Bright Africa

The drivers, enablers and managers of investment on the continent.

2015

riscura.com/BrightAfrica

Foreword

Drivers, enablers and managers of investments on the continent

Africa's investors have become markedly more sophisticated in recent years. They understand that the continent is one of the world's fastest-growing regions and that populations are young and urbanis ing. They also understand that Africa is rapidly adopting technology, is increasingly connected, and is playing catch-up to the rest of the world in terms of living standards.

Investors looking at Africa today want to understand this exciting continent in more detail. They want to look past the headline GDP numbers, and understand what is really happening in the countries and regions within the continent, and how they interact with the rest of the world.

The stage of economic development, the reliance on commodities, and the state of physical infrastructure also play an important role, as does understanding the state of local investment, the depth of markets, and how market dynamics are affecting company valuations. Lastly, Africa's investors want to know the most effective ways to harness Africa's growth.

This report, the third edition of Bright Africa, seeks to answer some of these questions by providing insight into the drivers, enablers and managers of investment on the continent. The report explores the status of local pools of capital as a major driver of Africa investment, and finds that African pension fund capital has reached $330bn and is growing rapidly. Increasing adoption of insurance is causing insurance company investment portfolios to grow, and are now estimated to be around $270bn. The creation of these local pools of capital, and the advent of intra-African investment, means that Africa is now one of its own key investors.

In Bright Africa the continent has been divided into nine meaningful investment regions, taking into account culture, geography, language and historic trade links. We show key economic metrics for each of these regions, analyse the export and import makeup, and highlight Africa's key trade partners around the globe. The report further analyses the state of infrastructure, a key enabler of growth, and benchmarks Africa's road, rail and electricity against other parts of the world. The report demonstrates that the makeup of GDP is quite different to the makeup of exports, highlighting that trade links with former colonial powers remain largely intact and that China has become a major African trade partner.

It is important to recognise that Africa is not a single investment destination with a single set of standardised risk factors and homogenous potential for reward. Although some high-level similarities are evident, as one digs down into the specifics of certain regions and countries, it becomes clear that Africa is comprised of a range of distinct investment destinations; each with its own attractions, flaws, cultural differences and business practices. Investors looking at Africa for the first time may begin by identifying the largest economies by GDP or the largest cities by population. While it is certainly useful to explore country- and city-level detail, it may be more pertinent to start at a regional level by identifying groups of countries with similarities. By assessing Africa at a regional level, one can get a better understanding of the strengths and weaknesses of an investment destination by not only analysing the characteristics of the country of interest, but also the support that it receives from its regional partners. It also allows investors to identify the long-term potential of an investment by better understanding the potential growth areas into neighbouring countries. RisCura has identified these meaningful markets by analysing cultural connections, interconnectivity through trade blocs, sharing of expertise, good business relations, and relative ease of transportation, among others. These regions are displayed in the adjacent map, and table below.

Rory Ord
Principal
RisCura

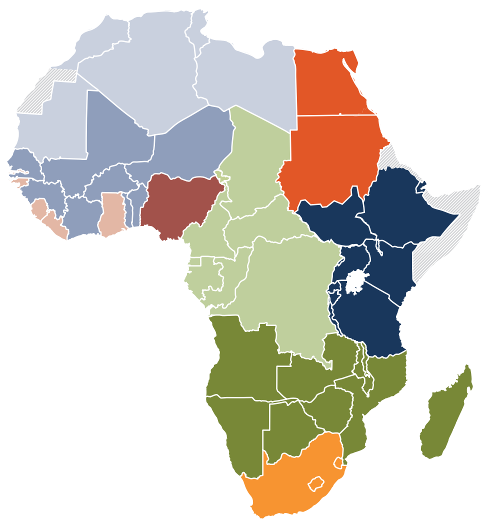
1 ♦ The story of investment in Africa

1.1 Segmenting Africa into meaningful markets

It is important to recognise that Africa is not a single investment destination with a single set of standardised risk factors and homogenous potential for reward. Although some high-level similarities are evident, as one digs down into the specifics of certain regions and countries, it becomes clear that Africa is comprised of a range of distinct investment destinations; each with its own attractions, flaws, cultural differences and business practices. Investors looking at Africa for the first time may begin by identifying the largest economies by GDP or the largest cities by population. While it is certainly useful to explore country- and city-level detail, it may be more pertinent to start at a regional level by identifying groups of countries with similarities. By assessing Africa at a regional level, one can get a better understanding of the strengths and weaknesses of an investment destination by not only analysing the characteristics of the country of interest, but also the support that it receives from its regional partners. It also allows investors to identify the long-term potential of an investment by better understanding the potential growth areas into neighbouring countries. RisCura has identified these meaningful markets by analysing cultural connections, interconnectivity through trade blocs, sharing of expertise, good business relations, and relative ease of transportation, among others. These regions are displayed in the table and adjacent map.

REGION	COUNTRY
Central Africa	Cameroon
	Central African Republic
	Chad
	Congo
	Democratic Republic of Congo
	Republic of Equatorial Guinea
	Gabon
East Africa	Burundi
	Djibouti
	Ethiopia
	Kenya
	Rwanda
	South Sudan
	Tanzania
	Uganda
Egypt & Sudan	Egypt
	Sudan
Francophone West Africa	Benin
	Burkina Faso
	Cape Verde
	Côte d'Ivoire
	Guinea
	Mali
	Niger
	São Tomé and Príncipe
	Senegal
	Togo
Maghreb region	Algeria
	Libya
	Mauritania
	Morocco
	Tunisia
Nigeria	Nigeria
Other West Africa	Gambia, The
	Ghana
	Guinea-Bissau
	Liberia
	Sierra Leone

REGION	COUNTRY
South Africa	Lesotho
	South Africa
	Swaziland
Southern Africa excl. SA	Angola
	Botswana
	Comoros
	Madagascar
	Malawi
	Mauritius
	Mozambique
	Namibia
	Reunion
	Zambia
	Zimbabwe



Note: The following countries are commonly excluded from the analysis due to insufficient data. When included, the impact is immaterial. Eritrea, Seychelles, Somalia, Western Sahara.

The **Central Africa** market is the same as that defined by the African Development Bank (AfDB) with the exception of Madagascar, which RisCura has classified as Southern Africa (ex-SA). On a GDP basis (PPP USD) and by population, the Central Africa region is on par with the Francophone West African region.

The countries constituting **East Africa** are a combination of the East African Community (Kenya, Tanzania, Uganda, Rwanda, Burundi), the LAPSSET corridor (Kenya, South Sudan and Ethiopia) as well as Djibouti, a crucial link to the Indian Ocean for Ethiopia and South Sudan. Kenya has traditionally headlined this region through consistently generating the largest GDP and acts as the primary route to international trade through the Mombasa port. (Note: Somalia and Eritrea are excluded from all analysis.)

Egypt & Sudan previously united under British rule, still share strong ties, as well as one significant commonality – the trade facilitation through transport on the Nile River. As Egypt does not fall within the Arab Maghreb Union, it is separated from the rest of North Africa. However, Egypt's strong economic and cultural ties with the Middle East bring natural trading partners, and it is often seen grouped with the Middle East for investment purposes.

Francophone West Africa is a commonly recognised region on the continent, and typically includes Mauritania. However, RisCura has allocated Mauritania to the Maghreb region as it is found to have closer ties to the North African countries. These French-speaking countries share more than just a language. Due to their common history as French colonies, they also share similar legal and socio-political systems.

The **Maghreb region,** or the western portion of Northern Africa, constitutes the countries that form the Arab Maghreb Union, established in 1989 (Note: Western Sahara is excluded from all analysis). The region was established with the goal of functioning as a unified political and economic grouping. Political unrest in the region has stunted progress since its inception but hope still remains that the Union will fulfil its purpose in years to come. The region includes important cities such as Casablanca, Algiers and Tunis.

Nigeria on its own is the size of the entire Maghreb region on an aggregated-GDP basis. While Nigeria is traditionally grouped with the rest of West Africa, its reliance on the rest of the region is less pronounced, likely as a result of its massive standalone GDP, its access to international markets via its four large ports, and its population of over 170 million people.

Other West Africa includes Ghana, Liberia, Sierra Leone, Guinea-Bissau and The Gambia. This 'region' is included in the analysis where appropriate. Of course, due to the geographic placement of these countries, an analysis of intra-regional trade or transport infrastructure linking the 'region' would not be meaningful. Where appropriate, Ghana has been compared at a country level, rather than as a part of the 'Other West Africa' region. Although Ghana's recent economic challenges have dampened investor confidence, the country remains an important economy.

South Africa, like Nigeria, is a large African economy on a standalone basis. Due to the developed nature of South Africa relative to the rest of the continent, it has not been included in the Southern African region. South Africa boasts the largest GDP per capita of all the regions (double that of Nigeria) and is the most advanced investment destination on the continent. The South African market includes Lesotho and Swaziland due to their reliance and proximity to SA. The Swazi lilangeni is pegged to the South African rand, which is also accepted as currency within the country.

Southern Africa excluding South Africa (ex-SA) incorporates those countries south of central and eastern Africa, and north of the South African border. This region offers substantial oil resources in Angola, copper in Zambia and has access to both the Atlantic and Indian oceans. The region has support from the most developed economy on the continent from the South, and access to capital coming out of South Africa as large companies look to expand into the rest of the continent.

1.2 How do Africa's regions compare?

What makes a region attractive to investors? RisCura has analysed Africa's regions from a number of perspectives to determine their relative attractiveness. The table below shows the aggregated sizes of the economies, their GDP growth, the amount of external investment they receive in the form of FDI, the sizes of the populations, the amount of trade that occurs within each region, as well as their rankings by ease of doing business and attractiveness (weighted according to GDP).

REGION	*Aggregate GDP PPP (2014) (USDbn)*	*Real GDP growth (2015)*	*Average FDI inflow (FY12-FY14) (USDm)*	*Population (2014) (million people)*	*Bilateral intraregional trade (2013) (% of GDP)*	*IESE Ease of doing business (rank out of 189)*	*VCPE Attractiveness Index (rank out of 118)*
South Africa	697	3%	6 363	57	N/A	38	31
Maghreb region	1 047	1%	7 241	93	0.5%	122	76
Nigeria	1 058	4%	7 184	174	N/A	175	76
Egypt & Sudan	1 105	3%	5 122	121	0.1%	121	57
Southern Africa excl. SA	423	3%	3 141	124	0.8%	148	101
East Africa	487	8%	4 140	252	0.6%	135	86
Francophone West Africa	230	6%	3 012	121	1.4%	160	109
Central Africa	243	4%	8 738	124	0.8%	165	108
Ghana	109	6%	3 248	26	N/A	69	76
Other West Africa	23	-1%	1 494	14	N/A	151	N/A

Sources: World Economic Outlook Oct2014 (GDP and population); Index of Economic Freedom (FDI Inflow); Trade Map (Intraregional trade); IESE Business School (Ease and Attractiveness).

On a purchasing power parity (PPP) basis, the largest regional GDPs are the Maghreb, Egypt & Sudan, and Nigeria. The most densely populated regions in Africa are East Africa and Nigeria, at least 50 million people larger than the other regions. East Africa is especially large with Ethiopia's population of 91 million (2014 estimates). GDP growth for 2015 varies from negative growth, to 8% real GDP growth forecast for the year, further highlighting just how different the characteristics of these regions are. The more developed regions on the continent including the Maghreb, South Africa, Egypt & Sudan and Southern Africa are expecting real GDP growth of around 3%. The Maghreb region is biased downwards because of negative growth expected in Libya, which impacts the region. Other West Africa is forecast to decline in 2015, as the countries worse-hit by the Ebola outbreak will take some time to recover.

More high growth areas include Francophone West Africa, Ghana, and East Africa (the frontrunner) with 8% forecast for the year. Nigeria, whose GDP growth forecast was approximately 9% for 2015 less than six months ago, has been adjusted downwards significantly due to the drop of global oil prices. The oil price decline has impacted the GDP of the country directly through lower oil revenue, and indirectly through increased inflation due to the depreciation in the currency. The uncertainty leading up to the elections that took place in March 2015, as well as the insecurity in the North of the country have also become deterrents to investors, further impacting growth. The result of the elections was very positive, with ex-President Goodluck Jonathan peacefully handing over power to newly-elected Muhammadu Buhari.

Southern Africa (ex-SA) has received erratic but improving FDI inflow, increasing from USD 1.6bn in 2012 to USD6.0bn in 2014. Egypt & Sudan have experienced a similar increase from USD 1.5bn to USD 8.6bn over the period. Nigeria's FDI inflow, on the other hand, has declined from USD 8.9bn in 2012 to USD 5.6bn in 2014 in the lead up to the 2015 elections and increased economic volatility on the back of the lower oil price.

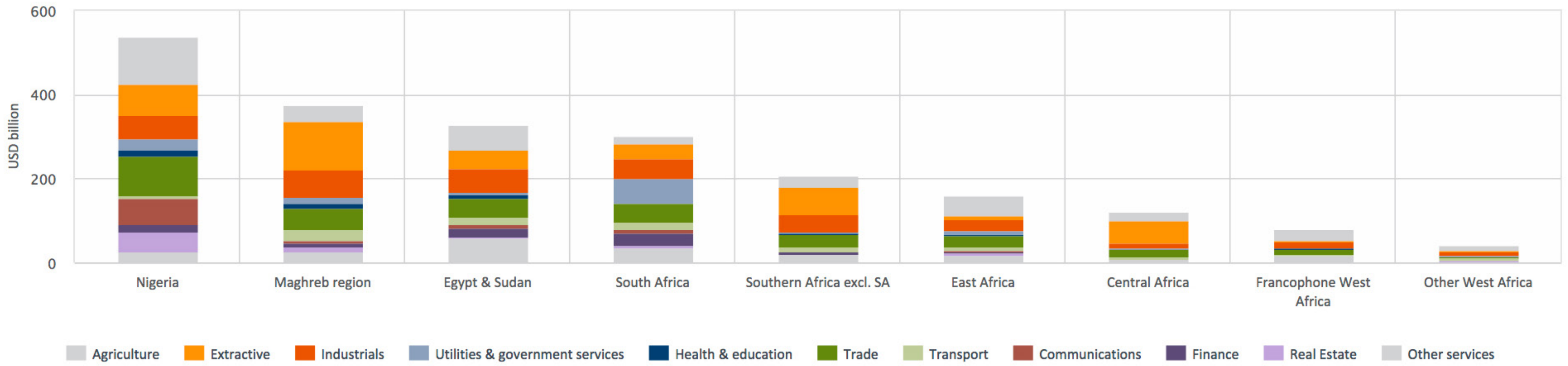
It is interesting to note that when it comes to trade, Francophone West Africa appears to be the region that relies most heavily on its neighbours. East Africa and the Maghreb region, however, score low on intraregional trade, showing less interdependence. Egypt's trade with Sudan is limited, which is understandable given Sudan's recent political history. It is worth noting that Egypt's trade with the Maghreb region far outranks that with Sudan, but in general, Egypt's trade within Africa has declined dramatically over the past few years to less than 3% of its total, with no African country, apart from Libya, making it onto the country's top 15 export markets (the Economist).

Looking at the rankings by ease and attractiveness, the Maghreb region and Nigeria for example, score the same on a weighted-average basis with respect to attractiveness, but when considering the ease of doing business, the Maghreb region far outranks Nigeria. In fact, Nigeria is considered in the top 15 most difficult places to do business, out of the 189 countries around the world that are ranked. Ghana and East Africa on the other hand, both have relatively strong rankings, falling behind only South Africa, Maghreb and Egypt & Sudan regions.

1.2.1 Components of GDP and exports by region

Domestic consumption is fairly well diversified

GDP (nominal GVA) output by region (2014)

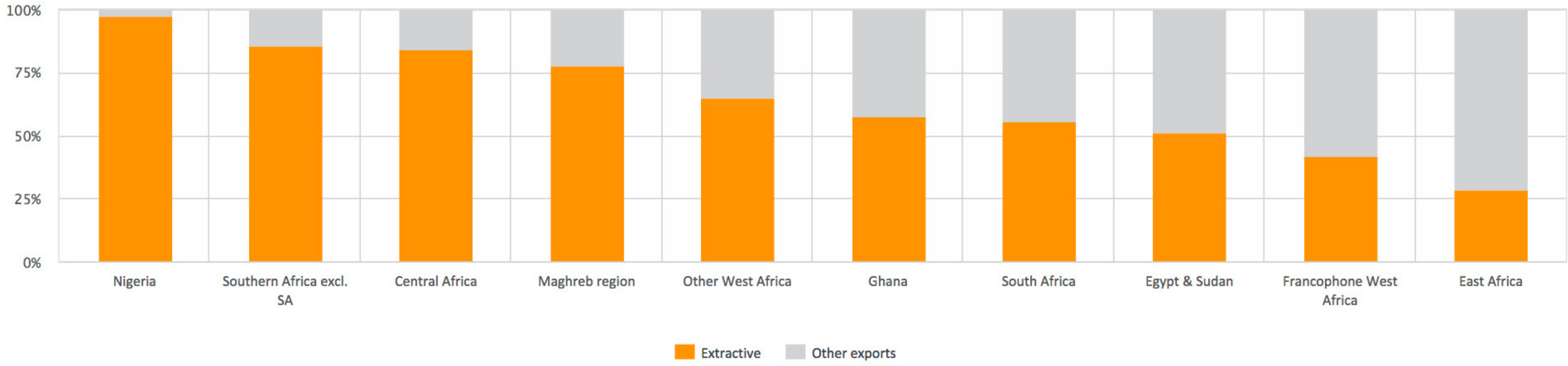


Source: BMI Research, RisCura analysis

The rebasing of Nigeria's GDP in 2014 has made it clear that the country has Africa's largest economy. It has also provided a much improved picture of the changing make-up of the country's GDP. While the country's exports are heavily focused on oil, extractive industries make up a much smaller proportion of GDP. This is true across all regions, where overall GDP is far more diversified than exports. Domestic consumption is the most important factor driving overall GDP, and in most regions this is fairly well spread across several sectors.

