a 5year average of 10.5% for traditional asset classes hence attracting investors and leading to the growth of the sector.

*Improvement in Infrastructure:* Infrastructural development has led to opening up of new areas for development e.g. along the Northern Bypass, Eastern and upcoming Western Bypass and the Dongo Kundu Bypass. The LAPPSET Corridor, The Standard Gauge Railway (SGR), expansion of airports and seaports, Special Economic Zones, sewer lines and mains water & power connections are all opening up Kenya to real estate development and will lead to increased development along the hubs in areas such as Ruiru, South Coast Kenya, Ruaka, Kikuyu, Lamu, Kisumu, Athi River and Marsabit.

*Growing Businesses and Entrance of Global Brands Locally:* Growth in the Small and Medium Enterprises (SME) segment as well as establishment of regional and continental offices in Kenya by global brands such as Bechtel, Johnson and Johnson, Boeing and Power China are leading to an increase in demand for office, retail and industrial real estate themes as well as residential units to house the incoming population.

*Devolution:* Devolution has opened up major towns across the 47 counties by attracting government institutions, private investors and entrepreneurs across all the counties headquarters. This has created demand for various real estate themes such as residential units, offices as well as demand for land.

*Domestic and MICE Tourism* – Increased domestic tourism as well as the growing Meetings, Incentives, Conferences and Exhibitions (MICE) tourism driven by improved security, growing businesses as well as county governments are greatly supporting the growth of hospitality industry.

Government Policies and Procedures: Various policies such as reduction of the corporate tax from 30.0% to 15.0% for developers constructing more than 400 affordable housing units per year, land administration reforms such as the waiver of the title search fees as well as digitization of procedures at the land ministry to enhance transparency and efficiency, have all been incentives for real estate developers to invest further in the sector.

## Challenges facing the real estate sector in Kenya

*High Land Prices and Construction Costs-* Land prices have increased exponentially at a 5 year CAGR of 19.4% between 2011 and 2016 in Nairobi Metropolitan Area, making it expensive to acquire land for development. This coupled with high costs of construction and financing as well as poor infrastructure in some areas have made it almost impossible to deliver affordable housing as well as units in other real estate themes. This trend have been experienced in major towns in the country.

*Difficulty in Fundraising for Developments* – The capital intensive nature of real estate development makes it difficult for developers to fundraise especially in the current challenging operating environment characterized by reduced lending by banks following the implementation of the Banking Amendment Act 2015, which stipulates the loan and deposit pricing framework. The law has resulted into a decline in credit growth to private sector, which slowed to 4.0% in the first quarter of 2017, way below the government target of 18.3%.

*Political tension-* Investors have adopted a wait and see stance as a result of elections scheduled for August 2017 hence a reduction in transaction volumes in the market.
Inadequate Infrastructure: Despite increased infrastruc-

tural development, large parts of the country have inadequate infrastructure with inaccessible roads, lack of sewerage, water supply and electricity making them unattractive for settlement. For a developer to successfully sell, they have to invest heavily in infrastructure which greatly reduce their margins.

## Real Estate Market Performance and Opportunity in Kenya

While the real estate market in Kenya has delivered high returns, these vary depending on location and themes as discussed below:

*Commercial Office:* After exponential growth over the last five years, the sector has slowed down mainly driven by increased supply, with office space completions increasing at a 4 year CAGR of 52.5% between 2012 and 2016 from 1.2 mn square feet in 2011 to 6.5 mn square feet in 2016. In 2016, the sector recorded average rental yields of 9.3% at 88.0% occupancy. Opportunity in the sector lies in Grade A offices in prime office nodes, which have the highest returns of 10.0% yields and in differentiated concepts such as serviced offices which also have attractive returns with average rental yields of 13.4%

*Residential:* Residential remains one of the most attractive real estate theme for investments in Kenya largely driven by high demand as a result of growing population and huge housing deficit estimated by National Cooperative Housing Union (NACHU) to be 2 mn units and growing by over 200,000 houses annually. The sector had average rental yields of 6.0% in 2016 at 83.6% occupancy. The opportunity in the sector is in the low to middle income segment which has the highest level of housing deficit.

*Retail:* The retail sector is rapidly growing with the mall concept overtaking the traditional small scale retail stores. Evidenced by the recent mall developments such as Two Rivers, Garden City and The Hub, which have increased the mall supply by a 24.3% CAGR over the last five years from 2.3 mn square feet in 2011 to 5.5 mn square feet in 2016. In 2016 the sector recorded average rental yields of 10.2% and an average annual occupancy of 89.3% with the average rental yields averaging 10.0% in Nairobi. Higher vacancies are however being witnessed in 2017, raising fears of oversupply in Nairobi which has approximately 90.0% of the formal retail supply in the country. The opportunity in the sector is therefore in Nairobi's Satellite Towns and county headquarters which have been attracting the middle class population.

*Industrial:* The industrial sector has started to pick up after sluggish performance over the last 5 years driven by (i) an increase in multinational firms and growing SMEs, (ii) demand from shippers who require facilities for temporary storage of cargo before distribution or onward transit, (iii) demand for warehouse space by landlocked neighboring countries that rely on Kenyan ports, and (iv) the rise of e-commerce, which has created demand for storage space for distribution centers. There is an undersupply of grade A warehouses with specialized facilities, sufficient height which are mechanized. In 2016, the sector had average rental yields of 5.8% and occupancy rates of 85.0%. The opportunity in the sector is in prime grade A warehouses and also in serviced land for industrial development.

*Hospitality:* The hospitality sector picked up in 2016 following the 4 year slow down from 2012 caused by the level of insecurity. In 2016, the number of tourists arrivals into the country increased by 16.7% from 752,073 in 2015 to 877,602 in 2016. Driven by improved security and an increase in the MICE segment with a number of global conferences, which were held in the country such as TICAD IV, Global Entrepreneurs Summit and the World Tourism Organization (WTO) Ministerial Conference. The average daily rates for hotels in the country was Kshs 21,200 in 2016. We expect the improvement in performance to be sustained in the long run due to the improving security situation as well as extensive marketing efforts by the Kenyan government. Opportunity in the sector lies in 3 star hotels in Maasai Mara, 4 star hotels in Nairobi and in serviced apartments which are growing in popularity due to their affordability and home away from home feel.

