sustainable investment in sub-saharan africa

Investment practitioner views of sustainable investment in private equity and asset management in South Africa, Nigeria, and Kenya

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Investment practitioner views of sustainable investment in private equity and asset management in South Africa, Nigeria, and Kenya

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Research and initial drafting by SinCo and RisCura.

about ifc

IFC, a member of the World Bank Group, creates opportunities for people to escape poverty and improve their lives. We foster sustainable economic growth in developing countries by supporting private sector development, mobilizing private capital, and providing advisory and risk mitigation services to businesses and governments. This report was commissioned by IFC through its Sustainable Investing Unit in the Sustainable Business Advisory Department. The conclusions and judgments contained in this report should not be attributed to, and do not necessarily represent the views of, IFC or its Board of Directors, or the World Bank or its Executive Directors, or the countries they represent. IFC and the World Bank do not guarantee the accuracy of the data in this publication and accept no responsibility for any consequences of their use.

This report was drafted by Graham Sinclair of SinCo, with Roselyne Yao. Analysis is based on research in 2010-2011 by SinCo and RisCura, led by Malcolm Fair[1]. The project was managed by Cecilia Bjerborn, IFC.

about sinco

SinCo is a boutique investment advisory firm specializing in sustainable investment in frontier and emerging markets. Since 2006, SinCo has integrated environmental, social, and governance (ESG) factors into investment processes for institutional investors, private equity funds, stock exchanges, and international organizations promoting long-term sustainable investment performance.

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about riscura

RisCura is a premier independent financial analytics provider and investment consultant with significant expertise in Africa. RisCura services institutional investors with over $180 billion in assets under management, as well as a significant number of hedge funds and private equity firms. RisCura is the leading provider of independent valuation, risk and performance analysis services to investors in Africa.

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foreword

foreword

Rachel Kyte
IFC Vice President,
Business Advisory Services

Thierry Tanoh
IFC Vice President, Sub-Saharan Africa,
Latin America and the Caribbean, and Western Europe

Although Sub-Saharan Africa is fast-becoming attractive to global investors, the region also faces major challenges, including conflict, health pandemics, water scarcity, and the impact of climate change.

Overcoming these challenges requires a coordinated effort by the public and private sectors. For that effort to succeed, massive investment is needed, presenting an opportunity to apply environmental, social and corporate governance (ESG) factors to projects that will improve lives and create opportunity across the continent.

IFC invests with sustainability in mind because what is good for society, the environment, and the long-term financial performance of businesses are inextricably linked. We apply our Sustainability Framework and corporate governance assessments to all our investments. Our sustainability standards, through the Equator Principles, are the benchmark for 70 financial institutions. IFC is also the first multilateral development bank to sign the United Nations Principles for Responsible Investment, underscoring our commitment to sustainability.

Sustainable Investment in Sub-Saharan Africa is part of IFC's efforts to help mobilize more institutional capital into sustainable and inclusive equity funds and indices. We support market efforts to reward companies that embrace a sustainable and inclusive strategy, and help investors recognize and value these practices.

The report finds that institutional investors would like to see all larger companies raise their sustainability reporting and standards, not just those in high-impact sectors such as the extractive industries. More than half of the 160 investment professionals interviewed acknowledged a strong link between ESG factors and investment performance.

Investors also expressed a willingness to pay a premium for good ESG performance. IFC would like to see investors put their funds where their instincts are, but a lack of data and awareness about how to evaluate corporate sustainability often holds them back.

South Africa, IFC's partner in this research, is moving quickly to provide the information sustainable investors need. Since 2010, the country's King Code of Corporate Governance has required companies on the Johannesburg Stock Exchange to integrate sustainability into their operations and report on their ESG performance. South Africa's Government Employees Pension Fund and business networks, such as the Principle Officers Association, are also seeking sustainable investment opportunities. Since South Africa – together with Nigeria and Kenya, which are also covered in this study – draws the bulk of investment to the region, these trends are likely to radiate across the continent.

IFC, in partnership with Norway, is also providing leadership and support for private equity and portfolio companies to manage ESG risks and opportunities in Africa. We are training fund managers, providing resource efficiency assessments for portfolio companies, and supporting research on clean technology. We have also developed an online Environmental and Social Management Toolkit to give fund managers a framework for how to deal with these risks and opportunities.

It is our hope that our efforts will catalyze sustainable investment across Sub-Saharan Africa.

preface

preface

John Oliphant
Head of Investments & Actuarial,
Government Employees Pension Fund, South Africa

As an African institutional investor committed to long-term sustainable investment performance, the Government Employees Pension Fund (GEPF) welcomes this IFC report. The report provides insights on current investor views on sustainable investment in this region, as well as proposals to promote such investment.

Global emerging market investors are demonstrating a new appetite for investment in Sub-Saharan Africa. Sound growth prospects in the region present unique investment opportunities associated with developing solutions to address poverty, poor economic and social infrastructure, declining food security, a lack of clean water supply, and HIV/AIDS.

Such challenges, of course, are not confined to the African continent. The global financial crisis has presented a major challenge to investors in both developed and emerging market economies. The financial crisis showed us that we cannot continue with business or investment as usual. We have now entered an era that requires us to critically assess and change investment models. Our investments should promote real and inclusive long-term growth for our members, beneficiaries, and broader society.

The GEPF made a commitment to sustainable investment in 2006 at the launch of the United Nations-backed Principles for Responsible Investment, of which we are a founding signatory. These principles enable us to collaborate with other signatories to promote responsible investment.

The GEPF's Responsible Investment Policy, launched in March 2010, shows our commitment to seek healthy returns for our members and pensioners, while directly contributing to the economic development of South Africa. A year later, in March 2011, the GEPF launched its Developmental Investment Policy, which aims to address some of the pressing socioeconomic challenges facing South Africa. This policy commits the GEPF to actively invest in critical economic and social infrastructure – including investments that will help South Africa move towards a green economy, and in job creation, enterprise development, and broad-based black economic empowerment.

These developmental investments enable the GEPF to achieve a greater level of diversification within our investment portfolio, while generating long-term sustainable returns to match the duration of our actuarial liabilities. Our commitment to this policy is a bold step toward investing in a sustainable future and has seen us commit 5 percent of our asset portfolio, which amounts to about $7 billion based on current assets.

This report confirms our view that private equity can be a strategic driver of sustainable economic development in Africa. To this end, the GEPF has made a major commitment to the Pan-African Infrastructure Development Fund, one of the largest African-focused private equity funds. This initiative will play a vital role in promoting economic growth by providing a financial platform to build new infrastructure, overcoming one of the major obstacles to African trade and development.

The conclusions and recommendations outlined in this report will contribute to the discussion on approaches to promoting sustainable investment in Sub-Saharan Africa. We look forward to engaging the investment industry and investment stakeholders in South Africa, Kenya, and Nigeria on the five recommendations of this report, and generating systemic change in institutional investment through our actions over the next several years.

about this report

This is the sixth in a series of reports commissioned by IFC on the topic of sustainable investment (SI) in emerging economies – and the first with a specific focus on private equity (PE). The report aims to determine the current state and trajectory of SI in South Africa, Nigeria, and Kenya, and provides recommendations to stimulate such investment over the next five years.

The report has been prepared by SinCo for IFC. The findings are based on research conducted by SinCo and RisCura, encompassing a literature review and empirical analysis, including interviews with investment practitioners. Primary research was conducted in 2010 and 2011. The authors conducted interviews and corresponded with over 160 investors, lawyers, analysts, consultants, academics, and advisors active in investment in South Africa, Nigeria, and Kenya.

IFC AND SUSTAINABLE INVESTING

For the past five years, IFC's Sustainable Investing Team has provided technical and financial support for projects that aim to mobilize sustainable capital flows into emerging markets. The goal is to increase the volume of investment that uses environmental, social, and governance (ESG) analysis as a standard practice in investment decisions.

IFC's approach is twofold:

1. To catalyze capital market flows into SI, IFC works to (a) promote the business case for SI by drawing on lessons from IFC's own portfolio, (b) establish frameworks to identify and assess new SI opportunities, and (c) develop new financial products (e.g. sustainability indices).
2. To support fund managers investing in sustainable companies, IFC works with PE funds in its portfolio to help establish ESG analytical processes, and with capital market participants to improve the environment for recognition of sustainability in corporate valuation.

IFC is committed to its work in partnership with key market actors to improve the enabling environment and address barriers to SI in emerging markets. To do this, IFC's work focuses on three areas: policies and standards, knowledge management, and investment vehicles. The Sustainable Investing Team is part of IFC's Sustainable Business Advisory Services, and benefits from the generous financial support of IFC and the governments of Japan, the Netherlands, Norway, Canada, South Africa, and Switzerland. For more information, please visit the Sustainable Investing website at www.ifc.org/sustainableinvesting.

IFC's Private Equity Africa Climate Change Investment Support program is funded by the Norwegian government and works with PE fund managers through:

SUPPORT TO FUNDS

- Portfolio diagnostic, mining the portfolio for opportunities.
- In-house training on the environmental and social management toolkit for funds.

SUPPORT TO INVESTEE COMPANIES

- Audits that identify energy, water, and cost savings for investee companies.
- List of sources of financing for sustainability improvement projects.

RESEARCH AND NETWORKING

- Clean technology sector research and best-practice publications of sustainable PE investing.
- Access to investor forums that promote SI.

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The authors thank the 13 asset owners, 37 asset managers, 52 private equity investors, and 59 investment stakeholders who contributed directly to this report by taking part in interviews (see Appendix 1). We also acknowledge the many investment and research colleagues inside and outside Africa who contributed to this report.

acronyms

ASISA	Association for Savings and Investment South Africa
AUM	Assets under management
BRIC	Brazil, Russia, India, China
BRICS	Brazil, Russia, India, China, South Africa
CAGR	Compound annual growth rate
CDP	Carbon Disclosure Project
COP 17	17th Conference of the Parties (UN Framework on Climate Change)
DBSA	Development Bank of South Africa
DFI	Development finance institution
EBITDA	Earnings before interest, taxes, depreciation, and amortization
EITI	Extractive Industries Transparency Initiative
ESG	Environmental, social, governance
FDI	Foreign direct investment
GDP	Gross domestic product
GEPF	Government Employees Pension Fund
GP	General partner
IDC	Industrial Development Corporation
IFC	International Finance Corporation
IMF	International Monetary Fund
JSE	Johannesburg Stock Exchange
LP	Limited partner
M&A	Mergers and acquisitions
NGO	Nongovernmental organization
NYSE	New York Stock Exchange
PE	Private equity
SI	Sustainable investment
SRI	Socially responsible investment
UN	United Nations

glossary

TERM	EXPLANATION / DEFINITION
Development finance institution	An agency that supports the development of specific countries or regions. Such institutions finance activities that promote development goals, such as poverty alleviation, economic growth, or private sector development.
Emerging market	A low- to middle-income economy in transition – increasing in size, economic activity, and/or level of market sophistication.
ESG-branded strategy	Approaches that are explicitly ESG inclusive and marketed as such.
ESG-integrated strategy	Approaches that include ESG factors, but which may or may not brand themselves as "sustainable", "responsible", "impact" or "green".
Frontier market	A small, low-income, less-liquid economy.
Private equity	Ownership interests in companies that are not publicly traded.
Sub-Saharan Africa	The African continent below the Sahara Desert, comprising 48 countries at most recent count.
Sustainable investment	Sustainable investment integrates environmental, social, and corporate governance factors into analysis, stock selection, and active ownership practices, in the belief that these factors can improve long-term risk management.

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1.

executive summary

Sustainable investment has a strong niche foothold in Sub-Saharan Africa, anchored in the region's largest investment market – South Africa. Yet more work is needed, at policy and portfolio levels, to grow this investment theme.

This report recommends measures to expand SI in Sub-Saharan Africa. It forecasts that over the next five years there will be considerable growth of ESG considerations applied to investment in South Africa, Kenya, and Nigeria. While these three countries form the basis of the study, the lion's share of data and observations emerged from South Africa, which is home to the continent's most developed capital markets. As SI grows, future reports may draw on new data and experience as institutional investment markets develop in Kenya, Nigeria, and elsewhere in Sub-Saharan Africa.

ECONOMIC GROWTH AND OPPORTUNITIES

In recent years, global emerging market investors have exhibited a new appetite for investment opportunities in Africa. As an investment destination, the continent's numbers are compelling. Africa comprises 54 countries (48 south of the Sahara), with the Republic of South Sudan[2] becoming the newest state in July 2011. Africa is expected to have a combined gross domestic product (GDP) of $2.6 trillion by 2020[3]. In 2009, African GDP per capita grew for the 15th consecutive year. The middle class is growing rapidly. Between 2001 and 2009 African real GDP rose by 4.9 percent – 1.5 percent more than the rate of global economic growth, although off a low base[4].

South Africa's capital market has outperformed that of the United States over the past five years.[5] South African domestic collective investment funds totaled $125 billion in 2010, with total invested assets of $600 billion. Apart from institutional and portfolio investment, direct investment policies by Brazil, Russia[6], India, and China (BRIC) provide a powerful economic boost. China is Africa's largest trading partner[7] and now accounts for 12 percent of exports from Africa's main markets.[8]

There are, however, significant barriers to both investment and business development in the region. These include poor infrastructure in much of the continent, limited access to information, the absence or failure of regulatory mechanisms, a limited pool of skilled and semi-skilled workers, and the small size of many domestic markets. Negative assumptions and obsolete perceptions about Africa play a major role in investment decisions. Political conflicts in West and North Africa in 2011 contributed to negative investment sentiment.

As foreign exchange restrictions are relaxed, new flows of capital from South Africa present an opportunity to grow the continent's capital base, and regional integration will encourage investment. African states are negotiating an expanded trading bloc,[9] with the opportunity for an $875 billion free-trade area crossing 26 countries with a combined population of 700 million people. Political borders reduce African competitiveness. Trade within Sub-Saharan Africa accounts for just 10 percent of total trade, compared with 60 percent within Europe, 40 percent in North America, and 30 percent in Asia.[10]

SUSTAINABLE INVESTMENT IN AFRICA TODAY

SI is developing organically in the region. There is growing awareness that SI can play an essential part in tackling myriad social and economic challenges and that the resulting economic growth will benefit African and global investors over the long term. SI is especially important for developing countries, which have limited resources to mitigate and/or adapt to climate change, rapid urbanization, agricultural production swings, or food price volatility.

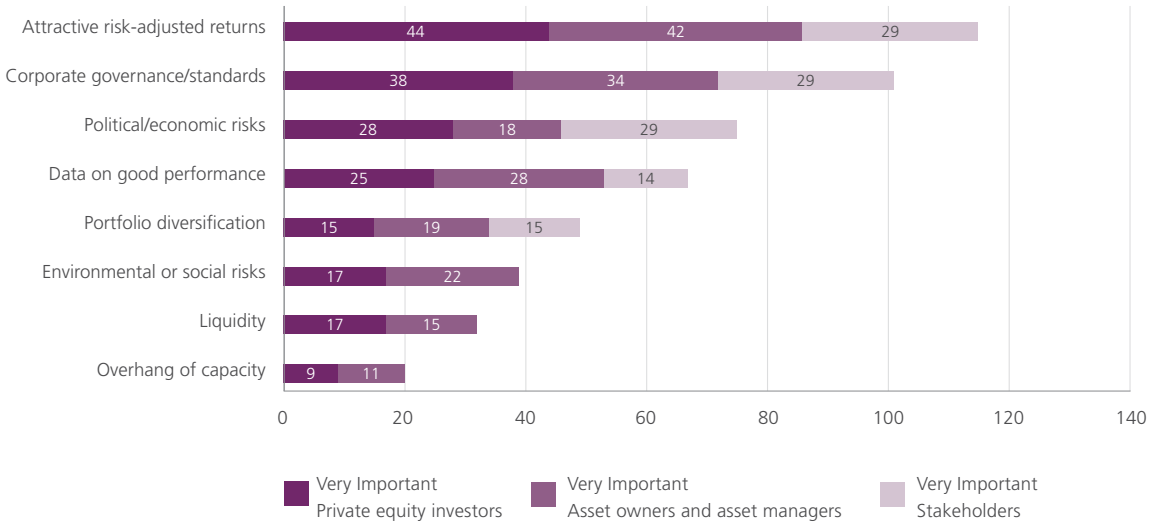
Definitions of sustainability in South Africa, Nigeria, and Kenya include issues that are common internationally, such as governance, climate change, water use, diversity, human rights, and worker health and safety. There are also topics of local concern, such as job creation, education, local ownership, community infrastructure development, the need for employee health care to supplement public health coverage for HIV/AIDS or water treatment systems. Such concerns will have an impact on the relative weighting of ESG factors in investment. In emerging markets, the private sector is expected to play a positive role in society. Screening out exposure to a country based on norms of an international convention may be of more concern to investors in New York or Tokyo than to investors in Lagos or Nairobi. Local investors in Africa may well rate the opportunity to grow new businesses where there are none as the most compelling SI rationale.

Companies operating in Africa in high-impact, high-visibility industries with global shareholders are more likely to take an active approach to sustainability concerns. This reflects their larger resources, greater osure to negative outcomes, and/or dual-listing requirements, as well as public expectations that they will be good corporate citizens.

The chart below captures the weight of various factors in choosing whether to invest in Sub-Saharan Africa. It is based on interviews conducted for this study.

RELATIVE WEIGHT OF FACTORS IN CHOOSING WHETHER TO INVEST IN SUB-SAHARAN AFRICA

Ranking results identified as "very important" on 4-grade scale
[8 options; n=48 PE investors + 44 asset owners and asset managers + 51 stakeholders]



A FOCUS ON PRIVATE EQUITY

Private equity is growing rapidly in response to improving regional economic fundamentals. PE fundraising activity in Sub-Saharan Africa nearly tripled from $800 million in 2005 to over $2.2 billion in 2008. More than $10 billion has been raised for PE investment in the region in the past decade alone.[11] PE funds manage an estimated $24 billion in the region, with South Africa accounting for $14 billion.[12] And more capital is coming: 92 percent of PE investors interviewed expect an increase in PE commitments into Sub-Saharan Africa over the next five years.

PE typically provides capital for growing firms. Of the two common PE management models – financial leveraging and value creation through active ownership – the latter is more prevalent in Africa. The active ownership model has both PE investors and their investee portfolio companies aligned on a longer time horizon (5-10 years). Moreover, they share a vested interest in growing firms with lower risks, higher returns, and better corporate governance to sell to prospective investors. While PE is a much smaller asset class when measured by assets under management (AUM), PE funds have greater exposure and experience in integrating ESG factors in the region than their general asset management counterparts. At first glance this appears counterintuitive, but the trend is supported by several factors.

The integration of ESG factors in PE has been driven mostly by client mandates, especially where development finance institutions (DFIs) are anchor investors. Nearly half of all PE funds in Sub-Saharan Africa have had DFIs as clients.[13] DFIs deploy capital through local PE funds, and will continue to anchor SI, with more demand for monitoring of ESG performance.

In addition, large South African institutional investors such as the Government Employees Pension Fund (GEPF) are already active in PE in Africa. Retirement funds sponsored by major employers such as South Africa's state-owned electricity utility Eskom, or transport agency Transnet, and multinationals such as SABMiller and Anglo American, have also invested in PE. Historically, Kenyan and Nigerian pension funds have had little appetite for PE, but this is changing. Regulatory reforms are enabling larger allocations to this asset class by major institutional investors.

SUSTAINABLE INVESTMENT MARKETPLACE SNAPSHOT

Sustainable investment that is specifically ESG-branded totals an estimated $5.5 billion in AUM (less than 1 percent of total AUM) in South Africa, Kenya, and Nigeria. However, using the broader definition to which this report subscribes (SI as an investment practice that integrates ESG factors in investment policy and/or process stages) this report estimates that SI in the three countries stands at over $125 billion AUM (20 percent of total AUM).

ESTIMATES OF THE PROFESSIONAL SUSTAINABLE INVESTMENT AUM IN SUB-SAHARAN AFRICA DECEMBER 2010 ($ BILLION)[14]

GENERAL ASSET MANAGEMENT					
	Total AUM	ESG-integrated	% ESG-integrated/total region AUM	ESG-branded	% ESG branded/total region AUM
South Africa	556.2	111.2	20.0	4.2	0.8
Kenya, Nigeria, and/or Sub-Saharan Africa ex-SA	18.3	3.5	18.9	0.0	0.0
TOTAL (sum of South Africa and ex-South Africa – except %)	574.5	114.7	20.0	4.2	0.7
PRIVATE EQUITY					
	Total AUM	ESG-integrated	% ESG-integrated/total region AUM	ESG-branded	% ESG-branded/total region AUM
South Africa	14.2	6.3	44.0	1.1	8
Kenya, Nigeria, and/or Sub-Saharan Africa ex-SA	9.8[15]	4.3	44.2	0.2	2
TOTAL (sum of South Africa and ex-South Africa – except %)	24.0	10.6	44.1	1.3	5

Sources: SinCo analysis from SinCo+RisCura data+analysis, 2010-2011; South African Reserve Bank, Quarterly Bulletin - No. 259, March 2011; South Africa National Treasury, 2010; Association for Savings and Investment South Africa (ASISA) Collective Investment Schemes, 2010; Company websites; Preqin, 2010; RisCura, South Africa Venture Capital Association/KPMG 2010; RisCura Analytics, 2011; Bloomberg; Factset; ThomsonReuters; Emerging Markets Private Equity Association/Collier 2010; Kenya Retirement Benefit Authority Kenya; Business Day.

The estimates for the ESG-branded category are based on a composite of funds marketed in each country. Estimates of the ESG-integrated market are based on analysis of available information, relying on self-reported ESG integration data.[16] These are big numbers – and large percentages by global comparison. The table below shows how the SI market penetration in the region compares with other markets, and is in fact higher than most as a percentage of total AUM.

GLOBAL SUSTAINABLE INVESTMENT MARKETS ESTIMATES 2009 - 2011[17]		
MARKET AND PERIOD	ESTIMATED TOTAL AUM RELATED TO SUSTAINABILITY (US$)	% OF TOTAL ESTIMATED AUM
European Union, 2010[18]	$7.26 trillion	47
United States of America, 2010[19]	$3.07 trillion	12
Canada, 2010[20]	$531 billion	19
Sub-Saharan Africa, 2010[21]	**$125 billion**	**20**
Australia and New Zealand, 2010[22]	$115 billion	13
Brazil, 2009[23]	$70 billion	12
Middle East and North Africa, 2010[24]	$54 billion	2
China, 2009[25]	$4 billion	1
South Korea, 2009[26]	$2 billion	1
India, 2009[27]	$1 billion	1

Yet there is great potential to broaden the region's SI base. The current composition of SI in Sub-Saharan Africa is marked particularly by the weight of the GEPF portfolio. Africa's largest institutional investor – and the world's sixth-largest pension fund – has a Responsible Investment policy for a portfolio-wide ESG-integration approach, and a Developmental Investment policy. During 2011, the GEPF allocated 5 percent of its assets (about $7 billion) to four subthemes under the latter policy.

In the next several years, more can be done to encourage investors to take up the ESG challenge, expanding the base beyond large institutional investors and specialist portfolios. The strongest growth is expected to be in the ESG-integrated segment. Growth factors will include demand from asset owners and DFIs, appetite from specialist SI practitioners, and legislative and regulatory drivers.

There will also be country-specific factors:

- South Africa accounts for 95 percent of SI in Sub-Saharan Africa. The huge asset base of the GEPF will continue to influence the take-up of ESG. Demand will increase partly in response to enabling legislation such as the amended Regulation 28 of the Pension Funds Act, which enables pension funds to take ESG factors into consideration, and opens up the opportunity for more SI on the continent. The revised regulation may be considered a global best practice.
- Kenya's and Nigeria's regulatory frameworks are more focused on governance issues. But government-led regulations or association-led initiatives such as the Extractive Industries Transparency Initiative (EITI) are having a positive impact.

This report concludes that there will be considerable growth of ESG factors in investment management in South Africa, Kenya, and Nigeria over the next five years – both in PE and general asset management. Yet this will require focused effort. Much of the existing activity is limited in its practice along the value chain. For example, coverage of ESG factors by analysts is patchy; growing this market requires better data and improved analysis. Demand for pure-play SI mandates is low, especially in general asset management. Investment managers complain of static demand from asset owners who request education and advocacy, but seldom fund mandates. More needs to be done to reduce barriers and reinforce drivers. This requires effective implementation of commitments from the investment policy level into the investment value chain, or through the profiling of ESG risks that affect long-term returns.

DRIVERS AND BARRIERS

The primary drivers of SI identified by participants in this study were:

- Good investment returns (a record of premium from ESG integration)
- Explicit and tangible ESG benefits/impact
- More information
- Government/regulator incentives
- Demands from clients/investor mandate/shareholder pressure.

The top five barriers cited by interviewees were:

- Lack of adequate information to evaluate investment target ESG-related performance
- Lack of evidence that ESG factors increase financial returns
- High costs of implementing ESG investment
- Lack of appropriately skilled advisors and necessary expertise
- Short-term reporting against prospect of long-term returns.

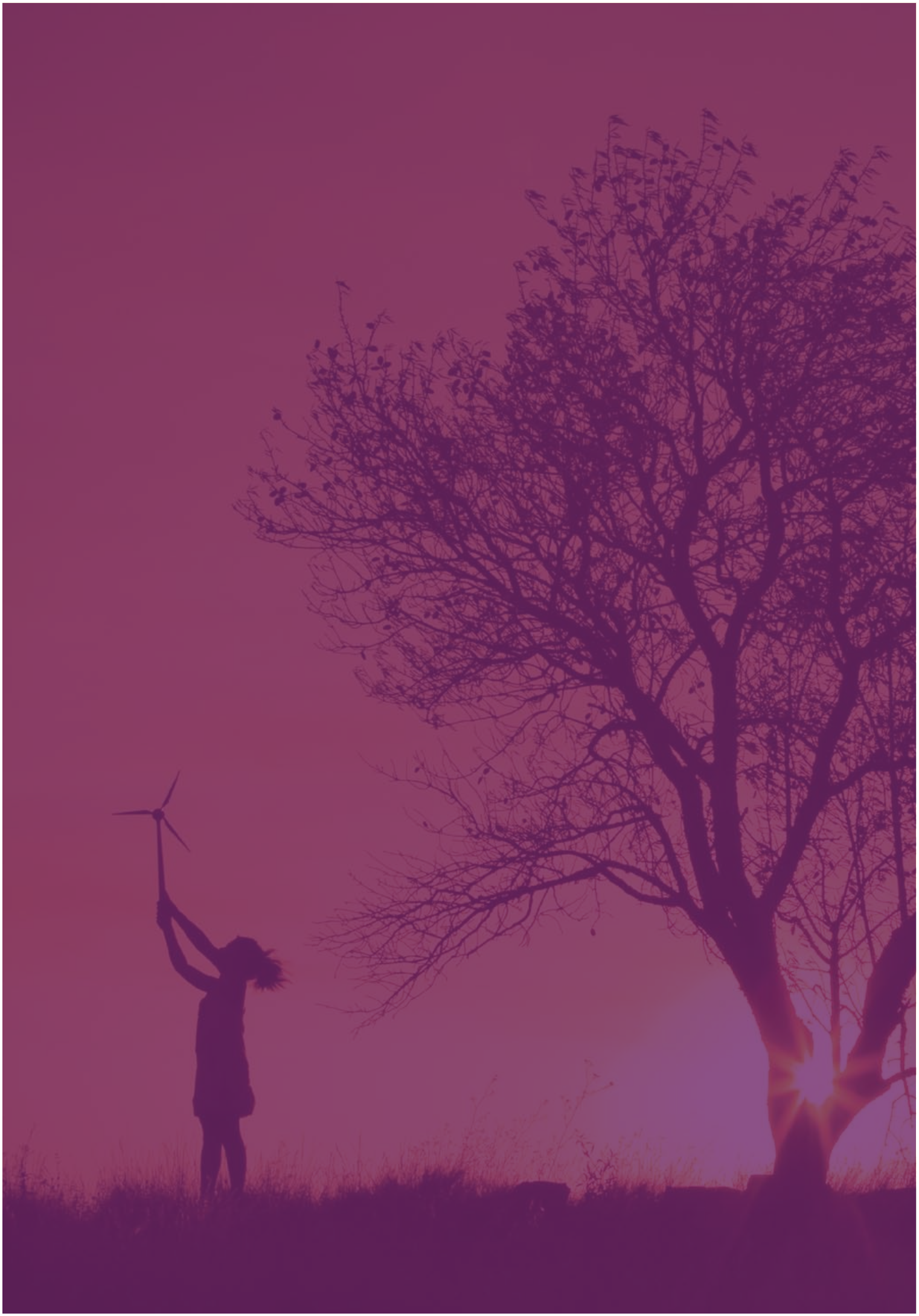
Barriers also include the "investment-as-usual" approach, the perception that SI consists only of "ethical" investment and/or negative screening, and the specialized "language of sustainability".

