The African Investment Landscape and Pension Funds Long-Term Investment Strategies

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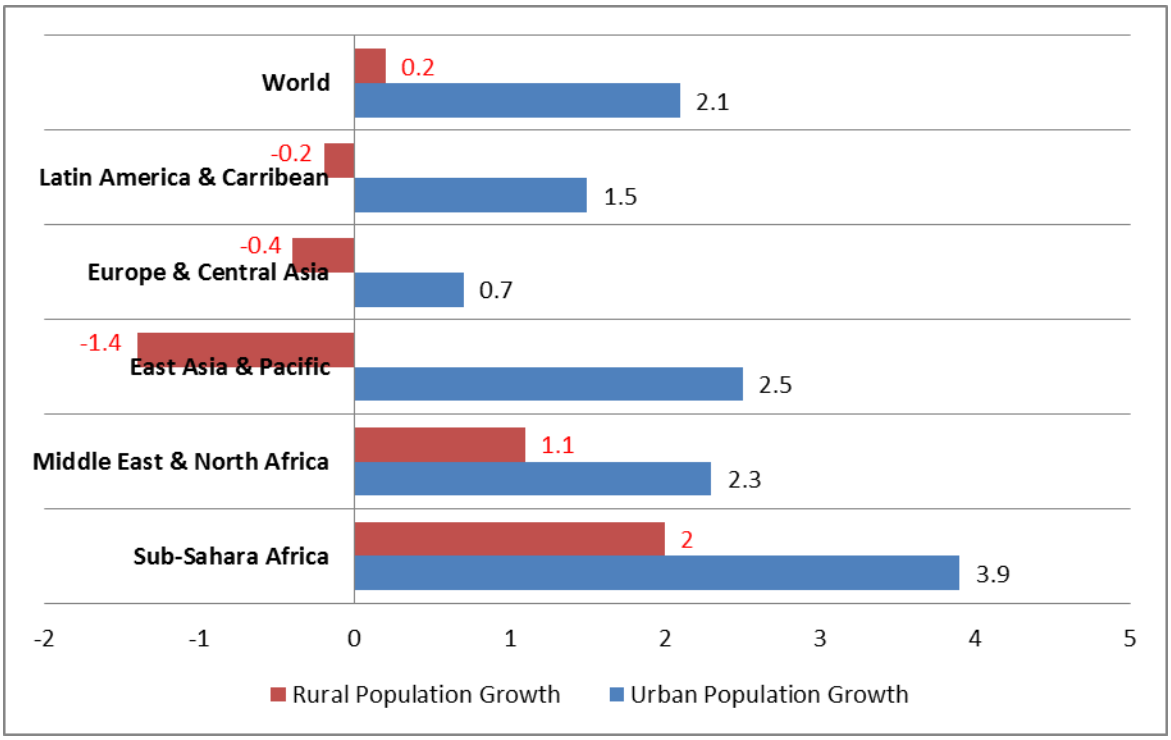
Introduction

Pension fund organizations are viewed by policy makers and different stakeholders and citizens as entities that hold idle financial resources and once ignited and channeled in the right areas can create vast benefits for society and retirees (Asher, 1998). Although pension fund organizations have well defined mission of providing retirement income to members, increasingly these organizations have come under pressure to fulfill and meet the needs and expectations of different stakeholders in addition to their members (Mitchell& Smith, R, 1991). Governments expect pension fund organizations to contribute to economic growth through the provision of long-term capital to finance local economic development, especially sectors that have multiplier effect on the economy. The expectations placed on these organizations have created a need for pension fund leaders to become increasingly accountable and to develop governance, management structures and performance measurement system that can support and fulfill current and future expectations. This paper discusses the role that pension fund organizations can play in the changing investment landscape of Africa.

Population and demographic dynamics

The African investment landscape is shaped by changing population and demographic dynamics, which in turn determines consumption and investment patterns. As shown in figure 1 below, Africa has experienced the highest urbanization over the past years and in 2013 the rate of urbanization was the highest in Africa compared to other countries. With rapid urbanization, middle class growth in Sub-Saharan Africa is expected to grow more than 80 percent by 2022, which is faster than any other region except the Asia-Pacific (Global Insight, 2012). Likewise, Sub-Saharan Africa is expected to lead all regions, except South Asia, in growth of food sales, which are expected to increase by nearly 60 percent over the next decade.