**Real Estate Returns in Kenya 2016**

| Theme | Yields | Occupancy |
|---|---|---|
| Retail | 10.0% | 89.3% |
| Commercial Office | 9.3% | 88.0% |
| Residential | 6.0% | 83.6% |
| Industrial | 5.8% | 85.0% |
| Average | 7.8% | 86.7% |

- *Real estate delivered high returns across all themes in 2016 with rental yields on average at 10.0% in retail, 9.3% in commercial office, 6.0% in residential and 5.8% in industrial*
- *The sector had total average returns of 25.8% (yield 7.8% + capital appreciation 18.0%)*

**We have a positive outlook for the real estate sector in Kenya driven by the huge housing deficit, increased infrastructural development, improving legal climate and increased the institutionalization of the sector. The sector's performance will however be constrained by inadequate infrastructure, high land and construction costs, as well as political uncertainty in 2017, which may slow down the activities in the real estate sector the short term.**

**Contributor's Profile**

Nancy Murule serves as a Research Analyst at Cytonn Investments Management Limited, having graduated from the Cytonn Young Leaders Program (CYLP). She has 2 years' experience, focusing largely on research and deal origination in the real estate and private equity markets in Kenya. Nancy holds a BSc. in Actuarial Science with IT from the Maseno University and is a candidate in the CIFA Programme Section IV. She has participated in the publication of several real estate reports including; Kenya Office Market Report, Kenya Retail Space Report, Kenya Hospitality Sector Report and Kenya's first Mortgage and Affordability Index Report.

# HEDGE FUNDS: UNVEILING THE MYSTERY

By **Devin Forbes,** Investment Analyst, Citadel Asset Management

Hedge funds remain a mystical financial tool to the average investor, perceived to be used only by high net worth individuals or an elite group of investment professionals. This is especially true as the modern day reference to hedge funds are eccentric high educated individuals investing in financial instruments unknown to the average person. However, hedge funds are becoming an increasingly important part of investment portfolios, especially given the increase in regulatory requirements within South Africa in particular. Explaining the various hedge fund strategies and unpacking the benefits will hopefully provide investors with a new perspective on hedge funds and remove any misconceptions.

Simply put, hedge funds are alternative investment vehicles that may use a variety of strategies and financial instruments to earn returns. At first glance this is not vastly different than your average equity mutual fund, however hedge funds typically use a number of financial instruments including derivatives on a variety of asset classes. Many hedge fund managers make use of derivatives – such as swaps, options, futures and contracts for difference (CFD's) to either enhance or hedge their portfolio. This is typically the point where investors get confused as to what exactly are these instruments and how they are implemented. It is important to note that the majority of hedge fund managers make use of typical mutual fund instruments, while derivatives will then be used to add protection to their initial positions. This is why it is important to understand the type of strategy that a hedge fund manager implements as well as their parameters and overall investment objective. Within the hedge fund world there are many 'cowboy' type managers that make use of excessive leverage and implement naked (risky) derivative positions. It is thus crucially important to understand these types of managers and their respective investment objectives and how they implement their positions.

The most commonly used hedge fund strategy is the equity long-short strategy. This strategy makes use of your typical, general long equity positions as well as short equity positions. By making use of short positions (make a profit when the underlying asset price falls) it decreases an investor's net exposure to the equity market. This is an excellent tool to make use of especially if you require equity exposure within your portfolio but at the same time want to reduce your dependence on the direction of the equity market. A large proportion of long-short hedge fund managers make use of pair trades (one long position vs. one short position) to profit from relative value deviations between two stocks.

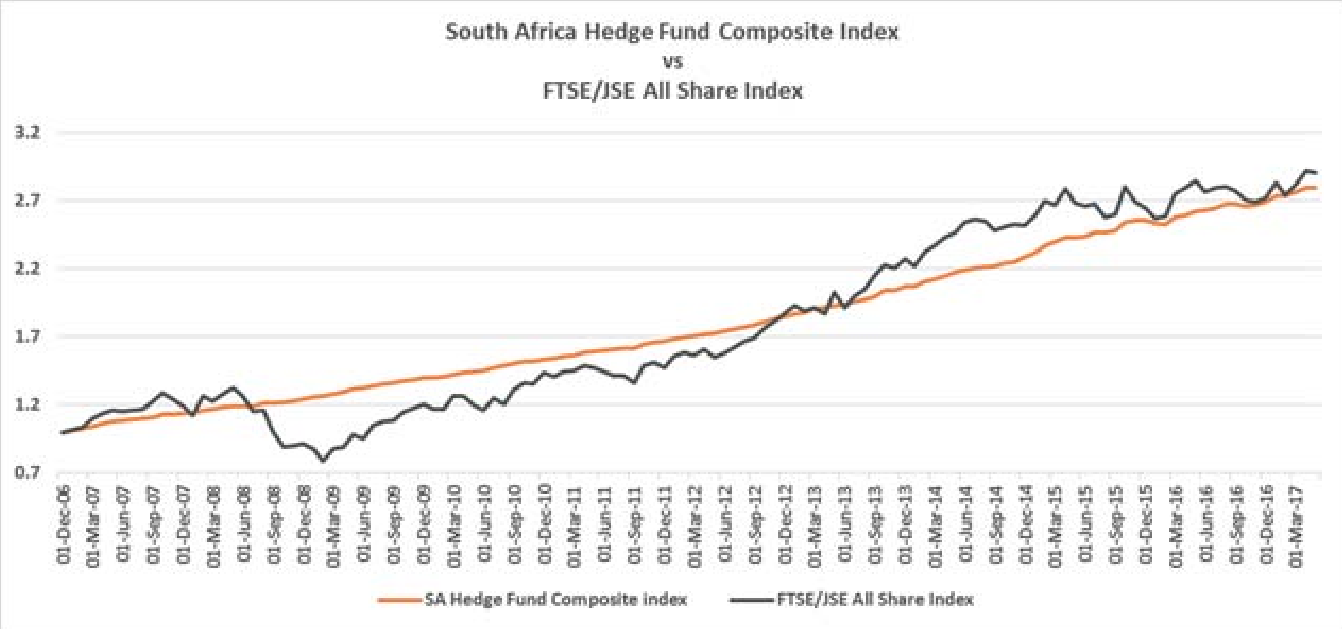
Another strategy implemented by hedge fund managers is equity market neutral. Similarly to equity long-short, they aim to derive their returns through the relative value between two assets. These hedge funds are run at extremely low levels of net exposure, further reducing an investor's dependence on broad equity market returns. Importantly, hedge funds use similar valuation and fundamental research tools that are used by mutual funds but have more freedom to implement their investment ideas with a variety of different instruments.

Fixed income hedge funds are also widely implemented in South Africa. These hedge funds have a large investment tool box such as bonds, bond futures, forward rte agreements (FRA's), interest rate SWAPs and credit default swaps (CDS) which can be used in a variety of ways.

Hedge fund strategies can also extend into soft and hard commodities, property, as well as event-driven and macro hedge funds (look to profit from economic and/or political changes) to name a few. Similarly to a multi-asset mutual fund where investment managers can pool together various asset classes, hedge funds have multi-strategy funds which make use of two or more strategies that are mentioned above. This increases diversification as well as reduces correlation to broad financial market indices.