RECOMMENDATIONS

A systematic approach will encourage more widespread integration of ESG factors in investment decisions in Sub-Saharan Africa, building on best practice examples identified in this study. To take this process forward, the report makes the following recommendations:

- Use the language of investors: The SI message should be presented in the language of investors. It should be driven by asset owners and investment practitioners, and appeal to advisors and asset managers open to exploring advances in investment practice.
- Streamline reporting: Reduce information gathering and execution costs by streamlining the ESG reporting approaches of major investors (especially DFIs), and increase comparability of ESG impacts through common reporting frameworks.
- Leverage local knowledge: Integrate local and regional insights into global best practice.
- Make the investment case: Make the case that SI has the potential to generate increased returns and/or reduced risks across all asset classes.
- Keep score: Performance metrics and analysis are essential. Investors need mechanisms and infrastructure to measure investment performance and ESG impact.

To ensure systematic growth from the relatively strong SI base in Sub-Saharan Africa, these recommendations should be implemented over the next three years.



2.

economic growth and investment in sub-saharan africa

Investment in emerging and frontier markets is driven by the search for higher returns and risk diversification. Since 1995, total equity returns in emerging markets have been about 130 percent (in real dollar terms). Emerging market returns have outperformed those of developed markets over the past decade, supported by surging economic growth, reduced currency volatility, and high commodities prices.

Africa too is benefiting from global interest. While African markets are currently a less compelling investment proposition than Brazil, India, or China, investor appetite for African equities and infrastructure investment is growing. Cameron Brandt, director of research at funds flow data provider EPFR Global, said that during 2010 there was "record net buying of African equity, to the tune of $5.98 billion." The International Monetary Fund (IMF) projects African GDP growth of 5 percent in 2011, up from 4.7 percent in 2010.[29]

Most Sub-Saharan African countries remain frontier markets for global investors. This is a function of both technical factors – such as the difficulty of obtaining investment expertise, trade executions, or accurate analysis – as well as country or political risk. Experience in West and North Africa in early 2011 underlines the reality that in emerging economies, politics are as important as economics – and prone to sudden change.

"Given the fact that many investors now are strategically oriented, this means they are also integrating the emerging markets into the benchmark. We clearly expect that volatility in the emerging markets will be lower compared to the past. So in a broad-based comparison, we expect that the risk return ratio of emerging market investments will further improve in the future."

Stefan Keitel
Chief Investment Officer at Credit Suisse[30]

2.1

prospects for economic growth[31]

KEY INDICATORS

As an investment destination, Africa's numbers are compelling, with nearly 1 billion people spread over 54 countries. The second-largest continent by land mass (11.7 million square miles), it is roughly equivalent to the combined area of China, the United States, Europe, India, Argentina, and New Zealand.[32] Over the past decade, Africa has experienced a marked improvement in political stability, increased investment in infrastructure, strengthened telecommunications networks, greater financial sector servicing, growing cross-regional trade and infrastructure demand, and a rising middle class driving the retail sector.[33]

Key points for investors include the following:

- Combined African GDP was forecast to reach as high as $2.6 trillion in 2020.[34]
- While about 2,000 languages are spoken on the continent, business in Sub-Saharan Africa is conducted largely in English, French, and Portuguese.[35]
- African regions are expected to improve their competitiveness compared with the BRIC group. South Africa joined what is now BRICS in 2011.[36]
- Consumer spending in Africa's top 18 cities is expected to total $1.3 trillion by 2030.[37]
- Some 40 percent of the population lives in urban areas, and this proportion is expected to increase over the next decade.
- Over the past 10 years, the weight of agriculture has decreased within many Sub-Saharan economies, as the industrial and services sectors have grown.
- The number of households with discretionary spending is expected to increase by 50 percent over the next decade to 128 million.[38]
- The African economy is expected to grow by 5 percent in 2011 – up from 4.7 percent in 2010.[39]

The continent's sound growth prospects are underpinned by generally improved macroeconomic policies, lower public debt, a reduction in political conflicts, and a young population.[40] Equity markets are a lead indicator of GDP growth and react strongly to changes in expectations about the future.[41] In the years ahead, investment levels will depend on an enabling environment with sound market regulation, investment skills, and strong institutions.

DEVELOPMENT INDICATORS, SUB-SAHARAN AFRICA[42]

	Sub-Saharan Africa	Nigeria	% of region	South Africa	% of region	Kenya	% of SSA region
GDP (current $) (billion, 2010)[43]	1,056	216.8	20.5	357.3	33.8	32.2	3
Population, total (million, 2010)[44]	798	156	19	49.9	6	39.7	5
Population growth (annual %, 2009)	2.5	2.3		1.1		2.6	
GDP per capita (current $, 2009)	1,126.8	1,118		5,786		738	
GDP growth (annual %, 2009)	1.7	5.6		-1.8		2.6	
Life expectancy at birth, total (years, 2009)	52	48		51		54	
Mortality rate, infant (per 1,000 live births, 2009)	81	86		43		55	
Literacy rate, youth (% females age 15-24, 2008)	67.0	65		98		93	
Prevalence of HIV, total (% population age 15-49 2007)	5.0	3		18		6	

South Africa, Nigeria, and Kenya are focal points for regional growth, though the pace of expansion varies considerably. The South African economy is projected to grow at 3.7 percent in 2011-2012,[45] reaching 4.5 percent growth in 2015.[46] Nigeria is set to grow more rapidly, with projected growth of 6.7 percent during 2011-2012,[47] moderating to 6 percent in 2015.[48] Kenya is set to grow 6.1 percent in 2011-2012,[49] reaching 6.6 percent in 2015.[50]

Projected per capita average annual GDP growth of 5 percent through 2015 is expected to translate into a 30 percent increase in spending power in Sub-Saharan Africa. Some analysts predict Africa's share of global GDP will rise from 4 percent in 2010 to 7 percent in 2030 and 12 percent in 2050.[51] This means *"more consumers are making the transition from the very low income level (below $1,000 per year) to the basic needs level ($1,000 to $5,000 per year), reflecting a rising African middle class. After a decade of above average real economic growth, the continent's performance is confounding many of its skeptics."*[52]

While coming off a low base, the future for African markets is positive. Today, only three African markets are tagged as "emerging" by MSCI,[53] and five as "frontier"; the majority is considered "least-developed countries" by the United Nations (UN).[54] Frontier markets tend to be higher risk than emerging markets: aggregate frontier markets have weaker balance sheets, larger external deficits, higher external debts, and smaller foreign exchange reserves. Many such economies are reliant on a single commodity export.[55] And globalization cuts both ways: while countries with strong links to the global economy, such as South Africa, benefit during a period of strong growth, they also suffer the consequences during a downturn. Moreover, Africa's economic outlook still depends largely on global factors such as commodity prices, external demand, and availability of cross-border credit.

Key sector performance information is summarized in the table below:

Key sector growth rates[56]				
	% CAGR[57] since 2000	% CAGR since 2000	% CAGR 2003 – 2007	% CAGR 2003 – 2007
Sector	Sub-Saharan Africa	South Africa	Nigeria	Kenya
Agriculture	3.18	1.70	7.04(**)	2.15
Manufacturing	3.09	2.58	Unavailable	3.74
Industry	4.41	2.31	4.49	4.23
Services	5.01(*)	5.78(*)	13.44	3.21

South Africa is the largest economy on the continent. The services sector accounts for more than half of the value added in the economy, and the weight of this sector has increased steadily over the past 20 years. Annual GDP growth between 2004 and 2007 averaged 5 percent, but fell to 3.7 percent in 2008 as a result of higher interest rates, power shortages, and weaker commodity prices. GDP contracted by 1.8 percent in 2009 as South Africa experienced its first recession in 18 years. Exports amounted to 27 percent of GDP in 2009. South Africa's major trading partners include China, Germany, the U.S., Japan, and the United Kingdom. South Africa has been described as a "two-tier" economy. In the formal economy, the mining, manufacturing, agriculture, financial services, and retail sectors are comparable to those in developed countries. Concurrently, a very large informal sector provides a range of goods and services in urban, peri-urban, and rural areas. The gap between these sectors is substantial, and South Africa is one of the most unequal societies in the world as measured by income levels and other indicators. South Africa had a higher Gini index level (57.8 in 2000) than Nigeria (42.9 in 2003-2004) and Kenya (47.7 in 2005-2006).[58]

In ***Nigeria***, agriculture accounts for about 33 percent of GDP and two-thirds of employment, providing a significant proportion (about 10 percent) of non-oil growth.[59] In 2010, Nigeria's oil industry accounted for 40 percent of GDP and 80 percent of foreign exchange earnings.[60] While the industrial sector has slowed down since 2003 (and shrank between 2006 and 2007), it still accounts for about 40 percent of economic activity. The services sector posted five years of consecutive growth between 2003 and 2007, and accounts for about 28 percent of the Nigerian economy. Arguably, Nigeria's biggest macroeconomic achievement has been the reduction in its external debt from 36 percent of GDP in 2004 to less than 4 percent of GDP in 2007. The economy continues to witness growth in the informal sector, which may make up as much as 75 percent of the total economy.[61] Nigeria's economy is relatively strong and resilient as a result of rapid growth in both its oil and non-oil sectors over recent years.[62]

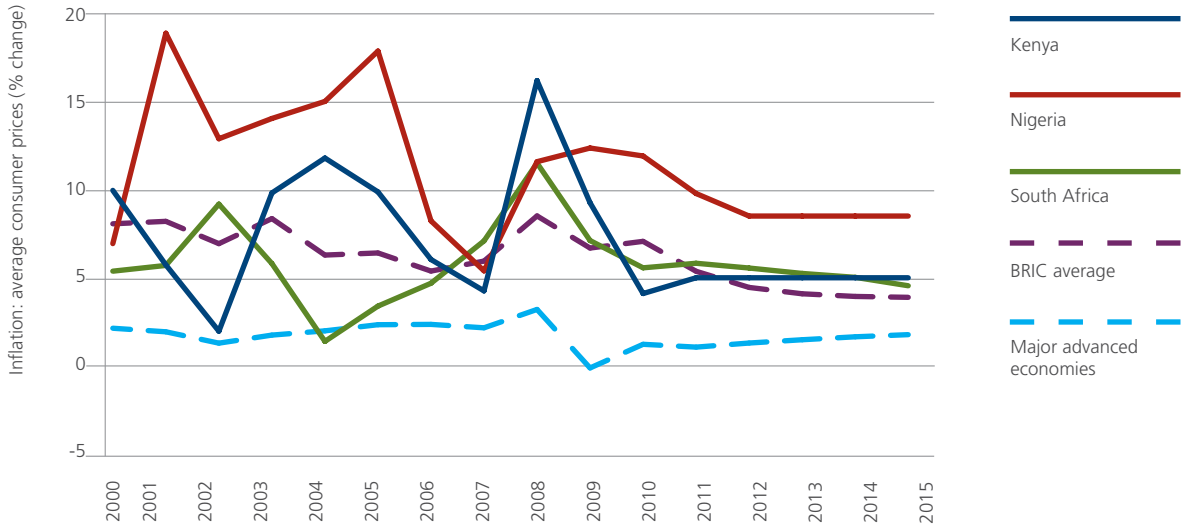
Kenya is the largest economy in East Africa, and a major trade and transport hub. Agriculture accounts for about a fifth of the economy, but has been unpredictable over the past 20 years, contracting almost every third year, on average. In contrast, Kenyan industry has recorded consistent growth since the turn of the century, apart from a 30 percent decline during the 2008-2009 global downturn. The services sector has grown over the past two decades and accounts for more than half of the value added in the economy. The Kenyan economy suffered the effects of political violence that broke out after the December 2007 general election, compounded by drought and the effects of the global financial crisis. Economic growth was less than 2 percent in 2008, with a modest improvement (2.6 percent) in 2009. The World Bank[63] forecasts 6 percent economic growth in 2011, largely due to the country's telecommunications revolution, improved macroeconomic management and investment in public infrastructure.

Environmental and social considerations will have both direct and indirect impacts on growth trends. Section 4 of this report discusses the expected effects of climate change in Sub-Saharan Africa. Failing to deal with the environmental and social impacts can put economic development at risk in Sub-Saharan Africa. On the other hand, SI can play an important role in boosting economic growth as African countries grapple with these issues.

TAMING INFLATION

Inflation reduces the real value of investment. The narrowing gap in inflation (percent change in consumer prices) between Sub-Saharan Africa and the major developed economies reflects improvements in the macroeconomic environment (as shown in the figure below).[64] As the figure below shows, inflation has been on the decline in South Africa, Nigeria, and Kenya, and is projected to be stable in the period ahead. For the region as a whole, the IMF predicts a stable average rate of 5 percent annual inflation over the next five years.[65]

DECREASING INFLATION



Source: International Monetary Fund (IMF). Data and Statistics: Inflation, average consumer prices. January 2011.

2.2

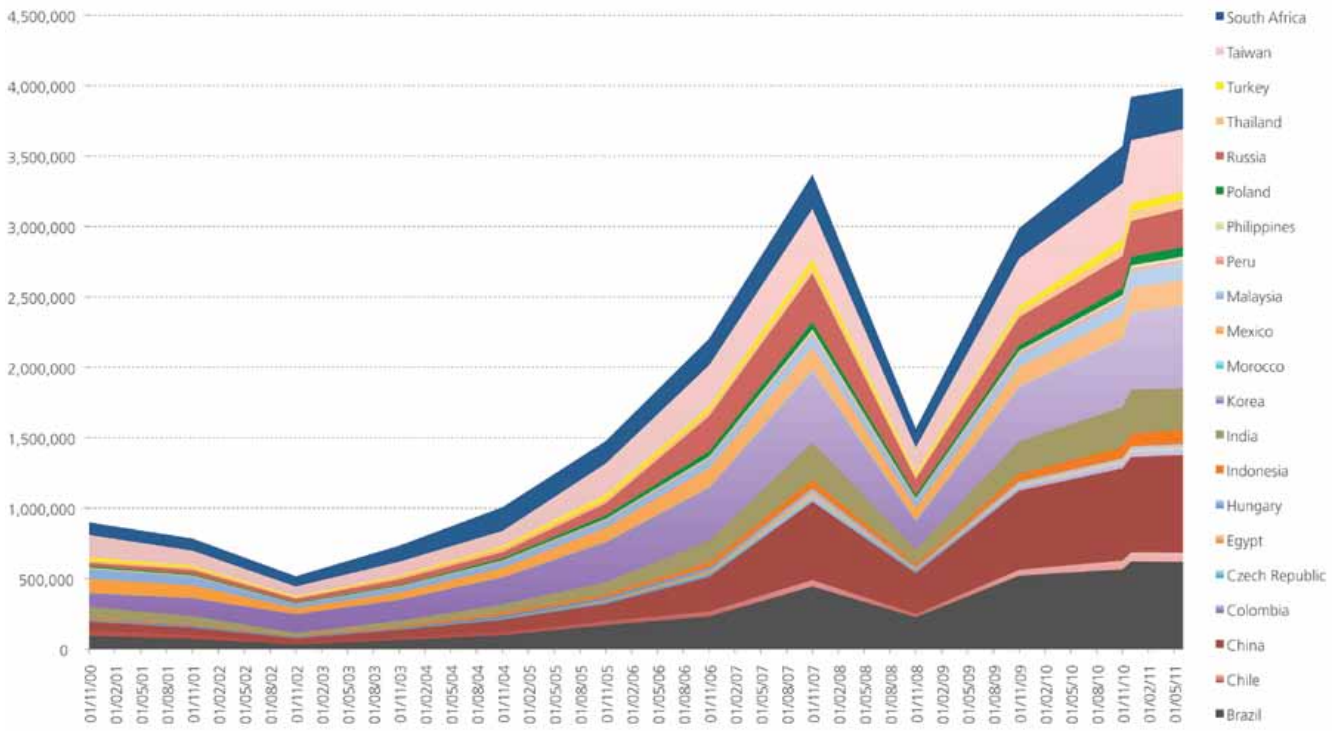
savings and investment

There is stiff competition for global capital flows, and Sub-Saharan Africa needs an active approach to draw in higher levels of investment. Among emerging markets, the BRIC countries have outstripped Africa in attracting investment and generating economic growth. For example, the South Africa country weight in the benchmark MSCI Emerging Markets Index[66] has shrunk from 9.1 percent in 2000 to 7.4 percent in 2010, with a commodity-boom driven peak of 15.8 percent in 2004. This decline is explained by the relative growth of other emerging markets, such as Brazil (2005: 9.8 percent to 2010: 15.9 percent) and China (2000: 6.9 percent to 2010: 18.3 percent).

As of December 2010, Africa accounted for 1.14 percent of global market capitalization (using the African countries represented in the MSCI All Country World Frontier Market index as proxy). However, more African countries have become represented in the investment marketplace in the last decade. The figure below benchmarks emerging markets by market capitalization. South Africa makes up 7 percent of this index.[67] Kenya and Nigeria are among the 31 countries in the MSCI Frontier Markets Index.

MSCI EMERGING MARKETS INDEX (MSCI EM) - COUNTRY MARKET CAPITALIZATIONS (USD $MLN) 2000-2010

Total USD 3,982,230 million @ 30 June 2011; 30 November 2000-30 June 2011 Source: MSCI Africa July 2011



Sub-Saharan Africa's most liquid and mature investment markets are in Southern Africa, with developing financial markets tied to economic development in East and West Africa. Global emerging markets investors are interested in Sub-Saharan Africa, but potential investors struggle with a lack of information and negative perceptions of the continent. The emergence of BRICS in 2011[68] has the potential to reduce these barriers, and open doors to greater trade between African and other developing-country markets.

SAVINGS

As shown in the table below, Sub-Saharan Africa's gross domestic savings stood at $232 billion during 2009, equivalent to about 16.4 percent of composite GDP. Developed countries were closer to a 13 percent savings rate, while China recorded a 54.2 percent savings rate in 2009.

GROSS SAVINGS[69]				
	2009	2009	2009	2009
	Sub-Saharan Africa	South Africa	Nigeria	Kenya
Gross savings ($ billion)	232	53	38	2.3
Gross domestic savings as % GDP	16.4	18.6	22	7.8

The accuracy and availability of market data on South Africa, Kenya, and Nigeria varies widely, reflecting different stages of market development. Detailed and sophisticated market statistics are available for major asset classes in South Africa, but are scarce and/or unreliable for other markets.

SOUTH AFRICA

In 2009, the net worth of South African households was estimated at $690 billion.[70] Of this, roughly a third was invested in pension funds.[71] Institutional investment in South Africa can be disaggregated into four underlying groupings: collective investment schemes (includes most retail assets), institutional asset management of pension/retirement funds, assets underwriting long-term insurance policies, and financial services balance sheets, as shown below.

South Africa: invested capital, 2010[72]			
	Assets (billion rand)	Assets ($ billion)	% total invested assets
SA pension fund assets (Reserve Bank)	**2,019**	**269**	**48**
Private self-administered pension and provident funds (Q3 2010)	652	87	16
Funds invested with insurers (Q3 2010)	302	40	7
Total private self-administered pension and provident funds	**955**	**127**	**23**
Official funds (administered by the Department of Finance, Transnet, Telkom, and the Post Office; deposit administration investments excluded (Q4 2010)	1,064	142	26
Total insurers (Reserve Bank)	**1,650**	**220**	**40**
Long-term insurers (Q3 2010)	1,564	209	37
Short-term insurers (Q3 2010)	86	11	2
Total institutional assets in SA	**3,366**	**449**	**81**
Collective investment plans[73] (ASISA)	**806**	**107**	**19**
Total invested assets in SA	**4,171[74]**	**556**	**100**

The size of domestic collective investment funds (see table below) was about $125 billion in 2010. The composition of the funds reflects the major role of the fixed income asset class in making financing available.

Collective investment funds (pooled investment), South Africa, end-December 2010[75]				
South Africa collective investment industry[76]	**Number of funds**	**% funds**	**Net assets ($ billion)**	**% assets**
Foreign	114	12	5	4
Domestic	791	84	119	95
Worldwide	38	4	1	1
Total	**943**	**100**	**125**	**100**
Type				
Fund of funds	361	-	16	
Institutional (including third-party institutional funds)	n/a		52	42
Retail (including third-party institutional funds)	n/a		73	58
Asset Class				
Equity	264	28	30	24
Fixed income	466	49	32	26
Asset allocation	184	20	59	47
Real estate	29	3	4	3
Total	**943**	**100**	**125**	**100**

In February 2011, a RisCura analysis of South Africa's top 25 asset managers estimated institutional fund assets to be $511 billion,[77] or $381 billion excluding the Public Investment Corporation, which invests funds on behalf of South Africa's public-sector entities. As of March 31, 2011, South Africa had $72.1 billion in retail AUM. An alternative sizing approach is the securities available in publicly listed equity and fixed income asset classes. The total value of equities listed on the Johannesburg Stock Exchange (JSE) was equivalent to about $556 billion as of March 31, 2010.[78] The nominal value of bond holdings[79] amounted to $136 billion on the same date.

> "South Africa may have a current account deficit, but capital keeps flowing into the country... Why? CalPERS, Hermes, Templeton – they all say they invest in South African firms because they regard our listed companies as among the best governed in the world. And they are."
>
> *Professor Mervyn King,[80] Chairman of the King III Commission and Global Reporting Initiative*

NIGERIA

A lack of accurate data from consistent, publicly available sources makes it difficult to offer a detailed analysis of the market. The Nigerian Pension Commission[81] estimates the country's pension fund assets at about $11.9 billion.[82] Between 2006 and 2009 the domestic bond market nearly quadrupled, and reached market capitalization of $15 billion in January 2010.[83] Net domestic assets totaled $9.4 million in the first half of 2009.[84] Publicly listed equities on the Nigerian Stock Exchange had a market capitalization equivalent to $66 billion as of December 31, 2010.[85] The effect of the newly created Asset Management Corporation of Nigeria is yet to be determined. This entity was conceptualized as a resolution mechanism to stimulate the recovery of the financial system by acquiring nonperforming loans from Nigeria's 24 banks.[86]

KENYA

Institutional investors holding pension fund assets dominate the marketplace. The size of the market at the end of 2010 was estimated at $5.25 billion.[87] At end-December 2010, about 25 percent of pension fund assets were accounted for by the National Social Security Fund, to which employees in regular employment make mandatory contributions.[88] The fund consists of about two-thirds fixed income and one-third equity, reflecting its preference for fixed income instruments.

INVESTMENT

Portfolio inflows to Africa, driven by the commodities boom, peaked in 2008. The UN Conference on Trade and Development estimates that foreign direct investment (FDI) inflows fell by 14 percent to $50 billion in 2010.[89] These flows varied from country to country. Rising FDI from developing Asia and Latin America to Africa did not compensate for the decline from developed countries. Cross-border mergers & acquisitions (M&A) are mostly in the extractive sector, and registered an increase of 49 percent. For example, in May 2011, Citic Group, China's biggest state-owned investment company, along with its partners, agreed to buy South Africa's Gold One International for about $469 million.[90] Similarly, Russian firms are looking to tap Africa's mineral wealth, as reserves in their home market become depleted and more expensive to extract, according to a study by the African Development Bank.[91]

In aggregate, the number and value of new FDI projects fell by about 10 percent in 2010. As demonstrated by the table below, FDI flows have varied significantly. In South Africa, exchange control reforms are expected to increase South African institutional investment into Sub-Saharan Africa beyond 2010 (see M&A section below). Nigeria[92] is a net importer of FDI, largely in the petroleum/mining and wholesale trade sectors.[93] Kenya[94] is also a net FDI importer. Its outward flow of FDI has been increasing and reached $46 million in 2009.[95]

FOREIGN DIRECT INVESTMENT[96]

	1995–2005 (annual average)	2006	2007	2008	2009
South Africa inward $ million	2,305	-527	5,695	9,006	5,696
South Africa outward $ million	799	6,063	2,966	-3,134	1,584
Nigeria inward $ million	1,945	13,956	6,087	6,814	5,851
Nigeria outward $ million	191	16	468	972	141
Kenya inward $ million	38	51	729	96	141
Kenya outward $ million	3	24	36	44	46

MERGERS AND ACQUISITIONS

The value of global M&A totaled $2.4 trillion during 2010, a 22.9 percent increase from 2009 and the strongest performance since 2008. Emerging markets accounted for 33 percent of this amount. African deals constituted $44 billion – about one-third of emerging market M&A.[97] Investors and analysts expect the pace of deals to increase in 2011, as more international companies and banks target the continent's rapidly expanding economies, growing middle classes, and rising trade.[98] The biggest M&A deal on the continent in 2010 was Indian telecom Bharti Airtel's $10.7 billion acquisition of the African assets of Kuwait-listed Zain (former Celtel).[99] South Africa was the most targeted country, as investors and companies used the soccer World Cup to enter into the region.

The role of ESG factors in M&A is poorly understood. In June 2011, Wal-Mart received regulatory approval for its $2.3 billion acquisition of South African-listed Massmart, but subject to conditions such as a moratorium on job losses for the first two years and local manufacturing protections.[100] These conditions were imposed by the competition authorities following pressure from local trade unions and sections of the government.[101]

Developing-to-developing country investment remains a strong theme in Sub-Saharan Africa. M&A deal flows between 15 developed economies (or groups of economies) and 13 emerging economies (or groups of economies) identified an average of 202 cross-border deals per year between emerging markets since the start of 2003, representing 1,518 deals struck in under eight years. South Africa is the biggest investor in Sub-Saharan Africa. These M&A deals are regionally material but too small to garner much international attention.[102]

In practice, the market attractiveness of Sub-Saharan Africa is demonstrated one deal at a time. In 2010, international PE funds and/or their investors made headlines with various deals. Among them:

- The African Development Bank committed $15 million to the Catalyst Fund, a Kenyan PE fund targeting small-medium-micro investments in East Africa. With a focus on Kenya, the Democratic Republic of Congo, Ethiopia, and Zambia, the fund will invest in food and personal care, financial services, telecoms, packaging, and agribusiness.[103]
- United Kingdom investor Aureos made a $10 million investment in West African banking group HFC Bank Ghana.[104]
- Evolution One, South Africa's first PE clean technology fund, invested $7.55 million into Enviroserv Waste Management in South Africa.[105]
- PE firm Actis acquired Vlisco Group, a West African fabric maker, for $151 million.[106]
- Royal Dutch Shell PLC entered into a $1 billion agreement to sell most of its downstream businesses in 14 African countries to the Vitol trading company and Helios, an African PE firm.[107]

Large companies headquartered in South Africa and major global firms seeking a footprint in Sub-Saharan Africa are looking northwards from South Africa. In 2010, a barrier to M&A activity for South African-based PE funds was lowered when foreign exchange control regulations were relaxed for South African companies. The need for central bank approval on a deal-by-deal basis for transactions outside of the common monetary area of South Africa, Namibia, Lesotho, and Swaziland was removed. The South African law now requires PE funds to obtain prior approval from the Reserve Bank for investment outside the common area; thereafter to provide annual reports on capital drawdowns and investment exits. The legislation allows non-residents to invest directly into South Africa-based funds, encouraging PE firms to locate more senior staff in South Africa.

2.3 factors influencing investment

Investors interested in long-term investment and joint ventures, especially those that use locally available raw materials and resources, have opportunities in the relatively large national markets of South Africa, Kenya, and Nigeria. Trading in these anchor markets can also open opportunities through regional groupings such as the Southern African Development Community and the Economic Community of West African States. The opportunities all require thorough due diligence. Investors require knowledge of socioeconomic context, legal and technical facilities, local conditions, and business practices.

The governments of South Africa, Nigeria, and Kenya are keenly aware that sustaining democratic practice and the rule of law, enhancing security for life and property, and rebuilding and maintaining infrastructure, are necessary preconditions to attract foreign investment.

Key factors influencing investment are discussed below; factors in global market accessibility are listed in Appendix 3.