Large reliance on extractive industries for exports

Breakdown of regional exports (2013)

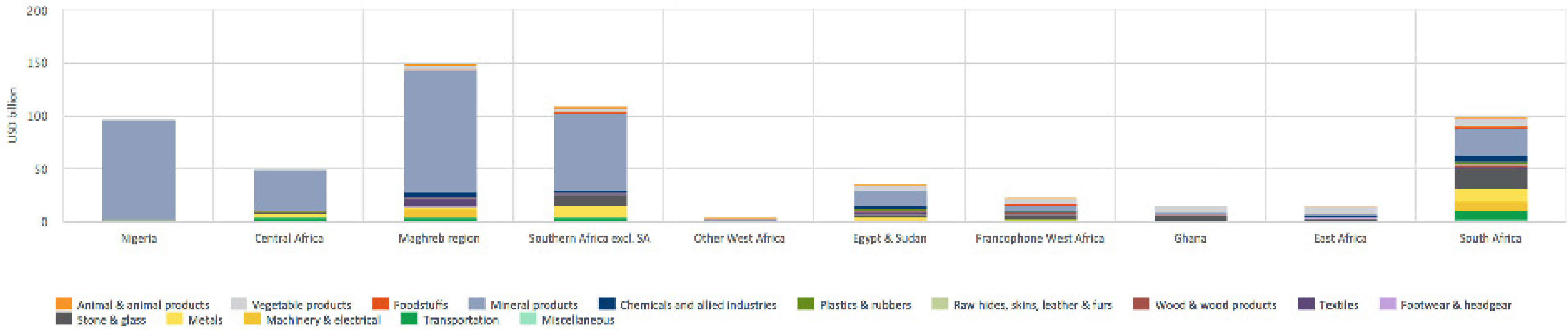


Source: Trade Map, RisCura analysis

Many African countries and regions rely heavily on extractive industries for exports. These include Nigeria, Southern Africa, Central Africa and the Maghreb region. Countries with more exposure to extractive industries have done well in the past decade as commodity prices have historically been at high levels, but as prices have fallen in recent times, the opposite side of the reliance on commodities has been exposed. Nigeria's reliance on oil has been well documented, and is the most obvious example, but many parts of the continent also have significant exposures. The most immediate impact on these economies when commodity prices fall is pressure on the currency, which must find a new demand/supply equilibrium. This is followed by an impact on government revenues, which can have a significant impact on the state's ability to fund commitments and balance budgets.

Exports concentrated on mineral products

Value of exports by product (least to most diversified) (2013)



Source: Trade Map, RisCura analysis

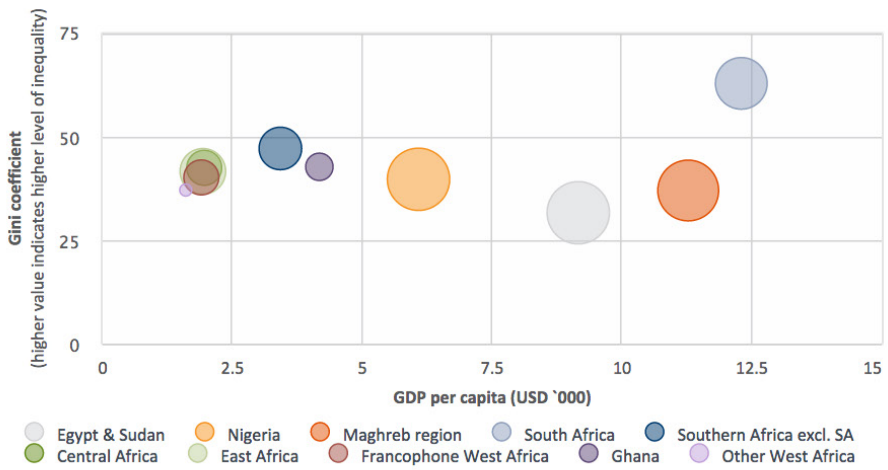
The graph showing the breakdown of regional exports by product is shown from the least diversified on the left of the graph to the most diversified on the right. The more diverse, or complex, a country's GDP output and exports, the more diverse the skills in the economy, the more resilient the region will be to adverse shocks to individual industries. Nigeria, the Maghreb region, Southern Africa and Central Africa have large exports compared to the rest of the continent (excluding South Africa), but the concentration of those exports on mineral products makes the regions highly sensitive to a decline in the crude oil price for example, something that is very pertinent in the current global economy. On the other hand, South Africa, Egypt & Sudan, East Africa and Francophone West Africa, have a far more diverse set of export products with which to generate foreign currency. Although some of the mentioned regions are much smaller than Nigeria or the Maghreb region, they will be more resilient to negative shocks in single sectors, and offer alternative areas of growth when particular sectors struggle.

Relative wealth of Africa's regions

The graph below compares the size of each market on a purchasing power parity basis (PPP) to the GDP per capita. The wealth of individuals is shown using GDP per capita as a proxy. It is apparent that in many African countries, although GDP is growing and very large in many cases, the wealth generated by the country's GDP is not filtered down to the average consumer. Specifically in Africa's largest individual economy, Nigeria, the GDP per capita is very low relative to its GDP when compared to the other regions. South Africa is the leader on an individual-wealth basis, with only the third largest GDP of the group, closely followed by the Maghreb region. The inclusion of Sudan in the Egypt & Sudan region biases the measure downward, as Egypt's standalone GDP per capita is USD 11 073 on a PPP basis, in line with the Maghreb region.

Wealth of individuals and equality not illustrated in GDP

GDP per capita, Gini coefficient and size of economy by region



Source: IMF WEO October 2014, Quandl, RisCura analysis

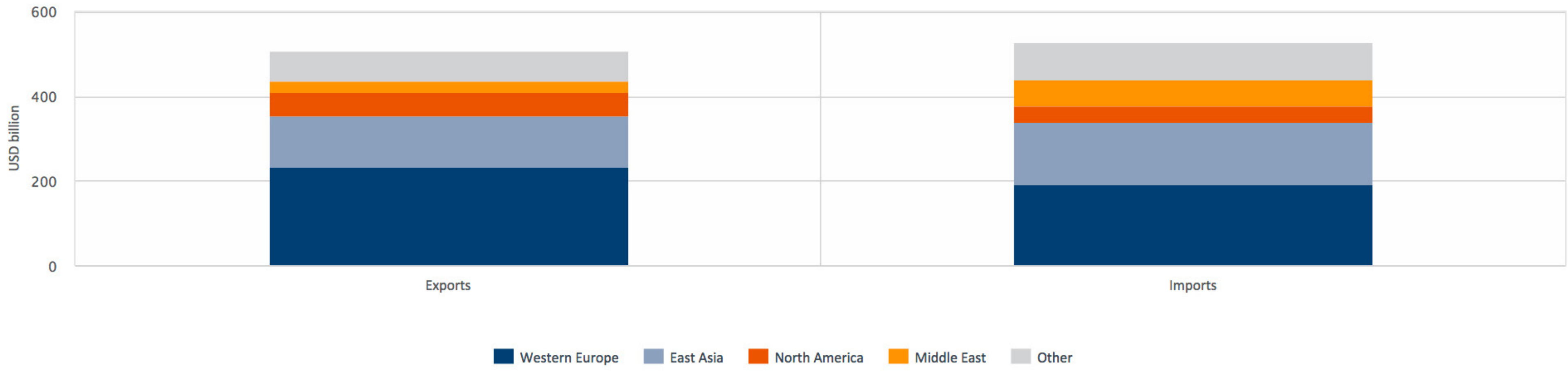
Note: The size of the bubble represents the size of the economy on a GDP (PPP) basis.

1.3 Africa's links to the globe

50 years after the end of European rule in most parts of Africa, more than a third of Africa's trade remains with Western Europe. This high concentration shows that historic ties still have a large influence on these markets, but the balance is beginning to shift as trade with East Asia increases. The nature of the imports compared to the exports reflect the fact that Africa almost exclusively exports raw materials, and has not yet begun to manufacture goods for export markets.

High concentration of trade with Western Europe

Africa's major trade partners by exports and imports (2013)



Source: Trade Map, RisCura analysis

Imports from Western Europe are mainly made up of capital goods such as machinery and vehicles, with refined oil and fuel products also making up a large share. Manufactured goods, plastics and pharmaceuticals also make up smaller contributions to imports. East Asia is the second largest source of imports, while relatively little is imported from North America, only slightly more than from Eastern Europe. The profile of imports from East Asia is similar to imports from Western Europe in many respects, with the obvious exception of refined oil and fuel where very little is imported from East Asia. It is interesting to note that ships are also largely imported from the East rather than Europe.

Capital and consumer goods imported from Western Europe and East Asia

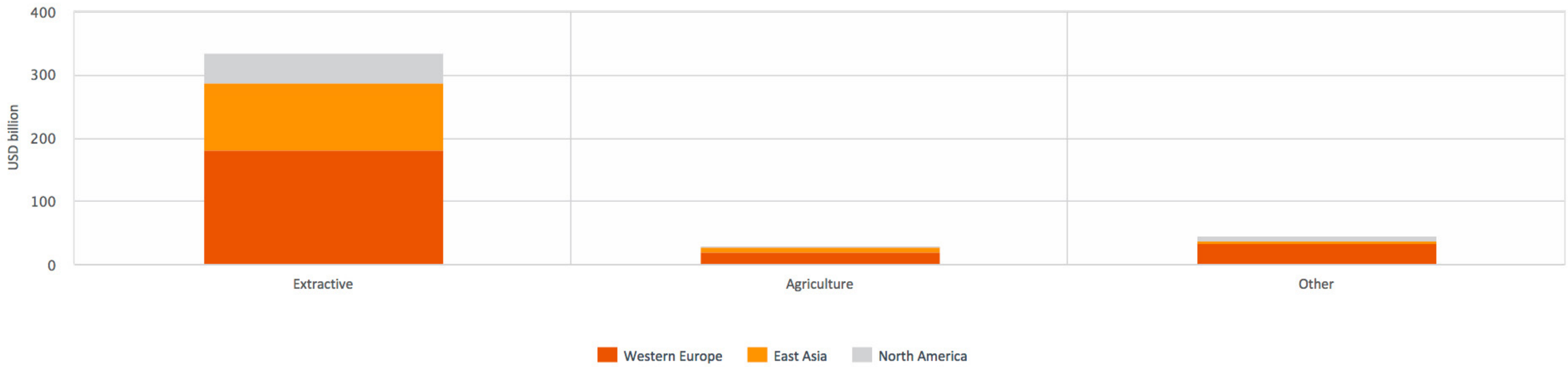
Africa's imports from its 3 largest trading partners (2013)

Source: Trade Map, RisCura analysis

On the export side, Western Europe and East Asia are Africa's largest trading partners, with two thirds of exports going to these regions. Almost three quarters of exports are of crude oil and gas, and more than 90% of all exports are extracted hydrocarbons and metals. Agriculture makes a small contribution in the form of cocoa, tea, coffee and fruit. Around 8% comes from other non-extractive industries such as the assembled electrical equipment and vehicles.
Exports to East Asia are even less diversified than those to Western Europe, with 97% of exports extractive in nature. The remainder is made up of agricultural products such as cotton, wood and plant oils. The trend in recent years has been a decrease in exports to the US, and a corresponding increase in exports to Western Europe and China. The main reason for this shift has been the advent of shale oil and gas in the US, which has led to lower demand for African crude oil in that market.

Extractives dominates exports

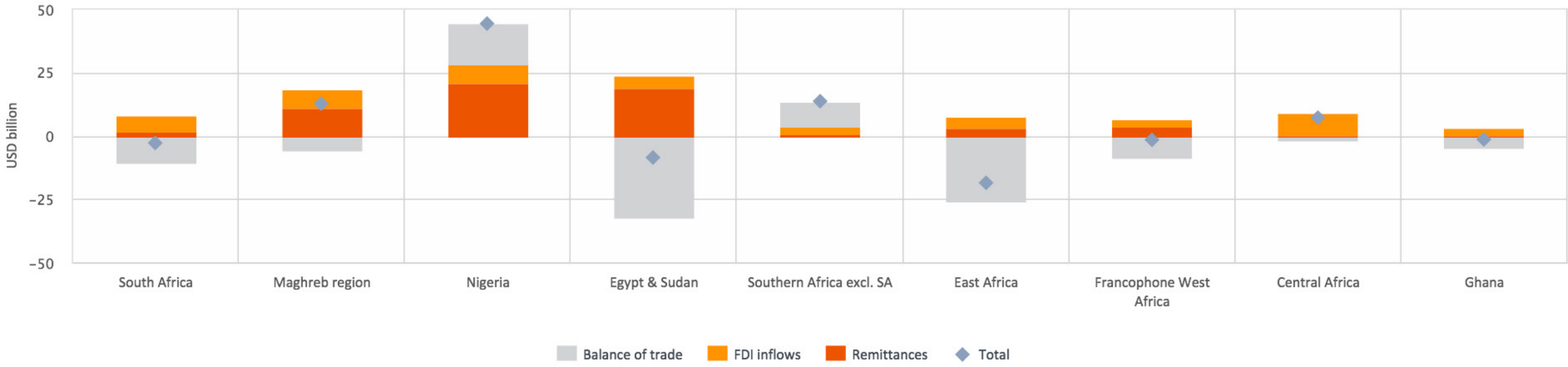
Africa's imports from its 3 largest trading partners (2013)



Source: Trade Map, RisCura analysis

Resource-rich countries maintain significant positive trade balances

Recurring souces of hard currency (2014)



Source: BMI Research, Heritage Index of Economic Freedom, World Bank Migration and Remittances Data, RisCura analysis

When one considers the export and import profile of the continent as a whole, Africa's trade balance is only marginally negative, which is expected within developing economies that attract investment capital allowing for higher trade deficits. However, on a regional basis the picture is very different, with resource-rich regions such as Nigeria and Southern Africa (ex-SA) being able to maintain significant positive trade balances, allowing for the purchase of capital goods to fuel economic growth. What has become apparent with the recent lower commodity prices and dramatic decrease in the oil price is that certain countries and regions are very vulnerable to shocks from commodity prices. In particular, Nigeria, Ghana and Zambia have experienced significant currency devaluations due to sudden large current account deficits. The reliance on commodities such as tea, coffee and sugar for export income by the East African zone has equally exposed this region to trade deficits and currency weakness in the 2014 period.

High macro-economic volatility due to large exposure to a single export product can increase investment risk in otherwise attractive markets by exposing investors to significant foreign currency risk and volatility in government finances.

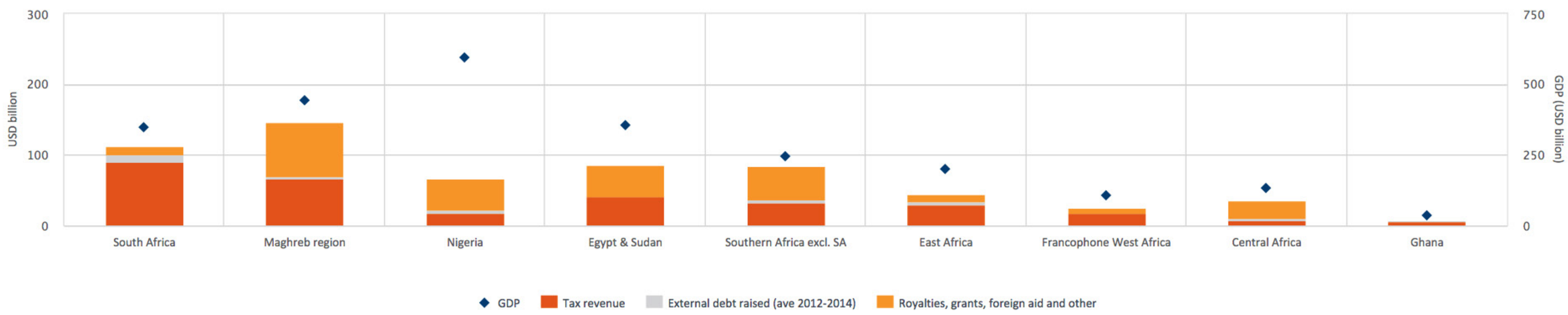
Another interesting point to note is the large role that remittance plays in Nigeria, Egypt & Sudan and the Maghreb region as a source of hard currency. The diaspora of people from these regions has resulted in significant money flows, which also support local currencies. These remittances have proven to be relatively consistent through the economic cycles, supplying a stable source of hard currency.

1.4 Infrastructure development in Africa

One of the factors that has been proven to enable high growth and development is the provision of high quality infrastructure. The World Bank estimates that the cost of redressing the infrastructure gap in Africa requires an annual expenditure of USD 93bn, or less than 5% of the total GDP of the continent. The example of China, which has consistently spent about 8%-9% of GDP per year in the construction of infrastructure to fuel its impressive growth in the last decades, points Africa toward the need to develop its infrastructure to fuel its growth-miracle. In China, almost half of the infrastructure expenditure was funded through central government sources. RisCura examines the sources and extent of government funding per region below in order to evaluate governments' abilities to raise capital to spend on the construction of infrastructure.

Consistent income crucial for infrastructure development

Sources of government funding (2014)



Source: BMI Research, IMF WEO October 2014, Heritage Index of Economic Freedom, OECD - Development Aid at a Glance 2. Africa (2014 edition), RisCura analysis

South Africa, the Maghreb, East Africa and Francophone West Africa have relatively large tax bases averaging 20% of GDP. This is a stable source of income that is crucial for accurate and reliable planning, and is an enabler of long-term projects requiring multi-year commitments from governments.

