SOVEREIGN WEALTH FUNDS as a driver of African development
Sovereign wealth funds (SWFs) are becoming important sources of development finance in many countries. African SWFs have been growing in recent years, as many countries joined the international trend in establishing SWFs, while many others are preparing to join. Growth of SWFs has been driven by rising commodity prices until 2014 and improving economic growth rates. At the same time, Africa continues to face a number of development challenges, raising the question of whether SWFs can play a role in fostering economic development on the continent. This paper analyses the dynamics and role of SWFs in promoting development in Africa. The paper notes that SWFs can play a more active role in Africa’s development by bridging the infrastructure funding gap, supporting industrial development and economic diversification, reducing macroeconomic volatility and enhancing intergenerational equity. For SWFs to be effective in delivering their mandates and supporting economic development, they need to have clear goals and objectives, improve their governance and transparency frameworks, improve their risk management frameworks and embrace the Santiago Principles. African governments need to develop more attractive frameworks and climates for SWFs to invest in the continent, especially in sectors that contribute more directly to addressing Africa’s development needs.
INTRODUCTION

Sovereign wealth funds are investment vehicles that manage portfolios of assets – owned and managed directly or indirectly by governments to achieve national objectives. They mostly derive their wealth from balance of payments surpluses, official foreign currency reserves, and fiscal surpluses and privatization receipts.

Traditionally, SWFs have focused on stabilizing fiscal and/or foreign exchange revenues and accumulating of savings for future generations. Recently, they have moved to support strategic economic sectors for economic development. SWFs have grown in number, size, scope and complexity, gaining prominence as important sources of finance for development. Globally, assets under management by SWFs have grown rapidly in recent years, topping US$7.4 trillion in 2016, more than double the asset base in 2008 (Sovereign Wealth Fund Institute, 2015). About 57 percent of assets under management of SWFs are derived from oil and gas. African countries have also joined the bandwagon in establishing sovereign wealth funds in recent years, with assets under management topping over US$159 billion (6.4 percent of Africa’s GDP) by 2015 (African Capital Markets, 2015). The rapid growth of SWFs has been driven by high commodity prices since the early 2000s.

The recent discoveries of oil, gas and solid minerals in many African countries (e.g. Kenya, Uganda, Tanzania, Madagascar, Mozambique, and Guinea), coupled with strong economic growth in most countries, has also led to the establishment of SWFs in recent years. Despite the plunge in oil and commodity prices since 2014, SWFs continue to increase in number and in assets under management.

The unprecedented growth of SWFs is happening at a time when Africa is facing a number of development challenges: high unemployment rates amid growing youthful populations, high poverty and inequality rates, macroeconomic volatility induced by recurring fluctuations of commodity prices and burgeoning informal sectors.
The continent also presents huge opportunities that can be tapped to foster economic development: favorable demographics of youthful populations, rapid urbanization, rising middle classes and abundance of natural resources. This disconnect raises the question of whether SWFs can play a role in catalyzing economic development in Africa.

This report analyses the potential role that SWFs can play in fostering economic development in Africa. It analyses the dynamics on SWFs and the current investment strategies, while evaluating ways in which SWFs can stimulate development of the continent. It also draws some lessons and best practices in managing SWFs to maximize their economic impact for the benefit of Africa’s citizens, based on international experiences.

The paper argues that SWFs present an opportunity to support economic development in Africa. They can help to cover Africa’s huge infrastructure financing deficit, support industrial development and economic diversification, help to reduce macroeconomic volatility, and enhance intergenerational equity by accumulating assets for future generations and catalysing innovation and productivity growth. For SWFs to be effective in delivering their mandates and support economic development, they need to have clear goals and objectives, improve their governance and transparency, have medium to long-term strategic asset allocation linked to their objectives, broaden their investment horizons and embrace the Santiago Principles, which set guidelines for best practices.

The structure is as follows: Section 2 analyses the dynamics of SWFs in Africa. Section 3 explores the asset allocation and investment strategies of African SWFs. Section 4 highlights Africa’s development challenges and contributions of SWFs to the continent’s development, while section 6 evaluates some lessons and best practices for managing SWFs. Section 5 concludes and provides policy recommendations.