INVESTABLE SECURITIES

Combined with investor mandates that restrict certain types of ownership, Africa's relatively limited availability of investable securities is obvious when measured in global terms. For example, while South Africa makes up close to 1 percent of global market capitalization, Kenya and Nigeria make up just 0.013 percent and 0.033 percent respectively – using the MSCI All Country World Frontier Market Index as a proxy (see table below).

MSCI ALL COUNTRY WORLD FRONTIER MARKET INDEX[108]			
Region	Number of securities	Free float adjusted market capitalization ($ billion)	Weight in Index (%)
All Country World Frontier Market Index	**2,586**	**26,262**	**100.00**
Developed markets	**1,656**	**22,572**	**85.95**
Emerging markets	**755**	**3,569**	**13.59**
South Africa	45	263	1.002
Egypt	10	17	0.063
Morocco	3	6	0.021
Frontier markets	**175**	**122**	**0.46**
Nigeria	9	9	0.033
Kenya	7	3	0.013
Mauritius	3	1	0.004
Tunisia	4	1	0.004

Regional and international exposure by South African-listed firms demonstrates the value of globalization: the top 10 companies by market capitalization generated about 43 percent of their revenues from outside Africa.[109]

In addition, investment products marketed in South Africa are developed to access the overall African investment marketplace. Major investment firms first began deploying "Africa funds" in the mid-1990s. The trend continues with new investment products. For example, in May 2011, Standard Bank introduced the Africa Equity Index Exchange Traded Note as "*a tradable liquid vehicle for both retail and institutional investors who would like to take advantage of Africa's growth story.*"[110] As of April 2011, this note covered 179 listed stocks in 29 African counties.

EASE OF DOING BUSINESS

The ease of doing business has a significant effect on economic activity and investment. The World Bank's Ease of Doing Business project[111] tracks objective measures of business regulations for local firms in 183 economies and selected cities. As shown in the table below, South Africa ranks relatively well in this respect – at 34th out of 183 countries – while Kenya and Nigeria rank at 95th and 125th respectively.

COMPARING REGULATION THAT ENHANCES BUSINESS ACTIVITY[112]			
	Rankings by countries (180+ countries; ranking 1=best)		
	South Africa	Nigeria	Kenya
Ease of doing business	**34**	**125**	**95**
Starting a business	67	108	124
Dealing with construction permits	52	162	34
Employing workers	102	37	78
Registering property	90	178	125
Getting credit	2	87	4
Protecting investors	10	57	93
Paying taxes	23	132	164
Trading across borders	148	146	147
Enforcing contracts	85	94	126
Closing a business	76	94	79

Similarly, the World Economic Forum Competitiveness Report ranked South Africa 54th out of 139 countries, Nigeria 127th, and Kenya 106th. South Africa was ahead of Brazil (56th) and Russia (63rd).[113]

CORRUPTION

Corruption, real or perceived, deters foreign and local investment. The Corruption Perceptions Index[114] ranks South Africa at 54th in the world, ahead of Nigeria (134th), Kenya (154th), Brazil (69th), Russia (tying Kenya at 154th), India (87th), and China (78th). At least seven African countries perform better than the BRIC countries on this index. International investors in Sub-Saharan Africa flagged corruption as an issue, but one which is also a concern in other emerging markets.

> "Poor legal and regulatory environments combined with bureaucratic obstacles encourages bribery and corruption, this increases the cost of doing business."
>
> *Asief Mohamed, Aeon Investment Management*

MEDIA

African and Sub-Saharan African desks for major business media, including CNBC Africa, the Wall Street Journal, the Economist and the Financial Times are based in Johannesburg, South Africa. These publications cover Nigeria and Kenya occasionally. Xinhua and Al-Jazeera are increasing their Africa coverage. However, the quantity and quality of media coverage of investment, economics, business, and civil society varies greatly in the region.

SI thrives on open, accurate reportage of ESG factors. SI should therefore thrive in regions with open media channels. Media freedom is an issue to be monitored and supported, especially in holding major public and private sector organizations accountable. While we are wary of generalizations in such matters, the annual Freedom House[115] survey of press freedom ranked South Africa, Nigeria, and Kenya as "partly free" in 2010. South Africa had been "downgraded" from "free". Only 10 percent (five of 48 countries in Sub-Saharan Africa) were rated for media freedom as "free".[116]

Social media is destined to play a growing role on the African continent – and indeed, it already has, as demonstrated by recent political ferment in North Africa. Over 50 percent of Africans have cell phones, with more and more being "smart phones" with multimedia capabilities. In the five years to 2008, Africa[117] had the fastest-growing mobile phone market in the world. Gabon, the Seychelles, and South Africa now boast almost 100 percent penetration.[118] The growth of social media could well lead to greater transparency by both the public and private sectors.

2.4

capital markets

Investment interest in Sub-Saharan Africa is trending upward. For example, NYSE Euronext Inc., the home of the New York Stock Exchange and other exchanges, has seen a threefold increase in the trading of African stocks on its exchanges over the past five years.[119]

African stock exchanges have registered significant growth in recent years. There are now over 500 companies listed across 19 different stock exchanges in Africa, presenting a wide range of choices for equity investors.[120] Apart from the 2008-2009 global financial crash, market capitalization and trading volumes have improved markedly since 2002, and the opportunities for accessing Africa with locally registered funds have broadened over the past decade.

The low liquidity of many African exchanges remains a barrier for pan-African or regional funds, especially for listed equity fund managers used to moving in and out of markets. Some African stock exchanges have weeks-long sale execution timelines. Turnover on the Nairobi Stock Exchange is relatively low compared to emerging and developed markets. In 2008 its turnover was 11.4 percent, compared with 21.9 percent on the Nigerian Stock Exchange and 71.8 percent on the JSE.[121] Relatively high transaction costs also reduce the appetite of global investors. Transaction costs in Nigeria, for example, range from 4 to 4.2 percent.

> "Equity markets are still not very liquid and relatively small. While banks still dominate the financial systems of all Sub-Saharan Africa frontier markets, capital markets are growing rapidly… The automation of trading systems, regional integration, and increased primary market activity are expected to boost size and liquidity in the future."
>
> *Marion Muhlberger, Deutsche Securities*[122]

FOREIGN TRADING ON CAPITAL MARKETS

The ***South African*** market remains appealing to international investors for its legislative framework and liquidity. Global investment on the JSE reached highs of over $160 billion during both 2007 and 2008. Foreign investors were net buyers of $4.9 billion of equities in 2010.[123] South Africa benefited from the wave of capital inflows to emerging markets during 2009 and 2010. The volume of fixed income sales in 2009 was $2.1 trillion, of which about 30 percent was accounted for by non-residents.

It is expected that there will be some reforms that will affect the listing of foreign companies on the JSE. In February 2011, South Africa's National Treasury announced its intention to *"consult on the complex issue of how best to define foreign and local assets for the purposes of prudential regulation".*[124] The consultation will only be forward looking, and will not affect the current status of foreign companies listed on the JSE. The "London Five" (Anglo American, BHP Billiton, SAB Miller, Old Mutual, and Investec), which make up 9 percent of all shares traded, 11 percent of the total number of trades and 24 percent of all value traded on the JSE, will continue to be treated as domestic companies despite foreign domicile.

> "It is important that finality is reached so that South Africa is able to attract more foreign listings into South Africa, so that South Africans can use South African infrastructure to diversify their investment portfolios, and so that the country can play a meaningful role as a gateway for investment into African markets."
>
> *Russell Loubser, CEO of the JSE*[125]

Kenya has recently attracted a surge in foreign investment. Global investor participation in equity market transactions increased from 0 percent in November 2004 to 28 percent in December 2010. Equity trading on the Nairobi Stock Exchange is largely driven by domestic investors (72 percent as of December 2010).

Nigeria's stock exchange has also experienced an increase in foreign investor participation. The exchange "statistics showed that purchases by foreign investors during 2010 were $2.54 billion, representing 48 percent of the aggregate turnover. This is an increase when compared with the $1.35 billion recorded in 2009."[126]

EXCHANGE RATES

Exchange rate volatility is a potential deterrent for some investors. Over the past decade, the exchange rates of the South African rand and Nigerian naira to the U.S. dollar have varied greatly. These variations were due in part to rising commodity prices. The Kenyan shilling, which is not as dependent on resources, has been less affected. Currency exchange rates over the past decade are shown in the table below.

> "There are signs that the rand's position as the most volatile currency in the world may be on the wane. [Since 2008] …the rand's volatility appears to have normalized in line with other emerging markets."
>
> *Andre Roux, Head of fixed income, Investec Asset Management*[127]

CURRENCY[128]	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Shilling:$	78.05	78.6	77.2	76	78.65	72.45	69.6	63.8	78.15	75.85	80.7
Naira:$	110.00	119.50	126.85	139.55	133.15	130.38	128.80	117.90	139.70	149.50	152.00
Rand:$	7.58	11.99	8.58	6.69	5.66	6.34	6.99	6.86	9.41	7.38	6.59

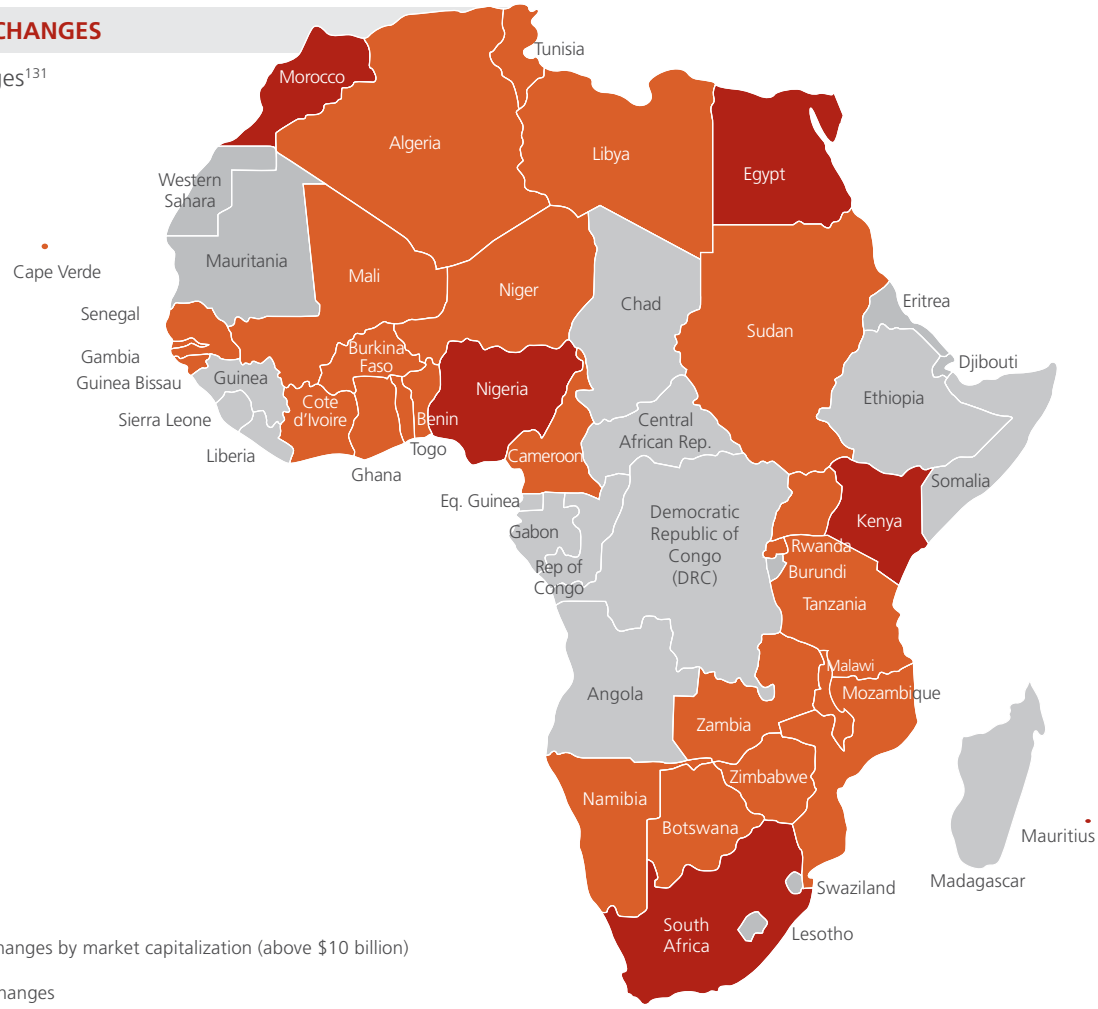
SOVEREIGN CREDIT RATINGS

Credit ratings reflect the investability of markets and move with investor confidence. Of the three countries in this study, only South Africa has an investable rating for global emerging markets investors using the ratings agency scoring (BBB+) applied by both Standard & Poor's and Fitch. In Sub-Saharan Africa, only Senegal, Nigeria, Ghana, and Gabon have international bonds outstanding. The highest yield was on the Senegalese bond, with 2014 maturities trading at about 8 percent in May 2011.[129] Coverage of ratings agencies has expanded to cover more securities within Nigeria and Kenya, as an indicator of increased investor and financier interest.

CREDIT RATINGS[130]			
	Kenya (Treasury bill)	Nigeria (Government bond)	South Africa (Government bond)
Standard & Poor's ratings			
Outlook	Stable	Stable	NEG
Foreign Currency LT Debt	B+	B+	BBB+
Local Currency LT Debt	B+	B+	A+
Foreign Currency ST Debt	B	B	A-2
Local Currency ST Debt	B	B	A-1
Standard & Poor's national ratings			
Natl LT Issuer Credit	-	ngA+	zaAAA
Natl ST Issuer Credit	-	ngA-1	zaA-1
Fitch ratings			
Outlook	Stable	NEG	NEG
LT FC Issuer Default	B+	BB-	BBB+
LT LC Issuer Default	BB-	BB	A
Foreign Currency LT Debt	B+	BB-	BBB+
Local Currency LT Debt	BB-	BB	A
Foreign Currency ST Debt	B	B	F2
ST Issuer Default Rating	B	B	F2

AFRICAN STOCK EXCHANGES

African stock exchanges[131]



JOHANNESBURG STOCK EXCHANGE

The market capitalization of the JSE at December 31, 2010 was $893 billion,[132] making it the 19th largest exchange in the world.[133] The annualized year-to-date liquidity at the end of October 2010 was 55 percent, compared with 38 percent in October 2009. In 2010 it acquired the Bond Exchange of South Africa to consolidate its role as the major securities exchanges and it is a listed company in its own right (JNB:JSE). The JSE recovered from a downturn in 2008 following worldwide market failure to a healthy 28.63 percent in 2009. The compound annual growth rate between 2001 and 2009 was 11.36 percent. The market is highly concentrated. As of December 31, 2010, the top 10 listed companies by market capitalization represented about 63 percent ($565 billion)[134] of the total JSE market capitalization.

MARKET PERFORMANCE: JOHANNESBURG SECURITIES EXCHANGE[135]										
	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
% return	28.07	-11.28	11.96	21.85	42.98	37.68	16.23	-25.72	28.63	16.09

NIGERIAN STOCK EXCHANGE

The market capitalization of the Nigerian Stock Exchange on December 31, 2010 was $66 billion. Since 1999, it has enjoyed a strong performance, although equity as a means to foster corporate growth is underutilized by Nigeria's private sector. Seven years of positive returns to 2007 turned negative in 2008 and 2009, though an upturn was evident during the first three quarters of 2010.[136] There is a large degree of concentration here too. As of December 31, 2010, the top 10 listed companies by market capitalization represented about 45 percent (about $29 billion)[137] of the total market capitalization on the exchange.

MARKET PERFORMANCE: NIGERIAN STOCK EXCHANGE[138]										
	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
% return	35.16	10.71	65.56	15.91	2.7	38.74	74.73	-45.77	-33.77	18.93

NAIROBI STOCK EXCHANGE

In 2010, the value of shares traded on the Nairobi exchange reached $1.4 billion, up from $0.5 billion in 2009. Market capitalization increased from the local currency equivalent of $5.8 billion in 2005 to $15 billion in January 2011. The turnover of the bonds listed on the exchange was about $613 million in February 2011.[139] The exchange invested about $1.25 million to improve the integrity of its trading systems.[140] Concentration is also a factor in Kenya. As of December 31, 2010, the top 10 listed companies by market capitalization represented about 47 percent (about $7 billion)[141] of the total market capitalization on the exchange.[142]

MARKET PERFORMANCE: NAIROBI STOCK EXCHANGE[143]										
	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
% return	0.70	-1.78	-1.55	3.49	-7.88	-3.93	-8.33	22.49	-2.94	6.39

> "We have started putting in place regulations related to full and timely disclosure by companies listed on the exchange to assist investors in making informed decisions. Most of them have realized it's no longer business as usual."
>
> *Emanuel Ikazaboh, acting chief executive officer of the Nigerian Stock Exchange*[144]

The table below provides a snapshot comparison of the African stock exchanges as of September 2010. The JSE is the only exchange on the continent that requires listed companies to disclose ESG-related information, positioning itself as having world-class corporate governance listing requirements.

SELECTED AFRICAN STOCK EXCHANGES[145]					
Exchange	Since	Listings	%	Market cap $ billion	%
Johannesburg Stock Exchange	1887	885	61	746	88
Nigerian Stock Exchange	1960	230	16	53	6
Nairobi Stock Exchange	1954	55	4	14	2
Sub-total for South Africa, Nigeria, and Kenya		1170	81	813	96
Bourse Régionale des Valeurs Mobilières (West Africa)	1998	40	3	5.7	1
Lusaka Stock Exchange	1994	20	1	5.35	1
Stock Exchange of Mauritius	1989	73	5	5	1
Uganda Securities Exchange	1997	13	1	5	1
Botswana Stock Exchange	1989	25	2	4	0
Dar es Salaam Stock Exchange	1996	15	1	3.7	0
Ghana Stock Exchange	1989	34	2	2.5	0
Zimbabwe Stock Exchange	1993	24	2	1.7	0
Malawi Stock Exchange	1994	15	1	1.5	0
Namibian Stock Exchange	1992	8	1	0.8	0
Bolsa de Valores de Moçambique	1997	2	0	0.2	0
Swaziland Stock Exchange	1990	5	0	0.1	0
Sub-total for Africa (excluding South Africa, Nigeria, Kenya)		274	19	36	4
Total Africa		1,444		848	

Additional information about listed companies and capital markets in each country is provided in Appendix 2.

THE INVESTMENT CASE FOR SUB-SAHARAN AFRICA

"While the resource boom has played a major role in Africa's leap into the 21st century, the continent's future growth is not solely reliant on the extractive industries. A number of other key sector industries are seen leading a wave for sustainable economic growth. These include financial services, telecommunications, information technology, oil and gas and infrastructure, supported by consumer-facing industries and agriculture."[146]

Johann Erasmus, Director Global Structuring Group at Standard Bank

Investors interviewed for this study were generally bullish on the investment case for Africa, as shown in the figure below. Most saw investment opportunity on the continent, tempered by reservations about corruption and liquidity (the ability to enter or exit investments when needed without large associated costs). Africa is still perceived as a risky investment environment, but for pro-Africa investors, this constitutes an advantage, being an effective barrier to entry.[147] For example, experienced PE firm Helios Investment Partners closed the continent's largest-ever buyout fund at $900 million in 2011.[148]

IMPORTANCE OF SELECTED FACTORS IN CHOOSING WHETHER TO INVEST IN SUB-SAHARAN AFRICA

Ranking results identified as "very important" on 4-grade scale

[frequency ranking from 8 options; n=48 PE investors + 44 asset owners and asset managers]

Investment data is patchy for most of Sub-Saharan Africa. But as investment activity increases, more data is being made available. New investment services firms and major industry players are launching regional offerings.

The longer-standing markets like South Africa, Botswana, and Namibia have a better pool of data-points and more sophisticated information, including companies with ESG data available through data providers. Country-specific funds are gaining traction (as shown below) to leverage established relationships and to provide the investors with pure-play country options. For example, in 2010, the Angolan PE fund Fundo de Investimento Privado Angola[149] raised $28 million for its first closing.

FUNDS WITH EXPOSURE IN AFRICA IN 2010 MARKETED VIA BLOOMBERG INFORMATION SYSTEMS[150]					
Focus	Alternative[151]	Asset allocation[152]	Listed equity	Real estate	Total
Africa	36	15	131		182
South Africa	8	256	324	22	610
Morocco		16	23		39
Egypt		6	23		29
Tunisia		3	2		5
Namibia		1	4		5
Mauritius			4		4
Libya		2			2
Nigeria			2		2
Botswana	1				1
Zimbabwe	1				1
Total	46	299	513	22	880
%	5	34	58	3	100

THE INVESTMENT VALUE CHAIN IN SOUTH AFRICA, NIGERIA, AND KENYA

South Africa dominates the Sub-Saharan African investment industry, with 69 percent of the 880 African funds marketed, as tracked by Bloomberg.[153] These funds represent 86 percent of "asset allocation funds" and 61 percent of listed equity funds available on the continent, while Nigerian funds have two with listed equity mandates. Kenya is not included on the Bloomberg database, although Kenya-registered funds exist in both equity and fixed asset classes. The gap in data reflected in Bloomberg illustrates the gaps in data across the investment industry in Africa, and limits the opportunities for both the fund managers and the data vendor profiling the global coverage.

Drawing in investment requires financial services to deliver accurate data, investment analysis, and technical execution of decisions. Much of Africa lacks such infrastructure. South Africa is the exception. The relatively small market and foreign exchange controls mean that the investment industry is concentrated. For example, the largest 10 asset managers account for about $426 billion, or 77 percent of assets in the South African investment industry. Of these top 10 asset managers, six are linked to large South African insurance or bank conglomerates.[154]

The institutional investment market in South Africa, Nigeria, and Kenya is often dominated by the relationships between service providers, such as asset managers and/or asset consultants, financial institutions, and asset owners. In South Africa, the model is similar to the United Kingdom, where the intermediary (investment advisor/asset consultant) acts as gatekeeper to the investment decisions of retirement funds. The institutional investment market segment far outstrips the retail segment. In South Africa, pension fund assets more than doubled between 2002 and 2009, from about $100 billion to $250 billion.[155]

Financial investment skills are in relatively short supply in emerging and frontier markets. Individuals with such skills are often recruited into developed-country markets and/or multinationals.

DOMESTIC AND INTERNATIONAL INVESTMENT

Global investment flows provide new capital to fund economic growth, as well as diversification benefits to international investors.

> "Africa is not yet on the radar screen of the more risk-averse institutional investors, which is ironic given the exceptionally low correlation of African equity returns (10-30 percent, and commensurately high risk-adjusted returns) in the context of a global portfolio."
>
> *Greg Barker, Sustainable Capital*

Over the past 15 years, South Africa has relaxed its foreign exchange requirements. In the 2010 Medium Term Budget Policy Statement, the Minister of Finance announced that *"the prudential framework for foreign investment by private and public pension funds, including GEPF, will be reviewed to support portfolio realignment and offshore diversification of these funds, especially in the rest of the African continent and into other emerging markets."*[156] The National Treasury announced a five-percentage point increase in the limit that institutional investors can invest offshore. This takes the offshore limit to 25 percent, with a further 5 percent allowance for investments in Africa to boost pan-African growth.

Investors tend to group African investment markets into three categories: South Africa, North Africa (often grouped with the Middle East), and the rest of Africa (an undifferentiated group of more than 40 countries in Sub-Saharan Africa). For example, in April 2008 Standard & Poor's launched three African indexes:[157] Standard & Poor's Africa 40 tracks the stocks of the 40 largest, most liquid African companies operating purely in Africa; Standard & Poor's Pan-African Index covers 12 African markets – Botswana, Côte d'Ivoire, Egypt, Ghana, Kenya, Mauritius, Morocco, Libya, Nigeria, South Africa, Tunisia, and Zimbabwe; and the Standard & Poor's Africa Frontier Index concentrates on eight less-developed markets, including Nigeria and Kenya. As of June 30, 2010, the one-year annualized returns of Standard & Poor's Africa 40, the Frontier Index, and the Pan-Africa Index were 27 percent, 0.5 percent, and 16 percent respectively.[158]

In recent years, regional investment has increased, and pan-African initiatives do exist. For example, Harith established a $600 million Pan-Africa Infrastructure Development Fund[159] in 2007 to support continent-wide projects in power-generation, energy, telecommunications, transport, property development, water, and sanitation. About 60 percent of these investments are in South Africa, Nigeria, Kenya, and Tunisia – and most of the assets invested originate with South African institutional investors. There is a pool of liquidity from institutional investment managers in South Africa that have specific Africa-focused mandates, and this pool is growing as more information about opportunities elsewhere on the continent becomes available, and as South African authorities relax exchange controls.

3.

regulatory frameworks and sustainable investment

3.1

savings, pensions, and investments[160]

South Africa, Kenya, and Nigeria each have their own multi-tiered financial regulatory systems (see table below). Finance ministries and underlying agencies are responsible for most regulatory bodies for savings, pensions, and investments, with cross-referencing legislation and administrative functions from other arms of government, and industry codes of practice.

Country	Government department	Regulatory bodies
South Africa	Ministry of Finance	Financial Services Board South African Reserve Bank Financial Intelligence Centre National Treasury
	Ministry of Trade and Industry	Department of Trade and Industry National Credit Regulator
Nigeria	Federal Ministry of Finance	Nigerian Insurance Commission Central Bank of Nigeria National Pension Commission Securities and Exchange Commission
Kenya	Ministry of Finance	Central Bank of Kenya Retirement Benefits Authority Insurance Regulatory Authority Capital Markets Authority

3.2

fiduciary duty

SOUTH AFRICA

Of the three countries, South Africa has the most advanced regulatory framework, with broad connections to international regulatory contexts. The most prominent regulations promoting SI/ESG concerns are under discussion. Insurance company funds, retirement funds, collective investment schemes, and medical aid pre-funding are all regulated with investment guidelines and criteria. The Financial Services Board is responsible for financial services regulation, apart from banks.

New activity in 2010 and 2011 focused on pension legislation. Modifications to the investment rules for pension funds have the potential to generate a significant change in the quantity of funds allocated to the PE asset class and the approach to ESG factors. Pension and retirement funds are regulated primarily under the Pension Funds Act.[161]

Regulation 28 of the Pension Funds Act is particularly important because it covers prudential investment guidelines and governs permitted levels of exposure to different asset classes. Up until recently, its provisions made no reference to SI. On February 18, 2010, the National Treasury published a proposed amendment to Regulation 28 for public comment,[162] which specifically mentions the importance of ESG considerations in sustainable long-term investment performance. The amended regulation states, in part: *"Prudent investing should give appropriate consideration to any factor which may materially affect the sustainable long-term performance of their investments, including those of an environmental, social, and governance character. This applies across all asset classes and should promote the vested interest of the fund in a stable and transparent environment."*[163] This revised regulation comes into effect from July 1, 2011 through December 31, 2011, and has the potential to be a strong driver for SI in South Africa and in the region.

Institutional investors also take cognizance of the Department of Trade and Industry's Financial Sector Charter in terms of the Broad-based Black Economic Empowerment Act.[164] From an SI point of view, the charter comprehensively defines "targeted investment" and increases transparency of ESG issues, even though a company's "empowerment" rating does not address the full spectrum of ESG considerations.

In South Africa, governance and fiduciary duty are not prescribed by statute, but by a history of common law and legal precedent. Two codes will play a role in industry self-regulation over the period ahead: the King Code for Corporate Governance[165] (first published in 1994 and updated in 2009, now called King III) and the Code for Responsible Investing by Institutional Investors in South Africa,[166] due to launch in July 2011.[167] The King Code,[168] first published in 1994 and updated in 2009, is widely supported by South African business, while the Code for Responsible Investing is an institutional investor initiative. Both codes operate under an "apply or explain" basis, placing the onus on the applicant to voluntarily apply the principles, explain how the principles have been applied differently, or why they have not been applied at all.[169] King III has also encouraged the launch of the Code for Responsible Investment in South Africa,[170] scheduled for July 2011 in Johannesburg. The latter code has the support of major capital owners and represents investments of about $298 billion.

NIGERIA

In Nigeria, regulations exist that provide codes and guidelines to promote SI in corporate governance, alongside general fiduciary duty. Codes and guidelines include:

- The Code for Corporate Governance for Licensed Pension Operators.
- The Code of Ethics and Business Practices for Licensed Operators.
- Whistle-blowing guidelines for pensions, providing guidance for reporting breaches by fund administrators, custodians, and administrators.