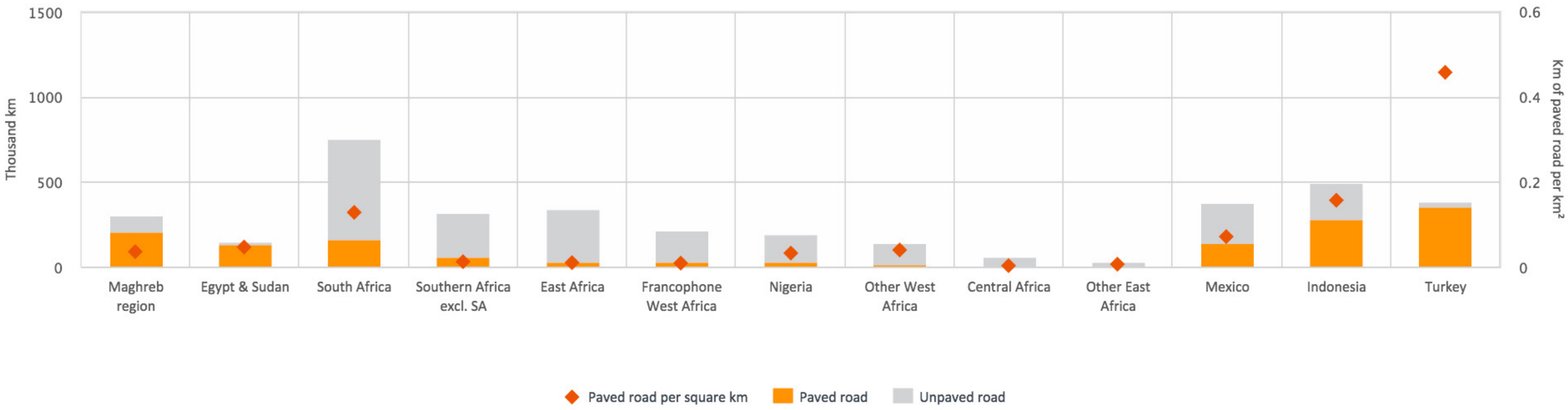
In contrast, in Nigeria, the tax base is very small, at only 3% of GDP, with government reliant on oil royalties for revenue. In Nigeria and some other countries, some of the funding in the "other" category includes royalty payments for the extractive industries, which has proven to be very volatile as these payments are linked to prices. In countries and regions with low tax bases this results in a low level of consistent income, which can be used to raise bonds for infrastructure projects as well as support the high levels of repairs and maintenance needed once infrastructure has been constructed or upgraded. The low level of government revenue thus represents a serious barrier to infrastructure development and has increased the focus on partnerships between public and private entities to develop infrastructure.

In recent years African governments have returned to international debt markets as global investors have searched for yield. While this availability of debt has been a positive source of funding for governments, it remains relatively small compared to other funding sources.

Africa's road infrastructure

Maghreb leads the pack on paved roads

Road infrastructure (latest available information)



Source: CIA World Factbook, RisCura analysis

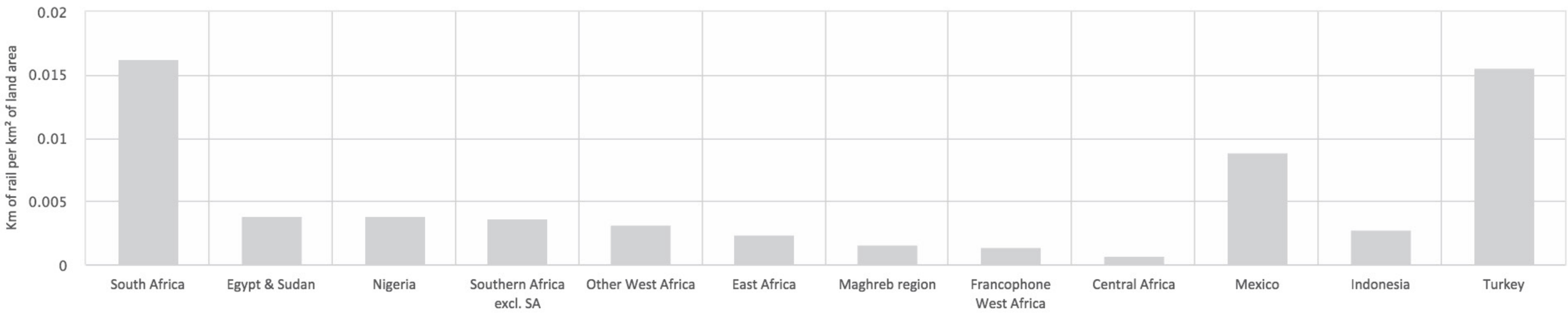
To analyse the investment in road infrastructure in various regions, the total kilometres of both paved and unpaved roads were aggregated. 67% of the road infrastructure in the Maghreb region is paved. Within the region, the top performers are Algeria, Tunisia and Morocco with over 70% of total kilometres of road being paved. Egypt has also invested in its road network having paved 92% of its total road network. The other major economic powerhouses on the continent: Nigeria, South Africa and Kenya have only paved 15%, 21% and 7% of their total respective road network.

Mexico, Indonesia and Turkey (MIT) serve as a benchmark to evaluate the performance of African economies. Excluding the North African countries, the rest of the continent has a long way to go to catch up with the MIT nations in terms of total paved roads. However, the road density in MIT is much higher than all the African regions, which serves as another reminder of the much-needed investment in Africa's road network.

Africa's rail infrastructure

Rail infrastructure in Africa lags its peers

Km of rail per km² of land area (latest information available)



Source: CIA World Factbook, RisCura analysis

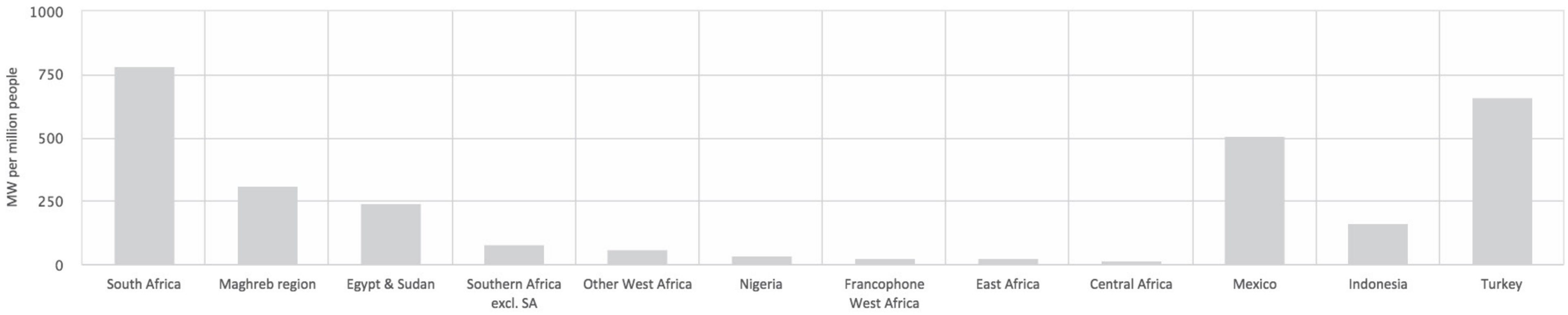
South Africa has 20 000 km of installed rail infrastructure and, given its relatively small size compared to other regional groupings, this translates to a high rail per land area. In absolute terms, the Maghreb region has 8 933 km of installed rail, however, if the underproductive land area were excluded from its total land area, the region would rank much higher. The East Africa region is expected to add an additional 3 234 km of rail infrastructure in the next three years, which would rank it third in absolute terms behind South Africa and Southern Africa excluding SA.

Indonesia has similar installed rail infrastructure per square kilometre as the rest of the Africa countries, with the exception of South Africa. This can be explained as the country is an aggregation of islands. South Africa has a similar amount of rail infrastructure as Turkey but more than Mexico.

Africa's energy infrastructure

Significant energy infrastructure needed in Nigeria and East Africa

Energy (MW) per million people (latest available information)



Source: CIA World Factbook, IMF WEO October 2014, RisCura analysis

South Africa's energy needs are served by 784MW of power per one million people. This is 2.5 times more than the region in second position (Maghreb region at 308MW). As expected Maghreb, Egypt and Southern Africa (ex-SA) round off the top four.

South Africa compares well with the MIT nations as its installed energy capacity per million people is greater than all the three nations. All other African nations excluding North Africa require a significant increase in energy investments to catch up with the MIT nations, in order to position themselves as attractive investment destinations.

2 ♦ Africa's institutional investors

The existence of institutional investors is one of the main drivers of the development of capital markets. In many parts of the continent, institutions have been slow to develop and development finance institutions (DFIs) have long filled this gap. In more recent years, regulatory reform in pensions in many countries has driven the creation of more reliable forms of savings for individuals. While the assets in African pension funds are still relatively small, most are fast growing, creating local pools of capital for investment. Insurance penetration has also been low historically, but strong growth is expected in coming years, also resulting in the accumulation of capital in insurance investment portfolios.

2.1 Pension funds and social security in africa

2.1.1 Social security in Africa

Countries across Africa are at different stages of creating comprehensive and inclusive social security systems. Although some are further along this journey than others, most have introduced some form of arrangement for pension provision or have social security as a strategic goal.

Similar to global trends, the vast majority of retirement income in Africa is funded by governments, derived from taxes or other forms of government revenue (essentially a pay-as-you-go system or PAYG). With a large proportion of formal sector workers concentrated in the civil service, pension funds for public sector workers are well established and benefits are often more substantial compared to the private sector. Defined Benefit (DB) schemes dominate across the continent although regional differences are notable. While DB schemes are common in many Francophone West African countries, the Maghreb region as well as Egypt & Sudan, Defined Contribution (DC) schemes (often provident schemes) are prevalent in English-speaking parts of Africa, especially sub-Saharan Africa (Stewart and Yermo, OECD paper).

Coverage on the continent however, is much lower compared to the rest of the world. Data from the International Labour Office's 2014/15 World Social Protection Report estimates that currently only 16.9% of older people in sub-Saharan Africa receive an old age pension. Although this number is higher in North Africa at 36.7%, it is still considerably lower than much of the developed world (90% in North America and Europe). A recent report on the pension sector in the East African Community estimates that between 80-90% of the population is not reached via public or private pension fund schemes.

In part, this is due to the unique circumstances in Africa including demographics (young population), a large informal employment sector, migration with limited pension portability, and dependency on government finances. The pace of regulatory reform has also led to divergent coverage trends between countries and regions.

To meet this challenge, Africa has been on a journey to plan, fund and deliver social security to the continent. Many countries have transitioned in line with the multi-pillar model proposed by the World Bank in their 2005 report[1] and subsequent refinements. While each country has forged its own distinctive path, two main areas of focus have emerged. The first is the introduction of a basic safety net or non-contributory pension for those who have no other income. Pension systems provide a way of securing long-term savings but also an indirect way to alleviate poverty, which affects many on the continent. A number of African countries including South Africa, Namibia, Mauritius and Lesotho[2] have used non-contributory universal pensions as a foundation for broad social security coverage. Many pensioners spend their pension income on books, school fees and health care for grandchildren. Research suggests transmission via a basic retirement income has the ability to significantly alleviate poverty and directly impact socioeconomic factors.

The second trend has been a move from unfunded to funded solutions, and DB to DC schemes, albeit at slower pace than in developed countries. This is a broad reflection of the increased pressure on government budgets, and the unsustainable fiscal burden that PAYG pension systems create.

African economies have made great strides to shape their social security systems. Importantly, the continent has been building institutions that account for African priorities and their unique challenges. Regulators have looked beyond the developed world experience to regions such as Latin America and Eastern Europe for their learnings. Nigeria for example was the first on the continent to explore the Chilean-style individual-funded accounts and also cites Mexico as a country they examined as part of their reform journey. Extending and ensuring an adequate level of social security remains a continually evolving process as governments and regulators across the world adapt to changes in the environment and financial markets, no less so in Africa.

Foot notes:

1. The World Bank proposed a conceptual frame work for pensions in their 2005 report, Old Age Income Support in the 21st Century: An International Perspective on Pension Systems and Reform. This note has seen subsequent refinements.

2. For example, research shows that 60 per cent of the monthly pension received by persons aged 70 or older in Lesotho is redirected consistently to children. Evidence also suggests that this mechanism has halved Lesotho's hunger rate (Croome and Mapetla, 2007)

2.1.2 Social security in Africa: pension fund assets

Pension funds globally have become significant investors, both as fiduciaries in global capital markets and in their capacity as investors in local and international development projects. At the end of 2014, global pension fund assets[1] were estimated at USD 36,119bn, representing a 6.1% rise from the 2013 year-end value. On average, these assets account for 84.4% of these countries' GDP.

The US continues to be the largest market at USD 11,690bn with Japan and the UK at USD 2,954bn and USD 1,755bn respectively. Together they account for more than 78.3% of total pension assets.

Africa is characterised by a diversity of cultures, with different social and economic factors driving capital market development, performance of asset classes, as well as currency movements. An aggregate estimate of pension assets for the continent is therefore on a best endeavours basis and can be time sensitive due to factors such as currency volatility. Our review uses 16 countries in Africa, representing circa 65% of Africa's 2014 GDP as measured by the IMF, and also those with significant economic influence in each region. An aggregate number hides variation between countries, while currency volatility increases the fluctuation of USD equivalent amounts. Pension fund assets in Africa are currently estimated at USD 340bn representing only 21% of these countries' GDP.

1. Towers Watson Study. Estimated using the sixteen major pension markets

REGION	COUNTRY	Year	Currency	Currency Code	AUM (LCL) million	AUM (USD) million	GDP (IMF 2014) billion	AUM as % GDP
East Africa	Burundi	2013	Burundian Franc	BIF	20 000	13	3.0	0.4%
East Africa	Kenya	2013	Kenyan Shilling	KES	696 700	7 696	62.7	12.3%
East Africa	Rwanda	2013	Rwandan Franc	RWF	383 500	557	8.0	7.0%
East Africa	Tanzania (including Zanzibar)	2014	Tanzanian Shilling	TZS	6 587 400	3 799	36.6	10.4%
East Africa	Uganda	2013	Ugandan Shilling	UGX	3 481 170	1 259	26.1	4.8%
Egypt & Sudan	Egypt	2013	Egyptian Pound	EGP	39 397	5 509	284.9	1.9%
Nigeria	Nigeria	(Q3 2014)	Nigerian Naira	NGN	5 491 900	30 011	594.3	5.1%
Other East Africa	Seychelles	2012	Seychellois Rupee	SCR	12 779	970	1.5	65.8%
Other West Africa	Ghana	2013	Ghanaian Cedi	GHS	6 300	1 960	35.5	5.5%
South Africa	South Africa	Q1 2014	South African Rand	ZAR	2 976 355	257 753	341.2	75.5%
South Africa	Swaziland	Q1 2014	Swazi Lilangeni	SZL	18 364	1 590	3.8	41.4%
Southern Africa excl. SA	Botswana	2013	Botswana Pula	BWP	58 651	6 174	16.3	37.9%
Southern Africa excl. SA	Mauritius	2015	Mauritian Rupee	MUR	25 1224	7 912	12.7	62.2%
Southern Africa excl. SA	Namibia	2013	Namibian Dollar	NAD	105 267	9 116	12.0	76.1%
Southern Africa excl. SA	Zambia	2013	Zambia Kwacha	ZMW	10 295	1 609	25.6	6.3%
Southern Africa excl. SA	Zimbabwe	Q3 2014	US Dollar	USD	4 500	4 500	13.7	32.8%
Total						340 427		

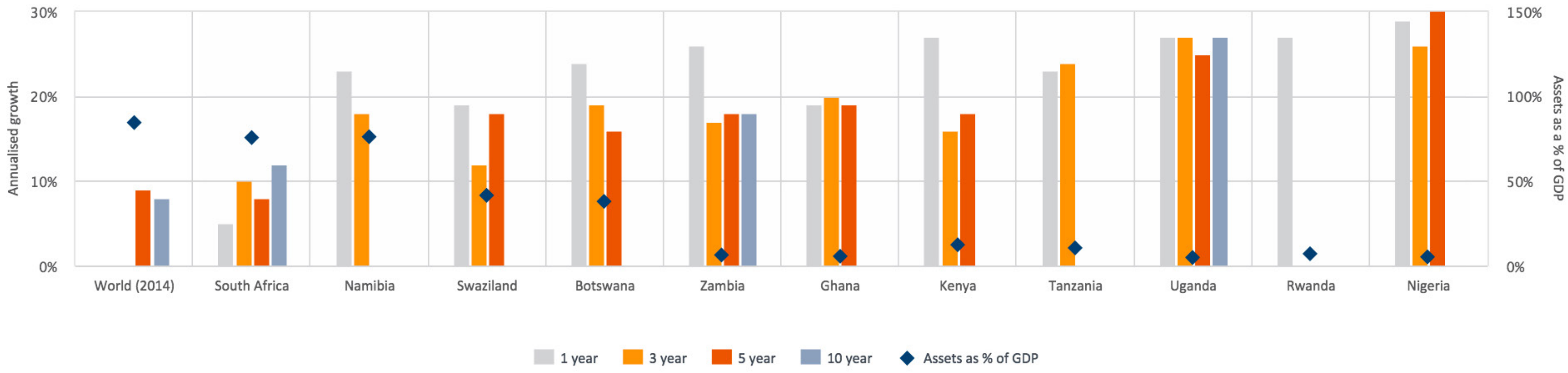
Source: Regulator annual reports and websites, other industry sources, EAC review of pension sector (Callund Consulting), Towers Watson Global Pension Study 2015, RisCura analysis
Note: GDP, Current Prices, IMF 2014, USDbn. Currency rates as at end 2014.

Similar to the global picture, the same big-country bias is present in Africa with 90% of the assets concentrated in Nigeria, South Africa, Namibia and Botswana. Within these countries, a number of large funds also tend to dominate. Examples include Government Employees Pension Fund (GEPF) in South Africa, Government Institutions Pension Fund (GIPF) in Namibia, Botswana Public Officers Pension Fund (BPOPF) in Botswana and a number of larger vehicles in Nigeria.

Pension fund assets globally are on the increase as countries move from unfunded to funded (or partially funded) status, and as many out-source pension fund management to private firms and move from DB to DC schemes. According to estimates by the OECD, private pension fund assets globally grew at an average annual growth rate of 8.2% over the period 2009 to 2013, overshadowing insurers and investment companies. In Africa, pension fund assets continue to grow for similar reasons, alongside an increase in coverage, as social security is extended to a larger portion of the population, formal and informal. The pension fund industry in Nigeria for example has grown from Naira 815bn in 2007 to Naira 5.492 trillion in 2014, which still only represents an average 7% coverage of the working age population (PenCom). The intro-duction of a basic safety net or retirement income as well as further introduction of private pension funds is likely to improve coverage and increase asset growth within the pension industry on the continent.

African pension assets growing at remarkable pace

Annualised growth rates (local currency) vs. Asset as a % of GDP



Source: Regulator annual reports and websites, other industry sources, EAC review of pension sector (Callund Consulting), Towers Watson Global Pension Study 2015, RisCura analysis
Note: Zambia figures exclude NAPSA GDP, Current Prices, IMF 2014, USDbn. Currency rates as at end 2014.

Africa has experienced tremendous growth in pension assets over the last five years. In much of sub-Saharan Africa where pension systems are older and more established, growth rates have been lower, ranging between 8% and 18% over the previous five years. Assets in East Africa have grown in excess of 20% on a consistent basis only overshadowed by Nigeria, which has seen growth between 25% and 30%. These trends are set to continue as this young continent moves towards increased coverage, and more inclusive and comprehensive systems.