Globally, assets under management by SWFs have grown rapidly in recent years, topping **US$7.4 trillion** in 2016 *more than double the asset base in 2008*
SOVEREIGN WEALTH FUNDS IN AFRICA

SWF assets have grown over recent years, accelerating between 2009 and 2013, riding on the super-cycle commodity prices. Since 2014, SWF assets have started to grow at a slower pace as commodity prices declined, amid sluggish global economic growth and a slowdown in the Chinese economy.

The resulting decline in export receipts and the reduction in foreign exchange reserves have lowered the rate of injection of new assets into SWFs and led to partial redemptions of SWFs to cover budget shortfalls. Global SWF assets, which increased by 18 percent between 2012 and 2014, slowed to about 1.4 percent between 2014 and 2016 to reach US$7.4 trillion assets in 2016 (Figure 1). PWC (2016) projects global SWF assets under management to exceed USD8 trillion by 2020. The largest SWF in the world is the Norwegian Government Pension Fund Global, with $922.1 billion of assets under management as of March 2017. While the biggest sovereign wealth funds are in Europe, Asia and the Middle East, African sovereign wealth funds have continued to grow in recent years. In 2009, assets under African SWF management were about US$114.27 billion, but increased by 39% to reach US$159 billion in 2015. They are expected to grow further as more countries set up their own SWFs (African Capital Markets, 2015).

Africa is the most dynamic region of the world in terms of sovereign wealth fund creation. It had 20 sovereign wealth funds as of 2016 (Table 1).

Fig 1: Total Assets under SWF Management in the world (US$ Trillion) 2008-2017

Source: SWFI, 2017
Before 2010, there were only 10 sovereign wealth funds. Fifty percent of SWFs were established in the last six years, including Ghana, Angola, Nigeria, Senegal, Rwanda, Tanzania, South Sudan, Kenya and Zimbabwe, illustrating the rapid growth of SWFs in Africa. Only six African SWFs have assets over US$1 billion, led by the North African oil producing countries (Algeria and Libya). Algeria’s Fonds de Régulation des Recettes, which was established in 2000, tops the league of SWFs with about US$77.2 billion in assets under management, followed by the Libyan Investment Authority (LIA) (set up in 2006), with an estimated US$67 billion of assets under management. Algeria and Libya’s sovereign wealth funds account for about 89 percent of SWF assets in Africa.

The Botswana Pula, established in 1994, is the oldest and third-largest SWF in sub-Saharan Africa, boasting US$6.9 billion in assets. It is followed by the Fundo Soberano de Angola (established in 2012), which takes the fourth place with initial assets of US$5 billion. Congo Republic and Morocco’s SWFs have US$1.64 billion and US$1.4 billion, respectively, while the sovereign wealth funds of Nigeria and Ghana are among the smallest and relatively newest on the continent with US$1.4 billion and US$0.54 billion respectively. Other countries with smaller SWFs include: Senegal, Chad, Equatorial Guinea, Gabon, Kenya, Mauritania, São Tomé and Príncipe, Sudan and Tanzania, which all depend on commodities, especially oil and gas. Rwanda and Senegal’s SWFs do not depend on mineral commodities. A number of countries, including South Africa, Egypt, Namibia, Sierra Leone, Uganda, Zambia, Liberia, Mozambique and Mauritius, are candidates likely to establish SWFs soon. However, the growth of SWFs in Africa is expected to slow down in the next few years because of lower commodity prices, which are not likely to return to historical super high prices soon, and the slowdown in China.