KENYA

According to the Retirement Benefits Authority of Kenya,[171] the two main fiduciary duties "imposed by equity" are a duty to not profit and to not delegate. Fiduciary duty is expressed in regulations as the need to ensure that no one in a fiduciary capacity stands to make a profit, or faces a conflict of interests in their personal and fiduciary roles. In addition, aspects of governance are covered in the obligations and duties of a trustee.[172]

3.3

environmental, social, and governance regulations

Each of the major countries in Sub-Saharan Africa has in place some regulation or governance that deals explicitly with ESG issues. In South Africa, "sustainable development" is considered a human right and is enshrined in the Constitution. The table below offers a simplified list of legal provisions relevant for investors and/or companies for ESG issues in each country.[173]

Country	Environmental	Social	Governance
South Africa	The Constitution: Section 24 The National Environmental Management Act Polluter Pays Principle Environmental Conservation Act National Water Act National Environmental Laws Amendment Act National Environmental Management: Protected Areas Act The Air Quality Act National Energy Regulator of South Africa: feed-in tariffs Pension Funds Act	Broad-Based Black Economic Empowerment Act Labor Relations Act Skills Development Act Housing Protection Measures Act Unemployment Insurance Act Basic Conditions of Employment Act Promotion of Equality and Prevention of Unfair Discrimination Act Pension Funds Act	The Companies Act King III Code of Governance Pension Funds Act
Nigeria	Federal Environmental Protection Agency Act Effluent Limitation Regulation: Pollution Abatement in Industries and Facilities Generating Wastes Regulations Environmental Protection Management of Solid and Hazardous Wastes Regulations Environmental Impact Assessment Act Harmful Wastes Special Criminal Provisions Act	Gender and Equal Opportunities Law (states of Anambra and Imo)	The Corrupt Practices and Other Related Offences Act
Kenya	Environmental Management and Coordination Act Ministry of Energy: feed-in tariffs Energy management regulation	Employment Act 1976	Governance, Justice, Law and Order Sector Reforms Program Public Officer Ethics Act Anti-corruption and Economic Crimes Act The Cabinet Committee on Anti-corruption

In the run-up to UN Framework Convention on Climate Change Conference of the Parties (COP 17),[174] which takes place in Durban, South Africa in November-December 2011, more climate change-related initiatives and regulations, including the implementation of the new Clean Air Act, will affect business and investment. For example, ArcelorMittal South Africa[175] has made a $400 million provision for environment-related expenses from 2011 to 2015.

INITIATIVES AND SELF-REGULATION

ESG reporting and voluntary activities are often driven by multinationals and firms with the highest degree of explicit ESG impact (such as mining or energy companies). Multinationals have an incentive to protect their brands and investments through reputation management. While there are notable exceptions, corporate citizenship work by major companies focuses on remedying the effects of their activities on local communities or improving their reputation with potential customers. As with other major emerging markets, "giving back" in South Africa through corporate social investment is an implicit operational requirement, with firms expected to spend about 1 percent of net revenues on such investment.[176]

Cross-border initiatives, especially partnerships between developed and developing nations, may have a positive effect on improving compliance. For example, the EITI[177] launched in 2002 at the World Summit on Sustainable Development in Johannesburg, or the Equator Principles[178] launched by major banks operating in emerging markets, may be adopted as standards of best practice across regions of differentiated regulatory strength. The EITI supports improved governance in resource-rich countries through the verification and full publication of company payments and government revenues from oil, gas, and mining. The Equator Principles are a set of voluntary standards for determining, assessing, and managing social and environmental risk in project financing.

The EITI includes 80 investment institutions that collectively managed over $16 trillion as of July 2009. Nigeria is a co-member of the EITI International Advisory Group and the federal government volunteered to pilot the new disclosure and validation methodologies, completing an audit of oil sector payments and state revenues from 1999 to 2004. However, while the government has passed implementing legislation on public procurement and fiscal transparency, it must still guide similar bills through Nigeria's 36 states.[179]

Internationally, industry self-regulation and/or NGO-driven initiatives play an important role in profiling ESG issues. For example, in November 2010 the Carbon Disclosure Project (CDP) released a report on water-related issues;[180] it relies explicitly on the influence of investor-driven disclosure requests to motivate companies to improve their reporting and compliance.

Global markets investors may develop their unique guidelines for emerging markets, such as the CalPERS Emerging Equity Markets Principles and Global Principles of Accountable Corporate Governance, initiated by the largest U.S. retirement fund.[181] Investors prefer to act in collaboration to maximize positive influence with local partners. The Emerging Markets Disclosure Project,[182] for example, is matching global and local investors in emerging markets to promote higher standards of company ESG reporting.

3.4 capital markets

SOUTH AFRICA

South Africa capital markets are regulated by the Financial Services Board and the National Treasury. The JSE is regarded as the most stringent African exchange, with extensive listing requirements.[183] From 2011, ESG factors are expected to play a much greater role in corporate reporting as JSE-listed companies move to adopt the King III report and integrated reporting standards.[184] South Africa is a world leader in this respect.

> "Integrated reporting is the evolution of financial reporting… The corporate identity of companies has changed and so reporting has to change. Stakeholders need to make informed assessments about the longer-term sustainability of a company and that it is operating as a responsible corporate citizen."
>
> *Professor Mervyn King,[185] Chairman of the King III Commission and Global Reporting Initiative*

NIGERIA

The Securities and Exchange Commission of Nigeria is tasked with protecting investors and market operators, and ensuring market integrity. The country is working on a regulatory framework to establish itself as the African hub for Islamic banking, trying to emulate other countries, notably Malaysia, that have had some success in this area.[186]

KENYA

Kenya's capital markets are regulated by the Capital Market Authority, under the Ministry of Finance. This authority defines eligibility requirements for public offerings of shares and market listing. The Nairobi Stock Exchange listing manual and trading rules provide extensive disclosure requirements,[187] but does not mention ESG disclosure in the list of reporting obligations.[188] Kenya has adopted the Organization for Economic Cooperation and Development's Principles of Corporate Governance, and the Capital Market Authority released its Guidelines on Corporate Governance Practices by Public Listed Companies in 2002.[189]

4.

key findings

This report concludes that while there is a small base of ESG-branded investment products and a larger ESG-integrated investment policy segment, there will be significant growth of ESG factors in investment management in South Africa, Kenya, and Nigeria through 2020. In a global context, SI market penetration in the region, estimated at 20 percent of AUM, ranks higher than both the U.S. and Brazil (both 12 percent of AUM). This is a strong base on which to broaden and amplify SI.

Progress in SI will be uneven, affected by national developments, the availability of investment mandates, the availability of investment skills, and investable opportunities in ESG themes. There is a gap between the supply of investable ideas and the availability of investment to fund sustainability. Many of those interviewed for this study say investable opportunities are available, but that there is no "easy money"; others complain that no new mandates have been forthcoming from asset owners. Inevitably, where some investment managers see risk in integrating ESG factors, others see opportunity (and risks where ESG is not integrated into investment decisions). The reality is every investment decision must be a trade-off in the context of imperfect information and uncertainty. Given its fit with SI, the active ownership PE model is likely to be a major pathway for ESG-integrated investment management, especially in markets outside of South Africa.

4.1

defining sustainable investment

Definitions of sustainability differ, as do the definitions of SI, and the execution of ESG in mandates across funds.

Sustainability presents different challenges in different regions. Many African countries are thought to be vulnerable to the effects of a changing climate, and are grappling with strategies to mitigate and adapt to climate change. Given its dependence on agriculture,[190] exposure to multiple stresses, and its low adaptive capability, Sub-Saharan Africa has good reason to be concerned. The Intergovernmental Panel on Climate Change estimates that between 75 million and 250 million additional Africans will experience increased "water stress" before 2020. Food supply is also a concern, because the area suitable for agriculture, the length of growing season and yield potentials are all expected to be adversely affected by climate change. According to some estimates, agricultural productivity in Sub-Saharan Africa could decline by as much as 50 percent by 2080, due to the effects of climate change.[191] For coastal economies, the costs of adapting to rising sea levels could amount to between 5 percent and 10 percent of GDP, yet without action losses could reach 14 percent of GDP. Mitigation costs for Africa are estimated at between $5 billion and $10 billion a year by 2030.[192]

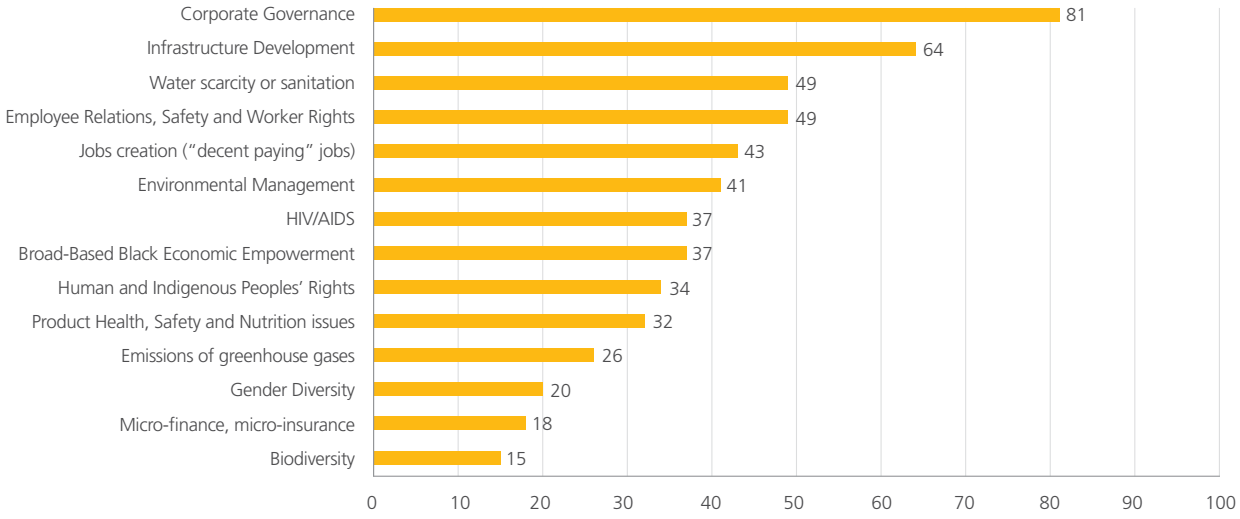
> "Pension funds need evidence that ESG factors have a direct bearing on investment returns, as opposed to just being a nice-to-have. The financial impact must be highlighted as much as the social impact."[193]
>
> *A pension fund chief investment officer*

For some emerging markets, a move to a low-carbon, low-water, climate-resilient economy may pose other difficulties. South Africa's per capita carbon emissions are among the highest in the world, courtesy of a coal-fired energy policy over the past 30 years. Using 2007 data, South Africa accounts for 38 percent of Africa's fossil-fuel emissions total; Egypt, Algeria, Nigeria, Libya, and Morocco combined account for 46 percent. But regulatory changes, alongside demand for new sources of energy and low-carbon economies, will also create opportunities for new markets and green jobs.[194]

Investors interviewed for this research indicated that the ESG-related primary drivers of future performance and the return impacts on portfolio performance are expected to be corporate governance, environmental management, water scarcity, employee relations and infrastructure development. The chart below provides additional detail.

INVESTOR OPINIONS OF IMPORTANCE OF ESG FACTORS IN EVALUATING THE FUTURE 3-10 YEAR PERFORMANCE OF INVESTMENTS IN KENYA, NIGERIA OR SOUTH AFRICA

4-scale; ranking of "very important"; n=98 PE investors/asset managers/owners; Jan 2010-May 2011



IFC defines SI[195] as investment that takes ESG factors into account. Applying such factors to investment analysis, stock selection, and ownership practices improves long-term risk management. In Africa, substantive attempts at comprehensive definition of "sustainable" or "responsible" investment are being developed by government bodies such as South Africa's Department of Economic Development, industry associations such as the Association for Savings & Investment South Africa, and international organizations such as AfricaSIF. In general terms, there are two types of investment strategies related to SI:

1. ESG-branded investment, which describes funds marketed explicitly profiling their ESG characteristics included in the labelling
2. ESG-integrated investment, which integrates ESG factors, but may or may not be marketed as such (by implication, any ESG-branded strategy is also an ESG-integrated strategy).

These differences are captured in the table below.

SUSTAINABLE INVESTMENT STRATEGIES AND METHODOLOGIES: KEY TERMS[196]

Category		Theme/Strategy/Stage	Description
SCREENING	1	Ethical/religious/norms-based	Removing companies involved in "unethical" activities from the investment set, such as the manufacturing of armaments, tobacco, etc.
	2	Positive/best-in-class	Only investing in companies that lead their peer groups/industry/sector in ESG performance at a given time.
IDEAS	3	Sustainability/ESG	Thematic investing based on trends/risks/opportunities arising from the pursuit of sustainable development.
	4	Sustainable finance	Investment enabling capital to be allocated to companies/projects that lead directly to sustainable development, new business models, new market segments. Includes community and impact investing.
ANALYSIS	5	Integrated analysis	Investment that includes ESG factors in valuations models. Applied to equity, fixed income, PE, and alternative asset classes.
HOLDING/ OWNERSHIP	6	Constructive engagement	Communication and collaboration between investors and management that encourages improvements to ESG performance.
	7	Shareholder activism	The use of shareholding to launch public campaigns against specific corporate practices.
EXIT	8	Investment exit	Go/no-go decision for continued holding of existing portfolio position or weighting, from 0 percent to 100 percent.

The Brundtland Commission (1987)[197] definition of "sustainable development" was cited by investors and stakeholders in this study. Often overlooked, the commission's definition includes *"the concept of 'needs', in particular the essential needs of the world's poor, to which overriding priority should be given; and (2) the idea of limitations imposed by the state of technology and social organization on the environment's ability to meet present and future needs."*

Investment practitioners interviewed for this study cited a range of definitions that stressed economic or social categories – or both. One investor defined sustainability as *"operating business activities in a manner that does not impact or deteriorate the future generation's ability to operate … conducting operations in a long-term manner with the capacity to endure."*[198]

Another described SI as *"the combination of economic, social, and environmental capital."*[199]

Respondents in this research suggest that specific immediate factors that should be considered when assessing SI in Sub-Saharan Africa are:[200]

- Investment within a socioeconomic context of a developing African nation with a large population of poor people, which needs to create jobs on a large scale.
- South Africa's broad-based black economic empowerment law, which aims to redress the imbalances of apartheid by favoring previously disadvantaged individuals for economic opportunities. Similar approaches in Nigeria and other countries require significant local, indigenous, ownership equity holding in major companies.
- The effects of climate change, particularly in societies dependent on agriculture.
- Labor relations, and worker health and safety conditions, that ensure a good supply of motivated and talented employees.
- Opportunities to grow small businesses and grow the economy.

"Sustainability… is about creating enterprises that create new jobs, increase skills, the businesses make a positive impact on the communities in which they invest, benefit the environment, improve the infrastructure, and improve the transparency and good business practice."

Stephen J. Bell, Shared Growth AM IC

"Sustainability mainly borders on environmental issues and corporate governance. Sustainability is the need to give back as much as has been taken. The continent has long been exploited of its resources and poor governance is a quality that must be eschewed."

Laolu Alabi, Silk Invest Limited

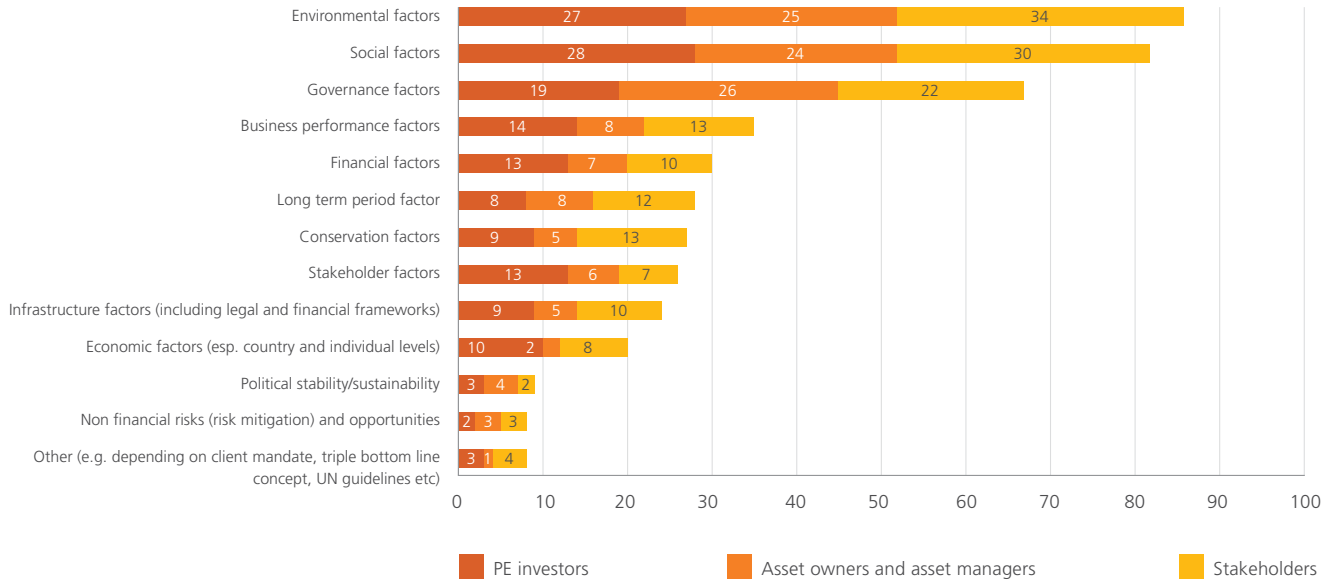
Language employed in the SI/ESG context[201] can be categorized into three main areas:

1. Economic development targeting infrastructure, jobs, and sustainable development.
2. Environmental concerns.
3. Long-term investment stewardship and/or risk management concerns.

Interviewees identified environmental and social factors as the two highest-ranking factors, followed by governance, in defining sustainability, as illustrated below.[202]

HOW DO YOU DEFINE "SUSTAINABILITY"? WHAT SUSTAINABILITY ISSUES - ENVIRONMENTAL, SOCIAL OR CORPORATE GOVERNANCE - ARE FRONT OF MIND FOR YOU IN AFRICA TODAY?

[open-ended; top 10 responses; n= 52 PE investors + 46 asset owners and managers + 59 stakeholders]



4.2

sustainable investment market snapshot

Sustainable investment in Sub-Saharan Africa has a strong foothold, with continued growth expected through 2020, dominated by the large institutional investment industry in South Africa.

In both the PE asset class and in general asset management, ESG-branded funds are relatively small, totaling just under $5.5 billion AUM (less than 1 percent of total AUM) as of December 21, 2010. But using a broader definition that covers self-reported integration of ESG factors into fund investment policy and/or process, SI in South Africa, Kenya, and Nigeria is estimated at $125 billion[203] AUM – equivalent to 20 percent of general asset management and 44 percent of PE in Sub-Saharan Africa. This puts the overall SI market in Sub-Saharan African ahead of the U.S., Brazil, or South Korea.

The relatively high proportion of ESG-integrated investment is largely due to the asset commitments of the largest asset owner in South Africa, the GEPF, which has $131 billion AUM, and the manager of 92 percent of its assets, the Public Investment Corporation. Both have adopted ESG-integrated sustainable, responsible, and/or developmental investment policies. These policies will create momentum, noting that the scale and the pace of GEPF and PIC implementation will take three years or more to execute. Impact measurement will be key. In this respect, the GEPF is a world leader, and there are thousands of other pension funds in South Africa that could adopt this best-practice approach if they are convinced of the business case.

The estimates for the ESG-branded category in Sub-Saharan Africa were developed based on a composite list of such funds (please refer to the table titled ESG-branded investment products in Sub-Saharan Africa 2010 in the section on sustainable investment supply later in this report). The estimate of the ESG-integrated market is based on an analysis of available quantitative information, along a spectrum of proxies:

- The percentage of respondents self-reporting that they manage assets for DFIs (which by definition requires ESG integration in investment mandates).
- The percentage of respondents (PE and general asset management) self-reporting their firms use a fully integrated ESG strategy applied to the majority of their investments.
- The self-reported gross AUM from members/signatories of initiatives such as the CDP or Principles for Responsible Investment.

ESTIMATES OF THE PROFESSIONAL SUSTAINABLE INVESTMENT AUM IN SUB-SAHARAN AFRICA, END-2010 ($ BILLION)					
General asset management					
	Total AUM	ESG-integrated	*% ESG-integrated / total region AUM*	ESG-branded	*% ESG-branded / total region AUM*
South Africa	556.2	111.2	*20.0%*	4.2	*0.8%*
Kenya, Nigeria, and/or Sub-Saharan Africa ex-SA	18.3	3.5	*18.9%*	0.0	*0.0%*
TOTAL (sum of South Africa and ex-South Africa – except for %)	574.5	114.7	*20.0%*	4.2	*0.7%*
Private equity					
	Total AUM	ESG-integrated	*% ESG-integrated / total region AUM*	ESG-branded	*% ESG-branded / total region AUM*
South Africa	14.2	6.3	*44.0%*	1.1	*8%*
Kenya, Nigeria, and/or Sub-Saharan Africa ex-SA	9.8[204]	4.3	*44.2%*	0.2	*2%*
TOTAL (sum of South Africa and ex-South Africa – except for %)	24.0	10.6	*44.1%*	1.3	*5%*

Sources: SinCo analysis from SinCo+RisCura data+analysis, 2010-2011; South African Reserve Bank, Quarterly Bulletin - No. 259, March 2011; South Africa National Treasury, 2010; ASISA Collective Investment Schemes, 2010; Company websites; Preqin, 2010; RisCura, South Africa Venture Capital Association/KPMG 2010; Bloomberg, Factset, ThomsonReuters, Emerging Markets Private Equity Association/Collier 2010; Kenya Retirement Benefit Authority, Business Day.

To increase the understanding and accuracy of SI/ESG themes and practices, this report recommends additional research with a qualitative review of ESG-integration and performance attribution being most important to differentiate intention from impact.

> "Evidence of improved returns will make sustainable investment more attractive."
>
> *Yemi Lalude, Adlevo Capital*

The table below puts Sub-Saharan Africa's SI levels in global context. Definitions vary internationally,[205] so the broadest definitions are applied here.

GLOBAL SUSTAINABLE INVESTMENT MARKETS ESTIMATES 2009 - 2011		
Market and period	Estimated total AUM related to sustainability (US$)	% of total estimated AUM
European Union, 2010[206]	$7.26 trillion	47%
United States of America, 2010[207]	$3.07 trillion	12%
Canada, 2010[208]	$531 billion	19%
Sub-Saharan Africa, 2010[209]	**$125 billion**	**20%**
Australia and New Zealand, 2010[210]	$115 billion	13%
Brazil, 2009[211]	$70 billion	12%
Middle East and North Africa, 2010[212]	$54 billion	2%
China, 2009[213]	$4 billion	1%
South Korea, 2009[214]	$2 billion	1%
India, 2009[215]	$1 billion	1%

THE CASE FOR SUSTAINABLE INVESTMENT IN SUB-SAHARAN AFRICA

Investment practitioners need better information to grow SI in Sub-Saharan Africa. Crystallizing the investment case regardless of asset class or company size will generate momentum by illustrating the costs, benefits, trade-offs, risks, and opportunities. Providing accessible and robust intellectual underpinnings will make SI more convincing to businesses and their investors, as well as to communities, governments, regulators, the media, and customers.

The case for SI has a ready audience. More than half (52 percent)[216] of respondents in this study think there is a strong case for SI. However, the SI case has been reinforced by local social and environmental crises, and corporate malfeasance. Moreover, 62 percent of respondents strongly agreed that integrating ESG factors would protect investments from hidden risks that later reduce returns; and 66 percent agreed that SI would increase performance by identifying new opportunities. More than 60 percent of those interviewed said that they would be willing to pay a 10 percent premium for better environmental and social performance – if choosing between two similar companies, they would prefer the one with the better ESG performance.[217] Most investors approach corporate governance as a "must have".

Analysis of survey responses reinforces the view that demand for SI exists because investors value any new and material information on the investee company. ESG factors offer direct and material information on these issues, and also enable investors to develop an over-arching view on company strategy, practice, and execution.

> "Most… asset managers and financial engineers are trying to construct portfolios with limited risk but they are only using historic (and mostly volatility) data to construct these. That means they are ignoring the whole range of physical, political, and social risks that could mean that the portfolios are actually exposed to a huge amount of risk… There should be an ability to do some 'what if' scenarios based on the impacts of carbon pricing, water prices, or pollution costs for example."
>
> *Dirk Visser, Cambridge Program for Sustainability Leadership*[218]

Asset owners (pension funds, insurance companies, institutional investors) are expected to play an important role in SI. The table below shows a diversity of investment characteristics from a sample of asset owners (DFIs and pension funds) represented in the survey.

While the South African pension funds industry is dominated by investments in local fixed income and equity assets, a growing allocation is being invested elsewhere on the continent. This is partly in response to the relaxation of exchange controls, which now allow for up to 20 percent to be invested abroad, and an additional 5 percent over and above that into Africa.

INVESTMENT CHARACTERISTICS OF ASSET OWNERS (DFIS AND PENSION FUNDS) IN SUB-SAHARAN AFRICA[219]

	Total investment portfolio/ market value	Investment allocation to Africa (Sub-Saharan Africa or Pan-Africa, see footnotes)		Investment allocation to PE		Investment allocation to ESG-integrated strategy		Investment allocation to ESG-branded strategy	
	$, million	$, million	% portfolio/ market value	$, million	% portfolio/ market value	$, million	% portfolio/ market value	$, million	% portfolio/ market value
Sample of development finance institutions investing in PE									
CDC (U.K.), 2010[220]	2,974	1,340	45%[221]	2,974	100%[222]	2,974	100%	n/a	n/a
Development Bank of Southern Africa (DBSA), 2009-2010[223]	6,019 [224]	6,019	100%[225]	62	3%[226]	6,019	100%	n/a	n/a
FMO (Netherlands), 2010[227]	7,560	2,117	28%	1,663	22%	7,560	100%	n/a	n/a
IFC, 2010[228]	38,865	5,156	13%[229]	2,113	5%[230]	38,865	100%	n/a	n/a
Industrial Development Corporation (IDC), (South Africa), 2010[231]	9,185[232]	9,185	100%	n/a	n/a	9,185	100%	n/a	n/a
Proparco, 2009[233]	1,601	705	44%[234]	n/a	n/a	1,601	100%	n/a	n/a
Sample of pension funds investing in PE and general asset management (composite)									
Composite of pension funds interviewed in the survey[235]	144,553	137,624	95.2%* 87.6%**	910	0.6%* 1.5%**	66,483	46.0%* 38.5%**	2,381	1.7%* 6.18%**

*% market value weighted **% equally weighted

Asset consultants based in Africa have been slow to tackle the SI theme. RisCura is the only asset consultant service provider in Africa that is signed to the Principles for Responsible Investment, along with multi-managers Advantage Asset Managers, 27Four, and Investment Solutions.[236] In South Africa, at least two major asset consulting firms (Alexander Forbes Asset Consulting and RisCura)[237] have met the investment market demand by offering regular performance reporting on SI/ESG-type portfolios. Attitudes from other asset consultants have been skeptical. But the attitude toward SI is changing, with asset consultants for large institutional investor clients now seeking better ESG coverage to advise their clients.[238]

OPPORTUNITIES

There is a lack of SI mandates in the region, especially in general asset management, but interest is growing. Investment by DFIs using local investment talent has had a positive systemic and thematic effect. Similar to other investment regions, overcoming the dominant short-term investment logic of "money-in, money-out", which does not embrace a fundamental evaluation using ESG integration, presents a major barrier. Overcoming this barrier will offer large new opportunities for investors in the region. Investors are already weighing up what they see as the major influencers on their 10-year performance (see table below).

