Manager View - Africa Equity

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What are the current effects of geopolitical issues on Africa Equity? The effects are quite diverse as there is no such thing as an African Stock Market or African Equity. When you look for instance at the Sub Saharan region we find 48 countries.

Like Nigeria is more dependent on a high oil price, as a lot of other markets for example Kenya benefit from a lower oil price and lower inflation numbers.

In general we find less correlation in the frontier markets of Africa with geopolitical issues. This is mainly due to the limited number of foreign investors in many African countries. This will change, when Africa will be become the Emerging Market story of the next decade, and foreign investors will start to allocate more towards African Frontier Markets.

What are the common concerns/challenges facing Africa Equity? The main concern is that the current developments are not supported by a stable political background. We need African leaders who commit to longer-term projects, such as infrastructure or housing construction. Due to the democratic transitions this stable political background generally is improving. Studies show that there is a strong correlation between democratic transitions, stability and economic progress. The new wealth is being distributed in a more equal way across the population as we have seen in the past. As the continent has the high economic growth numbers, the demographic advantage, the resource advantage and the ability to be "feeding the world", the ingredients to become the next Emerging Market story are all in place.

In the short term we think the resource heavy economies are vulnerable to a slowdown in China. China is the number one trading partner for 15 African nations. It purchases over 40% of the exports from seven of those nations. (CIA World Factbook). So a serious crash of the Chinese economy would be bad news for the resource exporting countries. A well diversified portfolio across countries and sectors could reduce this risk. But nevertheless the impact at this stage would be large.

Why should institutional investors consider investing in Africa Equity? In our view there are a number of reasons why institutional investors should consider investing in African Frontier markets. The first one is a technical one. Adding African Frontier markets will improve the risk/return features of a portfolio. Due to the lower correlations with global markets and low correlations between African Markets the overall volatility of the portfolio will be lower.

The other reason is that we think that history will repeat itself. Not exactly in the same way but it will look a lot like the developments we saw in the 80's in the Emerging Markets. The Dependency Ratio is improving (active vs non active part of the population) and will continue to do so for the coming years due to the favourable demographic situation. Africa has the youngest population in the world. In the stronger African economies, with a growing workforce, we see higher demand for goods, services, housing and infrastructure. The middle class consumers wil emerge.

Next to this we think some African shares are attractive from a valuation point of view. With generally lower price/earnings ratios than in Emerging or Developed Markets and higher dividend yields. This in combination with a high growth environment should make up for the higher political risk issue.

Which areas in Africa Equity do you find most attractive at the moment? We currently have a 38% allocation in Nigeria, 22% in Egypt and 17% in Maroc. Smaller allocations are found in Kenia 8% and Ghana 5% and Botswana 2%.

How do you as a firm go through the process of investing in Africa Equity? Our investment model is based on a bottom up High Dividend strategy. After a quantitative process focused on dividend yield, RoE, Altman Z scores and liquidity, we perform fundamental research on the companies from our quantitative database.

We are looking for relative attractive valuations across the continent, therefore the portfolio normally shows a high active share versus the traditional benchmarks.

The High Dividend Strategy has done very well in the African Equity markets in the last four years. But also our Global Frontier and Vietnam mandate are showing good outperformance with this strategy.

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