Each hedge fund strategy can make use of hedging through many different avenues. As financial instruments and financial markets are largely connected in one way or another, many managers would gain initial equity exposure for example and then hedge their exposure via a completely different asset class. This can provide a unique risk-return profile which is uncorrelated to financial markets in general. Within each strategy, managers have different styles that are implemented to achieve various investment objectives. It is thus important to look for a hedge fund most suitable for your portfolio which is correctly aligned to your risk profile as well.

The above hedge fund strategies are an example of how managers can make use of a variety of investment tools to provide uncorrelated returns. Most hedge fund managers also achieve lower drawdowns relative to equity markets especially given the tools at their disposal and the constant focus on risk management.




The above graph illustrates the returns of the South African hedge fund manager composite index compared to the FTSE/JSE All share Index (broad equity market). In terms of downside risk and drawdowns, the hedge fund composite index has done exceptionally well to remain consistent especially during the global financial crisis of 2008. This is even more impressive if the investor in question is continuously withdrawing from their portfolio as hedge funds can reduce the risk of having to withdraw at the bottom of a market cycle.

*"The most commonly used hedge fund strategy is the equity long-short strategy. This strategy makes use of your typical, general long equity positions as well as short equity positions. By making use of short positions (make a profit when the underlying asset price falls) it decreases an investor's net exposure to the equity market."*

South Africa recently changed the hedge fund regulatory structure with all hedge funds now being required to register as collective investment schemes. Qualified Investor Hedge Funds are funds that require a larger amount of capital investment or require investors to have a certain level of investment knowledge. Retail Investor Hedge Funds have become more accessible to the general public with lower capital requirements and limitations on leverage and value at risk. This is a step in the right direction for investors looking for hedge fund exposure as the industry is now more accessible than before.

The details above attempt to remove the negative stigma attached to hedge fund managers and explain the benefits of adding hedge funds to your portfolio. While there are a number of 'cowboy' type investment managers, the majority of South African alternative investment managers structure their hedge funds as risk management tools. Unknown investment instruments and complex jargon used by hedge fund managers can be perceived as 'risky' but, with a deeper look into the hedge fund world, derivatives are mostly used to protect a portfolio. Recent regulation chances especially within South Africa have made these investments more accessible to the average investor, increasing your investment universe and hopefully reducing the mystery associated with hedge funds.

*"Hedge funds remain a mystical financial tool to the average investor, perceived to be used only by high net worth individuals or an elite group of investment professionals. This is especially true as the modern day reference to hedge funds are eccentric high educated individuals investing in financial instruments unknown to the average person."*

**Contributor's Profile**

Devin Forbes joined Citadel Asset Management in 2016 as a Junior Investment Analyst, covering hedge fund research and monitoring. Devin completed his B.Com Honours in finance and investments at The University of the Western Cape in 2015 and is currently enrolled in the CFA programme.

# WHEN LOW ECONOMIC GROWTH BECOMES BOND BEARISH

By **Wikus Furstenberg,** Portfolio manager, Futuregrowth Asset Management
**Olga Constantatos,** Credit & Equity Process Manager, Futuregrowth Asset Management

In a textbook world, an economic growth rate below a country's potential growth rate would lead or at least contribute to a lower rate of inflation. In turn, this may open the door for a decrease in the official short-term policy interest rate; one of the main tools used by monetary authorities to boost economic growth in an environment of lower and stable inflation. The implication of this for nominal fixed rate bonds is positive since this market tends to be forward looking and would start pricing a lower policy interest rate in advance. In other words, since current long-dated bonds tend to price the future level of the official short-term interest rate, stronger demand for these instruments would boost its price and lead to lower yields. As a matter of fact, a well-developed bond market would tend to respond way in advance to monetary policy changes by even anticipating lower economic growth as it takes its cue from various short-term economic activity indicators, such as monthly retail sales, etc.

### The South African bond market

Getting back to the real world. Following a reasonable recovery post the 2008 global financial crisis, South Africa's Gross Domestic Product (GDP) growth rate has gradually slowed in an almost straight line and is currently caught at an annual rate of growth at levels hardly above 1%. Many different reasons are put forward as explanation, including so-called longer-term structural causes. Whilst the country experienced a period of what we would term mild stagflation (the combination of low growth and high inflation) until early this year, the rate of inflation has finally started to slow; thus some resemblance to our text book world. Unsurprisingly, the latest development served as the catalyst for many economic analysts and to some extent the forward interest rate market, to start calling for and pricing a reduction in the South African Reserve Bank's repo rate. These expectations are not unreasonable – under normal circumstances.

At face value, the nominal fixed rate bond and inflation-linked bond markets have behaved as expected at this point in the cycle. The JSE All Bond Index (nominal bonds) returned 4.9% for the first six months of this year. This is a reasonable, strong 10.5% when annualised. This compares favourably to the cash return of 3.2% (6.8% annualised). This implies that the bond market is indeed forward looking and pricing the text book outcome of looser monetary policy. Moreover, the JSE Inflation-linked Government Bond Index is lagging both nominal bonds and cash returns with a disappointing 1.0% (2.1% annualised) total return. This makes sense considering that falling inflation would induce the selling of inflation-linked bonds as the demand for inflation protection drops, causing real yields to rise.

We have reason to believe that the relative stellar nominal bond performance is unsustainable. Firstly, the strong global reach for yield most certainly contributed to the recent strong performance. JSE data shows that net non-resident purchases of South African rand denominated government bonds totals around R40bn for the first six months of the year (or about 30% of the South African government's annual long bond funding requirement). This helped to boost non-resident holdings to nearly 48% of total outstanding RSA government nominal bonds. In a way, the persistent global bond distortion caused by many years of very loose monetary policy continues to be a way out for emerging markets like South Africa with poor macro-economic management.

Secondly, although the newly-appointed Minister of Finance is doing his best to downplay risks to the previously carefully managed fiscal consolidation, it would take far more than a political undertaking to convince us that all is indeed well. We remain particularly concerned about the inability to lift the underlying economic growth rate to the much higher levels required. Persistent sub-trend economic growth and macro policy uncertainty have negative implications for fiscal consolidation. The first symptom of this will be missed tax revenue targets and we are not convinced that the political will is strong enough to reduce government expenditure sufficiently to balance the books. Moreover, the official nominal growth estimate used in the national budget process has already proved too optimistic relative to the latest expectations following a string of disappointing economic growth data, including GDP data for the first quarter of this year. The budget deficit will turn out worse than expected, in turn forcing National Treasury to increase the sale of new long-term bonds.

Strong negative sovereign rating downgrade momentum, caused mainly by sustained sub-trend economic growth as well as uncertainty about the fiscal outlook does not match the continued aggressive accumulation of local currency bonds by foreign investors. This mismatch continues to present a potential lethal mix for the local bond market. This time, the cycle will turn out to be different from a bond market perspective.