ESG ISSUES HAVING SIGNIFICANT IMPACT ON 10-YEAR PERFORMANCE, RANKED HIGHEST BY INVESTORS		
2010 IFC/SinCo+RisCura study Ranking of 12 options, n=45 PE + 43 asset owners/managers, SinCo analysis from SinCo+RisCura research, Jan 2010 – May 2011.		**2007 UNISA/UNEPFI/PRI study** Ranking of 10 options, n=19, UNISA research in South Africa, 2006[239]
PRIVATE EQUITY	**GENERAL ASSET MANAGEMENT**	**ASSET MANAGERS**
1. Corporate governance 2. Infrastructure development 3. Employee relations, safety, and worker rights. 4. Environmental management 5. Water scarcity/sanitation	1. Corporate governance 2. Infrastructure development 3. Water scarcity/sanitation 4. HIV/AIDS 5. Job creation	1. Infrastructure development 2. Corporate governance 3. Broad-based black economic empowerment 4. Employee relations 5. Sustainability

South Africa provides a useful reference point. Major investment stakeholders take part in significant global and/or emerging markets sustainability and SI initiatives. For example, all four major South African banks have adopted the Equator Principles.[240] The King III report includes an entire chapter on integrated sustainability reporting and disclosure being pursued by stakeholders in the Integrated Reporting Initiative.[241] JSE-listed companies have been required to adopt world-class ESG requirements in the reporting to standards influenced by King III, which have been integrated into the JSE listing requirements, and the integrated reporting requirement is currently in place for financial years on or after 1 March 2011.

Yet the reaction of institutional investors in South Africa has been described as "slow," with a "lack of understanding about sustainability issues".[243] As a result, initiatives such as the Code for Responsible Investing by Institutional Investors in South Africa have sought to develop an active investor response to investment in the context of King III.

Recent growth in ESG-integrated offerings suggests a more positive trend over the next decade. The growth in ESG-branded and integrated demand and supply will be led by mandate-driven institutional investors and specialist SI boutiques.

Investors seek companies that have a sustained competitive advantage. Sustainability offers a game-changing advantage that some businesses are seizing faster than others – and many smaller businesses are able to adopt more rapidly. For example, Global Carbon Exchange describes how a South African small/medium-sized shoe manufacturer[244] came together with a JSE-listed retailer on the strength of its "green" credentials. In this way, SI is appealing to strategic partners and investors. Another example is corporate advisory services firms targeting climate change as a potential theme on which to present companies to investors. Apart from country-specific operations, all four major accounting/auditing firms have expanded their Africa coverage, and added sustainability-type services.[245]

Sustainability concerns will be center stage as South Africa prepares to host COP 17 in Durban, with various initiatives planned to highlight ESG investment concerns.

4.3

sustainable private equity investing in sub-saharan africa

Private equity is a specialized form of investment that benefits from rigorous due diligence and active stewardship of investee companies, with the aim of creating value that is captured by selling the company at a much higher price after three, five, or even 10 years. PE is a small but strategic investment discipline in Africa, where it provides capital in frontier and emerging markets. The improving economic fundamentals explain why the PE sector is expanding in Sub-Saharan Africa as businesses grow and seek capital, and investors seek to share in the growth.

There are two distinct PE models:[246] firstly, the traditional focus on financial engineering and selective changes in the governance model of portfolio companies (with a 3-5 year horizon); and secondly, seeking value creation through active ownership (with a 5-12 year horizon). Of these two models, the active ownership model is best-suited to promote SI. In addition, in developing countries, PE investments tend to operate with relatively little corporate restructuring, such as leveraged buy-out or more financial engineering strategies, seen more often in North America and Europe.[247]

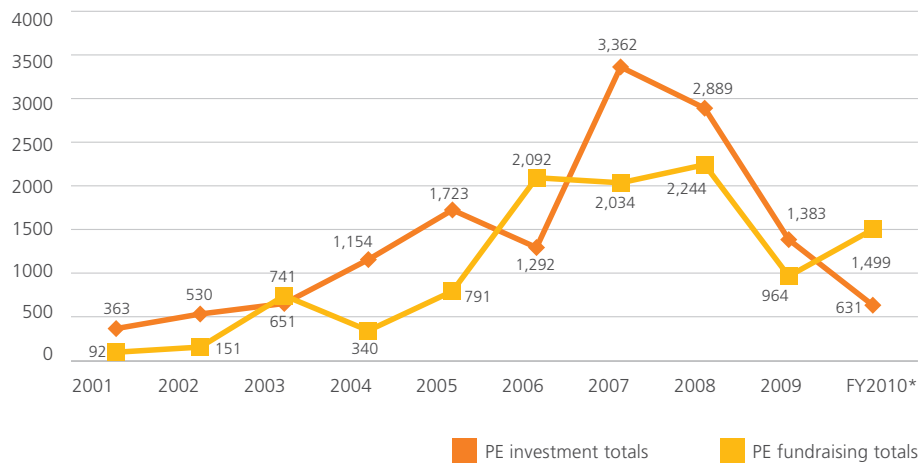
PE is a good fit with sustainability because the PE investor and investee company have the longer time horizon and a common interest in building a firm with lower risks, higher potential returns, and better corporate governance, to sell the company to prospective buyers or portfolio investors. This philosophy motivates that ESG issues be taken into account, both to ensure long-term returns for investors with the most complete risk/return trade-off, and to maximize positive economic impact in markets where money is invested.

While small by global standards, PE in Sub-Saharan Africa has seen more than $10 billion raised for investment in the past decade alone.[248] Investors and analysts expect the pace of PE deals in Sub-Saharan Africa to increase in 2011 and beyond, as more global corporations and banks target rapidly expanding economies, growing middle classes, and rising trade with emerging markets.[249] PE funds currently manage $24 billion in assets in the region. And more capital is coming – of the 52 PE investors interviewed, 92 percent expect an increase in PE commitments in the next five years and 65 percent expect the increase to be over 20 percent. PE investment in Sub-Saharan Africa picked up after the global financial crisis in 2008. Improvements in the African investment environment and "a series of spectacular African business successes ... have fuelled an unprecedented boom in the size and breadth of African private equity funds"[250] since 2008.

> "Fixing its hitherto largely dilapidated infrastructure is also making the continent more attractive to investors. In future, Africa could overtake the Asian countries to climb onto the top of the tables and dominate the growth trends in the private equity markets."
>
> *Michael Turner, Actis East Africa*[251]

The regulatory environment is becoming more enabling. Nigeria's regulatory body, for example, announced in December 2010 that Nigerian pension funds can now invest up to 5 percent of their AUM in PE.[252] In South Africa, the largest PE market and source of new M&A capital, changes to rules of institutional investment Regulation 28 covering investments by pension funds and institutional investors will raise the limit on PE from 5 percent to a 10 percent maximum with a total 35 percent to PE, hedge funds, and property.[253] The revised Regulation 28 will support greater investment into unlisted and alternative assets, promoting economic development that may be funded through such channels. In Kenya, the industry regulatory body, Retirement Benefits Authority, has encouraged retirement funds to explore the PE asset class.[254] Fund managers are especially bullish about the growth potential in the market for PE and hedge funds AUM in the small- and middle-tier pension funds.[255]

SUB-SAHARAN AFRICA PRIVATE EQUITY MARKET GROWTH ($ MILLION)[256]



> "Rising levels of international investment capital in African agriculture and agribusiness have taken the investment thesis directly into the intensely political arena of global food security and land rights."[257]

> "The latent interest in Africa is enormous ... [i]n 3-4 years you'll have 100 Africa funds and the biggest one won't be $2 billion, it'll be $20 billion."
>
> *Stephen Jennings, chief executive of Russian investment bank Renaissance Capital*[265]

RESPONDING TO NEW THEMES

PE funds have grown to support new themes, such as transport infrastructure and agriculture. For example, a PE fund makes the statement that *"[w]e believe it is our corporate responsibility to build and improve Africa's financial landscape, while at the same time pursuing profits."*[259] Examples of PE response to the SI theme include:

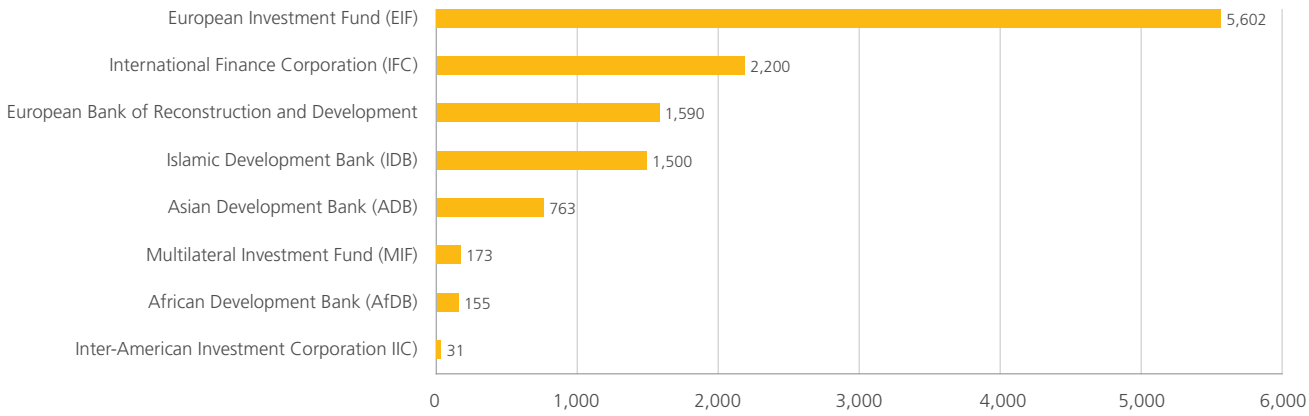
- The first regional ESG-branded clean technology fund ("Evolution One") was launched during June 2010, expanding into sustainable farming.[260]
- In December 2010, Shared Growth Asset Management[261] launched a Socially Responsible Affordable Housing Fund in South Africa.
- CDC committed $30 million to the African Infrastructure Investment Fund, targeting $600 million to invest in African transport and power infrastructure projects.[262]
- In 2010, the Public Investment Corporation (South Africa) Isibaya Fund[263] committed $306 million over a 12-month period to projects covering affordable housing, toll roads, small businesses, and micro-enterprise finance.
- Sarona,[264] which works in frontier markets, was active in the financial technology segment injected $0.3 million in Lusaka-based Mobile Transactions Zambia.
- The African Agriculture Fund,[265] a PE fund managed by Phatisa Group, has reached its first closing at $135 million in partnership with European DFIs.[266] The fund focuses on companies involved in food production, processing and distribution, agricultural and livestock farming, and agri-services.

> "With Africa's stock markets relatively shallow, illiquid, and underdeveloped, taking a stake in companies through private equity is one of the few ways investors can access some of Africa's emerging economies."
>
> *Peter Apps, Organization for Economic Cooperation and Development*[267]

While PE is an attractive asset class in frontier and emerging markets, challenges exist in PE in Africa, as referenced both by the 2010 Emerging Markets Private Equity Association/Collier survey[268] and this report. Among the 52 PE study respondents, the concerns about good corporate governance were a major barrier to investment in Sub-Saharan Africa. The relative role of environmental and social factors is important, but a comprehensive assessment of case studies and tracking of performance attribution is absent. Further research would clarify the stage of the investment lifecycle at which ESG factors become more important.

THE ROLE OF MULTILATERAL DEVELOPMENT FINANCE

2009 DFI COMMITMENTS TO GLOBAL PRIVATE EQUITY MARKET PARTICIPANTS ($ MILLION)[269]



As the figure above shows, DFIs play an important role in the PE industry in Africa, and have seeded many of the first PE funds into the region. In 2009, the largest multilateral DFIs[270] committed more than $12.5 billion to PE funds[271] and this study estimates at least 1 out of every 2 dollars deployed in African PE is DFI-linked.

At least 15 PE funds with more than $9 billion in AUM have a strong DFI limited partner (LP) base, including CDC Group Plc, the European Investment Bank, the African Development Bank, IFC, and the DBSA.[272] Norfund, a Norwegian government fund with 60 percent of its primary investments currently in Africa, opened offices in South Africa and Kenya, and planned commitments to up to 10 PE funds during 2010.[273] French DFI Proparco committed up to $43 million to PE funds focused in Africa by end 2011.[274] East African PE investor Catalyst Principal Partners launched a $100 million mid-cap Catalyst Fund I in the fourth quarter of 2010[275] with seed funding from the African Development Bank and others. The role of major new entrants such as the China-Africa Development Fund[276] in promoting ESG is still to be determined.

Apart from DFIs, asset flows from public pension funds and PE fund-of-funds managers are the two major sources of PE assets, and more asset flows expected in the coming years.[277] Global emerging markets multi-country PE funds with limited exposure to Africa may be a source of future fund flows. There is also enormous interest from the BRICS countries themselves, with the model of government-backed or facilitated trade and M&A activity that binds national interests and business/investment opportunities.[278]

AFRICAN PRIVATE EQUITY AND PENSION FUNDS

Opportunities to grow PE funds lie in strengthening relationships with other key players in African financial markets, particularly in domestic pension funds and long-term savings vehicles. After recycling through the various PE funds, DFI assets will be used elsewhere as risk capital.

Pension funds must limit their PE investment allocation according to regulations in each country, but very few pension funds are making use of the allowed investment levels. According to the annual survey for 2010 of the PE industry in South Africa *"most pension funds have been conservative in the past and have only taken up a portion of the regulated limit"*.[279] In Kenya's pension fund market the small allocation to PE by pension funds (about 0.04 percent as of December 2010)[280] is well below the potential $525 million investment (10 percent maximum allocation by law of total $5.25 billion AUM).[281] In Kenya, government securities and fixed income remain the preferred asset classes.[282]

Large South African institutional investors, such as the four major banks, insurers, the GEPF, and the Public Investment Corporation, are already active in PE in Africa. The retirement funds sponsored by Eskom, Transnet, and other large South African companies with large asset pools have invested in mostly South African PE funds as limited partners. A positive driver for increased PE allocations is South Africa's new Regulation 28, discussed earlier. For PE funds to diversify their longer-term asset gathering to attract institutions, the industry needs to improve reporting, valuation, comparable performance measurements, and the setting of reliable performance benchmarks.

In Nigeria, the idea of the PE asset class in the investment allocation of pension funds is still new. The Pension Fund Reform Act of 2004 only allowed the investment in three types of securities: equity, government bonds, and bank deposits.[283] With the growth in Nigeria's pension sector (with an estimated $13 billion in 2010[284] expected to grow to $30 billion over the next five years),[285] the regulatory investment limits became "untenable" for some.[286] The landscape is now changing. The director-general of the Nigerian National Pension Scheme has proposed new guidelines to increase the amount pension funds can invest in the domestic stock market by 5-10 percent by the first quarter of 2012, and that in terms of the proposed new guidelines, pension fund managers will be allowed to invest 5 percent in PE funds.[287]

The Kenyan government first encouraged venture capital and private equity in 2005, but with little take-up. In 2011, the Retirement Benefits Authority in Kenya[288] supported seminars for pension fund trustees on the PE asset class to enable trustees to learn more about the risks and opportunities of the asset class. Similar seminars were held for West African pension funds. Domestic pension funds in East and West Africa have an interest in diversifying their portfolios into PE. However, trustees and investment advisors need to be educated on PE to balance risk-adjusted returns expectations. High returns on government bonds and the perceived risks associated with an unregulated asset class are barriers to African pension funds.

Some of the bigger pension funds have well-developed PE programs, but South Africa's smaller, less-sophisticated pension funds perceive illiquid investments, like PE investment, to be high risk, despite the liquidity premium they offer. This perception has been exacerbated by extensive media coverage of a handful of bad PE deals. Pension fund trustees have an overriding concern that they cannot access the assets during the lock-in period (assets cannot be liquidated and returned), and indeed the secondary market (where PE fund commitments are traded out of without detriment to the underlying PE fund) is very thin. For smaller pension funds the effort of investigating the PE investment case may not be worthwhile given their small potential exposure and availability of opportunities. To help address this, PE funds can deliver offerings to medium and small pension funds as PE fund-of-funds.

DFIs need to share their experience with institutional investors new to PE, passing on their wealth of information on due diligence, ESG governance frameworks, and managing the relationship between general partners (GPs) and LPs.

"Private equity presents opportunities for pension funds across Africa. PE investment builds the small, medium, and micro-enterprise sector. This leads to job-creation, which leads to increased social security contribution. PE needs to be put in this development context so that trustees can see the bigger picture."

Nana Fredua Agyeman Pambuo,
former trustee, Social Security and National Insurance Trust, Ghana

PE AND ESG FRAMEWORKS IN AFRICA

In developing countries, PE investments tend to operate as venture capital or growth capital with relatively little corporate restructuring, such as leveraged buy-out or more financial engineering strategies, seen often in North America and Europe.[289] Many African PE funds use ESG frameworks developed by DFIs, and most reference IFC Performance Standards.[290]

Sharing knowledge and experience will reduce the barriers to PE asset gathering and moderate unrealistic expectations.

The positive impact of DFIs has a longer-lasting effect. Many PE funds that have or have had mandates from DFIs continue to "slipstream", mapping their frameworks to the DFI's ESG methodology. The IFC's PE environmental and social dashboard[291] has been rolled out as a tool to help PE investors and investee companies work through some of the ESG material. The base of knowledge offers the opportunity from which to organize and adapt material for broader input through practitioner workshops in Africa and dissemination online.

CONTRASTING PE AND LISTED EQUITY INVESTORS

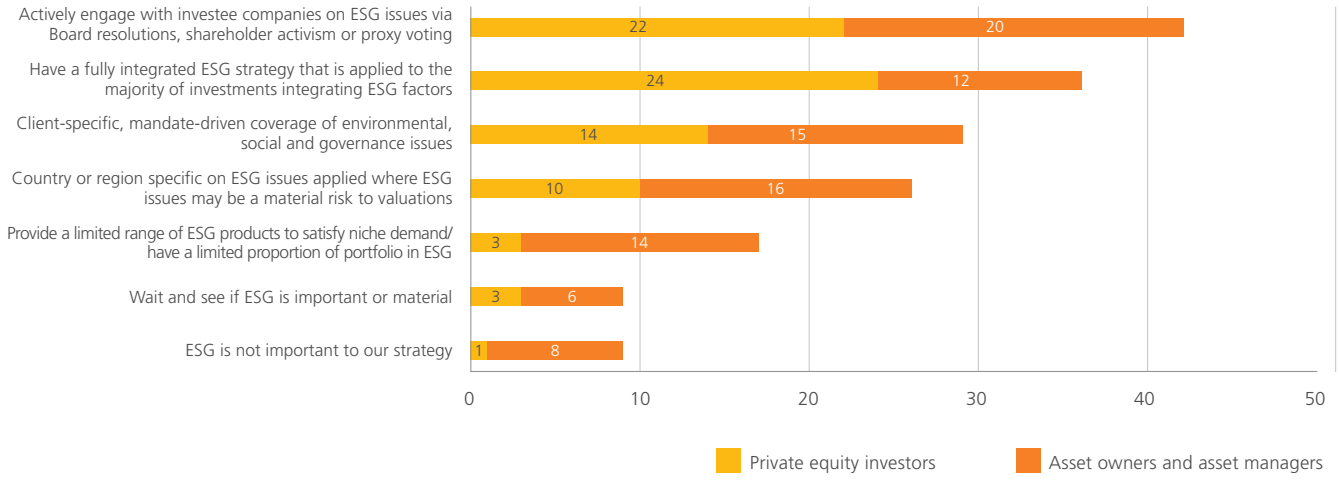
ESG integration by PE and general asset management firms differs. Of 97 investors who answered a question about integrating ESG factors in their activities, 56 explained that they currently have an investment policy that explicitly addresses ESG issues (82 percent environmental, 80 percent social, and 96 percent corporate). The graph below[292] offers some additional insights of investor approaches to SI and ESG integration in Sub-Saharan Africa.

The differences in approach between PE and general asset management are evident in the greater degree of client-driven mandates and limited range of offerings by the general asset managers, who need the scale of multimillion dollar portfolios to cover the fixed costs of their operations (PE firms also prefer scale, but require less).

From this study, it appears that PE has a greater proportion of integrated or active ESG policies in place, leading to the finding that proportionally, PE has better integrated ESG than general asset management.

FUND/PORTFOLIO APPROACH TO SUSTAINABLE INVESTMENT IN SUB-SAHARAN AFRICA

[7 options + "other" option; n = 51 PE investors + 44 asset owners and managers]



In Africa, long-term savings vehicles such as pension funds are uniquely positioned to manage the long investment term and limited liquidity of PE investment to capture performance premiums and diversification benefits.[293] Beyond the economic development benefits of PE by making new capital available, this form of financing and investment is by nature supplemented by assistance in business operations, contributing to economic efficiency and innovation.[294] PE investors are "hands-on" with a vested interest in good management and governance of their investee companies.

PE INVESTMENT PROJECTIONS

PE fundraising activity in Sub-Saharan Africa almost tripled from $731 million in 2005 to over $2.2 billion in 2008.[295] With this level of capital on hand, PE funds were able to maintain a steady pipeline of deals during the 2008-2010 period.

As African countries build roads, railways, airports, and water reticulation systems, the enormous SI opportunity in the next 10 years is to meet increasing energy demands through alternative energy technologies, smart grid networks, and energy efficiency. However, many investors are still waiting for more government clarity on the rules of the game. For example, in South Africa the government regulation of independent power producers and the revenues offered as feed-in-tariffs have yet to be finalized after nearly 10 years of deliberation. A recent call for private sector providers drew 300 applicants to the Renewable Energy Feed-in Tariff program. There are opportunities for companies, and PE investors, in investments in a low-carbon, low-water, climate-resilient economy. For example, of the estimated 12 million households in South Africa, 5-7 million will have solar heaters installed by the government by 2019. Similar regulations are coming into effect in Kenya to increase energy supply.[296]

Africa has historically been profiled as a high-risk investment region, but the perception of the level of risk is significantly higher than reality.[297] About 68 percent of PE respondents expect that PE investment commitments in Sub-Saharan Africa will grow by more than 20 percent over the next five years.[298] Investors are debating which countries, sectors, companies, and asset classes look most promising.[299] ESG considerations will factor into all of these decisions.

FUTURE PE INVESTMENT THEMES[300]	
N=52 PE investors; 13 answer options to question "investment in the following themes / sectors as an explicit asset allocation, exposure or investment focus"; SinCo analysis June 2011.	
Next 3 years	Next 10 years
Clean technology	Education
Alternative energy	Healthcare
Education	Alternative energy
Infrastructure development	Water
Healthcare	Clean technology

In the next three years, many PE funds are targeting clean technology, alternative energy, education infrastructure and healthcare.[301] In the next 10 years, PE investments are expected to flow into education, healthcare, alternative energy, water, and clean technology. Infrastructure will remain a key investment focus throughout the continent. Based on these observations, the deal pipeline for sustainable investment themed PE funds is promising. Also, in 2010, two agriculture-specific African PE funds completed multimillion dollar fundraising. But agriculture is a double-edged sword, given the highly politicized nature of food and land rights issues. PE funds need to establish *bona fides* in this sensitive area at the intersection of policy, society, community rights, and shrinking natural resources.[302]

Perhaps surprisingly, most PE firms do not consider South Africa's broad-based black economic empowerment policies to be a theme, but rather a business issue. This is partly because the empowerment "scorecards" required by the Department of Trade and Industry[303] have a legal and economic effect in procurement and business trading goods and services. This leaves open the question of whether PE funds consider ESG issues such as human rights or water scarcity as "non-business issues".

INVESTING IN AFRICA: PERSPECTIVES FROM INVESTMENT PRACTITIONERS			
Barriers preventing PE limited partners (asset owners, fund-of-fund managers) from starting to invest in Africa (% of respondents):		*Importance of these factors in choosing whether or not to invest in Sub-Saharan Africa today (% of PE respondents):*	
Lack of established general partners	60%	Attractive risk-adjusted returns	91%
Political risk	58%	Corporate governance/standards	80%
Weak exit environments	34%	Data on good performance	60%
Challenging regulatory / tax environment	29%	Political/economic risks	53%
Scale of opportunity to invest is too small	27%	Environmental or social risks	33%
Source: Emerging Markets Private Equity Association/Coller Capital 2010 survey[304]		Source: IFC-Sustainable Investment in South Africa, Nigeria and Kenya Report, 2011 analysis by SinCo from SinCo+RisCura survey 2010, n=47 PE general partners/limited partners[305]	

PE fund managers say there are plenty of possible deals in Sub-Saharan Africa; but potential deals are one thing, and actual deals another.[306] The barriers to executing these investment ideas may be the size of deals, the complexity of stakeholder relationships, and skill shortages. Investors interviewed expect an increase in PE investment for all target countries; but some distinguish between established investment destinations like South Africa with fewer risks and lower expected returns, versus countries such as Ghana or Rwanda, where investment managers expect higher returns for the higher risks undertaken.[307]

4.4

sustainable investment demand

INSTITUTIONAL INVESTORS

About 60 percent of ESG offerings in Sub-Saharan Africa are exclusively institutional, while 40 percent are marketed to fund wholesalers, funds-of-funds, and/or retail investors. The retail market for SI in South Africa is small, but there is a dedicated niche of retail clients. A June 2011 survey of principal officers showed that 51 percent of funds[308] today have investment policies that refer to integrating ESG, development, or similar considerations.

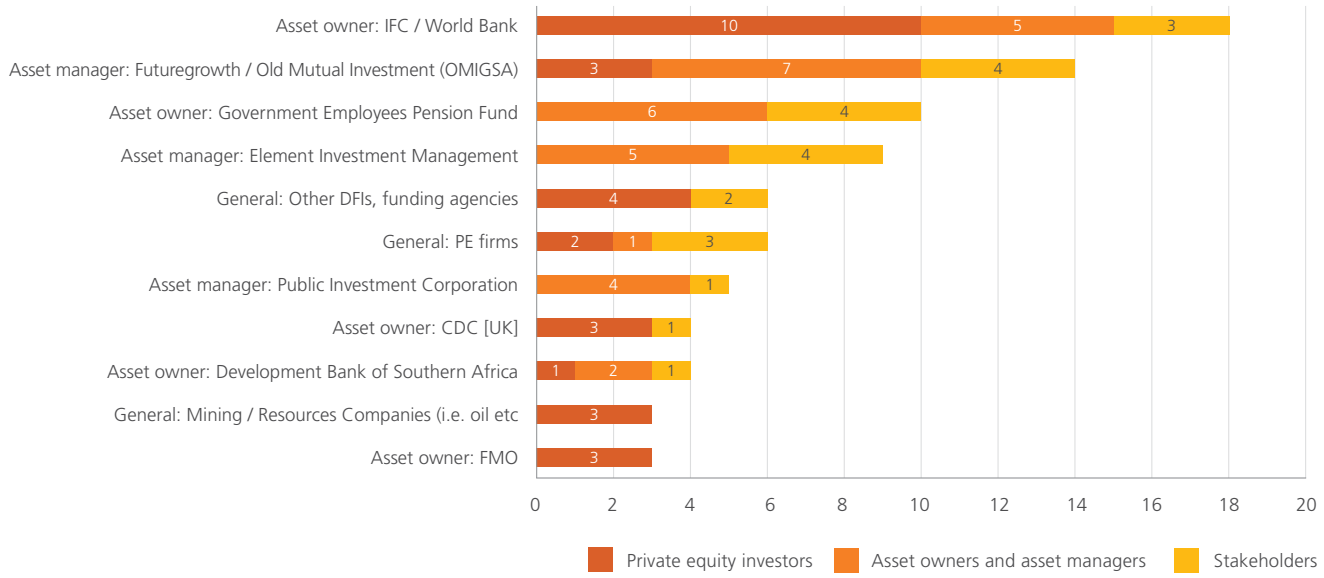
The eight largest multilateral DFIs have committed more than $12.5 billion globally to PE funds.[309] DFIs have exposed PE firms to ESG issues through screening approaches that imply that environmental, social, ethical, labor, health, safety, community, and governance filters are embedded in the investment process. National DFIs also play a role in this process.

> "It is fully consistent with the primary objective that trustees look at long-term growth of the fund they are responsible for, and not fall for short-term growth (which is unsustainable), and fall for herd-like behavior or the latest fashions and forget about the risks associated with such behavior."
>
> *Ismail Momoniat,*
> *Deputy Director-General, National Treasury*[310]

Where is leadership likely to come from? This study posed the question to investment practitioners, and the results are summarized in the chart below. The responses were varied, but the most-mentioned market leader was IFC/World Bank, while the asset manager most frequently named was Futuregrowth, which was a South African pioneer in the field in the 1990s.[311]

WHO ARE THE MARKET LEADERS IN SUSTAINABLE INVESTMENT/ESG IN AFRICA TODAY?

[open-ended + unprompted; most frequent answers; n= 28 PE investors + 25 asset owners and managers + 29 stakeholders]



Investment demand drives supply. The influence of a large asset owner is clear: investment managers who seek assets to manage are very sensitive to their clients. For example, the reaction by South African asset managers after the GEPF and the Public Investment Corporation issued ESG mandates in 2007 was a doubling of signatories from Africa to the Principles for Responsible Investment.