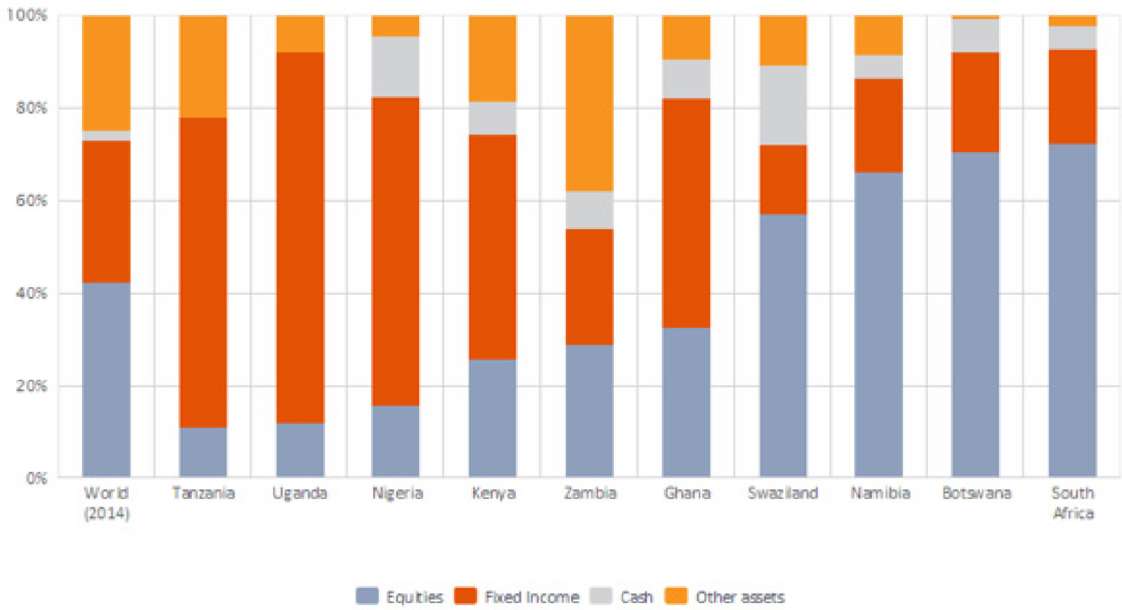
As African trade agreements are forged and trade blocs established, migration and labour mobility is set to increase, which raises the issue of pension portability. In recognition of this trend, some of the regions now have harmonisation goals, which will allow coordinated legislation and portability of pension benefits. An example of portability can be found in a memorandum of understanding that binds Burundi, DRC and Rwanda that allows portability of pension benefits between the countries. Portability is likely to gain importance as Africa continues to become increasingly connected by infrastructure, regional trading agreements; and as pension coverage reaches more of the working population.

Asset allocation

In most OECD and many non OECD countries, bonds and equities remain the two predominant asset classes for pension funds. While globally there is a larger allocation to equities (42.3%), the picture in Africa is more disparate. Broad asset allocation in sub-Saharan Africa has favoured equities the allocation of which, has shown a steady increase alongside the development of capital markets and regulatory change. In Nigeria and East Africa asset allocation is dominated by fixed income allocations, which predominantly constitute local bonds. When viewed alongside the high asset-growth in these regions, this is illustrative of regulation as well as local investment opportunities. It also typifies one of the larger challenges pension funds face; identifying appropriate local investment and development opportunities at the same pace as asset growth.

Significant allocation to fixed income in Nigeria and East Africa

Asset allocation of pension funds across Africa



Source: Regulator annual reports and websites, other industry sources, EAC review of pension sector (Callund Consulting), Towers Watson Global Pension Study 2015, RisCura analysis

Note: Zambia figures exclude NAPSA

Local regulation remains one of the main drivers of asset allocation. While much of African regulation is supportive of local investment, there are often significant differences between the regulatory allowances for pension funds, size of local capital markets and actual portfolio allocations. This is reflective of a number of factors, including familiarity with alternative asset classes, such as private equity, development of local capital markets and availability of investment opportunities. In many countries, assets are growing much faster than products are being brought to market, limiting investment opportunities if regulation does not allow for pension funds to invest outside of their own countries.

As pension assets continue to grow and international development assistance decreases, African pension funds have a pivotal role to play in facilitating inclusive growth and social stability. Larger pools of capital allow for investment in economic and capital market development locally and on the continent. Africa would benefit from local investment in longer term projects, including infrastructure. Local institutional investors lend credibility and a measure of validation, and often serve as a catalyst for greater external interest. Local investors also allow global peers to leverage local knowledge and networks. With longer investment horizons, pension funds can serve as anchor investors for infrastructure and social development projects.

While investment in private equity in emerging markets has historically come from DFIs, pension funds are slowly joining in. A number of countries including South Africa, Botswana, Nigeria and Namibia have led the way of alternative asset classes such as private equity. South African pension funds, for example, have been active in African private equity investment, both locally and across the continent, enabled by regulatory change. Since 2011, Regulation 28, which is the governing law for pension funds in South Africa allows up to 10% of pension assets to be invested in private equity, an increase from the previous 2.5% allowance for all 'other' asset classes. Nigeria first introduced broad pension reforms in 2004 when the National Pension Commission (PenCom) was established and laws were passed introducing mandatory contribution schemes for all unfunded public and private sector employees initiating the change from DB to DC schemes. Regulation in 2010 set the limit for private equity at a prudent 5% and also imposed certain minimum requirements for such investment including a minimum ten years' experience for investment professionals, a minimum 75% exposure to domestic Nigerian assets and required general partner (GP) investment. Draft regulation released for comment in early 2015 proposes to further relax these limits. While this enables investment, the requirements are quite prescriptive and have hampered practical implementation. Reforms continue and Nigeria is due to pass further legislation that will make provision for additional permissible investment instruments. This is expected to support development of local capital markets and increase allocations to equity markets.

Regulation can also enable regional and international diversification. Namibia for example allows up to 35% of assets outside the Common Monetary Area (Lesotho, South Africa, Namibia and Swaziland), however with a limit of 30% outside Africa, while Botswana allows up to 70% investment abroad. This allows pension funds the freedom to find suitable investment opportunities without being constrained by the current limitations of local market development. This is in contrast with East African countries such as Uganda and Tanzania where offshore investment is not allowed, although in the case of Tanzania it is unclear whether the restriction applies on a country or regional level (East African Community).

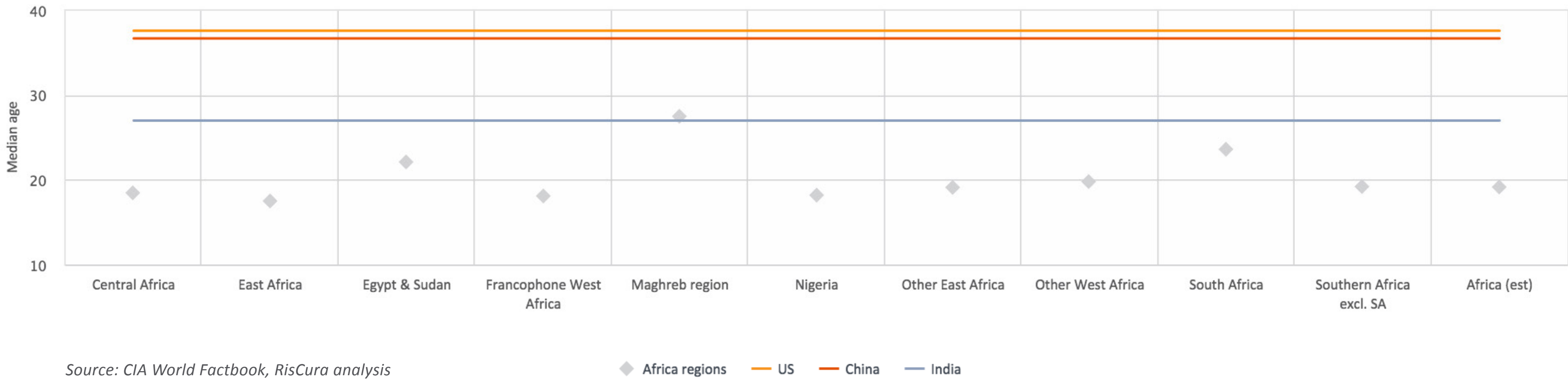
2.1.3 Demographics and labour market

The state of social security frameworks is typically a function of a country's environment as much as a response to it. While Africa proves no exception to trends of universally ageing populations, the continent still has a young population compared to the rest of the world. Uganda for example has a median age of 15 years, and also the youngest population in the world, the median ages across countries range from Uganda at the lower end, to 40 years of age or more in several European countries and Japan (CIA, 2013). There are a number of factors driving this demographic profile, amongst them higher than average population growth on the continent and an increase in life expectancy. Over time, a combination of these factors is expected to increase not only the percentage of the working age population in Africa, but also the number of years spent in retirement, creating greater demand for increased coverage and adequate pension provision. The combination of increased life expectancy and working age population is likely to lend strong support to growth in pension fund assets on the continent.

Population growth in africa is currently more than double that of the world population	*2013*	*2050 est**
Population growth (annual %) Sub-Saharan Africa	2.7%	
Population growth (annual %) World	1.2%	
*Africa as a % of world population	13.2%	22.7%

A youtful continent

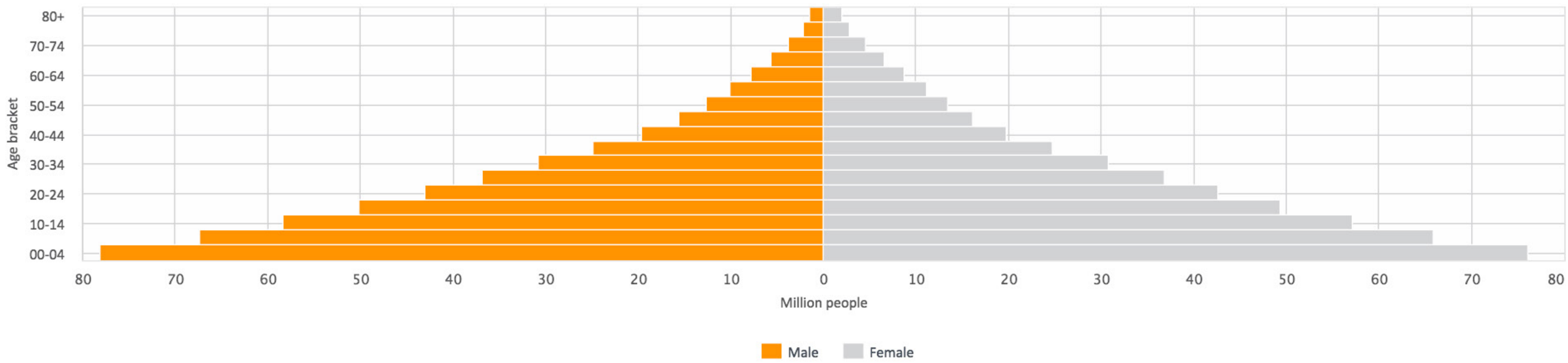
Median age of populations across regions



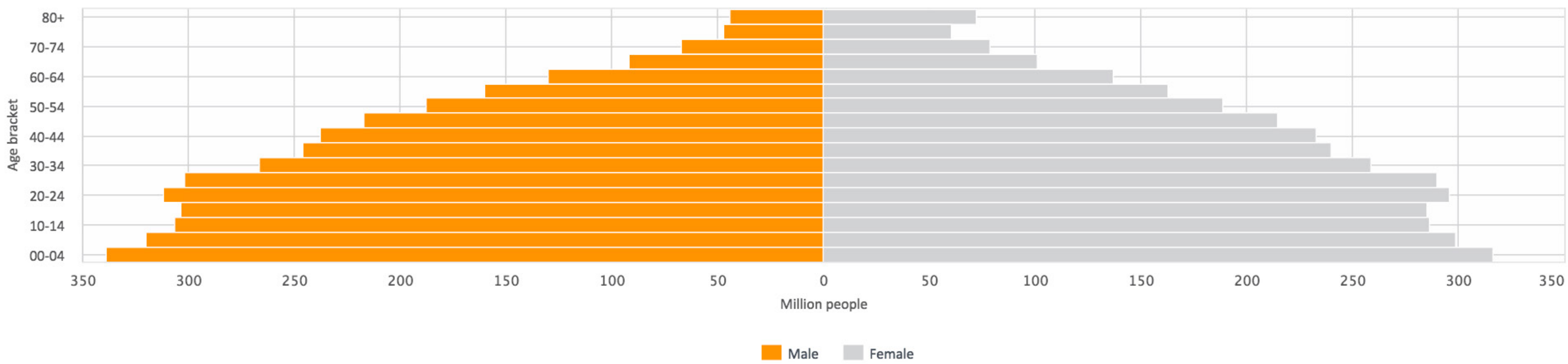
Source: CIA World Factbook, RisCura analysis

Working age population in Africa will increase, as will the number of years spent in retirement.

Population of sub-Saharan Africa (2013)

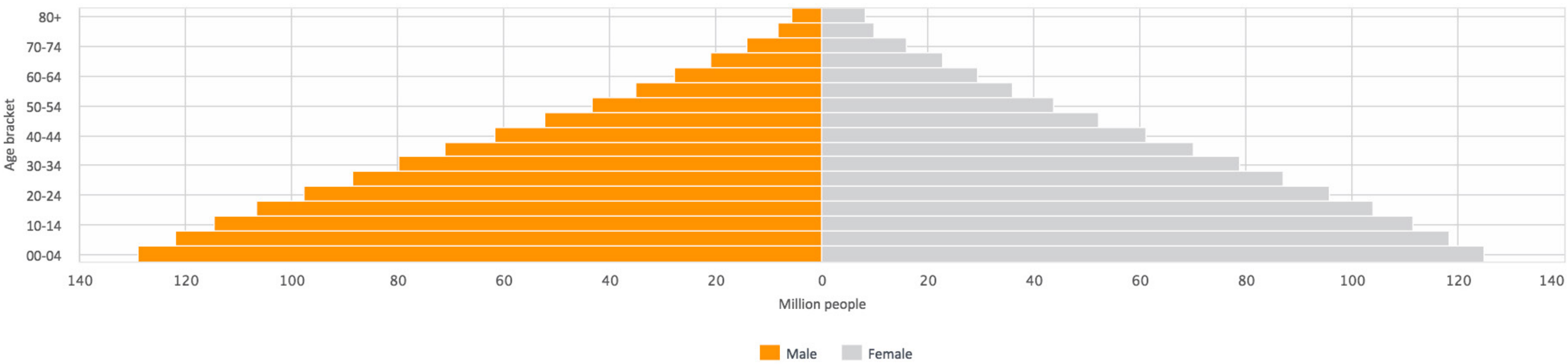


Population of the world (2013)

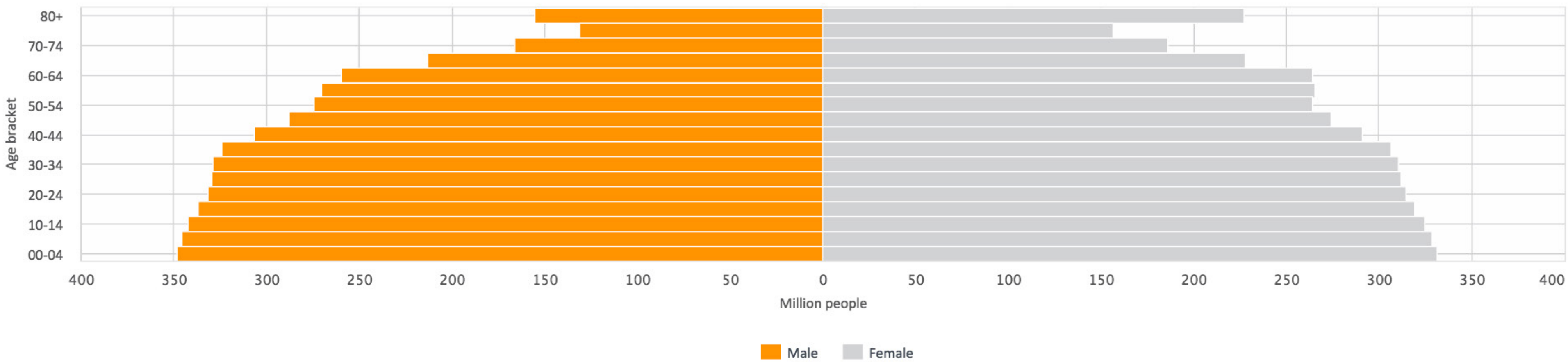


Source: World Bank, RisCura analysis

Population of sub-Saharan Africa (2050)



Population of the world (2050)



Source: World Bank, RisCura analysis

2.2 Insurance AUM in Africa

REGION	*Premiums (USDm)*	*Penetration Rate (Premiums/ GDP)*	*Population (m)*	*Density (Premiums per Capita, USD)*	*AUM 2012 (USDm)*	*Projected AUM 2018 (USDm)*
South Africa	54 871	14.28%	52	1 047	233 518	312 499
Maghreb region	5 097	1.18%	88	58	11 651	16 237
Southern Africa excl. SA	3 402	2.09%	40	85	8 577	14 678
Egypt	1 818	0.68%	81	23	6 127	11 289
Other	1 765	0.53%	466	4	4 477	7 164
East Africa	1 837	1.92%	139	13	3 972	8 778
Nigeria	1 828	0.68%	169	11	3 090	4 977
Other West Africa	791	2.00%	25	31	775	1 008
Francophone West Africa	244	1.33%	20	12	619	987
Central Africa	239	1.30%	2	149	606	850
Total	71 891	3.56%	1 082	66	273 412	378 467

Source: Swiss Re, UN Population Division, IMF, African Insurance Organisation, NKC Research, S&P Capital IQ, RisCura analysis

RisCura estimates that African insurance AUM totals approximately USD 273bn, with the vast majority of these assets coming from South African insurance companies. This is the result of an insurance penetration rate of more than 14% in South Africa, far higher than any other region on the continent, and one of the highest penetration rates globally. This is a further indicator of South Africa's global third place ranking in financial market development.

Insurance penetration is expected to grow significantly across all African markets, according to BMI Research, which has the potential to significantly increase insurance assets available for investment in those markets. In particular, East Africa, Egypt and Southern Africa (ex-SA) are expected to show strong increases in insurance penetration over the next five years.