### Impact of low growth on the SA credit market

It is true to say that, in general, a low growth economy results in weaker credit metrics, higher earnings and cash flow volatility, reduced access to funding, constrained liquidity and higher funding costs as investors seek to be compensated for the increased volatility and lower certainty/predictability of company cash flows.

The first quarter of 2017 saw a flurry of listed activity with the market seemingly anticipating a turn in the cycle. Listed credit issuance of R40.6bn was up 92% compared with the fourth quarter of 2016 (R21.2bn) and nearly triple that of the first quarter in 2016 (R15bn). The largest contributor to this increase was the influx of financial sector issuances from R7.3bn to R20.9bn quarter-on-quarter. The driving force behind this was likely improved investor confidence post the ominous 2016 experienced and growing demand for high quality assets.

Financial sector issuance of R20.9bn comprised 51% of total issuance during the period (compared to 34% in the previous quarter).

State owned enterprises (SOEs) issuance remained fairly stable at around R5bn and comprised 13% of total issuance during the period (compared to 25% in the previous quarter). Development Finance Institutions were the key drivers of issuance during the period, with the Development Bank of Southern Africa issuing R1.5bn and the Land Bank issuing R1.9bn.

Corporate issuance improved by 56% during the period, from R6.4bn to R10bn and comprised 25% of total issuance during the period. Property company issuance made up the bulk of corporate issues in this period.

The securitisation sector comprised 11% of total issuance during the period (compared to 9% in the previous quarter).

Both the primary and secondary credit market saw spreads narrowing. Banking spreads compressed by an average of 20bps. A likely contributor was improving investor confidence post the seemingly ominous 2016 experienced and growing demand for high quality assets.

Following the president's cabinet reshuffle on 30 March 2017, Standard & Poor's and Fitch downgraded the SA sovereign rating to non-investment grade in April. In June, Moody's downgraded the sovereign rating to Baa3, one notch above non-investment grade. This had a knock-on effect on the credit ratings of a number of SOEs and banks.

### Market outlook

While the outlook for 2017 was relatively positive in the beginning of the year, market sentiment is currently unknown post the sovereign downgrade. Arguably, the market was partially anticipating a downgrade.

The impact of the downgrades is likely to be felt in a future weaker economy, higher inflation, less investment, higher unemployment, lower growth, lower tax revenues and reduced cash flows for social spending, all of which will impact negatively on credit assets and their general outlook. We are of the view that a deteriorating economic climate is a leading indicator for increased credit defaults. A possible mitigant is that for the last few years, many SA corporates have been reluctant to invest - these corporate balance sheets are in a relatively better position to withstand the ongoing volatility and uncertain economic climate than others.

A consequence of recent events may be that SA corporates will further adopt a "wait and see" attitude before committing to new investments. Furthermore, we expect issuers to be more cautious in their public offering resulting in a preference for private placements. These can be evidenced by three public auctions being postponed.

The impact on State owned enterprises (SOEs) is likely to be significant. Many rely on government finances for capital injections and in certain instances, both explicit and implied guarantees of their liabilities to lenders. The institutional weakening in many SOEs coupled with the weakening ability of the sovereign to support SOEs may lead to further credit downgrades for the weaker SOEs. Consequently, investors may start to demand a higher credit margin to compensate for the increased risks.

**Turning to the banking sector**, there are many key considerations when assessing the credit quality of a bank; these include profitability, capitalisation and liquidity. Our assessment of the impact of these follows:

- As a result of a stressed economy, we can expect pressure on banking profits in the medium term. This would be driven by squeezed margins and the impact of a weaker economy on the quality of the loan book.
- From a capitalisation perspective, SA banks remain well capitalised.
- From a liquidity standpoint, one of the consequences may be reduced demand from investors in bank debt (both local and international).

### Contributors' Profiles

**Wikus Furstenberg** manages a range of institutional and retail fixed income portfolios which include income, core bond and flexible interest rate funds. He manages the following retail funds: Old Mutual Income Fund, Namibia Income Fund, Namibia Enhanced Income Fund and the interest bearing component of the Old Mutual Real Income Fund. He also heads up the Interest Rate team at Future growth.

**Olga Constantatos** is responsible for the management of the credit and equity investment process, including managing the investment analyst team and ensuring that the credit and equity process generates good quality and high-yielding assets for our clients' funds. Olga was part of the Future growth team heading up the Credit Process from September 2009 to December 2012

# AFRICA, THE GREATEST FINTECH PLAYGROUND

By **Tanya Knowles,** Managing Executive, Fractal Solutions South Africa

When hearing about blockchain, one could almost imagine the likes of a FinTech company furiously working in Silicon Valley to bring this innovative technology to a first-world nation. However, this may not be the case.

Rather, Fintechs are looking to Africa as the place where their blockchain dreams can come to life to bring about societal change that could revolutionise the market. When it comes to disruptive technologies, blockchain aligns perfectly with many Fintechs' purpose to create a fundamental shift in the way the world does things. Since Africa has fewer legacy systems and infrastructures in place, it's no wonder the continent is seen as the best playground to develop benchmarks for other regions across the globe.

Within financial services, blockchain technology promises to bring trust to an untrusted environment, ensuring immutability, transparency, accountability, as well as lowering existing barriers to entry for the unbanked in Africa. It has caught the attention of many financial market players across the world.

Theoretically speaking, blockchain technology is a perfect fit for various applications across the financial markets. For the capital markets, there is massive potential to introduce more efficient mechanism to process transactions in a secure and transparent manner where settlement occurs in real-time without the use of third parties.

A distinction must be drawn between unpermissioned and permissioned blockchains. Unpermissioned blockchains, such as the Bitcoin blockchain, are accessible to any person, whereas permissioned blockchains provide restricted access. Most of the experimentation in the financial services and capital markets area has been with permissioned blockchains due to concerns relating to privacy and security in highly regulated markets. Where permissioned blockchains are being implemented, there is increasing recognition that an independent party may be required to administer the platform. This is often referred to as "the warden of the ecosystem" where an existing financial markets infrastructure, such as a Central Securities Depository, is well positioned to play such a role.

Blockchains offer benefits for regulators by providing easy access to fully traceable transactions that are available in real time. This could serve to enhance transparency and oversight, mitigating potential systemic risk. The aftermath of the 2008 financial crisis has shown how difficult it is to trace transactions and liabilities in the financial services area, given the complexities of products and ownership. Blockchain solutions could provide better insight into the origins and movements of financial assets.

Within South Africa, the country's Central Securities Depository, Strate (Pty) Ltd, has formed Fractal Solutions as a new division tasked with looking at blockchain and other technologies for the financial markets. While many industry players don't foresee the technology replacing the current capital markets ecosystem, there are instances where the technology is being used to replace processes within the system as a complimentary solution that adds value to clients.