The GEPF is a top-10 global fund with about $131 billion AUM at the end of 2010,[312] 1.2 million active members and 320,000 pensioners. Its largest asset manager, the Public Investment Corporation, covers 92 percent of GEPF assets and also outsources asset management mandates, typically holding up to 15 percent of major listed companies on the JSE.

GEPF APPROACH TO SUSTAINABLE INVESTMENT	
Responsible Investment Policy	*Developmental Investment Policy*
This policy sets out the GEPF strategy for integrating ESG issues into investment decisions and ownership practices. It encourages "the companies we invest in to strike a balance between profits and being socially responsible, and to actively manage their environmental impact while maintaining high levels of corporate governance standards. The Isibaya Fund invests in black economic empowerment and infrastructure development projects that help to create jobs, relieve poverty and transform the economy."	*"The objective of this policy is to earn good returns for the GEPF members and pensioners while supporting positive, long-term economic, social, and environmental outcomes for South Africa. The policy rests on four pillars:* *Investment in key economic infrastructure for energy, commuter transport, water, broadband connectivity, liquid fuels, and logistics.* *Investment in social infrastructure in the form of affordable housing, education, and healthcare.* *Investment in a sustainable future in the form of renewable energy, energy efficiency, storage of energy, clean technology, environmentally friendly construction, recycling and green firms, buildings, and conservation.* *Investment in job creation, new enterprises, and broad-based black economic empowerment."*
Source: GEPF, 2011	

GEPF plans to integrate ESG factors in all asset classes, increasing transparency and accountability from its asset managers. The activity of GEPF and the Public Investment Corporation explains the large assets-weighted count of ESG-integrated activity in the region; many of South Africa's nearly 14,000 pension funds have not yet moved to explicitly integrate ESG factors. With the revised Regulation 28[313] in 2011, an increase in SI activity is forecasted.

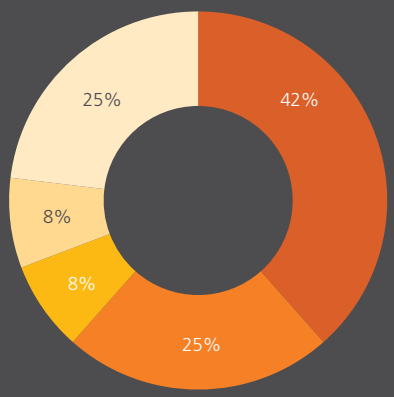
The revised rules for retirement fund investment place a new focus on the opportunity for SI in South Africa and Africa. The new Regulation 28 preamble[314] states: *"Prudent investing should give appropriate consideration to any factor which may materially affect the sustainable long-term performance of a fund's assets, including factors of an ESG character."* The new guidelines may be considered a global best practice: understanding and interpreting the fact that all factors influence the investment performance of portfolios, including ESG factors, and providing enabling regulations to the industry.

The figure below illustrates present demand for SI. It shows that the largest category (42 percent) of investors were asked specifically about ESG portfolios by fewer than 20 percent of fund members or investors.[315]

DEMAND EXPERIENCED FOR SUSTAINABLE INVESTMENT:
PERCENTAGE OF MEMBERS/CLIENTS REQUESTING ACCESS TO A PORTFOLIO EXPLICITLY INCLUDING ESG FACTORS (I.E. TO PURSUE RESPONSIBLE INVESTMENT?)

[6 options; n=12 asset owners]

	FREQUENCY
0 < 20%	42%
20 < 50%	25%
50 < 80%	8%
All	8%
None	25%



SUSTAINABLE INVESTMENT NETWORKS

Networks have been working throughout the continent to promote sustainable development; a representative list of networks is provided below. Some of these are global networks with an African connection, while others are based on the continent:

- The Southern African Venture Capital and Private Equity Association, the largest PE industry body in Africa with over 65 members, has begun to actively explore ESG issues for its members. The African Venture Capital Association is a smaller organization seeking to organize PE investors elsewhere on the continent.
- ASISA has a Responsible Investment Standing Committee, which has endorsed the Principles for Responsible Investment.
- The Global Reporting Initiative works to develop an international sustainability reporting framework, allowing investors to compare ESG performance in sectors and across regions.
- The Code for Responsible Investing South Africa integrates ESG factors for investors and launches in July 2011 in support of the King III code.
- The CDP acts on behalf of 534 institutional investors and large firms.
- The EITI sets global standards for transparency in the oil, gas, and mining industries.
- The International Corporate Governance Network works to raise governance standards.
- The Emerging Markets Disclosure Project works to improve disclosure in emerging markets.
- The Equator Principles are based on IFC's performance standards on social and environmental sustainability, and related World Bank guidelines.
- The Africa Sustainable Investment Forum promotes SI on the continent from africasif.org.
- The Global Impact Investing Network focuses on improving reporting on the impact of funding/financing/lending to low-income groups. A related but separate South Africa Impact Investing Network promotes social entrepreneurship and high-social impact entrepreneurs.
- Principles for Responsible Investment is an investor initiative in partnership with the UN Environment Program Finance Initiative and the UN Global Compact.

> "[There is] growing awareness among South African companies of the risks and opportunities of climate change, although much of this remains at a general level."
>
> *Carbon Disclosure Project 2009, South Africa JSE 100*[316]

4.5

sustainable investment supply

Buyers of SI portfolios express a range of opinions on the state of supply. There is clearly appetite for SI, and numerous new product ideas were floated during the period of this study. Improved demand should generate momentum for ESG data services, increased coverage by analysts, and corporate reporting. In the course of this study, several practitioners emphasized that of the three ESG factors, governance would make the most difference in bolstering supply.

The table below provides a composite of PE and general asset management ESG-branded investment products available today.

ESG-BRANDED INVESTMENT PRODUCTS IN SUB-SAHARAN AFRICA 2010 *SinCo Analysis January 2011, based on composite sources*[317]			
Fund name	**Type**	**Classification**	**Size $ million**[318]
TOTAL			**5,751**
Supply of PE fund/alternatives ESG-branded products			
Pan-Africa [sample]			**1,521**
Isibaya Fund	Institutional	Alternative/PE	746
Agri-Vie Fund	Institutional	Alternative/PE	300
Metropolitan African Wealth Creator	Institutional	Alternative/PE	165
Africinvest II Small, Medium, and Micro Enterprise Fund	Institutional	Alternative/PE	107
Evolution One Fund	Institutional	Alternative/PE	94
Global Environment Fund Africa Sustainable Forestry Fund	Institutional	Alternative/PE	84
African Agricultural Capital	Institutional	Alternative/PE	25
African Agriculture Fund	Institutional	Alternative/PE	N/A
Socially Responsible Affordable Housing Fund	Institutional	Alternative/PE	N/A
Supply of asset management ESG-branded products			
TOTAL [sample]			**4,230**
South Africa			**4,225**
Housing Impact Fund	Institutional	Pooled	613
Oasis Crescent Equity Fund	Retail	Unit Trust	588
Futuregrowth Infrastructure and Development Bond Fund	Institutional	Pooled	520
Futuregrowth Community Property Fund	Institutional	Pooled	440
Old Mutual Investment Group South Africa Alternative Investments IDEAS Fund	Institutional	Pooled	320
Community Growth Equity Fund	Retail	Unit Trust	320
27Four Black Economic Empowerment Incubator Fund	Institutional	Pooled	267
Investment Solutions Sharia Fund	Institutional	Pooled	150
Community Growth Gilt Fund	Retail	Unit Trust	147
Futuregrowth / Old Mutual Albaraka Equity Fund	Retail	Unit Trust	113
South Africa Infrastructure Fund	Institutional	Pooled	96
Cadiz Infrastructure Bond Fund	Institutional	Segregated	78
Element Earth Equity	Retail	Unit Trust	74
Futuregrowth Infrastructure and Development Equity	Institutional	Pooled	70
Oasis Crescent International Feeder Fund	Retail	Unit Trust	57
SRI Real Estate Fund	Institutional	Pooled	47
Investec IAL RI Equity Fund	Institutional	Pooled	46
Cadiz SRI Bond Fund	Institutional	Segregated	40
Sanlam Infrastructure Fund	Institutional	Pooled	38
Stanlib Sharia Equity	Retail	Unit Trust	33
Element Islamic Equity	Retail	Unit Trust	23
Sanlam (SIM) SRI Bond Fund	Institutional	Pooled	23
Cadiz Money Market Fund	Institutional	Pooled	17
Stanlib Wealth Development Fund	Institutional	Pooled	15
Investment Solutions Sakhiswe Fund	Institutional	Pooled	12
Investec Jadwa Africa Equity Freestyle Fund	Institutional	Pooled	11
Kagiso Islamic Equity	Retail	Unit Trust	9
27Four Sharia Fund	Institutional	Pooled	8
Sanlam SRI Equity Fund	Institutional	Pooled	8
Investec IAL TDI Balanced Fund	Institutional	Pooled	7
Mergence Balanced SRI Fund	Institutional	Pooled	7
Futuregrowth SRI Equity	Institutional	Pooled	6
Old Mutual Investment Group South Africa Quants SRI Fund	Institutional	Pooled	6
Momentum/Advantage Supernation Fund	Institutional	Pooled	5
Sasfin TwentyTen Fund	Institutional	Pooled	4
Community Growth Fund of Funds	Institutional	Pooled	4
Old Mutual Community Growth Money Market Fund	Institutional	Pooled	2
Futuregrowth SRI Balanced	Institutional	Pooled	1
Advantage Sharia Fund	Institutional	Pooled	1
Nigeria*			
Zenith Ethical Fund	Retail	Unit Trust	N/A
Coral Ethical Fund (Dissolved June 16, 2010)	Retail	Unit Trust	Withheld
Stanbic IBTC Ethical Fund	Retail	Unit Trust	N/A
Lotus Capital Halal Investment Fund	Retail	Unit Trust	N/A
Kenya			
First Ethical Opportunities Sharia Fund	Retail	Unit Trust	N/A
Mauritius			**5**
Sustainable Capital Africa Sustainability Fund	Institutional	Pooled	5

Source: Sinco analysis from composite resources and fund administrator data.

CORPORATE ESG TRANSPARENCY

A key element to the supply side of SI is relevant ESG data. Research coverage is slowly expanding in response to demand from strategic buyers and institutional investors. ESG coverage of local companies by sustainability research specialists is thin largely because of the scarcity of data. In recent years, however, there has been a notable increase in ESG reporting, and this trend seems set to continue.

Part-time or additional ESG analysis is often supplemented by a few dedicated external consultants. Transparency by companies is driven by stakeholders. Companies with the greatest ESG awareness and reporting are typically local blue chips. Higher levels of disclosure are shown by multinational businesses with diversified (often international) shareholder bases and/or dual-listings. According to PE investors, companies with the greatest ESG awareness are in the mining, oil and gas, banking, utilities, and pharmaceuticals sectors. This is driven by stakeholder reporting requirements.

In "high-impact, high visibility" industries, the business case of failing to address sustainability risks is clear. ESG awareness differs from company to company. For example, only certain companies engage with their investors on ESG matters. Civil engineering firm Murray & Roberts reported on mine deaths and safety at its 2010 annual investment analyst briefing. South Africa's Sasol also has a high standard of reporting, partly because it is one of the world's most carbon-intensive emissions companies (in Sub-Saharan Africa, South Africa has the highest carbon emissions).[319] In February 2011, directors of a mining company were criminally prosecuted for the first time under environmental pollution laws in South Africa.[320]

In the 2010 CDP report in South Africa[321] (the only African country covered) rating the JSE 100, Gold Fields and FirstRand qualified as the joint overall leaders, followed in joint second place by Anglo Platinum and Medi-Clinic Corporation. Of the 15 South African companies that form part of the Global 500 largest companies, only one (Anglo Platinum) made it into the Global 500 Carbon Disclosure Leadership Index.

> "Extractive industries are the most important – ESG awareness is a have to, not a want to."
>
> *Chris Derksen, Investec PE*

ESG AWARENESS

ESG awareness levels mirror corporate transparency trends: the most aware sectors tend to be those with large social or environmental impacts, which face greater public and media attention, and hence the burden to report and be accountable. Frameworks continue to challenge best practices (although the multiplicity of frameworks may be a challenge); for example, the new ISO 26000 framework has been released too recently to assess its impact on companies for analysis in this report.

WHICH SECTORS ARE MORE "ESG AWARE" (TOP 5) IN THE OPINION OF INVESTORS/STAKEHOLDERS		
Private equity	**Investors**	**Stakeholders**
Mining	Mining	Oil and gas producers
Oil and gas producers	Oil and gas producers	Banking and financial services
Banking and financial services	Banking and financial services	Mining
Gas, water, and multi-utilities	Gas, water, and multi-utilities	Electricity
Chemicals	Pharmaceuticals/healthcare	Pharmaceuticals/healthcare

The ESG research industry is still in development. The Global Reporting Initiative[322] plays an important role in encouraging investment managers to reference sustainability indicators in integrated reports. The International Integrated Reporting Committee is working to develop a globally accepted framework for accounting for sustainability factors.[323] The Integrated Reporting Committee of South Africa was formed to develop standards in response to the new JSE requirement that listed companies comply with the King III corporate governance report.

"To make our economy sustainable we have to re-learn everything we have learnt from the past. That means making more from less and ensuring that governance, strategy, and sustainability are inseparable… Integrated reporting builds on the practice of financial reporting, and ESG reporting, and equips companies to strategically manage their operations, brand, and reputation to stakeholders and be better prepared to manage any risk that may compromise the long-term sustainability of the business."[324]

Professor Mervyn King,
Chairman of the King III Commission and Global Reporting Initiative

DUAL-LISTED COMPANIES

Investor perceptions confirm that there is more ESG reporting from dual-listed companies. Companies with major business units and global investor exposure (especially dual-listed firms like SABMiller, Anglo American, Safaricom, Orascom Telecom, Goldfields, and Old Mutual) may demonstrate world-class sustainability reporting, although variations exist in the reporting quality and frameworks adopted according to primary listings and corporate culture.

RESEARCH COVERAGE OF ESG TOPICS

ESG data, research, and coverage is limited. Investors must rely on a mix of the coverage from specialist consultants, equity analysts, research firms, ratings agencies, and in-house teams of major investment houses. General country- or issue-level benchmarking exercises are useful tools, but investors often need more detailed and company-specific coverage.

New developments in company ESG coverage are being driven by the demand from PE funds, asset managers, and institutional investors such as pension funds. Corporate governance has been covered in South Africa by the major investment firms for some years. Beyond South Africa, such coverage is mostly absent, although the opportunity exists to engage local analysts who will support further African development of SI. Open media access and freedom of information are critical inputs to this process.

"The coverage of ESG topics by company analysts is minimal. There is a lot of good research and reading material by 'experts' in the ESG field, but I have seen very little by analysts and it is not something they focus on when reporting on companies."

Kate Rees, Brait

INVESTMENT ANALYSIS

Research and skills need to be developed. There is a small investment analyst base in South Africa that is now covering other areas in Africa.[325] Investment research on the continent will improve as demand increases. It is likely that leading analysis firms will close the ESG information gap, especially in South Africa, in the years ahead. Offering incentives for improved ESG coverage (for example through rewarding the best ESG houses with increased revenues and/or prize incentives) will encourage firms to provide quality, long-term research that considers material ESG issues beyond the ad-hoc coverage of, for example, climate change legislation or the impact of carbon taxes on the mining industry. ESG skills are typically outsourced through sell-side analysis, although investment manager UBS did rollout a local version of their ESG framework.[326]

"[UBS] view[s] access to increasingly constrained resources (such as energy, water, agricultural produce, minerals, and human capital) as fundamental to the ability of countries to develop in economic terms, and to the ability of companies to compete successfully in their sector. South Africa is particularly relevant to this theme, not only because a number of global companies depend on access to South African resources, but also because of resource-related issues that may potentially constrain growth or profitability for South African companies."

Julie Hudson, UBS [327]

Increased ESG research will depend on the creation of credible market incentives, encouraging research agencies to adopt updated, innovative approaches. Currently no research provider offers the ESG coverage and content that will be expected in the coming years in South Africa, Nigeria, and Kenya. First movers may have a significant advantage.

ROLE OF NGOs

International and national NGOs play an important role in galvanizing awareness of SI issues, and often provide vital services where public services are lacking. NGOs are able to integrate marginalized groups, act as watchdogs to keep governments, companies, and investors accountable, and raise public awareness of socioeconomic issues. Recently, for example, the Centre for Environmental Rights, Endangered Wildlife Trust, and the Environmental Monitoring Group have lobbied the JSE SRI index based on their rankings of eight firms with a record of environmental transgressions; the NGOs argue that these firms do not belong on an index rating ESG performance.[328]

Without the persistent and issue-specific advocacy of not-for-profit organizations, many issues and activities by the private and public sector would not receive the scrutiny they deserve, nor would investors be sensitized to the business impact that ESG issues may generate. Further research would help identify and support NGOs that provide a useful function of holding a mirror to business and investors.

4.6 drivers of sustainable investment

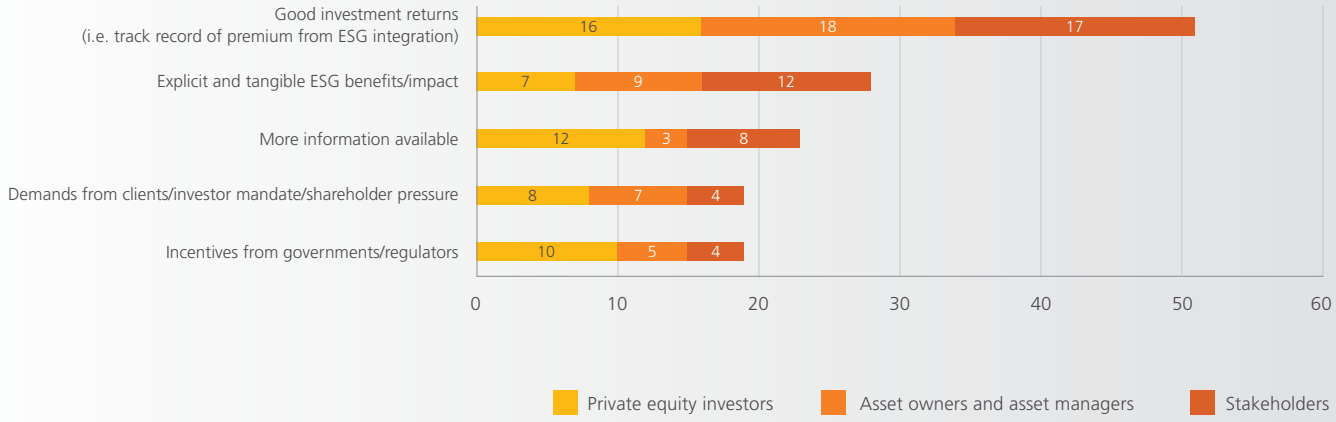
Using a broad definition of SI, Sub-Saharan Africa ranks highly by global comparison. The relatively high proportion of ESG-integrated investment is the result of the weight of the GEPF, the largest asset owner in the African market and the world's sixth-largest pension fund, which has allocated 5 percent of its assets (about $7 billion) to ESG investments. The Fund is a world leader in this respect. To grow SI, much more needs to be done to encourage investors to take up the challenge, broadening the base beyond the largest institutional investors.

SI drivers include institutional investor demand from select asset owners and DFIs, appetite from specialist practitioners, and legislative and regulatory drivers covering investment and/or business sectors. These drivers reflect many of the same dynamics found in other emerging markets as well as developed countries. This study confirms the existence of an "investment-as-usual" mindset in Nigeria, Kenya, and South Africa, with primary concerns focused on loss of performance and a perceived reduced investment opportunity. Previous studies have found similar attitudes among investors across emerging markets.[329]

Drivers for SI in South Africa, Nigeria, and Kenya reflect the tension between the investment case and the demands for more ESG information. In a capital-scarce context, the level of investment returns is critical to investment practitioners' ability to attract assets and retain their clients. Areas of investment practice where ESG factors may improve performance include the speed and size of asset-gathering opportunities, the longevity and health of relationships with asset owners, the understanding of the investee company's risks and opportunities, the assessment of the quality of management and business acumen, and the accurate assessment of how the investee company relates to its stakeholders. The chart below captures perceptions of key drivers of SI over the next 5 to 10 years.[330]

WHAT IS THE ONE THING TO MAKE SI/ESG INTEGRATION ATTRACTIVE TO YOU IN KENYA, NIGERIA AND/OR SOUTH AFRICA IN THE NEXT 5-10 YEARS?

[open-ended; n= 46 PE investors + 41 asset owners and managers + 45 stakeholders]



CLIENT MANDATES

As in other emerging markets, client-driven mandates to integrate ESG factors in investment are among the primary drivers:[331]

- Demand from local institutional investors, such as insurance companies, pension funds (apart from the notable exception of the GEPF), and asset managers, has been limited, but is increasing. For example, in South Africa the Actuarial Society, the Principal Officers Association, and the Pension Lawyers Association have addressed the issue with their membership, as has the Retirement Benefit Authority in Kenya.
- DFIs have been anchor investors in many Africa funds, and are important to PE firms and the funds they build. With a dual mandate to make good investment decisions while meeting ESG performance standards, DFIs have a mutual interest in raising the understanding and market for SI. DFIs have tried to connect their investment efforts through six-monthly meetings of investment and advisory teams, but harmonizing DFI-led ESG integration has not yet been tackled directly.

Investors interviewed expect demand to increase. Institutional investors express the preference to better understand the developmental impact of their portfolio, but few would attach social criteria to their investments without better empirical evidence of how these affect financial performance.[332] More investor clients are keen to explore multiple investment outcomes, including those with specific rural, job creation, and/or women-empowerment themes.

> "Financial institutions are a critical channel through which price signals, quality of entrepreneurship, and regulation can direct financial capital to more or less sustainable economic activity."
>
> *Adair Turner, Merrill Lynch*[333]

REGULATORY FACTORS

Investors prefer clear rules and certainty to ambiguity. A common refrain among SI investors is the need to regulate investment and company activities that have a negative impact on society and the environment. In the context of financial media asking tougher questions, and investment clients becoming more alert to exposure to risks, investment analysis is becoming more comprehensive. More international investors are now prone to asking how a company has interpreted existing laws and regulations in doing business.

While there are undoubtedly many regulatory failures or weaknesses, such failures may provide a catalyst for increased ESG investment that contributes to improvements over time. For example, in Nigeria, legislation has not been able to prevent serious environmental damage in the Niger delta, which led in part to the formation of the EITI[334] in 2002. In 2010, rising levels of acid water from old mines[335] began to threaten the watershed around Johannesburg, South Africa,[336] forcing the government to act. Corruption is still an unhappy and significant reality of ordinary business in many Sub-Saharan African countries.

Differing levels of ESG regulation and their enforcement generate an opportunity for the private sector to create products and services to fill this regulatory gap. With ESG-integrated processes, PE funds with DFI-funded assets may benefit because they will have flagged the issues earlier on. In markets with weaker regulation and enforcement, PE investors adhering to stronger ESG standards than the local norm may have a positive impact.[337]

Given their common commercial and fiduciary history, there may be a case for coordinating regulation and enforcement of company and investor activity across South Africa, Nigeria, and Kenya, which would support a common approach to fostering SI. As the pension industry grows in Nigeria (the new pension system may attract up to $2 billion a year in new retirement funding flows from 2012), Kenya, Ghana, Tanzania, and other countries, the prospects for better regulations, and rules for investment integrating ESG, present a positive opportunity.

At a national level, there have been various calls for the use of private capital in compulsory investments. Such calls can be expected to continue. In South Africa, some politicians have sought the use of "prescribed asset" allocations to define "development securities" aimed at increasing private sector capital investment in basic infrastructure,[338] but the debate over the roles of public and private sector finance, and the compulsory role of institutional investors, has yet to be clarified.[339] Some stakeholders, however, believe that there are inherent dangers in the use of prescription. They argue that this could limit investment opportunities, and result in too many assets chasing too few deals. A positive enabling environment will present the most compelling major "pull factor" to investors. Good deals always attract enough capital.

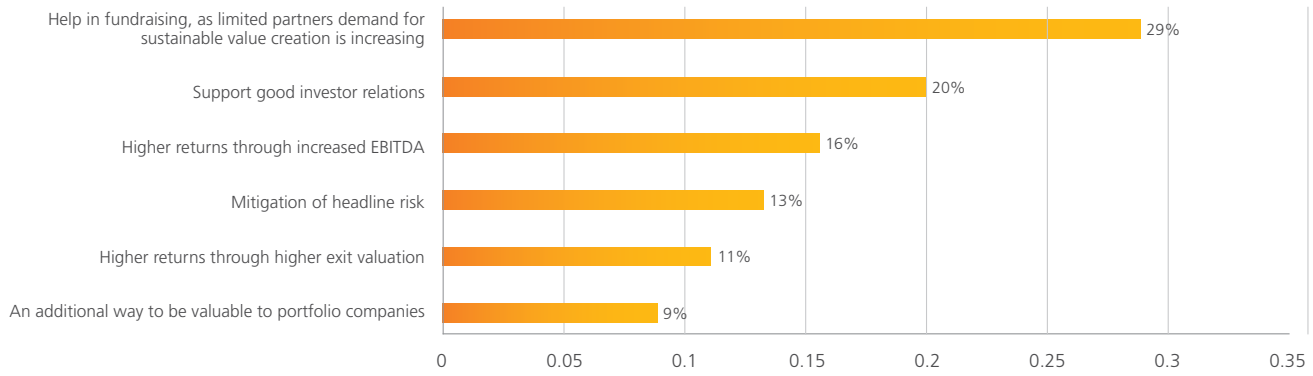
The investment management industry's license to operate reflects the need to deploy capital to help grow the economy. South Africa's pensions industry body, the Principal Officers Association, headlined its 2011 winter conference with a panel on SI in Africa. During 2011, a number of pensions industry regulators opened the door to expanding the PE asset class. For example, Namibia is to increase the allocation limit from 2.5 percent to 5 percent. The Nigerian regulator increased the ceiling for PE allocation to 5 percent.[340] The Retirement Benefit Authority in Kenya allows a 10 percent allocation.[341]

PRIVATE EQUITY

While few PE funds make explicit use of the SI label, many are seeking investment opportunities in sustainability themes – the top three being healthcare, infrastructure, and housing. Most PE investors (91 percent) expected an increased demand over the next three years from investor clients for asset management in the SI/ESG themes. But it appears that investor clients and risk issues will continue to have the greatest impact on PE firms. The main motivating factors for PE funds are shown in the figure below.[342]

MOTIVATIONS FOR PE GENERAL PARTNERS (PEGPs) INTEGRATING ESG FACTORS IN SUB-SAHARAN AFRICA TODAY

[7 answer options + "other" option; n=45 PE investors; January 2010-May 2011; SinCo analysis]



OTHER DRIVERS

Other potential drivers of SI identified by participants in this study are as follows:

- High-impact, high-disclosure companies. By presenting their case to all stakeholders, including investors, these large companies ensure that ESG issues are raised, and that investors may make decisions based on the ESG rating of companies.
- SI indexes, such as the JSE SRI index, help to channel SI, crystallize country-specific issues, and improve reporting. In December 2010, the JSE announced a joint project with GEPF to integrate ESG data into the JSE SRI index universe.
- Strategic buyers. With limited opportunities for initial public offerings in thinly-traded, mostly illiquid African stock exchanges, the most common exits for PE funds selling their portfolio companies is via the "trade sale" where strategic buyers purchase the company. This area deserves more research.

SI PROMOTERS

As noted earlier, DFIs will continue to play a decisive role in making the investment case for SI. Some observers suggest that an investment from a DFI creates a multiplier effect: for every dollar invested by a DFI, another five dollars of co-investment is created.[343] From the overseas aid perspective, PE, as a component of FDI, can help deliver the much-needed risk capital, skills, and support required to help grow sustainable businesses in developing countries.[344]

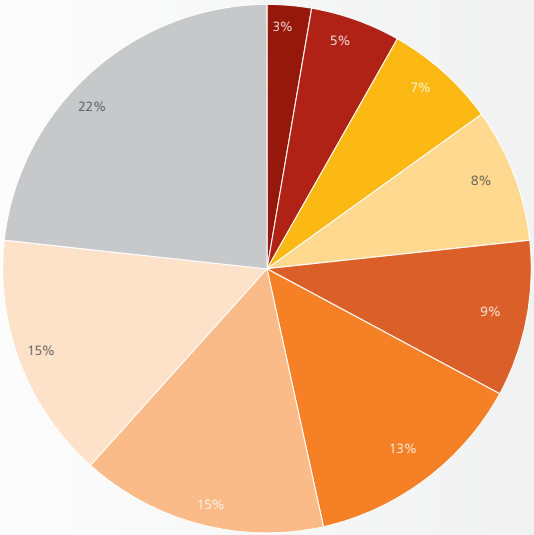
With frontier investors such as the CDC Group (the DFI owned by the United Kingdom's Department for International Development), the entrepreneurial development bank of the Netherlands, FMO (Nederlandse Financierings-Maatschappij voor Ontwikkelingslanden[345]), and IFC, the Sub-Saharan Africa PE asset class has become more accessible and has made some substantial investment returns.[346] For long-term SI growth, this needs to be complemented by local research and skills.