It is clear globally that higher penetration ratios lead to greater AUM, meaning that as penetration increases in Africa, insurance assets can be expected to grow, resulting in larger pools of domestic capital. The overall increase in AUM of African insurance companies from 2012 to 2018 is expected to be 38% compared to the combined GDP growth of 19% over the same period. Outside South Africa this growth is expected to be significantly higher.

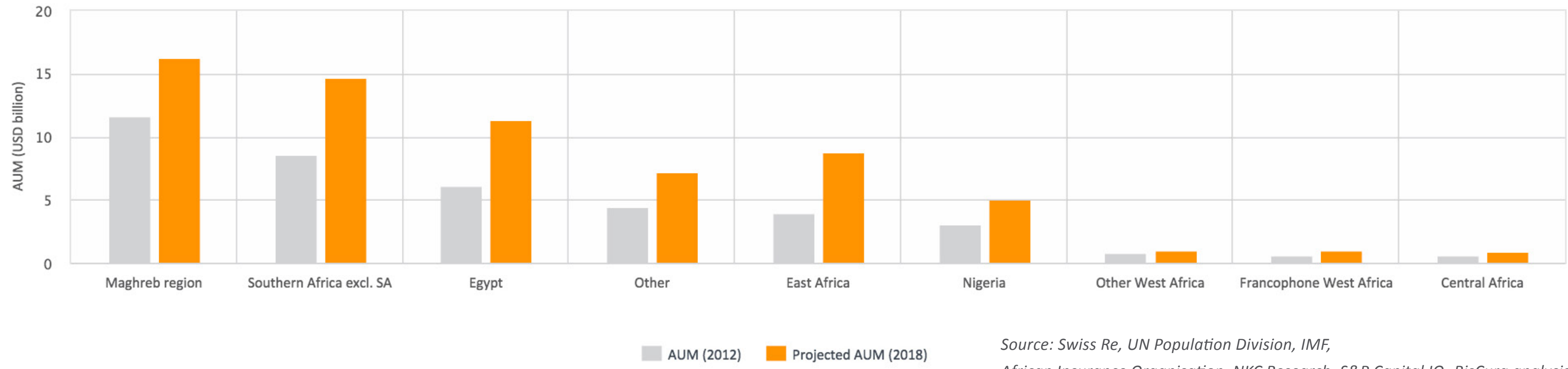
Across the world, 65% of insurance premiums written are contributed by the G7 economies, which only constitute 10% of the world's population. The average premium spend in G7 countries in 2012 was USD 3 910 compared to USD 120 for emerging markets including Africa. In 2012, Africa's contribution to all global premiums written was 1.55%, well below its portion of global GDP, and reflective of the under-penetration of insurance in Africa.

The East African insurance market is relatively well developed with Kenya leading the pack. An association of Kenyan insurers released a plan in 2011 to grow the industry by 22% p.a. by simplifying and modernising the products, using social media to advertise, and educating customers.

Public disclosure of insurance AUM is weak in many parts of the continent, but RisCura has estimated these assets based on publicly available information.

Significant growth in insurance AUM expected

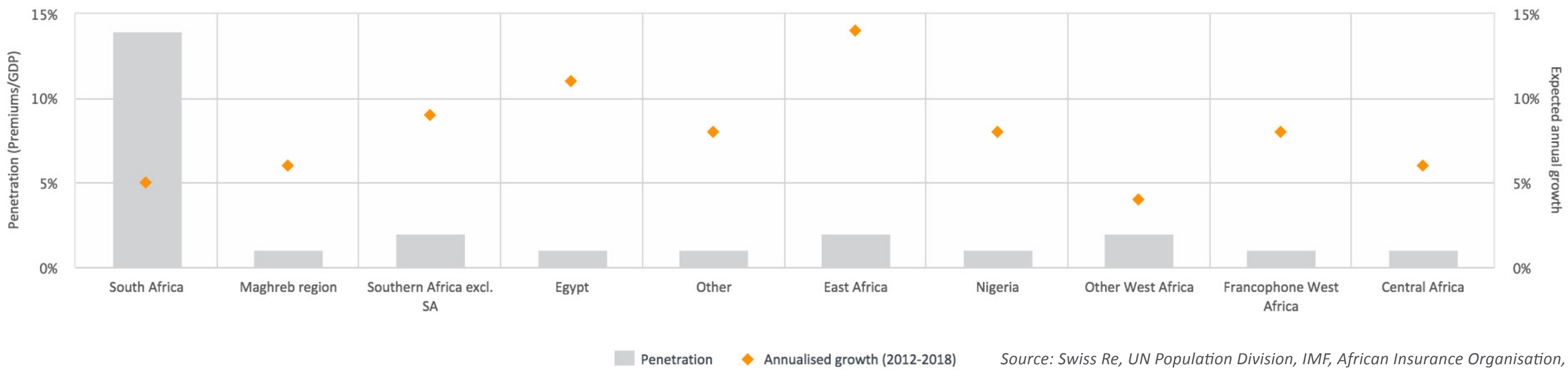
AUM by region in 2012 and 2018 (Projected)



Source: Swiss Re, UN Population Division, IMF, African Insurance Organisation, NKC Research, S&P Capital IQ, RisCura analysis

Potential for insurance growth

Insurance penetration and expected annual growth in AUM by region



Source: Swiss Re, UN Population Division, IMF, African Insurance Organisation, NKC Research, S&P Capital IQ, RisCura analysis

South Africa accounted for 76% of premiums written in Africa in 2012, with a penetration rate of 14.28% compared to the continent average of 3.56% and global average of 6.5%. The average penetration ratio in Africa (ex-SA) is 1.04%. Globally, life and non-life insurance premiums are roughly equivalent, but in Africa (ex-SA) life premiums are overshadowed by non-life premiums by more than three to one. The global average for annual life insurance premiums per capita is USD 373 compared to USD 5 for Africa (ex-SA). Individuals will only start fulfilling their life insurance needs once their short-term needs are fulfilled and with low income prevalent in Africa, this leads to many individuals not opting for life insurance. Additionally, in many parts of the continent there are traditional substitutes to life insurance such as community collections, as well as cultural attitudes to death that have limited the uptake of life insurance in some countries. In the case of death 0.3% of Africans make use of insurance products, 14% borrowed money and 25% make use of savings; a similar scenario is the case for serious illness. In the case of destruction of agricultural crops or livestock, only 0.2% made use of insurance, 45% had no way of mitigating the loss and 18.6% made use of their savings to offset the loss.

Improving economic prospects, as well as the trend of urbanisation, is beginning to change these practices, and forecasts of life insurance penetration have increased. As discretionary spending increases and asset-backed lending increases, short-term insurance penetration is also expected to improve, resulting in larger pools of insurance assets on the continent. Research has shown that the main contributors to an underdeveloped insurance market are a combination of costs, poverty, shortage of data, lack of distribution channels and underdeveloped financial systems. It is further clear that the more educated people are, as well as the wealthier they are, the more likely they are to buy insurance products. This supports the expected growth prospects for African insurance, as the growth of the middle class improves both education and income levels.

Hurdles in insurance growth

Reasons for not having insurance

Source: EFInA

2.3 Development finance institutions in Africa

Development Finance Institutions (DFIs) are government-funded institutions that make investments in sectors and countries that would not otherwise attract significant capital. DFIs generally aim to have a developmental impact in the markets in which they invest, alongside the requirement for sustainable returns. Over and above the primary impact of financing development projects, there is a significant secondary impact precipitated by DFI investments. Private investors often tend to follow suit in frontier markets pioneered by DFIs, enabling the second wave of investors to leverage off established expertise and a coordinated strategy.

In 2005, the combined committed portfolio of DFI investment (including loans, equity, guarantees and debt) amounted to USD 182bn (te Velde, Warner, 2007), with USD 45bn of new commitments being made, indicating a relatively high turnover ratio. Although, due to very limited information on DFI commitments, updated figures are not readily accessible, anecdotal evidence implies that this figure has, and continues to, increase significantly over time.

Some of the major DFIs investing in Africa are the International Finance Corporation (IFC), the Overseas Private Investment Corporation (OPIC), the CDC, as well as a number of European DFIs such as the European Investment Bank (EIB), Proparco, DEG, FMO, Swefund, Norfund, Obvium and a few others. There are also several African DFIs, the largest of which is the African Development Bank, and several regional DFIs.

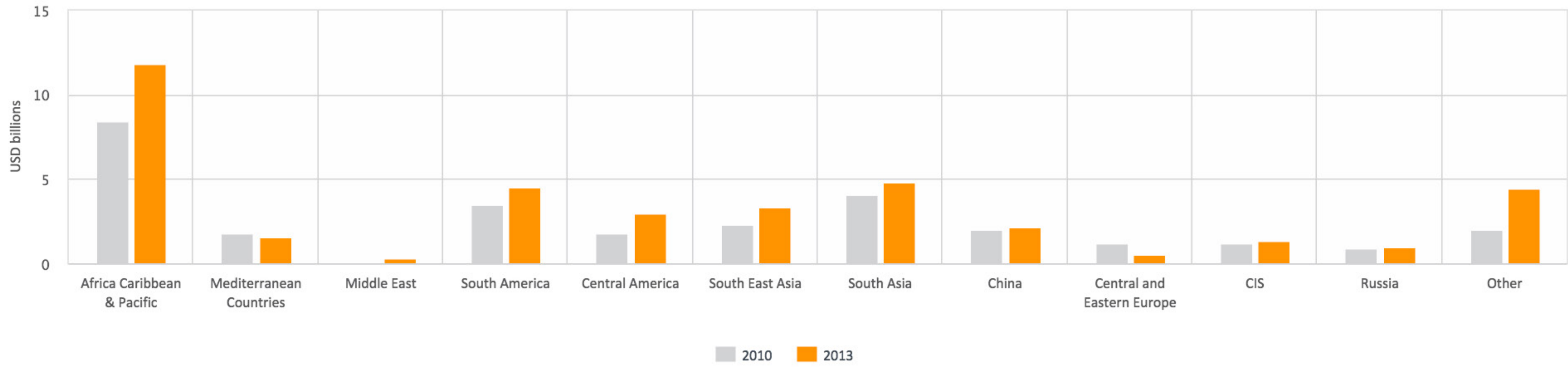
2.3.1 Global allocation of AUM

In a 2010-2011 African Private Equity survey conducted by Preqin, 92% of DFI respondents saw Africa as presenting "attractive investment opportunities". In addition to this, all DFI respondents active in Africa-focused Private Equity funds were set to make commitments the following year with an overwhelming 92% looking to increase or maintain their allocations in the long term. Although these results are purely qualitative, they reflect a clear positive sentiment towards DFI investment in Africa.

At the end of 2010 European DFIs (EDFI) total portfolios amounted to USD 29bn. By 2013 this figure had increased to USD 38.7bn. Unfortunately, the total allocation to Africa is not disclosed, but 30% (29% 2010) was invested in the Africa, Caribbean, Pacific (ACP) region, including 5% to South Africa. This translates to an increase in EDFI's investment in ACP of USD 3.4bn, from USD 8.4bn in 2010 to USD 11.8bn in 2013.

EDFI Investment in ACP regions is increasing

EDFIs global distribution 2010 and 2013



Source: EDFI Annual Reports, RisCura analysis

2.3.2 Global new deal allocation

The ACP region continues to attract the highest allocations of new capital from EDFIs, both in value and in number of deals. In 2013 EDFIs invested in a total of 202 new deals in ACP, amounting to USD 2.5bn of new investment. This level is significantly above the average of 51 deals amounting to USD 669m and the next highest; South Asia at 70 deals and USD 1.1bn.

Africa receives the lion's share of new deal flows from EDFIs

New deals 2013

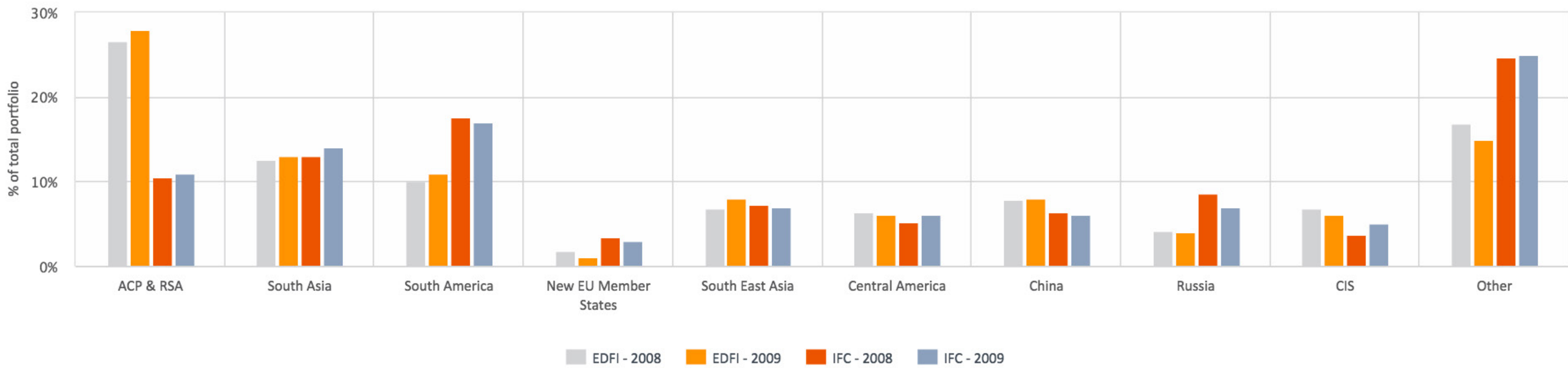
Source: EDFI Annual Reports, RisCura analysis

Comparing two DFIs

Comparing the allocations of EDFIs vs. the International Finance Corporation (IFC), the world's largest DFI in terms of the size of DFI investments, over the period of 2008-2009, EDFIs had a notable slant towards the ACP region. EDFIs continued to increase the value of their investment by 19%, marking an increase of 1% in its portfolio. By comparison the IFC continued its focus on South America, while keeping their overall nominal allocation constant.

EDFIs invest more of their portfolio in ACP, while the IFC deploys a greater portion in South America

Global EDFI distribution comparison 2008 and 2009



Source: ODI (te Velde) 2011, RisCura analysis

Despite the divergence of geographic focus, the increase in DFI investment in the wake of the Global Financial Crisis (GFC) signals a counter-cyclical element to the flow of DFI capital. It then follows that, in times of contraction, when conventional forms of funding such as debt, tend to diminish, there are greater investment opportunities for DFIs.

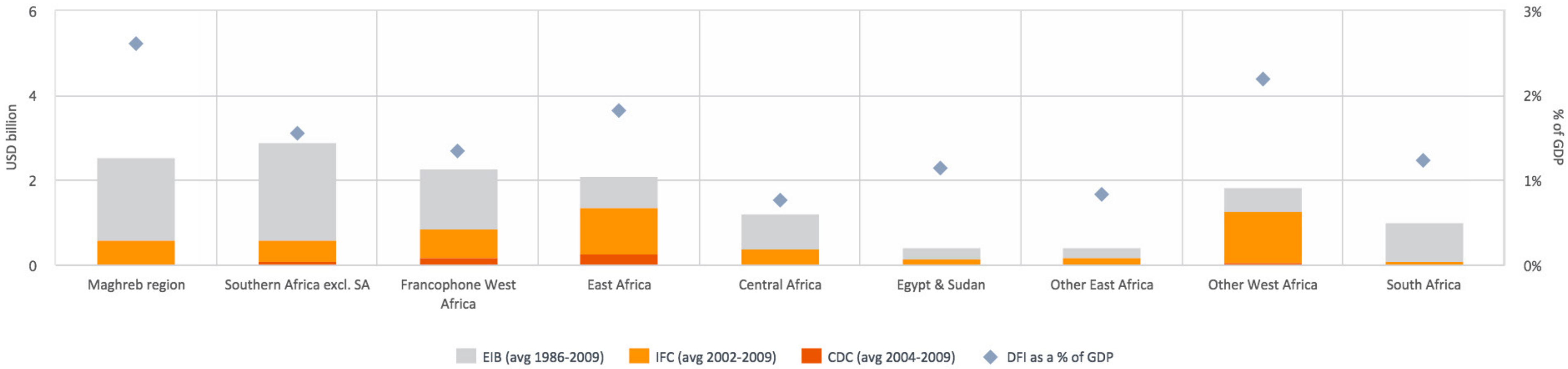
2.3.3 Regional DFI vs GDP

When comparing the regional distribution of DFI investments in Africa from three of the largest DFIs (IFC, EIB and CDC), Southern Africa (ex-SA) receives the highest nominal allocation of USD 2.9bn in contrast to Egypt & Sudan which receives USD 400m.

However, when comparing the investment to regional GDP figures the Maghreb region has the highest percentage, implying a higher overall impact for the region. By contrast, Central African DFI investment makes up the lowest portion of GDP.

DFI investment into the Magreb region is equivalent to almost 3% of its GDP

African regional DFI vs. GDP



Source: ODI (Kingombe, Massa and te Velde) 2011, RisCura analysis

2.3.4 DFI practices in Africa

The focus, and accordingly the investment allocation, of different DFIs can vary broadly. This can be driven by the relative wealth of investee countries, by sector or geography depending on the focus and the ultimate goals of each DFI.

Certain DFIs tend to target specific income sectors. For example, Proparco and COFIDES tend to focus on certain relatively wealthier countries, while others such as CDC and the IFC target more low income regions. CDC has an explicit strategy to make 75% of its investments in low income countries, i.e. countries with GDP per capita of below USD 905 (as per the World Bank 2006 definition).

Similarly various DFIs have specific a geographic focus. The IFC, for example, has an apparent focus on Latin America, while European DFI's tend to have a clear skew towards Africa. Again, CDC has a specific prescription to target 50% of its investments into sub-Saharan Africa.

The major sectoral focus of DFIs is typically toward infrastructure and finance. The main reasons for this are that these deals tend to be on a very large scale and, by their nature, are seldom funded domestically, and may be too risky for private capital. Typically there is far less DFI activity in sectors such as agriculture and industry, as these sectors are more easily catered for by the private sector, given the smaller scale and consequently lower barriers to entry.