As a starting point, Strate has partnered with its international counterparts to form a dedicated Working Group comprising some of the world's innovative Central Securities Depositories. These include Chile's DCV, Nasdaq (Nordic), Russia's NSD, together with Switzerland's SIX Securities Services and Strate. The Group has finalised what could be the Blueprint to an industry-wide accepted standard for an electronic voting solution using blockchain technology to manage annual general meetings. The envisaged solution will solve many of today's shareholder and issuer frustrations, by eliminating the current administrative and manual processes shareholders face when exercising their voting rights without attending the actual meeting.

At an international level, key parts of work have been presented to the International Securities Services Association (ISSA) and may define principles for an industry-accepted standard for e-Voting across the globe.

In addition, the SunExchange is a start-up that uses bitcoin to finance solar energy. Its website invites investors to buy solar cells and lease them to schools and businesses in developing nations. The SunExchange then arranges a monthly lease rental collection and distribution using the Bitcoin. The electricity generated by the solar installation can be repaid to the investor using Bitcoin wherever they are in the world. By using Bitcoin, it removes the friction and costs normally associated with international remittance.

*"Theoretically speaking, blockchain technology is a perfect fit for various applications across the financial markets"*

Beyond South Africa's borders, there's vast potential in other areas within Africa's financial markets where FinTechs have already shown success. BitPesa has become well known as a universal payment and trading platform in Africa. It provides an online platform to convert digital currency, such as bitcoin, into local African currencies to enable national and cross-border payments. BitPesa was the first company in the world to establish a market for Africa in respect of digital currencies. It lowered the cost of international payments by up to 75% and reduced the time to settle between currencies from 12 days to less than two hours. By facilitating seamless cross-border remittances, Bitpesa has offered a number of efficiencies and the potential for greater liquidity and more investor appetite.

Elsewhere, blockchain is addressing current challenges within the property land registration process by being the sacrosanct database required to store and distribute information between users. BenBen, a team of engineers, have dedicated themselves to improving Government Technology in Ghana using blockchain to connect all parties within a property transaction; the bank, the buyer, the seller and the Ghana Lands Commission, providing a central resource to access all relevant records (mortgage deeds, credit ratings etc.) instantaneously. It states that the system combats fraud by building a traceable history of land ownership and exchange, and helps to eradicate the current hold-ups in registering property titles, assigning new legal ownership and ultimately the release of funds by negating the need for each stakeholder to create their own separate online archives. This provides both an economic and effective solution.

One "shouldn't underestimate Africa bringing viable solutions to the market" that address socio-economic challenges across the continent.

That said, while 'the growing investment into Africa' isn't a new story, when you throw blockchain and distributed ledger technology into the mix, the story becomes far more interesting. Not only can FinTechs look at introducing new and unheard of solutions, but they can reignite older conversations to get older projects off the ground.

"The financial industry, has historically tried to get market-wide projects off the ground, such as a centralised Know Your Client (KYC). These projects have rarely taken off due to their complexities and costs of enabling market-wide change. Blockchain technology has reopened a number of these conversations, as the technology inherently supports the concept of a market-wide ecosystem and network effect." In addition, greater transparency and benefits of the technology could further mitigate fraud and risks for all market participants.

For blockchain to be an effective solution, the market would need to set up a minimum viable ecosystem where all stakeholders buy into the solution. While the integration of blockchain technology can be as challenging as traditional solutions, consensus needs to be reached with everyone.

However, investors of FinTechs looking at blockchain and distributed ledger technology need to be cautious. There is a lot of hype around disruptive technologies and many FinTechs are emerging as a result, but that's not to say those FinTechs will exist in a few years' time. The World Wide Web is 28 years old this year, and the Internet is 48 years, yet Google is only an 18 year-old company.

*"I encourage you to hedge your bets because those FinTechs of today might not be winners of tomorrow. We're still in the early stages and you could miss out in investing in the Google of this next era,"*

**Contributor's Profile**

Tanya Knowles is the Managing Executive of Fractal Solutions, a Division of Strate (Pty) Ltd. She has been with the company for 15 years and has successfully filled various Executive positions within Strate including Head of the Project Management Office, Strategy, International Relations, Marketing and Human Resources.

She was appointed the Managing Executive of Fractal Solutions, a new division established August 2016 with the mandate to drive exciting innovations within the company, such as Blockchain. Tanya holds a BA, PDM and MBA from the University of the Witwatersrand and Wits Business School.

# HOW ARE AFRICA'S BANKS PROTECTING THEIR DIGITAL CHANNELS?

By **Jolette Roodt,** Writer/Analyst, Entersekt, South Africa

Many African countries are undergoing what is called "financial deepening" – a process of increasing the banked population, improving market infrastructure, widening funding access, and diversifying investment options. According to Bernhard Kotanko and Jason Ekberg of the Nikkei Asian Review, efficient and deep financial markets are a prerequisite for macroeconomic growth and prosperity. Moody's also predicts that the fast growth of mobile banking across Africa, and the accompanying increase in access to financial services, will boost economic growth and create opportunities for banks to expand across the continent.

A large proportion of the African populace nevertheless remains unbanked. Penetration is as low as 36 percent in some of the larger economies, according to KPMG. Commercial bank branches and ATMs are expensive to establish and maintain, and thus not well suited to the large and widely dispersed populations in many African countries. To bridge this gap, banks have started to explore alternative operating models, one of which is mobile banking. The emergence of mobile technology and the rapid spread of affordable cellular communications throughout the continent have allowed for financial services to be provided to lower-income households that often reside in isolated rural locations.

## Current security trends in Africa

Mobile banking or a mobile payments functionality offers banks a great opportunity to expand their client base. The trouble is that the security of the current offering of online and mobile banking services in Africa leaves much to be desired. A quick investigation that I conducted, which entailed clicking through several African banks' websites and login pages, was an eye-opener in this regard.

As protection for Internet banking, the majority of banks appear to rely on only the traditional username and PIN/password combination, with no second factor. Another outdated feature that cropped up often was so-called challenge questions, where users answer a preselected question in order to prove their identity. This approach is too easily overcome through, for example, simple sleuthing on social media.

Virtual keyboards for completing sensitive fields also seem to be a popular safety precaution, because they are trusted to be immune to keylogging. However, this is not necessarily the case – some commercially available virtual keyboards have failed penetration testing.

## The next step in defence

The pivotal problem of digital banking technology is this: greater convenience brings greater risk. If a bank cannot fully protect its users' data and transactions, there is only so much it can reasonably allow those users to do. Additional security measures, on the other hand, increase friction, defeating the "on-the-go" appeal of new digital functionality.

It is clear that Africa's banks must improve their approach to digital security, whether they offer only mobile banking, only Internet banking, or both. Every bank needs a security solution that will grow with them as they embrace digital technology, so that they are able to keep offering their users more, securely.