It is never easy to build SI, as previous IFC studies on Brazil, India, and China have demonstrated.[347] Africa's challenges in this regard are substantial. DFIs will remain a key asset base for SI. DFIs as first capital into funds provide a pilot study for international investors interested in investing but uncertain of the risks and rewards in the region.

Most investment practitioners interviewed expect that a group of market participants will drive higher levels of SI, led by international organizations (including DFIs), finance and investment regulators, asset owners, and asset consultants. Networks and associations will play an important role in this process.

TOP PERCEIVED PROMOTERS OF SUSTAINABLE INVESTMENT AND GREATER ESG AWARENESS IN SUB-SAHARAN AFRICA IN THE NEXT 5 YEARS

[highest ranked of 14 answer options; n=76 investors; January 2010-May 2011, SinCo analysis]



International professional bodies (e.g. CFA Institute)	3%
Business/investment media	5%
Accounting or auditing standards bodies	7%
Stock exchanges	8%
Environmental regulatory authorities	9%
Asset consultants	13%
Finance and investment regulatory authorities	15%
Asset owners [e.g. pension fund trustees]	15%
International organizations (World Bank, UN, OECD)	22%

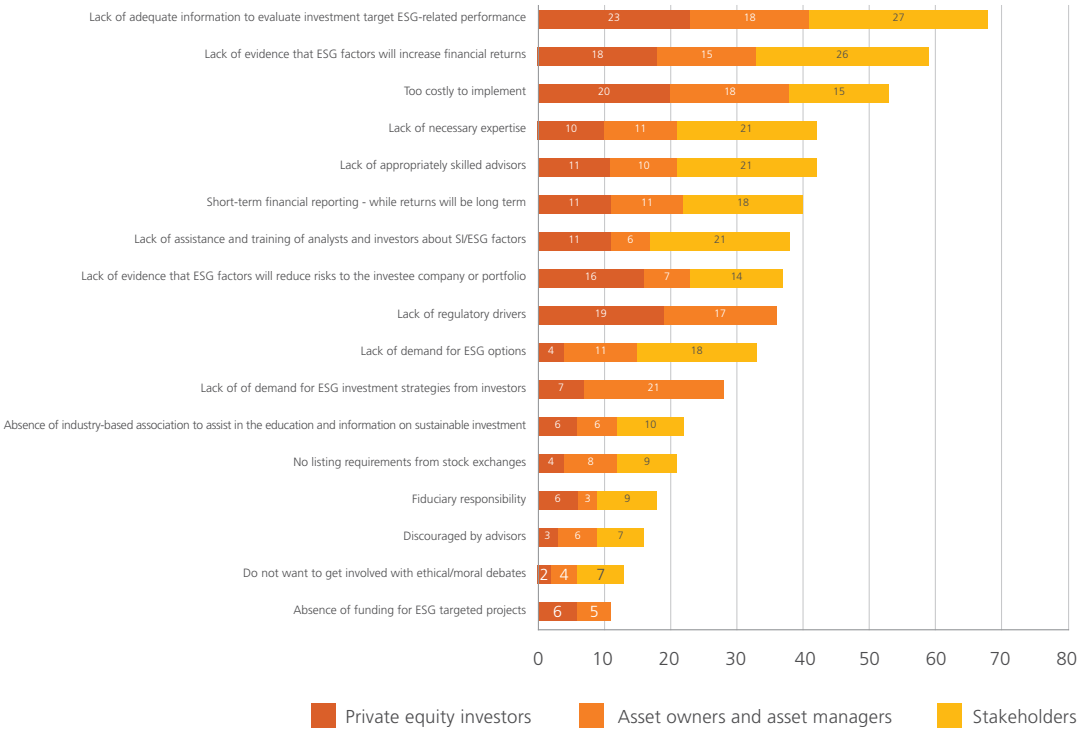
4.7

barriers to sustainable investment

Barriers to SI in Sub-Saharan Africa are similar to those in other regions. They include knowledge gaps, dominant investment practices that are hard to change ("investment-as-usual"), poorly applied regulations at country, company, and/or investor levels, and the incorrect perception of SI as only "ethical" investment and/or negative screening in the investment process. The chart below[348] shows the ranking of perceived barriers to SI in the region over the next three to five years. The fiduciary responsibility argument, often cited to explain why more asset management decisions are not explicitly integrating ESG factors, did not rank in the top 10.

WHAT DO YOU SEE AS IMPORTANT BARRIERS TO ESG IN INVESTMENT IN SUB-SAHARAN AFRICA IN THE NEXT 3-5 YEARS?

[Ranking of 17 options; n=45 PE investors + 43 asset owners/asset managers + 49 stakeholders; January 2010 - May 2011]



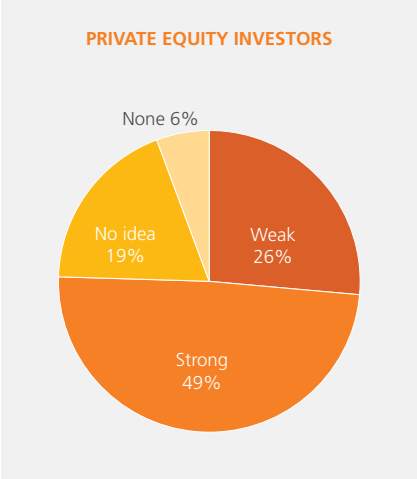
PE and general asset management face similar barriers, but there is an important difference: most PE investors point to gaps in ESG information, while most general asset managers identify lack of direction in the market and/or lack of demand.

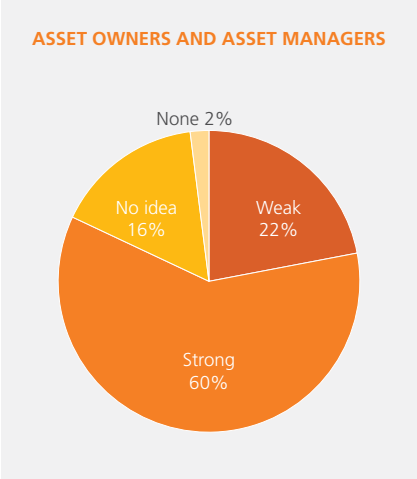
> "The violence in Tunisia and Côte d'Ivoire will send a lot of the new portfolio money straight back out of the region, even though the trouble is confined. Non-specialist money dislikes event risk and Africa offers that in abundance."[349]
>
> *Keith Mullin, Reuters*

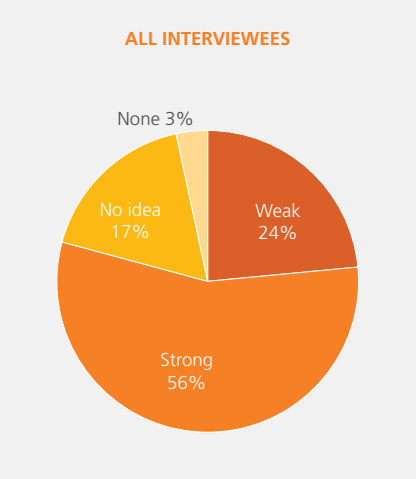
Eighty percent of respondents make the link between ESG and investment performance, and 20 percent either see no link at all or an unknown link (see charts below). The self-selection bias accounts for some of this positive result, but the overall tone reflects the reactions from the broad spectrum of interviewees: the case is intuitively possible, but often unclear.

LINKING ESG FACTORS WITH SUSTAINABLE INVESTMENT PERFORMANCE

"From experience, how strong is the link between actions on ESG issues and long-term 10-year risk-adjusted return performance?"
[4 answer options; n=51 PE investors + 46 asset owners and managers + 53 stakeholders; January 2010-April 2011]







Each link in the investment value chain has a role to play in making SI happen. In general, most respondents, especially the PE group, have much longer histories in investment management than in sustainability issues, which links to the barriers of expertise and training: it is unlikely they were trained in integrating ESG factors at undergraduate, graduate, or industry levels.

Barriers identified by investors reflect both investment supply (availability of investment targets – companies, projects, funds) and demand (investors and asset owners). The approaches of investors (asset managers and asset owners) and the PE group point to a close overlap on what the major barriers will be in the next five years.

> "Understanding ESG issues and the investment case for these is quite possibly one of the biggest gaps in the pan-African market today."
>
> *Malcolm Gray, Investec*

5.

recommendations

This study presents five recommendations to increase SI in Sub-Saharan Africa through 2020:

- **Use the language of investors:** The SI message should be presented in the language of investors, and should be driven by the asset owners and investment practitioners, appealing to advisors and asset managers open to exploring advances in investment practice.
- **Streamline reporting:** Reduce information-gathering and execution costs by streamlining the ESG reporting approaches of major investors (especially DFIs), and increasing comparability of ESG impacts through common reporting frameworks.
- **Leverage local knowledge:** Integrate local and regional SI insights into new global best practices.
- **Make the investment case:** Make the case that SI has the potential to generate increased returns and/or reduced risks across all asset classes.
- **Keep score:** Performance metrics and analysis are essential. Investors need mechanisms and infrastructure to measure investment performance and ESG impact.

To generate support for these recommendations, and to develop the momentum for longer-term SI market growth, these recommendations should be implemented over the next three years and reviewed at the end of the decade.

	RECOMMENDATIONS				
How the five recommendations for action in next three years will tackle barriers and promote drivers for sustainable investment through 2020	Use language of investors	Streamline SI/ ESG reporting	Leverage local knowledge	Make the SI/ESG investment case	Keep score
Negative barriers addressed					
Absence of demand	✔				✔
Challenges in scaling up reporting activities		✔		✔	✔
ESG reporting high time, money, and implementation costs		✔		✔	✔
Lack of adequate information	✔	✔	✔	✔	✔
Lack of evidence of returns and/or risk-reduction from ESG integration	✔		✔	✔	✔
Lack of expertise	✔		✔	✔	
Lack of government legislation/ enforcement regulations	✔	✔		✔	✔
Positive drivers leveraged					
Demand from clients, investors' mandates, shareholder pressure	✔	✔	✔	✔	✔
Explicit and tangible ESG impact / benefits		✔		✔	✔
Good investment returns (track record of ESG premium)	✔		✔	✔	✔
Incentives from governments / regulators		✔	✔	✔	
More information available	✔	✔	✔	✔	✔
Proven risk reduction	✔			✔	✔
Legend ✔	*Will have impact and/or has direct/indirect link to intended outcome/s*				

5.1

use the language of investors

The investment case for sustainability needs to be articulated in a language that is relevant to ordinary investment practitioners. PE and general asset managers – whether they are based in Lagos, Nairobi, Johannesburg, London, Paris, Hong Kong, Dubai, or New York – all speak a common investment language. The language of sustainability may be lost in translation. The specialized ESG/SI terminology can be confusing, foreign, or unclear. This first recommendation is to make the SI case, and to make it in plain investment language. This will help investors to lead by example.

WAY FORWARD

Institutional investors will play an important role of developing a clear, consistent message that makes sense as investors seek long–term, positive, risk-adjusted SI performance. The SI message will increase awareness of the risks and opportunities among investors, legislators, regulators, civic society, and the media. A consolidated messaging strategy will also press for developing updated investment industry frameworks that consider all aspects of investments, especially in the PE asset class.

5.2

streamline reporting

Streamlining reporting on ESG factors will promote SI. The business of investment seeks to reduce back-office costs, which are a drag on net investment returns performance. The costs may take the form of time, money, data, and/or implementation. A coordinated effort to streamline the ESG reporting requirements would generate systemic change. The opportunity exists to update and adapt existing ESG frameworks, working from DFI models already in use and accepted as best practice, to increase the volume of comparable reporting while reducing the overall reporting burden.

Streamlining will reduce reporting and screening costs for medium-sized and smaller PE firms, and reinforce other recommendations in this report (make the SI case and keep score). PE firms already "streamline" behind the work of major DFIs in general and on ESG in particular, leading in a short space of time to new benchmarks being more broadly adopted.

The value of the ESG frameworks is recognized by funds-of-funds and new fund entrants into Africa, which use the ESG approaches of DFIs, especially IFC, as a proxy for good ESG analysis. A more focused, active, and Africa-centric approach is needed to ESG investment reporting frameworks.

"There is a complexity of multiple frameworks. Some investors do not want to invest in something that is highly ESG oriented. There is a dissonance between investors, a conflict of demands. We are wanting to start a sustainable investment fund, but the reactions [are] mixed, some investors said it would be a strain on resources."

Anthony Hewat, Metier

HIGH REPORTING COSTS

The complexity, volume, and special requirements of ESG reporting are disincentives to SI. IFC has begun to address this challenge by building an online, web-based environmental and social screening tool rolled out in 2009/10.[350] Reporting to investors on ESG factors may be a significant cost, at least in the initial stages. One major European firm reported spending $150,000 per year on staff to complete investor ESG questionnaires. Companies reporting to investors, initiatives, and indexes are rationalizing their efforts, choosing which questionnaires to answer and which telephone calls to return.

BENEFITS OF STREAMLINED REPORTING

An industry-wide approach is recommended to streamline the range of ESG frameworks, first by focusing on a single asset class (PE) in Sub-Saharan Africa. The benefits of such a process include:

- Lower reporting and due diligence costs.
- Incentives to share knowledge.
- Increased scaling opportunities.
- Greater ESG integration in investment practice.
- Improved trust from investors.
- Better transparency across DFIs and intermediary institutions.
- Enhanced opportunities to transfer framework from PE into listed equity.

WAY FORWARD

The recommendation is to work with a pilot program of the major DFI-affiliated LPs to seek out ways to streamline their ESG approaches and/or reporting, encouraging fund managers to adapt their investment processes, perhaps using some DFI advisory capabilities for technical advice/support, and helping the DFIs execute on their capacity-building mission in frontier markets. This type of collaboration will send a strong positive signal to the market, help to consolidate lessons learned, and chart a way forward.

A positive example of the DFI-led approach to ESG can be seen in a modest real estate project announced by the World Bank[351] in April 2010, when IFC signed its first deal to finance Chinese investment in Africa. IFC expects this move to help discourage violations of human rights and environmental standards. The project is to help finance a commercial complex in Dar es Salaam, Tanzania. The IFC capital commitment is less than 30 percent of the total funds for the project, but observers believe "it is the reputation of IFC and its corporate governance, environmental, and human rights standards that will encourage other parties to invest".[352]

To encourage the structured collaboration that is necessary to bring about more streamlined reporting, this report recommends that a working group of DFI-led LPs work with major African GPs to develop a common, easy-to implement, and low-cost ESG investment reporting framework – a simplified version of one already in use. The IFC's Environmental and Social framework is already widely in use and could serve as a starting point.

The process of adapting ESG guidelines can be expedited by using examples from reviews conducted recently by IFC[353] as part of its Sustainability Framework standards review.[354] This new Africa-centric framework for ESG reporting in PE may aim to have an 80 percent core of common reporting requirements, while allowing for 20 percent unique or investor-specific reporting. In addition, the existing collaboration of DFIs could be referenced and built upon, using the semi-annual meetings of DFI LPs to collaborate on a streamlined framework and matrix dashboard project in 2012.

5.3

leverage local knowledge

To promote greater awareness and education of investors, the SI community needs to increase the investment skills base on the continent, to make greater use of local knowledge of concepts and execution, and to share this knowledge throughout the region. There is an existing body of practice in SI in Africa (developed mostly out of South Africa) dating back to the early 1990s.

By incorporating this knowledge, new approaches may be developed that blend IFC and other DFI best global practice in ESG integration with local realities. The leadership of African institutional investors will add a new and material diversity to the thinking and reality of how SI is practiced in emerging and developed markets.

SHARE KNOWLEDGE

Those interviewed for this study identified lack of expertise as a major obstacle to incorporating ESG factors in their investment processes. And while the SI knowledge base is growing around the world, experience in Africa can play a major role in increasing understanding of the challenges of implementing SI in frontier markets.

Building, nurturing, and maintaining a cohort of local experts is a major objective that will generate systemic improvements. Ensuring that knowledge is developed from an African perspective – and not just transplanted from other regions or investment paradigms – is essential given Africa's history. Given huge social and economic development needs, companies in the region are already demonstrating local forms of corporate citizenship[355] that investment analysts have yet to evaluate and appreciate.

Many experimental and cutting-edge social, financial, and policy innovations are being tested, including in the context of impact investing and social return on investment metrics. The SI knowledge base in Africa and globally will benefit from sharing this knowledge.

DEVELOP RELIABLE LOCAL DATA, TRAINING, AND NETWORKS

An increase in ESG expertise will raise the level of available information in opaque markets. At present, there is a small investment analyst base in South Africa, Kenya, and Nigeria, supported by a handful of SI practitioners (mostly in South Africa). Research coverage is slowly expanding in the rest of the region. When it comes to ESG coverage of local companies, research is thin. By generating a demand for better ESG-integrated company research, the platform of shared learning will help improve access to better data and analysis.

DEVELOP ESG CONTENT AND DISTRIBUTION STRATEGIES

Using existing networks and organizations will increase access to information. Industry practitioners recognize the link between network activity and risk reduction: reduced risks lead to increased asset gathering and deal flows. Networks and associations are critical to distributing content. SI content and materials development partners include the World Bank, DFIs, academic networks, and educational bodies connected to the investment industry. In terms of distribution, an initial rollout and face-to-face "train-the-trainers" is recommended. Online training and remote tools can reduce distribution costs and increase the quality by delivering the most current material.

DEVELOP LOCAL TRAINING

It is time to look beyond traditional competition and seek ways to collaborate. An education program will provide tools to evaluate the wide array of available investment materials. Most importantly, this education can establish a framework to develop new narratives of PE and ESG in Africa and generate case studies to use in training. Existing sample case stories have been developed by asset managers and DFIs (for example, IFC with the Emerging Markets Private Equity Association). The major pension funds association in southern Africa, the Principal Officers' Association, has expressed interest in SI material for its members.

WAY FORWARD

To develop local ESG knowledge in the investment value chain, there is the need to leverage country-specific networks, pan-African initiatives, and subject-matter experts. Knowledge should be referenced to global initiatives and frameworks, but developed by Africans for Africa and the world. Along with in-person training, distance-learning modules can be developed to reduce costs and enable mid-career professionals to take part. Two other factors will help leverage education and training: the connecting role played via alumni of such programs, and the ability to partner with existing firms, networks, and NGOs promoting investment in Africa and/or sustainability in general.

5.4

make the investment case

This study has found that the SI proposition in Sub-Saharan Africa is undervalued, misrepresented, and/or poorly articulated. While more than half of investors interviewed say that there is a positive link between better ESG performance and investment outcomes,[356] many are unsure of how to state the SI case.

Making the SI case – whether highlighting financial returns and/or articulating the ESG impact – will be a major contributor to future asset flows, new products, and the growth of SI in Africa.

FOCUS ON PRIVATE EQUITY

As demonstrated earlier in this report, the active ownership model of PE most commonly applied in Sub-Saharan Africa is a good fit with SI, and many PE funds in the region have experience of integrating ESG factors in the investment lifecycle. SI practices applied today in PE may be adapted and/or applied as investment approaches to general asset management.

MAKE THE CASE WIDELY

Every stakeholder in the investment value chain needs to be educated about SI. From big-picture themes such as urbanization, job creation, and climate change, to local phenomena such as acid mine drainage and corrupt compliance officials, the SI/ESG investment case has to be made in a contemporary and quantitative way. Making the case in this way also enables practitioners to combat the effects of poor journalism or sub-par analytical work by advisors and researchers. Investment and company perspectives do overlap. The investment case and the business case must be presented in a complementary way, for example, by adopting an investor/company mapping similar to that used by the CFA Institute in 2008.[357]

DEVELOP MARKET INCENTIVES TO PROMOTE RESEARCH

Greater quality and quantity of ESG research depends on the creation of credible market incentives that encourage research agencies to stay up-to-date, innovate, and increase coverage in Africa. By driving new demand for research that explicitly covers ESG factors, it is reasonable to expect that PE and listed equity managers will gain access to data identifying sectors and companies expected to outperform over the long term. Investors will also be able to avoid sectors that may underperform as sustainability issues play out. Research providers will be attracted to meet the needs of the demand-driven market.

WAY FORWARD

The report recommends developing at least 10 case studies demonstrating the case for ESG integration into investment decisions for PE investors, with an option to develop more general versions or additional case studies for general asset managers. The SI case studies would provide sufficient diversity of location, investment style, ESG issues, and company sector. Investment analysts serving both PE funds and general asset management should be encouraged to explicitly cover ESG factors in sell-side investment research and company reports, using demand-driven industry mechanisms such as a buying pool of investor client contracts awarded to vendors of the best of such coverage, similar to efforts in Europe and Australia.

5.5

keep score

Regular, reliable, comparable, and investment-appropriate surveys of SI marketplace activity and performance benchmark indexes will support growth of SI on the continent over the next decade.

REGULAR MARKET SURVEYS

Accurate information drives better decision-making. A single composite SI marketplace report based upon a respected, authoritative data set, presented with trend analysis, will provide information on the benefits of improved SI messaging as the industry evolves a common language and platform. The regular survey should be aligned with global practices.

This study of South Africa, Nigeria, and Kenya forms a solid basis for a facts-based market analysis. It is the first attempt to provide a comprehensive view of SI products in Sub-Saharan Africa.[358]

REGULAR DATA POINTS

Analysis must be based on accurate, measurable, and easily-collectable industry data. In much of Africa, even simple investment data is scarce. Given the lack of information, obtaining such data may present a competitive advantage, even without analysis.

SUSTAINABILITY INDEX

The report recommends the design, testing, and launch of a benchmark index of SI in Africa and/or Sub-Saharan Africa. The benchmark of investable companies, will promote the concept of sustainability in Africa and spur the development of new portfolios and products that explicitly integrate ESG factors. The index concept builds on the experience of the two current African SI indexes, the JSE SRI index and Egyptian Standard & Poor's EGX ESG index,[359] as well as lessons learned in the process of establishing the African Investor SRI indexes.[360] The sustainability index idea also leverages IFC's knowledge using indexes as focal points for investment to promote ESG, such as the Standard & Poor's ESG India[361] index developed in 2008[362] and the Middle East and North Africa ESG index[363] launched in 2011.[364]

WAY FORWARD

The report proposes an annual survey of trends and opportunities in SI. The survey should include benchmarks and scorecards tracking investment value chain components for progress in ESG activities, whether branded or integrated. The survey should be conducted in a transparent manner, with a pro-Africa bias. A Sub-Saharan Africa index series would provide an important complementary tool to the marketplace survey. Finally, a simple, clear summary of this study would be valuable, updated and distributed at regular intervals.

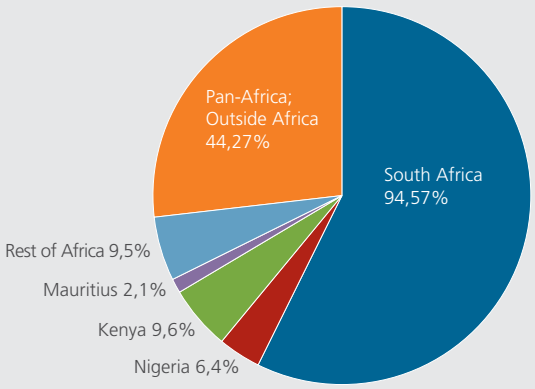
By promoting SI across all asset classes, it is possible to realize systemic change in investment patterns in Sub-Saharan Africa. Wherever possible, existing investment infrastructure should be leveraged for maximum impact at lowest cost. With ambitious objectives grounded in empirical research, and strategies implemented in a methodical fashion over the next three years, sustainable long-term investment performance may be achieved for the benefit of Africa, and investors in Africa.

appendices

APPENDIX 1: CONTRIBUTORS

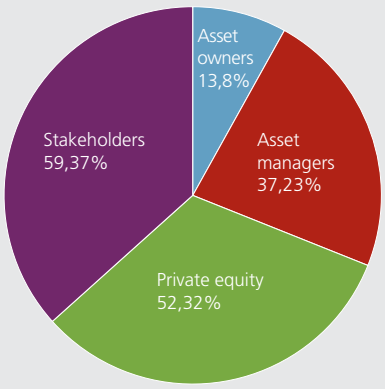
INTERVIEW RESPONDENTS BY COUNTRY LOCATION

161 categorized individuals interviewed Jan 2010-May 2011
Category [overlap possible], number, % of respondents



INTERVIEW RESPONDENTS BY TYPE

161 categorized individuals interviewed Jan 2010-May 2011
Category [overlap possible], number, % of respondents



Below is a list of organizations that contributed to this report in the form of interviews, online surveys, and correspondence.

INVESTORS

Private equity[365]

Absa Capital Private Equity; Actis Private Equity; Acumen Fund Inc; Adlevo Capital; African Agricultural Capital; African Alliance; Alitheia Capital; Alliance Capital Partners Limited; Altius Associates; Ariya Capital; ARM Investment Managers; Bain Capital Limited; Brait Private Equity; Capitalworks Equity Partners; CDC Group Plc; Databank Group; Development Bank of Southern Africa; East Africa Capital Partners; Emerging Capital Partners Investments; Ethos Private Equity; Fanisi Venture Capital Fund; Glenhove Fund Managers (Pty) Limited; Goldman Sachs Private Equity Group; Helios Investment Partners; Horizon Equity Partners; IDFC Capital (Singapore) PTE Limited; Kingdom Zephyr Africa Management; Masazane; Medu Capital; Metier; Mezzanine Partners; Musa Capital; Old Mutual Investment Group South Africa; Overseas Public Investment Corporation; Phatisa; Public Investment Corporation; Rand Merchant Bank; Sanlam Private Equity; Shared Growth AM IC; Silk Invest Limited; South Suez Advisory (Pty) Limited; Stanbic Nigeria; Standard Bank Private Equity; Stimulus Private Equity; TransCentury Limited.

Asset owners

Actis Private Equity; Eskom Pension and Provident Fund; FMO; Government Employees Pension Fund; Imbewu Capital Partners; Johannesburg Pension Fund; Mine Employees Pension Fund; Motor Industry Fund Administrators; Nigeria Closed Pension Fund Administrator Limited; Telkom Retirement Fund.

General asset managers

27 Four Investment Managers; Aeon Investment Management; Afena Capital (Pty) Limited; African Alliance; Allan Gray Limited; Argon Asset Management; Bank Sarasin & Co. Limited; Cadiz Asset Management; Coronation Fund Managers; Element Investment Managers; Futuregrowth Asset Managers; Grindrod Asset Management; Insparo Asset Management; Investec Asset Management; Investec Capital Markets; Kagiso Asset Management; Mergence Africa Investments (Pty) Limited; Metropolitan Asset Managers; Plexus Asset Management; Prescient Investment Management; Renaissance Asset Managers; Sanlam Investment Management; Stanlib Asset Management; Sustainable Capital.

STAKEHOLDER, SERVICE PROVIDER, AND/OR ADVISORS

Abu Dhabi Future Energy Company (Masdar); Advantage Asset Managers; African Alliance Securities; African Venture Capital Association; Alexander Forbes; Association for Savings and Investment South Africa; BiD Network; Bowman and Gillfillan; CAL Bank; Capital Markets Authority; Carbon Disclosure Project; Carne Group; Corporate Africa Limited; Credit Suisse; DEG; Deutsche Bank Research; Deutsche Securities; Emerging Markets Private Equity Association; Environmental Resources Management; Ernst and Young Inc; Exotix Limited; Galileo Global Advisors; Glacier by Sanlam; Glamis Research Institute; Hermes Investment Management; ISI Emerging Markets; Johannesburg Stock Exchange; KPMG; Legae Securities; Mettle; MSCI; Nairobi Stock Exchange; National Business Initiative; Old Mutual Investment Group South Africa; Old Mutual Life Insurance Company; Principles for Responsible Investment; Radix Corporate Governance (Pty) Limited; Raizcorp; RisCura; SA Finance Direct; Securities Africa; Shell Foundation; South African Venture Capital Association; Stanbic Nigeria; Summit TV; Teachers Insurance and Annuity Association, College Retirement Equities Fund; Thomson Reuters – Asset 4; University of South Africa; University of Stellenbosch Business School Unit for Corporate Governance in Africa; Unlimited Energy Resources; Webber Wentzel; World Resources Institute.

