AFRICA

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KATIE KOCH
SENIOR PORTFOLIO STRATEGIST, GOLDMAN SACHS

Katie Koch, Senior Portfolio Strategist and Chief of Staff for the Goldman Sachs Asset Management Office of the Chairman, joined Goldman Sachs in 2002 as an analyst and was named Managing Director in 2011.

Her colleague, Jim O'Neil, now Chairman of Goldman Sachs, coined the term BRIC in 2001 to identify Brazil, Russia, India and China as the world's fastest growing economies.

ANTHONY EATON
MANAGER, JM FINN GLOBAL OPPORTUNITIES FUND

Anthony Eaton joined JM Finn in 2001 and started managing the Global Opportunities Fund in 2004. Africa is an area he is particularly positive on.

He notes the average income on the continent is rising, boosting the spending power of 1bn people. In addition 50% of the population is under 15 years old, leaving huge scope for growth in future consumption. Approximately 25% of revenue generated by companies in the portfolio comes from Africa, and he also manages a specialist Africa fund.

MARK DAMPIER
HEAD OF INVESTMENT RESEARCH, HARGREAVES LANSDOWN

Mark joined Hargreaves Lansdown in 1998 as Head of Research and is one of the most quoted figures in the national media, making regular appearances on TV and radio.

He contributes to The Times and The Telegraph and writes a weekly column for the Independent on Saturday.

Today we're going to focus on Africa. Political unrest and corruption continue to make investors wary of this region and have done little to enhance its lowly reputation. However, Africa is now considered by many to be one of the developing regions with the most potential.

The continent has a population of over a billion with growing urbanisation. By 2025 there will be over 60 cities with more than a million inhabitants. It also benefits from vast mineral resources, being home to 8% of the world's oil reserves and 7% of natural gas reserves, and a major exporter of both.

To discuss the investment case for Africa we have interviewed Anthony Eaton, manager of the JM Finn Global Opportunities Fund, Katie Koch, Senior Portfolio Strategist at Goldman Sachs Asset Management, and Mark Dampier, Head of Research at Hargreaves Lansdown.

Q: Anthony, you've highlighted the investment case for Africa for several years. Why are you so excited about the opportunities there?

Anthony Eaton: The average age in Africa is about 20. In Asia it's about 30. In contrast, in Europe it's 40 and in Japan they sell more diapers for old-age people than babies.

The African population is also

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growing at 2.2% annually compared to around 0.9% in Asia. In about 15 years' time, the African population is forecast to be about 1.5 billion, so by then it will be one of the biggest working populations on the planet.

Productivity has also been rising in Africa since 2000. Previously growth in Africa relied on population growth alone but now you are seeing growth in productivity on top of that. This is all feeding through into rising consumption, which is the widest-margin story in Africa. Exporting commodities is a low-margin trade and gets them off the ground, but it's when they start to consume internally that the story gets really interesting.

Income has virtually doubled since 2000, and private consumption in Africa is already as big as it is in India and Russia, which are much more universally understood investment areas. Most forecasts anticipate consumption in Africa will double again by 2020, which would put it at the same level as China in 2009.

Another reason I like Africa is because where knowledge is least, margins are greatest. I was talking to a global container terminal operator for example. In Africa margins per container are $250, in Latin America $125, in Asia $100 per container and in China $50. Africa has got everything going for it in my view.

Q: Do you think concerns such as political instability and corruption outweigh the advantages you've just outlined?

Anthony Eaton: I think that view is out of date. There was a survey done by Ernst and Young recently that showed the businesses who operate in Africa rate it second only to Asia as a place to do business. Some of the respondents who don't do business in Africa rate it as the worst place in the world to do business, so the people who are aware of what's going on have really moved on from this thing about corruption.

One definition of corruption is where a buyer and a seller trade with each other on a non-competitive basis, a cosy deal in other words. That definition of corruption has really expired in Africa.

For instance, the Democratic Republic of Congo (DRC) is an area people perhaps fear and perceive to be corrupt. Six or seven years ago they were short of money and dished out mining licences on a non-competitive basis, which you could argue is corrupt. However, since then all those contracts have been renegotiated on a bidding basis. The DRC government told the miners to pay more or sell out and 90% of the miners agreed. The one outfit that resisted was First Quantum Minerals; their licence was taken away because they wouldn't pay more and was given to Eurasian Natural Resources. They all went to court in the DRC, the process of law resolved the issue and DRC paid billions of dollars to First Quantum.

So I don't think you need to worry about corruption in Africa; if you look at Europe, it's rotten to the core!

Q: Mark, do you think the view of Africa as a corrupt place still puts people off investing?

Mark Dampier: Absolutely. It's mainly a Western media thing, although some of it may be true. It's going to be hard to dislodge people from that view. 25 years ago when I first saw and liked the concept of emerging markets, there were all sorts of political and economic problems in those countries, but here we are 25 years later: emerging markets have become mainstream.

Africa is where global emerging markets were perhaps 20 years or so ago. If Anthony's right, what a fascinating area to invest in. However, if you are investing purely in Africa it should probably be a very small part of a larger portfolio and one you would put in the bottom drawer and hold for the next 20 years. I wouldn't be trying to trade in and out of Africa because I don't think that's the way to look at it.

Q: Anthony, are there any particular countries you would pick out as offering the best opportunities?

Anthony Eaton: Our interests lie in Sub Saharan Africa, not in North Africa. The two regions are very different. We are interested in the middle belt of countries such as Nigeria, Congo and Kenya, where we see the most progress.