The only way to do this is for the bank to create a completely isolated, end-to-end-encrypted communication channel between their servers and their users' mobile phones, over which users can then authenticate themselves. No other system protects against so many of the prevailing attack vectors – man-in-the-middle (MITM) or SIM swap attacks, malware, and brute force. No other system requires so little input from the user – no passwords (static or once-off), and no challenge questions. And no other system can be applied to so many different use cases: e-commerce, payments, business banking. Africa's digital banking users already have their mobile phones with them all the time – all banks need to do is to leverage this.

Text box: How will biometrics benefit African banks?
**Biometrics continues to show great potential as a second factor of login and transaction authentication, particularly in Europe and the United States. How should African banks take advantage of this technological development?**

**Gerhard Oosthuizen, CIO, Entersekt:** "Over 400 million people in Africa have no official ID, so biometrics can help banks establish an identity where none formally exists. Also, retail banking in Africa is mobile, and the nature of the device and how people interact with it requires that we limit as many clicks and taps as possible. Biometrics enablement on the smartphone offers a simple, quick alternative to passwords and PINs. Push-based authentication on the mobile does too, as it allows users to respond to authenticate prompts with a simple tap on their phone."

## Contribitor's Profile

**Jolette Roodt** is a Writer/Analyst at Entersekt's head office in Cape Town, South Africa. She holds a Master's degree from Stellenbosch University.

# WHAT IS THE EXPECTATION ABOUT AFRICAN ECONOMIC OUTLOOK IN 2017?

**Gabon's economy is expected to grow about 1 percent in 2017**, down from 2.1 percent last year, largely due to weakness in the oil sector and a recession in the commercial and service sectors, the International Monetary Fund said. Gabon has been hard hit by a more than 50-percent drop in oil prices since 2014 as well as its struggle to diversify the economy away from oil, as the IMF has advised.

**Mali's economy is forecast to grow by 5.3 percent this year** and 5 percent in 2018 on the back of public capital spending and a strong agricultural sector, the International Monetary Fund (IMF) stated. Fragile security conditions, however, pose a downside risk to the robust projections. Inflation, meanwhile, is expected to hit 1 percent by the end of December and 1.4 percent next year, the IMF said in a statement.

**Morocco's macroeconomic policies and performance remained sound,** despite volatility in agricultural output, weak growth in trading partners, and elevated external risks, the International Monetary Fund (IMF) reported. Overall, macroeconomic fundamentals and the prospects for 2017 are sound: following last year's drought, growth is expected to rebound this year to 4.8 percent, driven by strong recovery in the agricultural sector.

**Mozambique's economy is likely to grow 4.6 percent in 2017 year,** the World Bank reported, driven by recovering of coal, aluminum, gas and improved farm output. The government said the southern African nation's gross domestic product expanded by 3.3 percent in 2016. "Strengthening prices for coal, aluminum and gas, a post el Niño recovery in agriculture, and progress in the peace talks, could steer growth to 4.6 percent in 2017, and towards 7 percent by the end of the decade," the World Bank said in a report on Mozambique's economy.

**Nigerian economy to grow 0.8 percent in 2017, but risks remain,** the International Monetary Fund reported. The threats to recovery remained elevated and the economy will not grow enough to reduce unemployment and poverty. "Concerns about delays in policy implementation, a reversal of favorable external market conditions, possible shortfalls in agricultural and oil production, additional fiscal pressures, continued market segmentation in a foreign exchange market that remains dependent on central bank interventions, and banking system fragilities represent the main risks to the outlook," the IMF said.

**Uganda's new-found oil reserves may account for as much as 4 percent** of its economy annually in coming years if managed well, the International Monetary Fund's country chief says. IMF Mission Chief for Uganda Axel Schimmelpfennig writes in a blog post that the country also needs some strategic infrastructure investment and better debt management. According to IMF figures, growth was around 4.7 percent in 2016, currently above average for Africa. The IMF projects gross domestic product will grow at 5.7 percent in 2018, but Schimmelpfennig sees greater growth beyond.

**Zambia's target of 4.3 percent expansion of gross domestic product in 2017** remains feasible due to expansion in key sectors in the economy and tighter spending by the government, Finance Minister Felix Mutati hinted. "This is mainly driven by observed growth in the major sectors of agriculture, mining, construction, transport and storage, and the wholesale and retail trade," Mutati said in a mid-year economic update.

**Egypt H1 trade deficit narrows by 46 percent on sharply lower imports:** Egypt's trade deficit for the first half of 2017 narrowed by 46 percent year-on-year to $13 billion, the trade ministry stated. Imports declined by 30 percent to $24 billion and exports increased by 8 percent to $11 billion, it said in a statement. Import-dependent Egypt has been trying to curb a big trade deficit and boost domestic industries after a years-long hard currency shortage that has sapped its ability to purchase from abroad and has hit business activity.

**South Africa's trade surplus rises to 10.67 billion rand in June:** South Africa's trade surplus rose to 10.67 billion rand ($813 million) in June from a revised 7.22 billion rand surplus in May, data from the revenue agency showed. Exports fell 0.6 percent to 102.14 billion rand on a month-on-month basis in June, while imports were down 4.2 percent to 91.47 billion rand, the South African Revenue Service said in a statement.

**Mauritius' trade deficit widened by 18.6 percent to 8.25 billion rupees** ($245 million) in May from the same period a year earlier, driven by higher imports of mineral fuels and lubricants, the statistics office stated. Imports rose 6.3 percent to 15.28 billion rupees, with minerals fuels and lubricants up to 2.66 billion rupees from 2.41 billion rupees in May last year. Export revenue fell 5.3 percent to 7.02 billion rupees, Statistics Mauritius said in statement.

**South Africa's private-sector activity barely improved in July:** South Africa's Standard Bank Purchasing Managers' Index (PMI) rose to 50.1 in July from 49.0 in June, inching just above the 50 mark that separates growth from contraction.

**Kenya private sector activity slowdown moderates ahead of polls:** The Markit Stanbic Bank Kenya Purchasing Managers' Index (PMI) edged up to 48.1 during the period, froma series low of 47.3 in June. The PMI fell below the 50.0 level which separates growth and contraction in May.

# AFRICAN INFLATION WATCH: PRICES DROPPED IN EAST & WEST AFRICA IN JUNE 2017

**Angola's inflation slowed to 30.51 percent year-on-year in June** from 32.58 percent in May, according to the national statistics agency. Price increases on a month-on-month basis fell to 1.52 percent in June from 1.6 percent previously.

**Botswana consumer inflation remains at 3.5 percent year-on-year in June,**+ according to the Central Office of Statistics.

**Burundi's inflation rate eased to 15.1 percent year-on-year in June,** from 18.8 percent in May, helped by lower food price growth on local markets, according to the Institute of Economic Studies and Statistics. Food price inflation fell to 20.8 percent from 27.8 percent in May.