Figure 1: Urban and Rural Population (Annual % Growth)

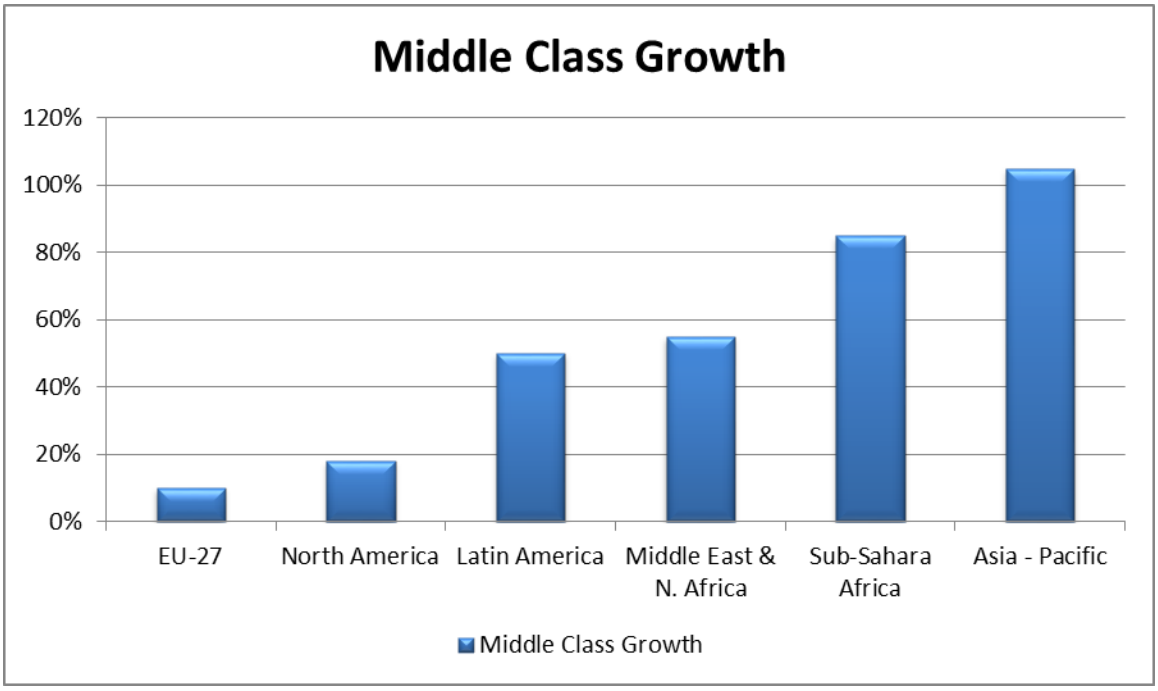


Source: World Bank

Trends in Africa Middle Class Growth

Africa's population is relatively young and has a huge population in the age bracket of 25-35, with rising income and high spending behaviors. African leaders have come to the realization that not only is Africa's middle class crucial for economic growth, but they are essential for the growth of democracy and will play a key role in rebalancing the African economy. Consumer spending by the middle class has reached an estimated $680 billion in 2008 or nearly a quarter of Africa's GDP and by 2030 this figure will likely reach $2.2 trillion and Africa will comprise about 3 per cent of world-wide consumption (World Bank, 2013). The World Bank analysis shows that the African middle-class households are likely to spend more on private education and health, as well as on household assets such as televisions and refrigerators. Figure 2 below presents a forecast of increase in middle class in various regions and middle class growth in Sub-Saharan Africa is expected to grow more than 80 percent by 2022 (Global Insight 2013), which is faster than any other region except the Asia-Pacific.