South Africa has political issues; they're not as bad as they are represented in the Western media, but they do exist. South Africa also has a relatively small population (around 50 million whereas Nigeria has around 160 million people with an average age below 20, so it is much more exciting).

In addition, it's worth pointing out the comparison between Africa now and Asia 20 years ago. Twenty years ago Asians were slaughtering each other in the Mekong Delta; the continent was at war until very recently. Countries like the Philippines and Indonesia, which are now go-to areas for investment, were run by dictators. In Africa today there are no large-scale wars at all. Most of the countries in Africa are democracies and most have had several elections by now, including DRC.

Q: Katie, I know you are particularly interested in Nigeria as an investment opportunity. Why is that?

Katie Koch: Yes, absolutely. I think investors sometimes make the mistake of looking at Africa as homogenous. In the North you have countries that are more tied to the Middle East, in the very South you have South Africa, which is a much more mature economy, and has a much less exciting demographic profile. Then you have a huge range of other countries across Sub Saharan Africa and by far the one we're most excited about is Nigeria.

Investing by definition is a forward-looking endeavour. When we look at which countries are going to matter most to the world in the future, Nigeria is one of them. It has 160 million people with a median age of 19, so it is incredibly attractive demographically. We think it's one of the countries most likely to rank among the BRICs in terms of importance to the global economy in the future.

There are two investment themes in Nigeria I would highlight as being particularly interesting.

The first is the consumer opportunity generated by that very attractive demographic profile. You need to think of the consumer on a small scale. For example, we have exposure to a company that makes chicken stock cubes. In a country where most of the people are living on less than $2 a day, they can't afford the protein but they can afford protein flavouring. Chicken stock cubes are fortified with iodine, which is very important for brain development. The advertising targets Nigerian mothers who care greatly about the welfare of their children. It's a product that is small in scale but huge in terms of impact. 50 million of those are sold a day throughout Nigeria.

The second theme I would highlight is infrastructure. This country is literally in the process of being built and that is throwing up all sorts of interesting investment opportunities. In order to grow strongly, Nigeria needs to address its power issues. Specifically, only 20% of power in the country is generated off the main power grid. The rest of the power is generated off diesel power generators which are a very inefficient and expensive power supply. Solving these power issues is going to massively speed up growth rates, and there's lots of investment opportunities set to profit by being focused on the power sector.

Q: Do you invest directly in companies based in Africa or through Western companies doing business there?

Katie Koch: We invest directly in companies in Africa. In the case of Nigeria we are invested in companies listed on the Nigerian stock exchange, although we have to be very selective. It's a very interesting story but we need to do all the due diligence. We are not invested in the full public equity market but we do find a couple of companies benefiting from some of those schemes that I highlighted, run by good management teams, with strong balance sheets and attractive valuations.

There are also a lot of well-run companies in South Africa benefiting from growth in other parts of Sub-Saharan Africa and Nigeria. For example, there are mobile phone operators listed in South Africa that have a lot of subscriber growth in Nigeria. Mostly, however, we invest directly in Sub-Saharan Africa.

Q: Anthony, what is your approach to investing in Africa?

Anthony Eaton: Our interest in Africa is threefold: what the continent can export to the global economy that the global economy needs; the domestic consumption that triggers by bringing money from the outside world; and thirdly the infrastructure it builds. By definition, we are taking a top-down view and are led to bigger-scale businesses. Some of the best businesses operating in Africa have colonial origins and are not listed there. For example, we have a business with five million acres of hardwood forest in Gabon in Congo, West Africa. That company is listed in Paris. We have a business that operates more port concessions, warehouses and trucking fleets in Africa than any other business in the world, also listed in Paris, so you don't only need to invest in Africa-listed businesses.

Indeed, some of the best businesses from our perspective aren't there. Do we want to invest in a computer peripherals business in Nairobi? No, we're not interested in that. We are interested in the businesses that are going to build the eleven billion project from Lamu seaport up to South Sudan, and put in place all the logistics for the entire East Africa area.

Q: Could you give us some more examples of companies that you are particularly excited about?

Anthony Eaton: I've just come back from Africa where I did a lot of internal flights. When I read the in-house magazines I was very struck by the commercials which were for nightclubs, Range Rover Discoveries, cosmetics, education, hospitals etc. These are adverts for Africans not for foreigners.

On the same vein we have built up positions in several fashion businesses listed in South Africa, operating across Africa. One we are invested in is called Foschini. It sells expensive, fashionable stuff to young Africans on their way out to the nightclubs. There's a fortune to be made from the rising consumption in Africa.

There is a Knight Frank index of the world's property hotspots. Last year the greatest rise in desirable properties took place in Nairobi and on the Kenya coast. Value is being added in Africa so quickly and so strongly.

Q: Mark, what do you think is the best way for investors to access this growth potential?

Mark Dampier: Anthony runs an African fund and a global fund focused on urbanisation. What Anthony is saying, you could have said in 18th and 19th century England and in America as well. It's just a huge industrialisation story – everything we take for granted in the West is what they want and are beginning to get.

This is why it's quite difficult for the West. In a normal recession the price of oil would have probably dropped to $10 or $20 a barrel but it's still over $100 a barrel. Why? Because all these people want what we have so I think that's the most exciting story.

How you access that depends really on your own risk profile. Clearly the potential is there but people have heard potential before. You could invest a very small part of your portfolio (1-2%) in a single country fund or an African fund, or go for a more general fund. You could specifically invest in the companies yourself, but now we are really drilling down to higher risk. I think most investors should take the theme and buy the funds.