3 ♦ Africa's listed equity

3.1 Performance

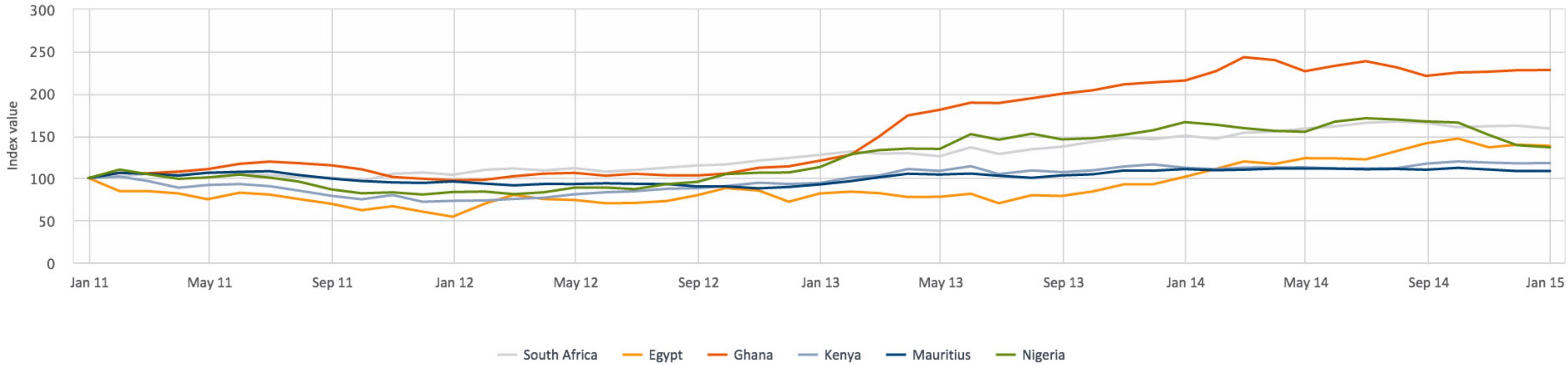
Over the last five years, local currency returns of the major African listed equity markets have performed consistently with the continent's growth expectations. Certain markets have suffered from political strife, but have recovered well to continue returning significant growth to investors. 2014 was a year categorised by general underperformance relative to global markets as commodity prices slumped; however some of the smaller markets did well with Egypt returning to stellar performance.

Although index returns will be quoted in local currency, international investors will assess the return on their investment in their domestic currency, for example the US dollar. Exchange rate fluctuations of African currencies to the US dollar, primarily due to the heavy reliance on commodity prices for exports, add additional volatility to the local currency return. The success of currency pegging and exchange control regulations to reduce exchange rate fluctuations has been mixed, resulting in the persistence of this risk.

Much work is being done by providers across the continent to enable the hedging of currencies. This is still a relatively expensive exercise as the derivatives that are written rely on the liquidity of the underlying currencies. As with the equity markets in general, the liquidity of African currencies is improving, with spreads narrowing over time. Macro-economic shocks do tend to significantly affect the tradability and liquidity of currencies.

African indices have recovered after lows in 2012

Major index returns in local currency

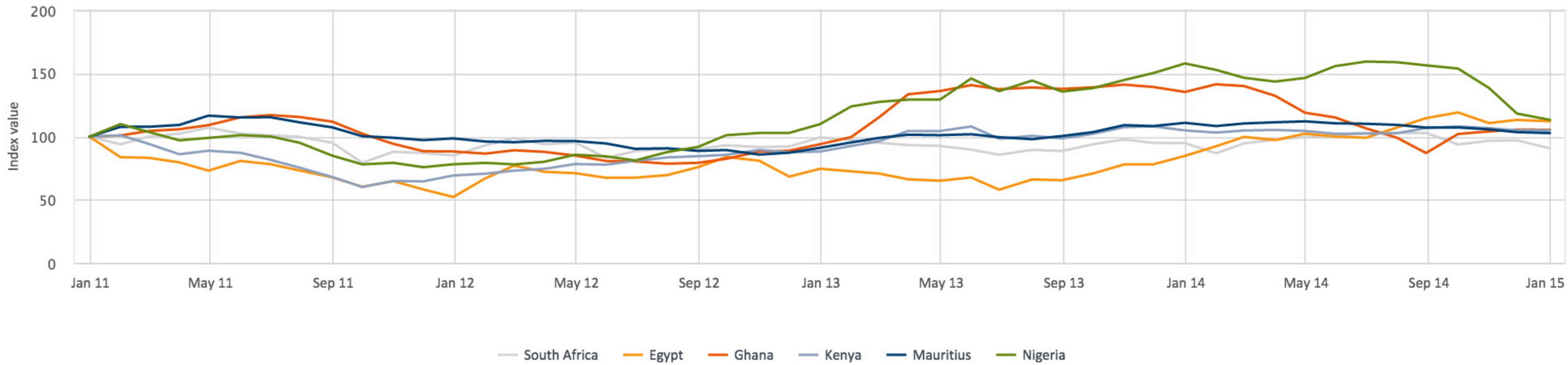


Source: S&P Capital IQ, RisCura analysis

The maximum period for analysis is 4 years as the date of inception of the GSE Composite Index (Ghana) is January 2011.

USD returns are more volatile

Major index returns in USD



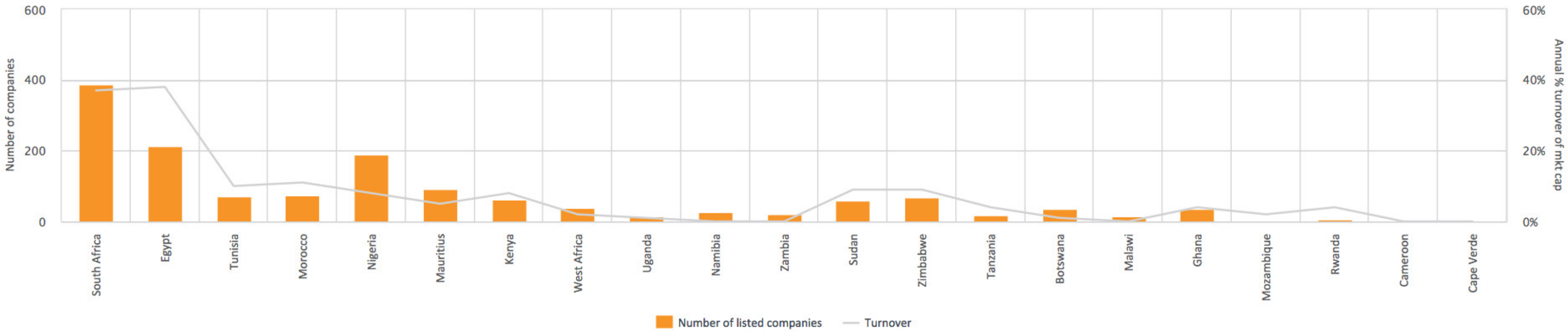
Source: S&P Capital IQ, RisCura analysis

The maximum period for analysis is 4 years as the date of inception of the GSE Composite Index (Ghana) is January 2011.

3.2 African stock exchanges

Liquidity still poor, but improving

Number of companies listed vs number of companies traded



Source: ASEA (African Stock Exchange Association), RisCura analysis

There is also a significant disparity between the level of development, size and liquidity of exchanges across Africa. However, African stock exchanges as a whole continue to develop at a rapid rate. Organisations such as ASEA (Africa Securities Exchange Association) have done much to enhance governance and promote the development of all its member exchanges. ASEA's stated goals are to improve Africa's securities exchanges by focusing on increasing the number of listings of strong local companies; improving technology, reporting and data availability; reducing fees and other innovations to increase ease of investing.

Churn is a good indication of the liquidity of a market. South Africa's JSE leads the way turning over close to 35% of its listed market cap annually with the remainder of the continent's exchanges below 10%, with the exception of North African markets.

Interestingly the disparity between the actual quanta of listings amongst the exchanges is relatively small when compared to the market capitalisation, though the proportion of traded counters to the number listed does show some stagnation. This is, however, much improved over previous years.

As a result of many factors, liquidity on African stock exchanges is low when compared to international markets. This is often the result of the small number of listed companies, and the tightly-held nature of those companies that result in relatively low free floats. Whether as a result or a cause of this, high transaction fees also play their part in restricting trading activity on African exchanges. This poor liquidity is a significant inhibitor to international investment, and can also have the consequence of poor pricing of markets when only small quantities of shares trade.

3.3 Investability of Africa's listed markets

Indices provided by data vendors are used by institutional investors as proxies for African markets by return (performance benchmarking), valuation, liquidity and diversification. There are numerous choices as most are designed for a specific type of investor, as well as what their perceived idea of "Africa" is. It is interesting to note that the worst performing index is S&P Access Africa, the only index with exposure to shares listed outside the continent with 36% in South Africa, 28% in UK and 22% in Canada. The main reason for this was the 56% sector bias of these ex-Africa listed shares to the energy and resources sectors.

The best performer was MSCI FM Africa with no exposure to South Africa, no exposure to shares listed outside the continent and 50% exposure in Nigeria. This index had a 50% exposure to financials.

Variety of Return Characteristics of Africa Indices

INDEX	*S & P Pan Africa BMI*	*S & P Access Africa*	*S & P Africa Frontier BMI*	*MSCIEFM Africa x South Africa*	*MSCIEFM Africa*	*MSCIFM Africa*
1year	4.37%	- 20.16%	- 16.79%	- 5.43%	4.25%	- 12.88%
3year	26.88%	- 30.73%	- 65.57%	58.80%	22.2%	75.75%
5year	44.17%	- 22.31%	50.17%	22.60%	42.51%	70.80%
Ann. 5 Year	7.59%	-4.92%	8.47%	4.16%	7.34%	11.30%

Source: MSCI Indices; S&P Dow Jones Indices; RisCura Analysis

These indices attempt to represent the investible portion of the markets they cover, by investing via the following geographical locations:

Listing Allowance of Africa Indices

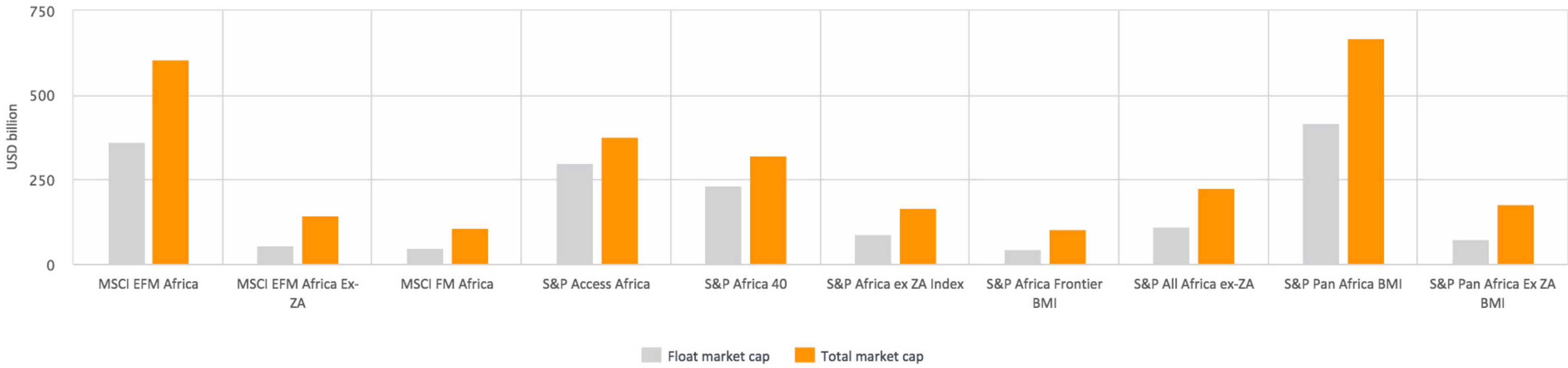
INDEX	*South Africa Listings*	*Ex-Africa Listings*
S & P Pan Africa BMI	yes	no
S & P Access Africa	yes	yes
S & P Africa Frontier BMI	no	no
MSCI EFM Africa x South Africa	no	no
MSCI EFM Africa	yes	no
MSCI FM Africa	no	no

Source: MSCI Indices; S&P Dow Jones Indices; RisCura Analysis

Company ownership traits in Africa imply relatively lower free float in comparison to the larger emerging and developed markets as shares are usually held with a longer term view as a function of lower capital mobility - parent companies owning a large percentage of issue as well as a large proportion of family owned businesses coming to market. Of the Africa indices on offer, the average investable ratio is 54%, compared to the UK listed market, which is 85% investable. By decreasing the gap between Total Market Cap and Float Market Cap there will be more liquidity in the market that will lead to improved price discovery.

What proportion of indices are investible?

Free float market cap vs. total market cap

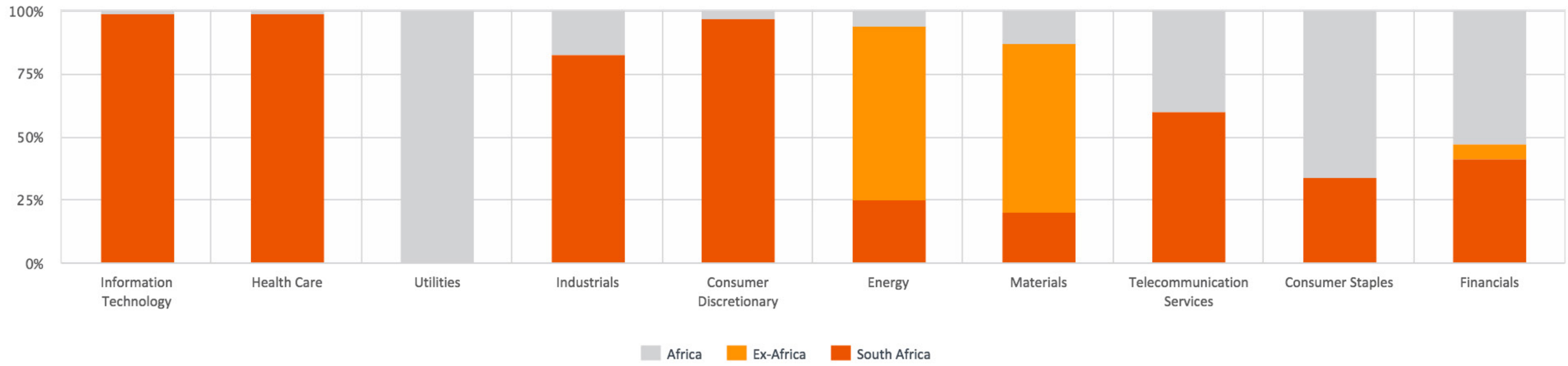


Source: MSCI Indices, S&P Dow Jones Indices, RisCura analysis

By merging all African Indices together and separating them by sector, it becomes clear that exposure to energy and materials (mining) companies can be gained predominantly though African companies listed in the UK, Canada and the US. IT, healthcare, industrials, consumer discretionary and telecoms are predominantly listed in South Africa, while utilities, consumer staples and financials are accessible through a broader range of African markets.

Energy and Materials predominantly accessible ex-Africa

African indices listings according to sector exposure

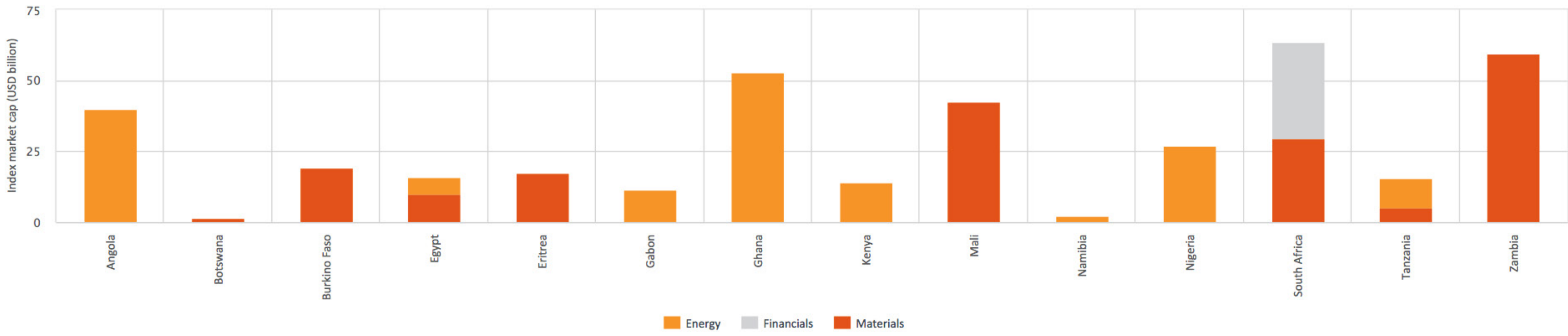


Source: MSCI Indices; S&P Dow Jones Indices; RisCura Analysis

Looking to ex-Africa listings, investors are able to gain access to countries without stock exchanges. Unsurprisingly these are countries dominated by GDP exposure to the materials and energy sectors. Including ex-Africa listings also improves liquidity.

Ex-Africa listings improve access to Africa's resources sector

Large ex-Africa listings by sector



Source: MSCI Indices; S&P Dow Jones Indices; RisCura Analysis

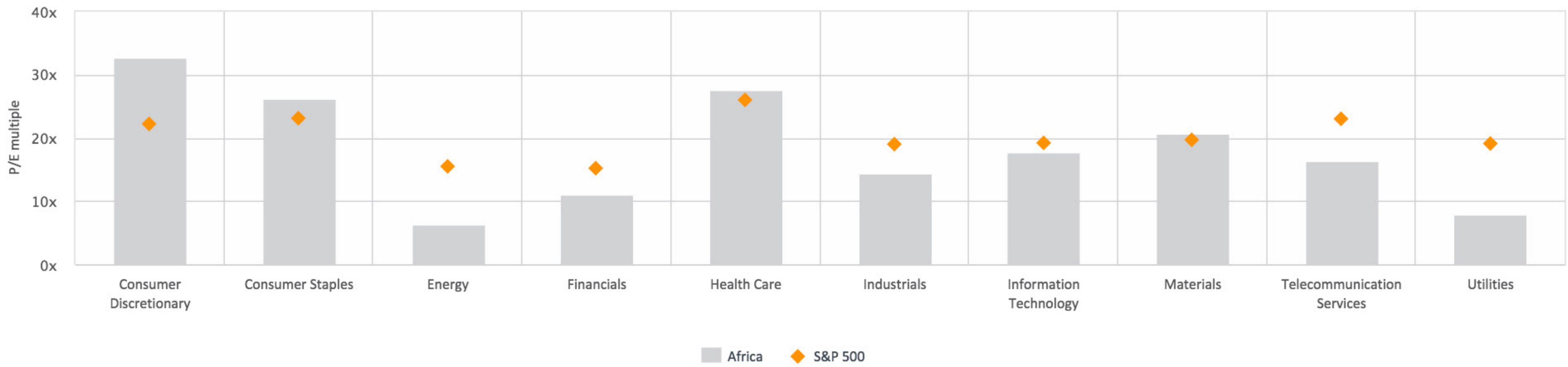
Previous versions of this report have spoken to the disconnect between what is accessible in Africa via the listed markets in relation to the GDP outputs of the countries in Africa , which are linked to expected growth prospects. By including all available access mechanisms for listed investing (Africa, South Africa and Ex-Africa) the numbers begin to change. Nonetheless this is still an issue in many sectors across countries.