Figure 2: Forecast Increase in Middle Class (2012 – 2022)



Source: Global Insight

Agriculture as an Asset Class for Pension Funds in Africa

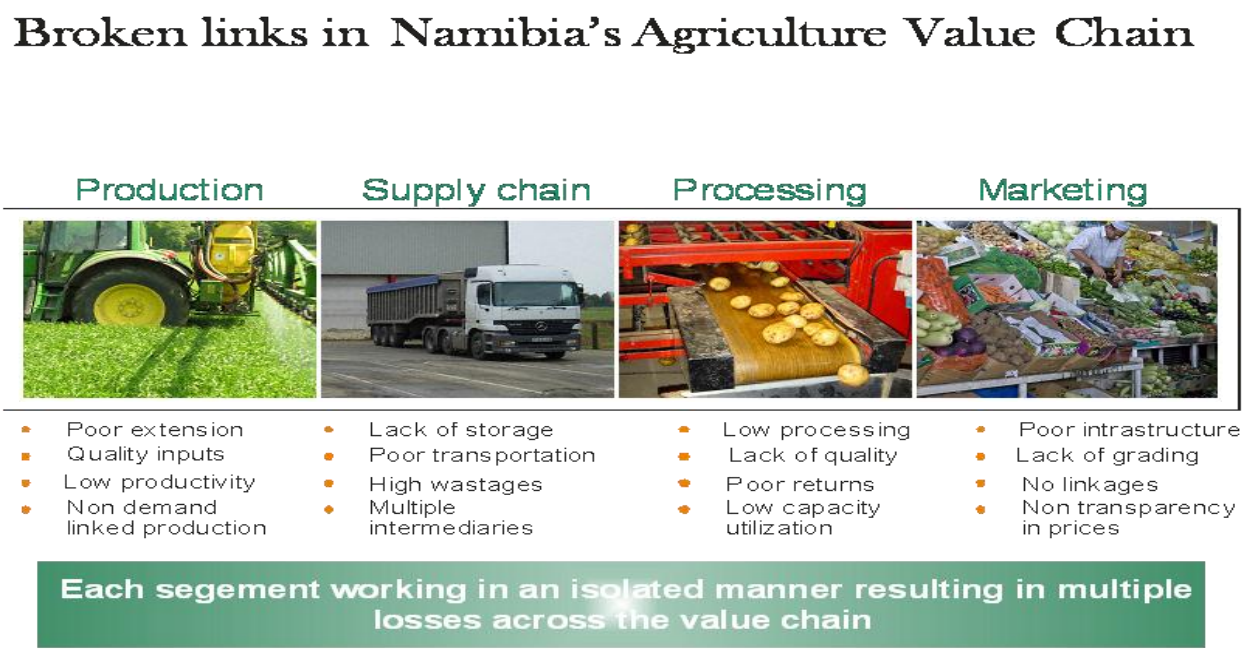
Africa imports close to 80% of its food needs and in 2013 more than U$45 billion dollar was spent on food imports (Global Insight, 2013). With the rising size of the middle class, this trend is expected to continue and without significant investment in agriculture and address the missing links within the African food value chain, Africa will continue to rely on imports. Fast growing population, rising income, healthy economic growth and surging food demand in Sub-Saharan Africa pushed food imports to a record high in 2011, with the region's total agricultural imports from all suppliers reaching U$43.6 billion and this was estimated to have increased to U$48 billion by 2013. According to Global Insight, at nearly $6 billion, wheat was a major contributor to Sub-Saharan Africa's record agricultural imports in 2011. Wheat was followed by rice, vegetable oil, and dairy products. The region's leading agricultural importers are Nigeria, South Africa, and Angola. Taken together, these three markets comprise 39 percent of Sub-Saharan Africa's imports. The region's 46 other countries account for the remainder. Many countries outside Africa are exploiting these market opportunities and with a 27-percent market share, the EU is the largest exporter to Sub-Saharan Africa, followed by Brazil (10 percent) and India (8 percent) while the USA's market share is also increasing.

Agriculture is emerging as an important asset class in the portfolio of many pension funds in developed countries as they take advantage of the expanding market for food and agricultural products in Africa. Short-term bank loans are not suited for financing of agriculture as the sector requires long-term form of funding. Investment is needed along the agriculture/food value chain to enable the efficient delivery of cost effective, safe food products to the market and pension funds are in a better position to provide long-term equity funding to unlocking agriculture sector development in Africa.

Figure 3 below shows the broken links in Namibia's agriculture sector. To minimize risks and enhance returns, pension funds should diversify their funding along the agriculture value chain to ensure that all the segments operate in tandem and if that

is done, current multiple losses which are being experienced would be a thing of the past.