**Egypt's core inflation rose to 31.95 percent year on year in June** from 30.57 percent in May, according to the Central Agency for Public Mobilization and Statistics. Over the same period, annual urban consumer price inflation rose slightly to 29.8 percent from 29.7 percent.

**Ethiopia's year-on-year headline inflation crept up to 8.8 percent in June,** from 8.7 percent in May, the Central Statistics Agency stated. Food inflation slowed to 11.2 percent in June from 12.3 percent the previous month while the non-food inflation was at 6.7 percent in June, up from 4.7 percent in May.

**Ghana's annual consumer price inflation fell to 12.1 percent in June** from 12.6 percent in May, the statistics office stated. Food inflation dipped to 6.2 percent compared to 6.3 percent in May while non-food inflation dropped to 15.1 percent in June from 15.8 percent.

**Ivory Coast Consumer price inflation climbed to 1.6 percent year-on-year in June** from deflation of -0.4 percent in May, data from the National Statistics Institute showed. Food and soft drink prices dropped 2.2 percent, while housing and utilities prices jumped 8.8 percent. Transport costs declined 1 percent.

**Kenya's inflation fell to 9.21 percent year-on-year in June,** from 11.70 percent a month earlier, according to the Kenya National Bureau of Statistics. The fall is partly due to a drop in food prices and month-on-month inflation was minus 1.2 percent.

**Malawi's consumer inflation slowed to 11.3 percent year-on-year in June** from 12.3 percent in May, official data from the National Statistical Office reported. Food inflation continued to soften with recordings at 9.3 percent from 11.2 percent in May while non-food inflation fell to 13.2 percent in June from 13.5 percent in May 2017.

**Mauritius' inflation rose to 6.4 percent year-on-year in June** from 5.9 percent in May, the statistics office.

**Mozambique annual consumer inflation eased to 18.1 percent in June** from 20.45 percent in May, data on the National Institute of Statistics showed.

**Namibia's consumer inflation slowed to 6.1 percent year-on-year in June**d from 6.3 percent in May, the Namibia Statistics Agency reported. Inflation on a month-on-month basis was at 0.1 percent in June, unchanged from the previous month.

**Nigeria's inflation dropped to 16.10 percent year-on-year in June,** compared to 16.25 percent in May, the National Bureau of Statistics reported. It is the fifth consecutive decline in the rate of inflation since January 2017. On a month-on-month basis, the headline index increased by 1.58 percent in June 2017, 0.30 percent points lower than the rate of 1.88 percent recorded in May 2017.

**Rwanda's inflation fell to 4.8 percent year-on-year in June** from 6.5 percent a month earlier, according to the National Institute of Statistics of Rwanda.

**South Africa's headline consumer inflation slowed more than expected to 5.1 percent year-on-year in June** from 5.4 percent in May, according to data from Statistics South Africa. On a month-on-month basis, inflation slowed to 0.2 percent in June from 0.3 percent in May. Core inflation, which excludes the prices of food, non-alcoholic beverages, petrol and energy, was at 4.8 percent year-on-year in June, unchanged from in May.

**Sudan's annual inflation rate dropped for the first time in more than a year in June,** falling to 32.63 percent from 35.52 percent in May, the central statistics office stated. Before the June figures, year-on-year inflation had climbed every month since March 2016, when it stood at 12.94 percent.

**Seychelles' inflation rose to 3.69 percent year-on-year in June** from 3.18 percent in May, the statistics office reported.

**Tanzania's inflation slowed to 5.4 percent year-on-year in June** from 6.1 percent a month earlier due slower rises in food prices, the National Bureau of Statistics of Tanzania (NBS) reported. The food and non-alcoholic beverages inflation rate fell to 9.6 percent in June from 11.6 percent in May. Month-on-month inflation fell by 0.1 percent in June from 0.2 percent previously.

**Uganda's year-on-year inflation dropped to 6.4 percent in June** from 7.2 percent the previous month due to falling food prices, the Uganda Bureau of Statistics stated. The food inflation reduces to 18.1 percent in June down from 23.1 percent in May.

**Zambia's annual consumer inflation quickened to 6.8 percent in June** from 6.5 percent in May, according to the Central Statistics Office (CSO).. On a month-on-month basis, inflation rose to 0.6 percent from 0.1 percent.

**Zimbabwe's inflation rate slowed to 0.31 percent year-on-year in June** from 0.75 percent in May, according to the Zimbabwe National Statistics Agency (Zimstat). On a month-to-month basis, prices fell by 0.24 percent after increasing 0.03 percent previously.

## AFRICAN EQUITY MARKET INDICATORS AS AT 31-JULY-2017

| Country Name | Index Name | Index at 31-JuLY | 1-month % Δ | YTD % Δ | 1-Year % Δ | 1-Year Low | 1-Year High | 30 Days Volatility % |
|---|---|---|---|---|---|---|---|---|
| Botswana | BSE DCI | 9,078 | -1.80 | -3.44 | -7.75 | 9,006 | 9,842 | 4.377 |
| BRVM | IC Comp | 251 | -4.49 | -14.22 | -13.39 | 245 | 298 | 19.110 |
| Egypt | EGX 30 | 13,419 | 0.18 | 8.70 | 68.10 | 7,873 | 13,970 | 11.202 |
| Ghana | GSE ALSI | 2,257 | 14.88 | 33.61 | 25.64 | 1,508 | 2,264 | 10.677 |
| Kenya | FTSE NSE15 | 161 | 5.51 | 21.01 | 13.32 | 120 | 161 | 8.085 |
| Malawi | MSE ALSI | 16,877 | 7.00 | 26.70 | 26.12 | 12,861 | 17,010 | 7.136 |
| Mauritius | SEMDEX | 2,185 | 2.94 | 20.84 | 22.29 | 1,780 | 2,219 | 6.032 |
| Morocco | MORALSI | 12,201 | 1.54 | 4.78 | 23.47 | 9,852 | 12,951 | 8.786 |
| Namibia | Local | 1,107 | 9.19 | 3.56 | 6.44 | 982 | 1,144 | 11.613 |
| Nigeria | NIG ALSI | 35,848 | 8.24 | 33.39 | 27.98 | 24,547 | 37,655 | 23.530 |
| Rwanda | RSEASI | 124 | -0.30 | -2.22 | -4.06 | 124 | 130 | 6.314 |
| South Africa | JSE ALSI | 55,207 | 6.97 | 8.99 | 4.56 | 48,936 | 55,367 | 9.562 |
| Swaziland | SSX ALSI | 390 | 0.57 | 2.53 | 5.91 | 368 | 390 | 1.324 |
| Tanzania | DAR ALSI | 2,205 | -0.54 | 0.31 | -19.80 | 1,979 | 2,830 | 28.509 |
| Tunisia | TUNIS | 6,143 | 1.99 | 11.92 | 14.66 | 5,315 | 6,248 | 6.140 |
| Uganda | USE ALSI | 1,750 | 4.30 | 18.46 | 4.49 | 1,331 | 1,750 | 9.077 |
| Zambia | LuSE ALSI | 4,749 | -0.23 | 13.18 | 1.09 | 4,010 | 4,776 | 2.458 |
| Zimbabwe | IDX (USD) | 203.25 | 3.71 | 40.63 | 105.64 | 98 | 203 | 4.472 |