3.4 Fundamentals

Price to earnings (P/E) ratios are an indication of how highly listed markets are valued at a point in time. Looking at the S&P 500 and the combination of African Indices gives some insight as to how African companies are priced in relation to developed market valuations. Interestingly, the analysis shows no clear trend, as some sectors are more expensively priced in Africa, some are cheaper and some are in line.

How expensive are African sectors compared to America

P/E ratios in Africa compared to the S&P 500

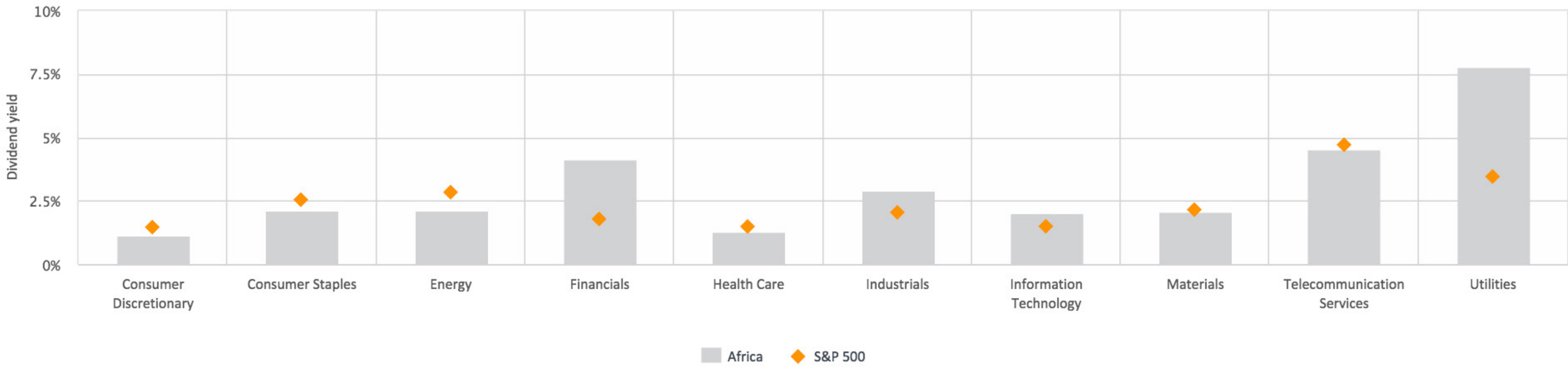


Source: MSCI Indices; S&P Dow Jones Indices; FactSet; RisCura Analysis

The yield available from a dividend perspective is also quite interesting by certain countries. Looking at the S&P 500 and the combination of African Indices as stated above, the dividend yields are mostly in line except on Financials, Industrials and especially Utilities where the African indices have a higher yield.

Earnings on investments for African sectors compared to America

Dividend yields of African sectors compared to S&P 500



Source: MSCI Indices; S&P Dow Jones Indices; FactSet; RisCura Analysis

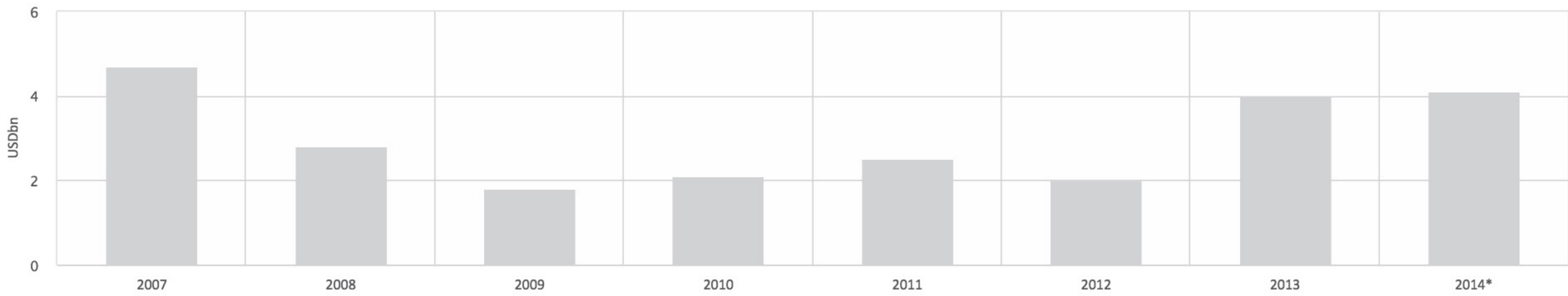
4 ♦ Africa's private equity markets

4.1 Private equity fundraising over time

The uptick in private equity (PE) fundraising across the continent over the last two years is an exciting indicator of good things to come in the industry. With the huge increase of dry powder, one can expect far larger volumes of cash invested in Africa in the coming years. This has already started to materialise as USD 8.1bn worth of deals took place in 2014, the second highest on record (AVCA). One of the biggest opportunities for investment in Africa is small and mid-cap companies in East and West Africa, where there is a huge demand for capital and insufficient supply (McKinsey 2014).

Fundraising reaching pre-crisis levels

PE fundraising in Africa over time



Source: AVCA Private Equity Data Tracker

**Note: Fundraising in 2014 is estimation.*

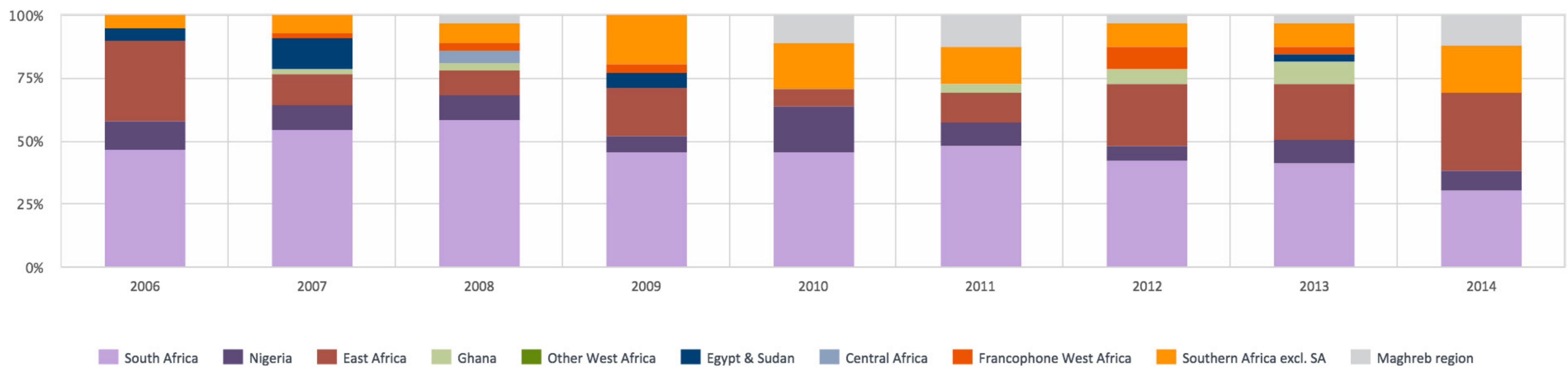
4.2 Africa's PE geographic focus

South Africa's portion of the pie appears to be diminishing marginally each year, as investors realise the potential elsewhere on the continent. Additionally, South Africa has recently gone through a period of difficulty with major strikes in the minerals sector disrupting business and an energy crisis putting strain on the manufacturing sector and economic growth.

East Africa has seen a significant amount of activity in the last three years compared to the five year period prior to 2012.
Note: RisCura has found it difficult to access transactions data from the Maghreb region and Egypt & Sudan.

South Africa losing dominant position

Number of PE entry transactions by region



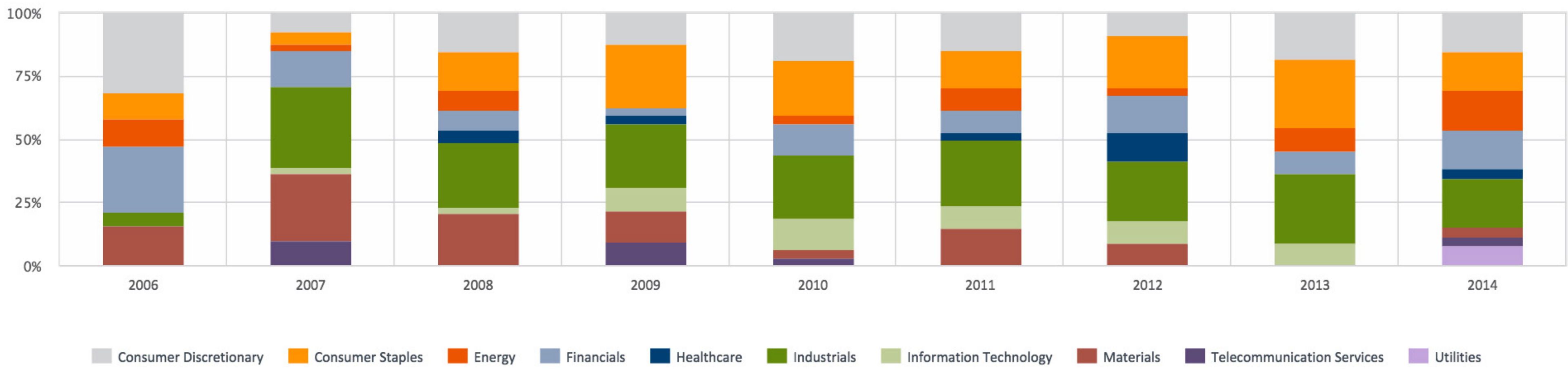
4.3 Africa's PE sector focus

There has been an increase in activity in the Energy sector in 2014 with transactions taking place across the continent within the oil & gas and renewables industries.

Industrials and financials remain popular targets for investment as the continent has high growth prospects in transportation, logistics and banking.

Uptick in Energy investment

Number of PE entry transactions by sector



Source for both graphs: RisCura

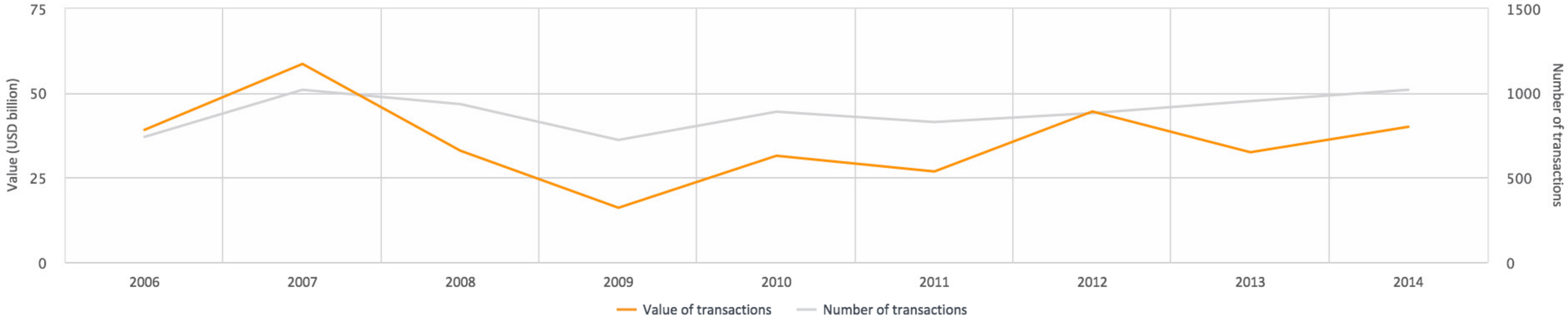
4.4 M&A activity in Africa

M&A activity across the continent has continued to trend upward both in value and number of transactions.

M&A activity continues to recover

M&A transactions in Africa over time

Source: S&P Capital IQ, RisCura analysis

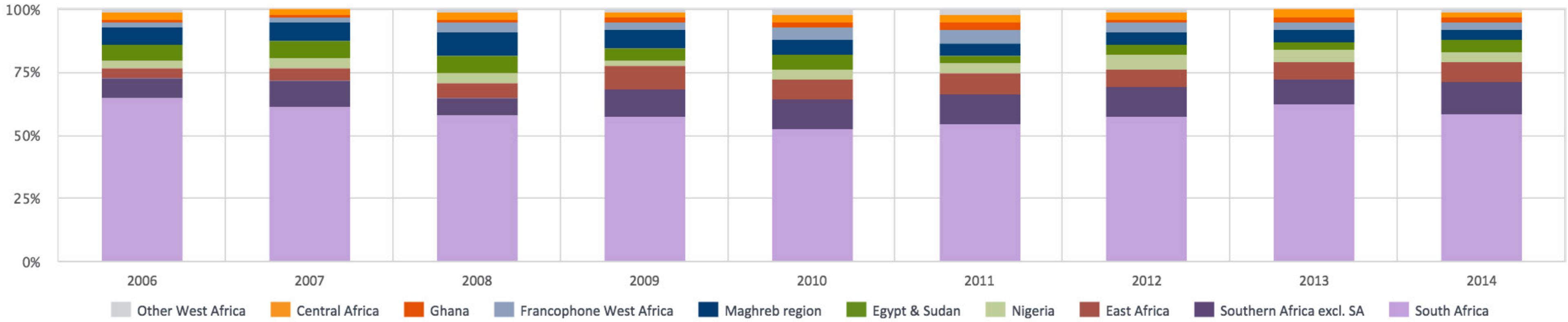


The Maghreb region has seen a decline in activity as a percentage of the continent over the past few years, as political unrest and slow growth relative to the rest of the continent characterise these markets.

A very clear growth in activity is evident in Nigeria from 2009 to 2013, while in 2014 activity slowed marginally relative to the continent. This could be attributed to the uptick in Boko Haram-related violence over the year and more recently to the gloomy outlook in the Oil and Gas industry in the country, one of its largest drivers of growth over the past few years, as well as investors exiting due to continued theft, spills and insecurity in the industry.

South Africa continues to attract the majority of M&A deals.

Number of M&A transactions by region



Egypt and Sudan understandably saw a major decline in activity over the 2011-2013 period compared to 2010, as Egypt underwent sustained political unrest and South Sudan seceded from Sudan, causing much uncertainty in the region. There was a notable uptick in activity in 2014, as Egypt's economy began to recover from the period of turmoil.

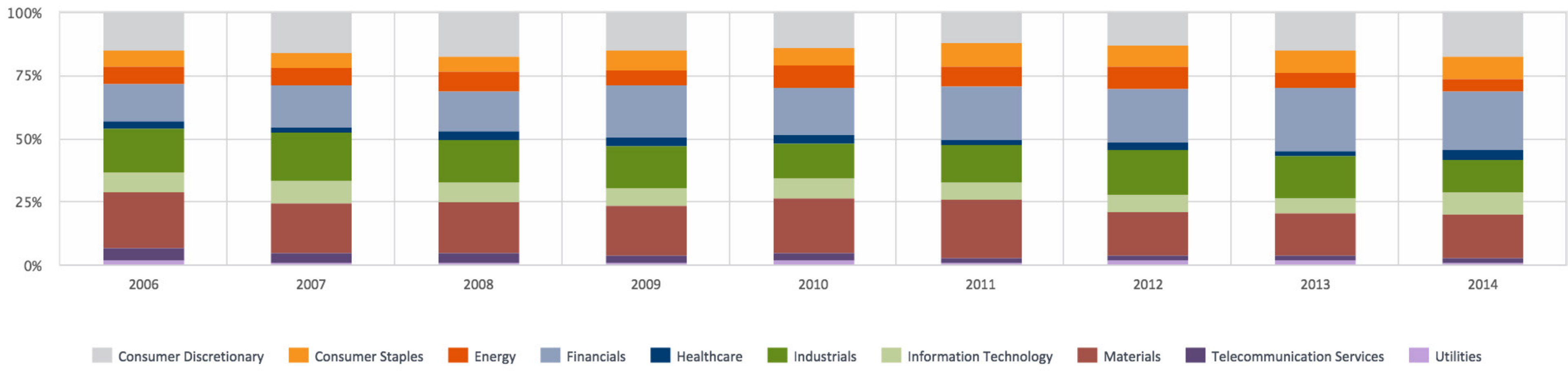
Southern Africa (ex-SA) and East Africa make up the largest portion of M&A activity on the continent (ex-SA). These regions remain a persistent place of interest for investors and inter-regional activity. South Africa has constituted between 53% and 63% of all activity over the period under review.

Activity in the consumer discretionary industry has steadily increased from 2011 to 2014, with transactions in the tourism, vehicles and textiles industries standing out in 2014. Financials and Industrials remain strong industries for investment, in line with the trends of the PE transaction activity.
The decline in the telecoms industry activity is not necessarily an indicator of a slowdown, as this industry has been lumpy in the past (see 2011).
This is due to the large size of individual projects and infrastructure build that occur sporadically.