APPENDIX 2: COMPANIES AND MARKETS

TOP 10 COMPANIES BY MARKET CAPITALIZATION[366]			
Ticker	**Company**	**Market cap local currency, million**	**Market cap, $ million**
Johannesburg Stock Exchange (South Africa)		**3,815,134**	**565,205**
BIL	BHP Billiton Plc	1,477,067	214,644
AGL	Anglo American Plc	460,624	66,777
CFR	Compagnie Financiere Richemont SA	399,550	60,394
SAB	SABMiller Plc	373,211	56,412
MTN	MTN Group Ltd	247,405	37,395
SOL	Sasol Ltd	228,151	34,486
AMS	Anglo Platinum Ltd	182,496	27,585
SBK	Standard Bank Group Ltd	161,112	24,353
NPN	Naspers Ltd	145,639	22,014
IMP	Impala Platinum Holdings Ltd	139,876	21,143
Nigerian Stock Exchange (Nigeria)		**4,472,023**	**29,421**
DANGCEM	Dangote Cement Plc	1,859,282	12,232
NB	Nigerian Breweries Plc	583,076	3,836
F BILLION	First Bank of Nigeria Plc	448,037	2,947.6
GTB	Guaranty Trust Bank Plc	414,113	2,724
GUN	Guinness Nigeria Plc	281,062	1,849
NES	Nestle Nigeria Plc	243,445	1602
UBA	United Bank for Africa Plc	236,690	1557
AB	Access Bank Plc	154,490	1016
FLOURMIL	Flour Mills Nigeria Plc	129,666	853
WAPCO	Lafarge Wapco Plc	122,165	804
Nairobi Stock Exchange (Kenya)		**570,430**	**7,069**
EABL	East African Breweries Ltd	158,946	1,970
BBK	Barclays Bank of Kenya Ltd	84,868	1,052
SCBK	Standard Chartered Bank Ltd	74,066	918
BAMB	Bamburi Portland Cement Co	67,873	841
KCB	Kenya Commercial Bank Ltd	67,531	837
BAT	British American Tobacco	27,000	335
NMG	Nation Media Group	26,239	325
DTK	Diamond Trust Bank of Kenya Ltd	22,010	273
KQ	Kenya Airways	21,234	263
CFC	CFC Stanbic Holdings Ltd	20,663	256

INITIAL PUBLIC OFFERINGS ON EXCHANGES IN SOUTH AFRICA, NIGERIA, AND KENYA DURING 2010			
Board	**Ticker**	**Company**	**Listing date**
South Africa[367]			
Main	OPT	Optimum Coal Holdings	2010/03/29
Africa Board	WIL	Wilderness Holdings	2010/04/08
AltX	RGT	RGT Smart Market Intelligence	2010/04/14
Main	CCO	Capital and Counties Properties	2010/05/10
Main	RACP	RECM and Calibre Limited	2010/06/08
Main	LHC	Life Healthcare Group	2010/06/10
Main	RSG	Resource Generation	2010/07/14
Main	HSI	Health Strategic	2010/08/16
Main	RIN	Redefine Properties International	2010/09/07
Nigeria[368]			
Main	UHOMREIT	Union Homes Real Estate Investment Trust Plc	2010/07/02
Kenya[369]			
No listings during 2010			

DUAL-LISTED SOUTH AFRICAN COMPANIES[370]			
Code/ticker	**Name**	**Market cap, local currency billion**	**Market cap, $ billion**
South Africa			
BIL SJ Equity	BHP Billiton Plc	1,657	241.4
AGL SJ Equity	Anglo American Plc	481.9	70.1
SAB SJ Equity	Sabmiller Plc	386.7	56.1
MTN SJ Equity	Mtn Group Ltd	246.4	35.8
SOL SJ Equity	Sasol Ltd	229.7	33.4
CFR SJ Equity	Financiere Richemont-Dep Rec	227.8	33.2
AMS SJ Equity	Anglo Platinum Ltd	198.1	28.8
SBK SJ Equity	Standard Bank Group Ltd	169	24.6
NPN SJ Equity	Naspers Ltd-N Shs	163.9	23.8
KIO SJ Equity	Kumba Iron Ore Ltd	151/3	21.9

APPENDIX 3: GLOBAL MARKET ACCESSIBILITY[371]

Openness to foreign ownership

	Investor qualification requirement	Foreign ownership limit level	Foreign room level	Equal rights to foreign investors
Egypt	++	+	++	++
Morocco	++	++	++	+
South Africa	++	++	++	++
China (Internat.)	++	-/?	++	+
Brazil	++	-/?	++	-/?
India	+	-/?	-/?	+
Turkey	++	++	++	+
Russia	++	++	++	+

Legend: ++: no issues; +: no major issues, improvements possible; -/?: improvements needed / extent to be assessed

Ease of capital inflows/outflows

	Capital flow restriction level	Foreign exchange market liberalization level
Egypt	++	++
Morocco	+	++
South Africa	++	++
China (Internat.)	++	++
Brazil	++	-/?
India	++	-/?
Turkey	++	++
Russia	++	-/?

Legend: ++: no issues; +: no major issues, improvements possible; -/?: improvements needed / extent to be assessed

Efficiency and operational framework (market entry and market organization)

	Investor registration and account set up	Market regulations	Competitive landscape	Information flow
Egypt	++	+	++	+
Morocco	+	+	++	+
South Africa	++	++	++	++
China (Internat.)	++	+	++	++
Brazil	-/?	+	-/?	+
India	-/?	++	+	++
Turkey	+	+	+	-/?
Russia	-/?	+	++	-/?

Legend: ++: no issues; +: no major issues, improvements possible; -/?: improvements needed / extent to be assessed

Efficiency of the operational framework (market infrastructure)

	Clearing & settlement	Custody	Registry/ depository	Trading	Stock lending	Short selling
Egypt	+	++	++	++	-/?	-/?
Morocco	+	++	++	++	-/?	-/?
South Africa	+	++	++	++	++	-/?
China (Internat.)	++	++	++	++	++	++
Brazil	+	++	++	++	++	++
India	-/?	++	++	++	+	+
Turkey	+	++	++	++	++	+
Russia	-/?	++	-/?	+	-/?	-/?

Legend: ++: no issues; +: no major issues, improvements possible; -/?: improvements needed / extent to be assessed

Stability of institutional framework

Egypt	+
Morocco	+
South Africa	+
China (Internat.)	+
Brazil	+
India	+
Turkey	+
Russia	+

Legend: ++: no issues; +: no major issues, improvements possible; -/?: improvements needed / to be assessed

APPENDIX 4: ESG COUNTRY COMPARISONS

The tables and graphs below give a comparison between Sub-Saharan Africa, Northern Africa, and other emerging markets along key ESG indicators.

ENVIRONMENTAL FACTORS					
African vs. other emerging markets					
Country	2010 EPI* score (out of 100)	EPI water (effects on humans)	EPI climate change	Biodiversity & habitat	Agriculture
Brazil	63.4	79.3	46.4	61.3	90.7
China	49	70	40.2	57.2	69.1
Egypt	62	79.2	62.1	59.2	73.5
India	48.3	50.1	60.3	38.7	35.7
Kenya	51.4	30.4	66.9	76.4	48.4
Morocco	65.6	69.6	56.6	25.5	82.1
Nigeria	40.2	15	75.8	74.7	59.1
South Africa	50.8	71	39.5	62.4	64.3
Tunisia	60.6	86.4	58.8	10	43.9

Source: Environmental Performance Index, 2010, http://epi.yale.edu/Countries *EPI = Environmental Performance Index

SOCIAL FACTORS						
African vs. other emerging markets						
Country	HDI – rank	Ratification of basic workers' convention (out of 8)	Rigidity of employment (out of 100)	Gender empowerment measures	Gender gap index (out of 1)	Hiring and firing practices index (out of 7)
Brazil	73	7	46	50.40%	0.67	2.8
China	89	4	31	53.30%	0.69	4.07
Egypt	101	8	27	28.70%	0.59	3.86
India	119	4	30	N/A	0.62	3.69
Kenya	128	7	17	N/A	0.65	4.9
Morocco	114	7	60	31.80%	0.58	3.95
Nigeria	142	8	7	N/A	0.61	5.2
South Africa	110	8	35	68.70%	0.75	2.5
Tunisia	81	8	40	44.3%*	0.63	4.2

Sources: Human development index (HDI) - 2010 rankings , http://hdr.undp.org/en/statistics/
Source of ratifications: International Labor Organization, Database of International Standards. November 8, 2010. http://www.ilo.org/declaration/lang--en/index.htm
Rigidity of employment index: World Bank Doing Business 2010 Report
Gender empowerment: UN data website available, http://data.un.org/DocumentData.aspx?q=gender+empowerment&id=182
Gender gap index: The Global Gender Gap Report 2010
Hiring and firing practices index: WEF Global Competitiveness Report 2010-2011
Legend:
*No data, substituted with regional score from Jordan, Kuwait, Lebanon, and Tunisia; N/A, no data available

GOVERNANCE FACTORS			
African vs. other emerging markets			
Country	"In the past three years, how has the level of corruption in this country" **decreased**?	"In the past three years, how has the level of corruption in this country" **stayed the same**?	"In the past three years, how has the level of corruption in this country" **increased**?
Brazil	9%	27%	64%
China	25%	29%	46%
India	10%	16%	74%
Kenya	48%	14%	39%
Morocco	11%	77%	13%
Nigeria	17%	10%	73%
South Africa	24%	14%	62%
Sub-Saharan Africa	24%	14%	62%

Source: Global Corruption Barometer 2010, Transparency International, http://www.transparency.org/policy_research/surveys_indices/gcb/2010/results. Accessed December 10, 2010.

OTHER GOVERNANCE FACTORS						
African vs. other emerging markets						
Country	Director liability score (out of 10)	Extent of disclosure score (out of 10)	Strength of auditing and accounting standards	Efficacy of corporate boards	Ethical behavior of firms	Corruption perception index
Brazil	7	6	4.76	4.55	3.55	3.7
China	1	10	4.79	4.4	4.18	3.5
Egypt	3	8	4.83	4.42	4.13	3.1
India	4	7	5.13	4.47	3.86	3.3
Kenya	2	3	4.7	4.3	3.3	2.1
Morocco	2	6	4.16	4.62	3.77	3.4
Nigeria	7	5	3.4	4.1	3.1	2.4
South Africa	8	8	6.4	5.8	4.5	4.5
Tunisia	5	5	4.98	4.91	5.18	4.3

Sources: Director liability: World Bank, Doing Business, Investor Protection Index, 2009
Extent of disclosure index: World Bank, Doing Business, Investor Protection Index, 2009
Strength of auditing and accounting standards: World Economic Forum Global Competitiveness Report 2010-2011
Ethical behavior of firms: World Economic Forum Global Competitiveness Report 2010-2011
Corruption perceptions index: Transparency International, http://www.transparency.org/policy_research/surveys_indices/cpi/2010/results

APPENDIX 5: AFRICAN POSITIONS ON GLOBAL CLIMATE TALKS

Fifty-four African state parties (including 45 from the Sub-Saharan Africa region) participated[372] in the 16th Congress of the Parties (COP16) on global climate change. In preparation for this meeting, the African Heads of State and Government on Climate Change convened at the African Union headquarters in Addis Ababa, Ethiopia in November 2010. The positions of the Nigerian, Kenyan, and South African representatives on the COP16 talks are presented in the boxes below.

COP 17 takes place in Durban, South Africa, during November and December 2011.

nigeria

"The urgency of global warming, its complexity and potent danger has become one of the greatest challenges to humanity and sustainable livelihood. In Copenhagen 2009, the aspiration of the global community to achieve substantial outcome sadly did not yield the expected result. The issue of lack of transparency, entrenched regional differences and lack of commitment to up-hold the Kyoto Protocol contributed largely to that failure…

"It is imperative that the two-track approach to climate change negotiations continues towards ensuring a post-2012 commitment to the Kyoto Protocol. My delegation therefore, calls the annex 1 parties to show the commitment to the political will required to see the process to a logical conclusion. In a similar manner, we call on other Parties to commit themselves to the need for utmost transparency and openness in this process…

"As part of a balanced package, we are firmly committed to seeing that current areas of contention with respect to the financial mechanism, governance structure for long term financing, adaptation means and institutional arrangements, technology transfer and capacity building are resolved to the benefit of all Parties. Nigeria also believes that reducing emissions from deforestation and forest degradation is a key instrument for countries in Africa to mitigate and adapt to climate change. We urge the international community to reach an agreement on reducing emissions from deforestation and forest degradation here in Cancun."[373]

John Odey, Minister of Environment of the Federal Republic of Nigeria

kenya

"The process of consensus building through UN Framework Convention on Climate Change has become painfully slow, more so for us in Africa where our populations continue to bear the rising costs of vulnerability with reduced water, food, and energy...

"We all know that expectations for Cancun are somewhat dampened with only few process-related decisions to be the likely outcomes. It is our view that Africa should continue to push for a balanced package of decisions for both further commitments under the Kyoto Protocol as well as the Long-term Cooperative Action leading to a legally binding instrument to curb emissions…

"Some of the areas that continue to generate mistrust include the status of fast-track financing. We all know the reality of the fast-track financing of $30 billion pledged as part of the Copenhagen Accord. It is now a year later and the funds have remained largely pledges! Neither do we have any clarity on how the finances will flow or be accessed.

"We are all aware that our leaders in Copenhagen agreed that fast-start finance would be new and additional money. There are however differences amongst our western partners on how to interpret additionality. Africa should therefore continue to insist that fast-start funding is indeed new and additional money, and that this funding should be disbursed in a transparent and timely manner. The credibility of the negotiation process will continue to be linked to the timely release of fast-start funding.

"It is also our view that mechanisms for financial management should remain within the control of the Conference of Parties in order to give Ministers of Environment a role to provide guidance. As a country Kenya has taken bold steps and has developed a National Climate Change Response Strategy to guide our national programs on climate change."[374]

John Michuki, EGH, MP, Kenya Minister for Environment & Mineral Resources

south africa

"At the talks, South Africa, along with most other developing countries in Africa, among Small Island States and Least Developed Countries, called for a two-track legally binding outcome; where on the one hand, a track where developed countries who joined the Kyoto Protocol agree to a second commitment period under the protocol. Whilst, on the other hand, a second track where developed countries who did not join the Kyoto Protocol, will take comparable commitments under the Convention with the collective effort of all developed countries adding up to a level of ambition required by science (a 25-40 percent aggregate reduction from 1990 levels by 2020).

"Under this second track, developing countries would also contribute to the global solution to the climate crisis, where their climate action will be provided with finance, technology, and capacity building support. While some progress was achieved in relation to how developed country mitigation targets are reflected, in Cancun there was no agreement on a second commitment period for the Kyoto Protocol. Further negotiations on this matter will be forwarded for decision to the Climate Change Conference in Durban next year…

"Despite the above progress, the Cancun outcome was not able to answer many difficult political questions and these have been forwarded to (COP17) …"[375]

Edna Molewa, South Africa Government Minister of Water and Environmental Affairs

Progress was made during the 2010 Cancun talks: a global climate change treaty was shaped, a new Green Climate Fund was created, governed by an equal number of developed and developing countries administered by the World Bank, and developed countries were called to raise $100 billion by 2020 in long-term finance to help developing countries. The Green Climate Fund will fund adaptation support and efforts to reduce greenhouse gas emissions. COP 17 will address some of these issues.

"We [the African Union] are working towards the creation of an Africa Green Fund, which will be administered by the African Development Bank - we want Africa's share of money to flow through that… African countries are responsible for a negligible amount of emissions. We want most – at least 60 percent of the funds – to flow for adaptation."

Dr Edward Kofi Omane Boamah, Ghana's Deputy Minister for the Environment[377]

APPENDIX 6: SPOTLIGHT ON THE JSE SRI INDEX

The JSE SRI index was launched in May 2004 and was the first index of its kind among emerging markets.[378]

2010 REVIEW

In December 2010, the JSE SRI index released its 2010 review update: 74 out of the 106 companies assessed were selected (67 out of 100 in December 2009)[379] – which makes it the highest number of companies ever selected.[380] The most common cause of exclusion from the index was environmental policy and reporting. The 2010 review process was updated to reference King III.[381]

METHODOLOGY

According to the JSE, the "SRI index comprises listed companies which meet criteria related to their ESG policies, management practices and reporting. The intention of the index is two-fold: to encourage companies to operate responsibly and transparently and to prompt institutions to consider ESG factors when evaluating potential investments."[382]

"The SRI index has distinctly South African criteria in the form of mandatory performance around black economic empowerment and HIV/AIDS. For the first time this year, climate change criteria were introduced, with an initial focus on gauging risks and encouraging senior responsibility. Also new in 2010 is a mandatory requirement that a lead independent non-executive director be appointed in cases where the chairman of the board is not independent. To be an SRI best performer, a company must appoint only an independent chairman."[383]

Corli Le Roux, the legal counsel and head of the JSE SRI index, explained that *"the index mostly tracked the all share index because (of the same) weightings methodology."* She said that the JSE might consider different ways to weight performance from next year, although large-cap companies tend to dominate in terms of inclusion and performance. This dominance is demonstrated in the SRI index's inclusion of every materials and mining company listed in the Top 100.[384]

INDEX FUTURE

The index team stated that *"(strengthening) investor relationships, particularly with fellow signatories of the PRI, will be a focus area for 2011. Another focus area for the JSE is to expand the availability of analysis on company performance from the SRI Index process, an area which has been highlighted as a need for investors to strengthen their engagement with and investment in companies. The JSE will continue to identify opportunities to encourage transparency and responsibility in relation to ESG concerns."*[385]

2010 COMPOSITION

The 2010 constituents of the SRI index are in alphabetical order. The companies in bold correspond to the best consistent performers for four consecutive years (2007–2010).[386] According to the JSE SRI index, *"best performers are companies that meet their relevant environmental threshold, all relevant core indicators in relation to society and governance and related sustainability concerns, and all climate change indicators, as well as have an independent chairperson."*[387]

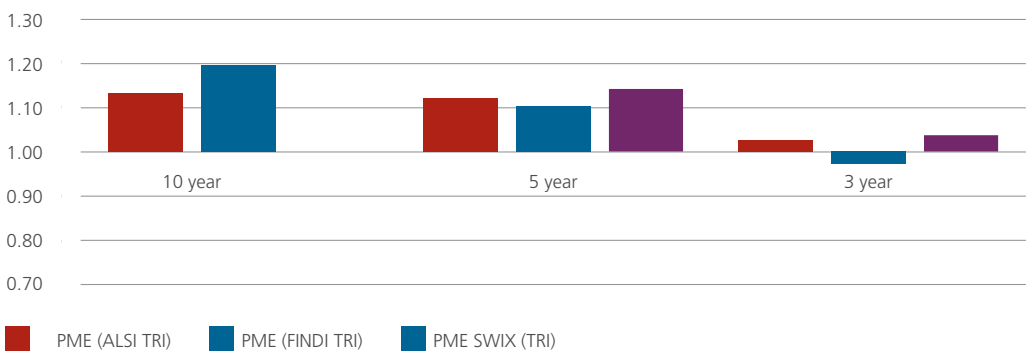
2010 CONSTITUENTS OF THE JSE SRI INDEX	
Absa Group	Evraz Highveld Steel and Vanadium Limited
Advtech Limited	Exxaro Resources
AECI Limited	Firstrand
African Bank Limited	The Foschini Group Limited
African Oxygen	**Gold Fields Limited**
African Rainbow Minerals Limited	Grindrod
Allied Electronics Corporation Limited	**Group Five**
Allied Technologies Limited	Growthpoint Properties
Anglo American plc	Harmony Gold Mining
AngloGold Ashanti	Hulamin
Anglo Platinum	Illovo Sugar Limited
ArcelorMittal South Africa	Impala Platinum Holdings
Aspen Pharmacare Holdings Limited	Imperial Holdings
Aveng	Investec Limited and plc
Barloworld Limited	JSE Limited
BHP Billiton	Kumba Iron Ore
The Bidvest Group	Liberty Holdings Limited
Blue Label Telecoms	Lonmin plc
Business Connexion Group	Massmart Holdings Limited
Capital Shopping Centres Group plc	Medi-Clinic Corporation Limited
Caxton and CTP Publishers and Printers Limited	**Merafe Resources**
Clicks Group Limited	MMI Holdings (previously Metropolitan Holdings)
Discovery Holdings Limited	Mondi Limited and plc
DRD Gold Mining	MTN
Murray & Roberts Holdings Limited	Sanlam
Nampak	Santam Limited
Nedbank Limited	Sappi
Northam Platinum	Sasol
Oceana Group Limited	**Standard Bank Group**
Old Mutual	Steinhoff International Holdings
Palabora Mining	Sun International
Pick n Pay	Telkom SA Limited
Pretoria Portland Cement Company Limited	Tiger Brands
Rainbow Chicken Limited	**Tongaat Hulett**
Remgro Limited	Truworths Limited
RMB Holdings	Vodacom Group Limited
SABMiller plc	Woolworths Holdings

APPENDIX 7: AFRICAN PRIVATE EQUITY MARKET SNAPSHOT

SAMPLE LIST OF AFRICAN PRIVATE EQUITY FUNDS[388]			
Fund name	**Fund manager**	**Fund type**	**AUM $ million**
Africa-focused funds closed between 2009- 2010			**6,258**
InfraMed Infrastructure	InfraMed Management	Infrastructure	1,258
African Global Capital II	Och-Ziff Capital Management	Balanced	1,000
African Infrastructure Investment Fund II	African Infrastructure Investment Managers	Infrastructure	1,000
Ethos Private Equity Fund VI	Ethos Private Equity	Buyout	750
Helios Investors 2	Helios Investment Partners	Buyout	650
EVI Capital Buyout Fund	EVI Capital	Buyout	400
EVI Capital Mezzanine Fund	EVI Capital	Mezzanine	400
EVI Capital Partners Real Estate Fund	EVI Capital	Real estate	400
Vantage Capital Mezzanine II	Vantage Risk Capital	Mezzanine	400
Africa-focused funds			**3,435**
Pan-African Infrastructure Development	Harith	Infrastructure	630
ECP Africa Fund III	Emerging Capital Partners	Expansion	613
Pan-African Investment Partners II	Kingdom Zephyr	Expansion	492
African Development Partners I	Development Partners International	Expansion	405
Aureos Africa Fund	Aureos Capital	Balanced	381
South Africa Workforce Housing Fund	International Housing Solutions	Real estate	240
AfricInvest II	Tuninvest - Africinvest Group	Balanced	189
GroFin Africa Fund	GroFin	Venture (general)	170
Capital Alliance Property Investment Company	African Capital Alliance	Real estate	165
EuroMena II	Capital Trust Group	Expansion	150

PE PERFORMANCE, RELATIVE TO PUBLIC EQUITY MARKETS, RISCURA FUNDAMENTALS MAY 2011

PUBLIC MARKET EQUIVALENT RESULTS



	PME (ALSI TRI)	PME (FINDI TRI)
10 year	1.13	1.19
5 year	1.12	1.10
3 year	1.03	0.97

PME = public market equivalent

PUBLIC MARKET EQUIVALENT

This measure equates the heavily timing-dependent returns of PE funds with the returns of public market indices. The measure is a ratio of the net outflows from PE funds reinvested into the public index until the end of the fund's life, divided by the inflows into a PE fund invested in the public index until the end of the fund's life. A ratio of above 1 reflects outperformance of PE, while a ratio under 1 reflects underperformance. This analysis shows that PE has outperformed several listed indices over most time periods. 10 year: n=20, 5 year: n=17, 3 year: n=15

Source: RisCura Fundamentals, June 2011.

AFRICAN PRIVATE EQUITY FUNDS: KEY DATA POINTS	
PE market scale	
Total African-focused PE funds (seeking commitments)	71
Total committed capital sought ($)	24,900
Source: Fundraising & Investment Update – 1H 2010. Emerging Markets Private Equity Association. In correspondence with authors. Preqin Special Report: The Private Equity Market In Africa, 2010, http://www.preqin.com/docs/reports/Africa.pdf. Accessed September 25, 2010. Fundraising & Investment Update – 1H 2010. Emerging Markets Private Equity Association. In correspondence with authors. Preqin Special Report: The Private Equity Market In Africa, 2010, http://www.preqin.com/docs/reports/Africa.pdf Accessed September 25, 2010. Africa Investor, July-August 2010, http://content.yudu.com/Library/A1oasg/AfricaInvestorJulyAu/resources/34.htm	
Total funds raised: 2005 ($)	800 million
Total funds raised 2008 ($)	2.2 billion
Source: Emerging Markets Private Equity Association, 2009.	
Total funds raised through mid-2010 ($)	1.5 billion
Source: Emerging Markets Private Equity Association. "Emerging Markets Private Equity Association Insight – Special Edition: Private Equity in Sub-Saharan Africa." November 2010.	
Total funds raised in the past 10 years leading to 2010 ($)	10 billion
South Africa PE firms contribution	60%
Egypt PE firms contribution	25%
Mauritius PE firms contribution	5%
Morocco PE firms contribution	4%
Anna Strumillo, Preqin Blog, January 6, 2010	
Total number of active PE investors who previously invested or would consider investing in vehicles targeting opportunities in Africa	270
Source: Preqin.	

PRINCIPLES FOR RESPONSIBLE INVESTMENT AFRICA SIGNATORIES AT DECEMBER 31, 2010

south africa

- 27Four Investment Managers
- Advantage Asset Managers
- Avior Research
- Brait Private Equity
- Cadiz Holdings
- Coronation Fund Managers
- Corporate Governance Accreditation
- Element Investment Managers
- Empowerdex
- Eskom Pension and Provident Fund
- EVI Capital Partners
- Futuregrowth Asset Management
- Government Employees Pension Fund
- Investec
- Investment Solutions
- Johannesburg Stock Exchange
- Kagiso Asset Management
- Mazi Visio Manco
- Mergence Africa Investments
- Prescient Investment Management
- Prudential Portfolio Managers
- Public Investment Corporation
- RisCura
- Sanlam Investment Management
- STANLIB Asset Management
- TriStar Investments

nigeria

- Access Bank

mauritius

- Sustainable Capital Ltd

Source: www.unpri.org, accessed October 2010

CARBON DISCLOSURE PROJECT AND CDP WATER SIGNATORIES BASED IN AFRICA

Project	Financial institution/investor
Carbon Disclosure Project[389]	
CDP 2010	Element Investment Managers Sanlam Nedbank Limited Firstrand Limited The Standard Bank Group Government Employees Pension Fund, South Africa Advantage Asset Managers (Pty) Limited Cadiz Holdings Limited Futuregrowth Asset Management Sustainable Capital
Water Disclosure Project[390]	
CDP Water Disclosure 2010	Element Investment Managers Advantage Asset Managers (Pty) Limited Cadiz Holdings Limited Firstrand Limited Government Employees Pension Fund, South Africa Nedbank Limited Sanlam The Standard Bank Group Sustainable Capital

ENDNOTES

[1] Acknowledgements include the RisCura team led by Malcolm Fair. The RisCura team on IFC/SinCo Project 2010-2011 includes: Malcolm Fair (Director and Head of RisCura Analytics), Rory Ord (Head of RisCura Fundamentals), Claire Rentzke (Head of Manager Research: RisCura Consulting), Jacobus Troveri (Head of RisCura Transition), Kerry Kilcullen Sinclair (Head of Marketing), Thibaut Takadong, Nischal Baijnath, David Moore, Madelein van Wyk (RisCura Consulting Namibia), Rebecca Smith, and Daria Alkhovik (RisCura Operations).

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[13] This study took a conservative approach to estimates based on the limits of self-reporting. The actual prevalence of DFI-funded PE over the past decade may be as high as 60-70%.

[14] Generalized cross-rate applied unless note is South African rand:US dollar ZAR7.5: $1.

[15] SinCo+RisCura analysis from SAVCA/EMPEA/RisCura data, June 2011.

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