## SELECTED AFRICAN CURRENCY EXCHANGE Vs. US DOLLAR AS AT 31-JULY-2017

| Country Name | Currency Name | Index at 31-JuLY | 1-month % Δ | YTD % Δ | 1-Year % Δ | 1-Year Low | 1-Year High | 30 Days Volatility % |
|---|---|---|---|---|---|---|---|---|
| Algeria | Dinar | 108.27 | -0.44 | 1.97 | 1.53 | 107.60 | 112.17 | 4.014 |
| Angola | Kwanza | 166.85 | 0.68 | 0.86 | 1.42 | 163.78 | 169.65 | 5.581 |
| Botswana | Pula | 0.10 | 0.31 | 4.59 | 3.82 | 0.09 | 0.10 | 7.082 |
| CFA Franc | CFA Franc | 562.50 | 2.87 | 11.99 | 6.03 | 561.95 | 636.39 | 6.031 |
| Egypt | Pounds | 17.87 | 1.39 | 1.51 | -50.33 | 8.77 | 19.67 | 3.955 |
| Ethiopia | Birr | 23.40 | -0.64 | -4.33 | -5.62 | 21.88 | 23.46 | 6.299 |
| Ghana | Cedi | 4.39 | 0.34 | -3.53 | -10.02 | 3.79 | 4.82 | 5.272 |
| Kenya | Shillings | 103.94 | -0.24 | -1.38 | -2.44 | 100.65 | 104.18 | 1.687 |
| Malawi | Kwacha | 726.17 | -0.14 | 0.18 | -0.80 | 715.00 | 730.00 | 0.942 |
| Mauritius | Rupee | 33.33 | 3.47 | 7.94 | 6.62 | 33.07 | 36.47 | 8.577 |
| Morocco | Dirham | 9.44 | 2.11 | 7.26 | 3.42 | 2.75 | 10.32 | 4.849 |
| Mozambique | Metical | 61.11 | -1.24 | 16.82 | 13.12 | 58.58 | 79.38 | 6.743 |
| Nigeria | Naira | 320.50 | 0.55 | -1.61 | -1.25 | 293.50 | 350.25 | 20.225 |
| Rwanda | Franc | 840.76 | 0.05 | -2.23 | -5.96 | 425.00 | 847.00 | 6.173 |
| South Africa | Rand | 13.23 | -1.17 | 3.86 | 5.20 | 12.31 | 14.75 | 14.736 |
| Tanzania | Shilling | 2,227.00 | 0.00 | -2.07 | -1.71 | 2,137.00 | 2,272.50 | 3.555 |
| Tunisia | Dinar | 2.40 | 1.91 | -3.68 | -8.16 | 2.15 | 2.58 | 10.185 |
| Uganda | Shilling | 3,607.25 | -0.14 | -0.30 | -6.41 | 3,365.00 | 3,655.41 | 2.485 |
| Zambia | Kwacha | 8,874 | 3.0202 | 11.99 | 15.51 | 8,766 | 10,590 | 8.995 |

## SELECTED AFRICAN GOVERNMENT INTERNATIONAL BONDS AS AT 31-JULY-2017

| Country Name | Maturity | Price at 31-July | Mid-Yield at 31-June | 1-month Yield Chg (%) | YTD Price Change (%) | Price 1-Year Low | Price 1-Year High | Amount Outstanding (US$ M) |
|---|---|---|---|---|---|---|---|---|
| Angola | 12-Nov-25 | 106.879 | 8.329 | -0.246 | 9.871 | 86.206 | 109.254 | USD |
| Cameroon | 19-Nov-25 | 117.758 | 6.674 | 0.039 | 9.047 | 100.807 | 119.358 | USD |
| Congo | 30-Jun-29 | 72.824 | 9.942 | 1.435 | 13.463 | 63.766 | 81.661 | USD |
| Cameroon | 19-Nov-25 | 117.758 | 6.674 | 0.039 | 9.047 | 100.807 | 119.358 | USD |
| Egypt | 30-Apr-40 | 96.143 | 7.221 | -0.108 | 9.786 | 85.885 | 100.290 | USD |
| Ethiopia | 11-Dec-24 | 100.890 | 6.469 | -0.306 | 8.968 | 87.394 | 101.633 | USD |
| Gabon | 16-Jun-25 | 99.838 | 6.975 | -0.038 | 5.930 | 81.889 | 102.405 | USD |
| Ghana | 14-Oct-30 | 124.780 | 7.720 | -0.080 | 4.982 | 106.494 | 126.194 | USD |
| Kenya | 24-Jun-22 | 102.138 | 6.484 | 0.063 | 7.560 | 91.157 | 103.937 | USD |
| Ivory Coast | 31-Dec-32 | 98.423 | 5.995 | -0.334 | 5.902 | 88.498 | 101.499 | USD |
| Morocco | 11-Dec-42 | 112.090 | 4.680 | -0.054 | 9.738 | 100.880 | 118.426 | USD |
| Namibia | 29-Oct-25 | 103.334 | 4.755 | -0.055 | 4.997 | 98.076 | 108.052 | USD |
| Nigeria | 12-Jul-23 | 104.378 | 5.501 | -0.227 | 7.488 | 89.886 | 105.025 | USD |
| Rwanda | 02-May-23 | 103.094 | 5.979 | -0.020 | 3.451 | 95.826 | 103.831 | USD |
| Senegal | 30-Jul-24 | 106.730 | 5.094 | -0.190 | 6.544 | 96.756 | 106.761 | USD |
| South Africa | 24-Jul-44 | 98.653 | 5.471 | -0.093 | 0.028 | 91.188 | 116.008 | USD |
| Tanzania | 09-Mar-20 | 104.838 | 5.464 | 0.073 | -0.418 | 102.708 | 106.272 | USD |
| Tunisia | 19-Sep-27 | 109.645 | 6.908 | -0.017 | 3.192 | 106.090 | 110.396 | USD |
| Zambia | 30-Jul-27 | 108.649 | 7.712 | -0.290 | 9.552 | 87.808 | 109.092 | USD |

*Compiled by Capital Markets in Africa*

# ››› More than finance
# DEG at a glance

KFW DEG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as at January 2017

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