Rising interest in Financials in Africa

Number of M&A transactions by sector

Source: S&P Capital IQ, RisCura analysis



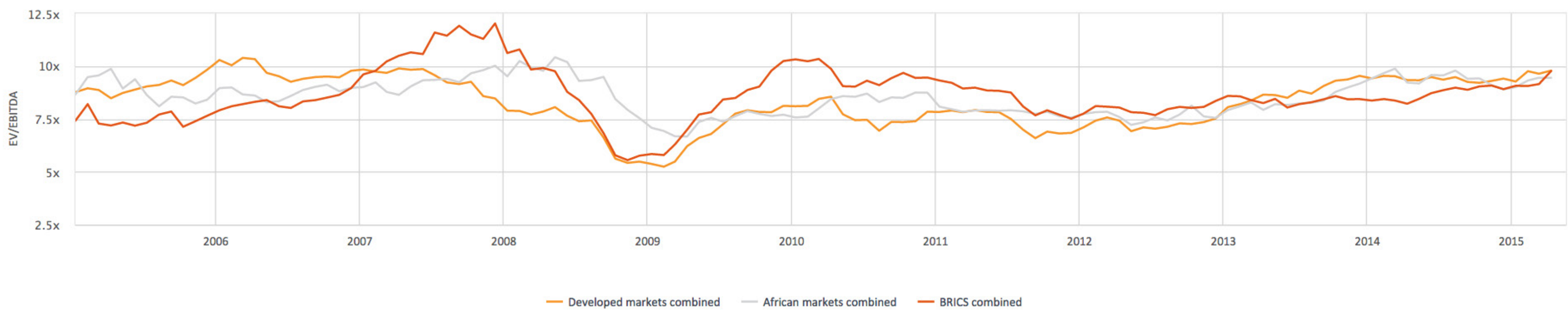
4.5 Listed EV multiples

Africa's listed markets' reactions to the global financial crisis in 2008 were very much in line with that of the rest of the world, when compared to both developed markets and the BRIC countries. While the BRICs appeared to be lagging from the start of Q3 2013, they showed a strong recovery in Q2 2014, which brought them in line with the developed and African markets, driven by a strong increase in market multiples in India. The strong growth in African prices over 2013 appears to have slowed in 2014. The price of African markets at 31 December 2014 was 8.90x, lower than the 9.17x at the end of 2013.

The reason for the decline in prices in 2014 can be more closely analysed by country. While Ghana appears to be one of the major drivers for 2013's strong performance, the market multiple fluctuates significantly over 2014, ending the year 20% below the previous year. Nigeria's stock market traded down 35% from August to December 2014, with uncertainty and continued violence leading up to the national elections.

Growth in African multiples slows in 2014

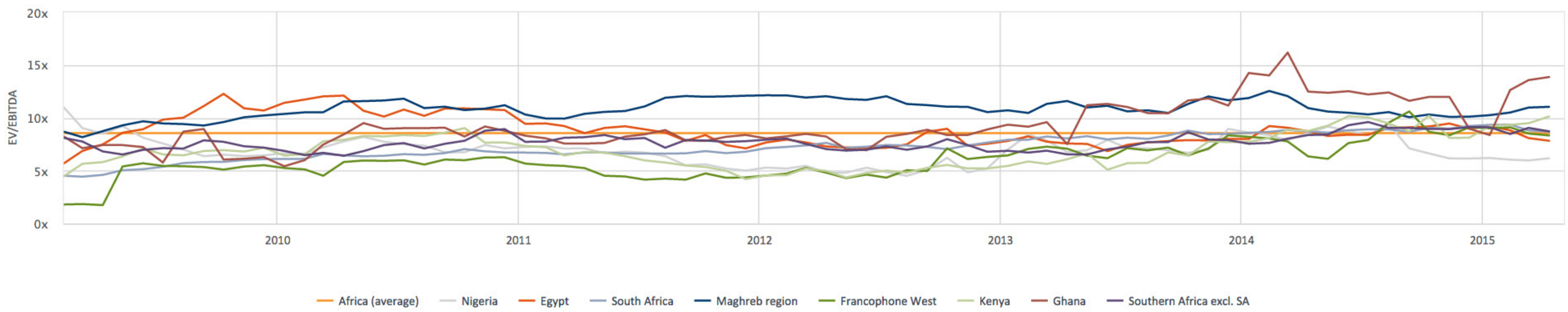
Listed EV / EBITDA multiples over time



Source: S&P Capital IQ, RisCura analysis

Nigerian listed multiples dip in 2014

Listed EV / EBITDA multiples over time



Source: S&P Capital IQ, RisCura analysis

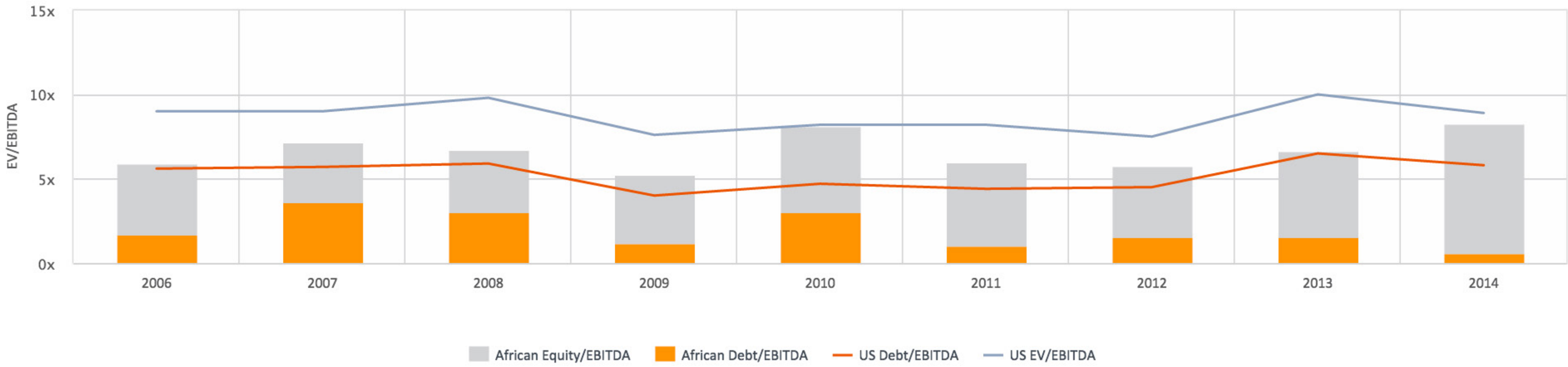
4.6 Private equity multiples in Africa

African private equity deal multiples have been lower than those in other parts of the world, although there have been some exceptions to this rule. In 2010, several large deals took place on the continent where fairly high multiples were paid to secure these investments. The sample includes an average of 32 African private equity deals per year for the 2006 to 2014 period and is considered indicative of the level of transaction multiples paid over time.

The area where African deals differ markedly from other parts of the world is the use of debt as part of the financing of deals. African debt markets are relatively undeveloped, with the exception of South Africa, which results in difficulty sourcing debt funding for deals. Consequently, African private equity deals have used an average of approximately 1.2x EBITDA in debt financing over the past four years, compared to approximately 5.3x in the US. This very low level of debt means that these deals do not rely on leverage for returns.

African prices rise with equity multiples

African vs. US / EBITDA multiples



Source: RisCura, Pitchbook

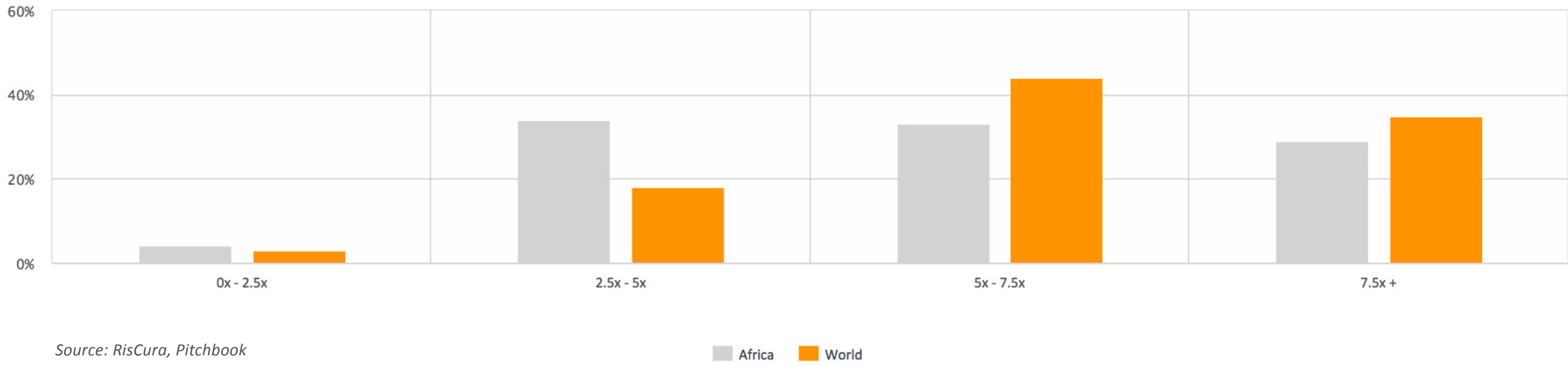
The use of debt in Africa was higher in 2007 when large deals were still being done with debt in South Africa. Since then, however, debt levels have declined and have not fully recovered. In contrast, debt multiples in the US have recovered significantly since the dip in 2009, and appear to be the main driver behind increased purchase price multiples to 2013. Interestingly in 2014, the use of debt in US transactions has declined, causing a decline in US EV/EBITDA multiples, while at the same time, EV/EBITDA multiples have increased in Africa while using even lower levels of debt funding.

Relatively fewer transactions take place in the more expensive 7x+ price bracket and the majority of transactions take place in the lower 2.5x - 5x bracket. In general, it can be seen that African deals are more common in lower price groupings than globally where 35% of deals are priced in excess of 7.5x EBITDA.

This lower pricing of African deals is the result of many factors including higher risk perceptions and lower debt availability in African markets.

African deal making occurs over a large price range

Count of deal EV / EBITDA multiples by price categories



Source: RisCura, Pitchbook

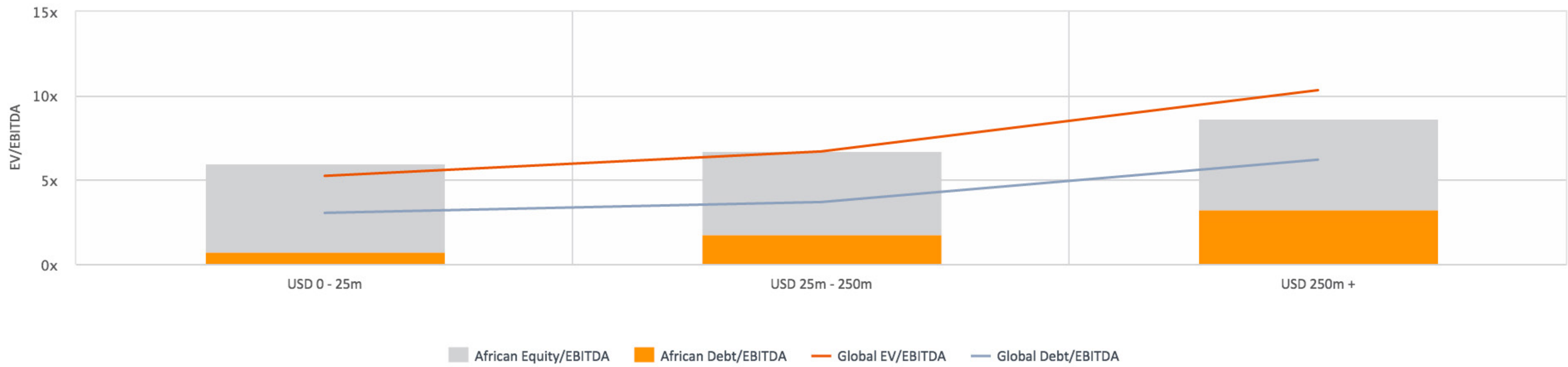
The global trend of higher multiples and more debt on larger deals holds true in Africa. Small and medium sized transactions are priced similarly to global levels, while large transactions are priced lower in Africa. The supply of capital for large cap opportunities in Africa is outstripping the demand for capital (McKinsey 2014), which pushes the price of transactions in the large cap sector higher. Additionally, small and mid-caps are underfunded across the continent, with the exception of North Africa (McKinsey 2014). This keeps the price within a lower range as competition among investors is lower.

The use of debt across all deal sizes in Africa is far lower than globally, with the largest deals averaging only 3.24x Debt/EBITDA. Even deals involving companies with Enterprise Values of over USD 250m are only 37% debt-financed compared to the global average of 60%.

This is due to a number of factors including poor access to debt markets in parts of the continent, the relative risk aversion of South African banks and generally high interest rates across the continent.

Leverage in Africa is low

Average EBITDA multiples by enterprise value



Source: RisCura, Pitchbook

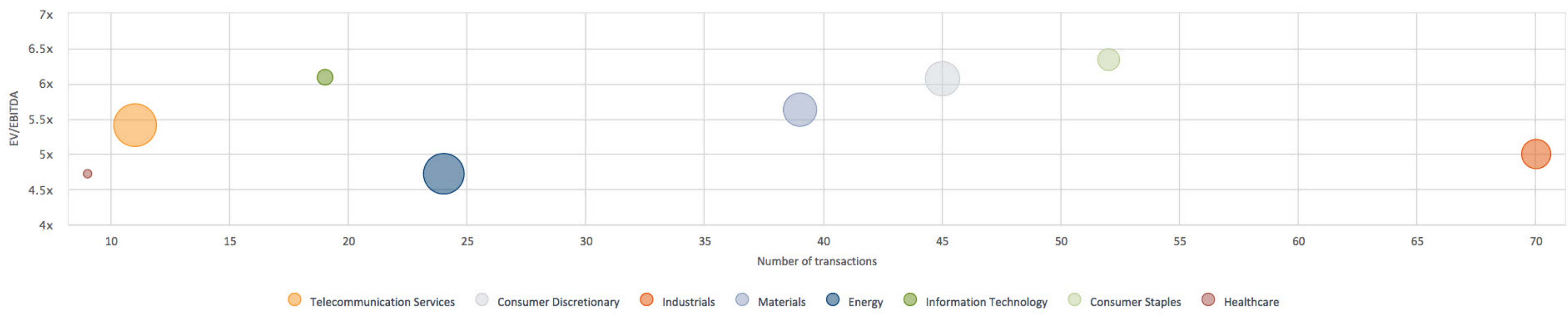
Interestingly there is a relatively small range of multiples between sectors, from the Energy sector with a multiple of 4.72x to the Consumer Staples sector with a multiple of 6.6x.

The chart shows the relatively small average size of transactions that are executed in the Healthcare, Consumer Staples and Information Technology sectors, in contrast to large transactions in the Energy and Telecoms industries.

The supply and demand for capital in the Real Estate and Extractives industries is relatively balanced (McKinsey 2014), preventing undue upward or downward pressure on pricing. Infrastructure is still demanding more capital than is being supplied (McKinsey 2014) keeping prices low.

Range of multiples across sectors is small

Deal mutilples by sector



Source: RisCura

Note: The size of the bubble represents the average transaction size of the sector.

5 ♦ SOURCES

2015 Annual US PE Breakdown Report, Pitchbook
2015 Index of Economic Freedom, The Heritage Foundation
4Q 2014 Global PE Deal Multiples and Trends Report
BMI Research
CIA World Factbook
Development Aid at a Glance 2. Africa (2014 edition), OECD
Gini index by country, Quandl
McKinsey 2014. Uncovering hidden investment opportunities in Africa. Alastair Green, Conor Kehoe, and Farid Sedjelmaci.
Migration and Remittances Data, World Bank, October 2014
Private Equity Data Tracker, AVCA, 2015
S&P Capital IQ
Trade Map
World Economic Outlook, IMF, October 2014
te Velde, Warner, 2007
ODI (te Velde) 2011
ODI (Kingombe, Massa and te Velde) 2011

6 ♦ TERMINOLOGY

AVCA: African Venture Capital Association
BRIC: Brazil, Russia, India, China
BRVM: Bourse Régionale des Valeurs Mobilières SA. The regional stock exchange serving Benin, Burkina Faso, Guinea Bissau, Ivory Coast, Mali, Niger, Senegal and Togo
CDC: CDC Group, Plc
COFIDES: Compañía Española de Financiación del Desarrollo
DRC: Democratic Republic of the Congo
EBITDA: A proxy for operating income [Earnings before interest, tax, depreciation and amortisation]
EIB: European Investment Bank
EV: Enterprise value, A measure of a company's value [Market cap plus debt, minority interest and preference shares]
EV/EBITDA: Earning multiple calculated as Enterprise Value divided by EBITDA Foreign direct investment
Free-float-adjusted: Market capitalisation of a company, adjusted to reflect the number of shares readily available in the market
GDP: Gross domestic product
PPP basis: Purchasing power parity basis, taking into account the relative costs of a basket of goods in each country, reported in current international dollars
Nominal basis: GDP at current prices
GFC: Global financial crisis
IESE VC&PE: Refers to the IESE Business School Venture Capital and Private Equity
IFC: International Finance Corporation
IMF: International Monetary Fund
M&A: Mergers and Acquisitions
Market capitalisation: Total dollar market value of all of a company's outstanding shares
MIT: Mexico, Indonesia and Turkey
MINT: Mexico, Indonesia, Nigeria, Turkey
MSCI: A US-based provider of equity, fixed income and hedge fund stock market indexes, and equity portfolio analysis tools
PE: Private Equity
P/E: Price to Earnings multiple
Rebasing of Nigeria GDP: The Nigerian GDP was recently rebased to a base year of 2010. This means that the National Bureau of Statistics recalculated GDP using a base year of 2010 (previously 1990), taking into account the production structure and prices in that year
Sample period: RisCura private equity deal database covering transactions from 2003 to 2013
SAVCA: Southern African Venture Capital Association
SWIX: Shareholder weighted index
Turnover ratio: A measure of stock liquidity calculated by dividing the total number of shares traded over a period by the average number of shares out standing for the period
UNCTAD: United Nations Conference on Trade and Development
WFE: World Federation of Exchanges

7 ♦ INFORMATION

7.1 Acknowledgements

RisCura would like to thank all those from the industry who contributed their data to this report and provide insights, as well as the RisCura executive team for supporting the production of Bright Africa 2015.
Finally, thank you to the Bright Africa project team for putting the report together: Debbie O'Hanlon, Heleen Goussard, Tom Esterhuysen, Janca Steenkamp, Mark Lucani, Clinton Patterson, Kashiefa Krieling and Courtney Atkinson.

7.2 Key regional contacts

Malcolm Fair
Managing Director (South Africa)
mfair@riscura.com

Andrew Slater
Managing Director (UK)
aslater@uk.riscura.com

Kerry Sinclair
Principal (North America)
ksinclair@riscura.com

Loth Angula
Director (Namibia)
langula@na.riscura.com

Gerald Gondo
Principal (Zimbabwe)
ggondo@zw.riscura.com

Rosemary Nantambi
Consultant (East Africa)
rnantambi-amiri@ug.riscura.com

Charity Siwela
Consultant (Zambia)
csiwela@zm.riscura.com

Juliet Philips
Principal (Mauritius)
jphillips@mu.riscura.com

7.3 Disclaimer

For more information please contact Rory Ord at rord@riscura.com or +27 21 673 6999.

RisCura

info@riscura.com | riscura.com/BrightAfrica