Figure 3: Broken Links in Namibia's Agriculture Value Chain



African Housing/Property as an Asset Class for Pension Funds

The demand for housing in Africa is at its highest as more than 40% of the continent's one billion people now live in cities compared to 28% in 1980 and by 2030, this is projected to rise to 50% and Africa's top 18 cities will have a combined annual spending power of US$1.3-trillion. Despite increased urbanization and growth in the middle income class, the supply of housing falls short of demand causing a massive housing deficit and continued rising property prices. The housing market is set to undergo a shift as major players are re-aligning themselves to the new realities of urbanization and the housing deficit. Pension funds are well suited to invest in housing and property market given the long-term nature of their asset holding.

Infrastructure as an Asset Class for Pensions Funds

Infrastructure is considered to be a vital part of every country's growth and development. Unlike Western developed nations, the case of Africa's infrastructure is considered to be in a dire state; hence, requiring intensive investment. From the road networks to infrastructural facilities that provide basic amenities to citizens such as hospitals and schools, African governments are constantly faced with a huge infrastructural gap. Traditional sources of financial resources have mainly been from foreign investors, foreign aid and meager revenue from national taxes. Billions if not trillions of dollars is what African countries need to finance the construction of airports, ports, bridges, electricity power lines and roads. Although some African countries still have a low pension cover among the working citizens, African governments have come to a realization that pension fund savings provide a stable and long term source of infrastructural financing. Through investment opportunities such as infrastructural bond, pension fund have been encouraged by African governments to make investment in the infrastructure sector. A case in point is in Nigeria where the government has allowed pension funds to invest as much as 15 percent into infrastructural bonds. Nigeria's ARM infrastructure is working towards raising about 250 million dollars in is called an infrastructure fund for investing building of transportation systems and energy utility. In the case of South Africa, liberalized regulations have allowed pension funds to use up to 15 percent of their capital assets in investing in alternative investment opportunities such as infrastructure.

Contributions of Pensions Funds towards Poverty Alleviation

Poverty is a thorny issue in the African continent which has the highest records of citizens living below the poverty line. A number of factors can be attributed to the rising levels of poverty in Africa, which range from high unemployment levels, low literacy levels to lack of proper government poverty alleviation policies. By fostering and growing the small and medium sectors, African governments understand the role this sector of the economy can play in alleviating poverty levels in the continent. This is where pension fund savings and assets can contribute by establishing **social entrepreneurial funds** for entrepreneurs that wish to borrow money for start-ups or expansion of their small and medium enterprises. Pension fund savings and assets can contribute to alleviating poverty among the elderly citizens in an African country. According to the International Labour Organization (ILO), Africa has the lowest level of social security coverage in the world and Sub-Saharan Africa has less than 10 percent of the population covered by any social security fund. Economic analysts point to the fact that provision of social support to the public can enhance the process of development just like other sectors of the economy such as health and education. In particular when it comes to the elderly citizens, pension fund savings and assets providing financial support for them to meet their basic needs such housing, clothing and food can alleviate poverty at this level significantly. In South Africa, 46 percent of pension spending among the elderly persons goes to food, which is followed by 12 percent under utilities. In fact there is a correlation between increasing social spending on the elderly as they become less dependent on their siblings and the entire community who might have other numerous financial commitments.

Conclusion

It is evident that pension funds have become major institutional investors at the global level. In the case of African pension funds, there is still immense untapped potential, which requires the efforts of the government, the private sector and the general public in order to unlock such potential. This is because Africa as a continent has a huge hunger for economic development but is short on much needed capital for growth and development. The fact that Africa is a youthful continent of over a billion people, with a growing working-age population and rapid urbanization, will further support rising income and middle class expansion. This, combined with strong economic growth prospects, will offer great opportunities for both marketers and investors. Africa's middle class are aspirational. They value education for their children, as they want to break the poverty cycle. As a result, the education sector will present good growth prospects, as educational providers in the private sector can fill in the gap left by state schools. The rise of the middle class in Africa will also offer opportunities for the financial services sector, as aspiring middle-class consumers will be increasingly willing to take up loans, consumer credit and other financial services.

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