Table 1: Sovereign Wealth Funds in Africa

<table>
<thead>
<tr>
<th>Country</th>
<th>Name of SWF</th>
<th>Establishment</th>
<th>Assets under Management (US$ Billion)</th>
<th>Source of Funding</th>
</tr>
</thead>
<tbody>
<tr>
<td>Algeria</td>
<td>Fonds des Régulation des Recettes</td>
<td>2000</td>
<td>77.2</td>
<td>Oil</td>
</tr>
<tr>
<td>Libya</td>
<td>Libyan Investment Authority</td>
<td>2006</td>
<td>67</td>
<td>Oil</td>
</tr>
<tr>
<td>Botswana</td>
<td>Pula Fund</td>
<td>1994</td>
<td>6.9</td>
<td>Diamonds</td>
</tr>
<tr>
<td>Angola</td>
<td>Fundo Soberano de Angola</td>
<td>2012</td>
<td>5</td>
<td>Oil</td>
</tr>
<tr>
<td>Gabon</td>
<td>Gabon Sovereign Wealth Fund</td>
<td>1998</td>
<td>2.4</td>
<td>Oil</td>
</tr>
<tr>
<td>Congo Republic</td>
<td>Fonds de Stabilisation de Recettes Budgetaries</td>
<td>2005</td>
<td>1.64</td>
<td>Oil</td>
</tr>
<tr>
<td>Nigeria</td>
<td>Nigeria Sovereign Investment Authority</td>
<td>2012</td>
<td>1.4</td>
<td>Oil</td>
</tr>
<tr>
<td>Morocco</td>
<td>Morocco Sovereign Wealth Fund (Ithmar Capital)</td>
<td>2012</td>
<td>1.4</td>
<td>Oil</td>
</tr>
<tr>
<td>Senegal</td>
<td>Senegal Fonsis</td>
<td>2012</td>
<td>1</td>
<td>Non Minerals</td>
</tr>
<tr>
<td>Ghana</td>
<td>Ghana Petroleum Funds</td>
<td>2011</td>
<td>0.54</td>
<td>Oil</td>
</tr>
<tr>
<td>Mauritania</td>
<td>National Funds for Hydrocarbon Reserves</td>
<td>2006</td>
<td>0.3</td>
<td>Oil and Gas</td>
</tr>
<tr>
<td>Equatorial Guinea</td>
<td>Future Funds for Generations</td>
<td>2002</td>
<td>0.08</td>
<td>Oil</td>
</tr>
<tr>
<td>Chad</td>
<td>Fonds de Stabilisation de Recettes Budgetaries</td>
<td>2006</td>
<td>0.03</td>
<td>Oil</td>
</tr>
<tr>
<td>São Tomé and Príncipe</td>
<td>National Oil Account</td>
<td>2004</td>
<td>0.01</td>
<td>Oil</td>
</tr>
<tr>
<td>Sudan</td>
<td>Oil Revenue Stabilisation Fund</td>
<td>2008</td>
<td>0.2</td>
<td>Oil</td>
</tr>
<tr>
<td>Rwanda</td>
<td>Agaciro Development Fund</td>
<td>2013</td>
<td>0.041</td>
<td>Non Minerals</td>
</tr>
<tr>
<td>Tanzania</td>
<td>Natural Gas Reserve</td>
<td>2013</td>
<td>–</td>
<td>Gas</td>
</tr>
<tr>
<td>Kenya</td>
<td>Kenya Sovereign Wealth Fund</td>
<td>2014</td>
<td>0.12</td>
<td>Minerals</td>
</tr>
<tr>
<td>South Sudan</td>
<td>Oil Revenue Stabilisation and Future Gener. Fund</td>
<td>2013</td>
<td>–</td>
<td>Oil</td>
</tr>
<tr>
<td>Zimbabwe</td>
<td>Zimbabwe Sovereign Wealth Fund</td>
<td>2014</td>
<td>–</td>
<td>Minerals</td>
</tr>
</tbody>
</table>

African SWFs are largely commodity based, with 15 being sourced from oil and gas, three from other minerals, and two from non-commodity sources. About 83 percent of African sovereign wealth fund assets are drawn from oil and 17 percent from minerals and other sources. Partly given their role in smoothing out economic and fiscal cycles, most African SWFs have at least a stabilization purpose. According to the SWFI, African SWFs have low levels of transparency, as measured by the Linaburg-Maduell Transparency Index, compared to other SWFs of the world. However, there is visible progress, with more SWFs adopting the Santiago Principles.

Historically, SWFs have been established for the purpose of economic stabilization, and intergenerational savings accumulation and wealth diversification. But recent developments have seen sovereign wealth funds being used for domestic economic development (e.g. infrastructure development). Economic stabilization advances the goal of smoothing revenues and expenditures, which are associated with fluctuations in commodity prices. The stabilization motive aims to manage and mitigate the effects of high volatility of government revenues and expenditures emanating from volatile natural resource revenues. Macroeconomic stabilization is the most common objective of SWFs in Africa. The investment horizon of this mandate is usually short to medium term and places a lot of emphasis on liquidity.

The intergenerational savings motive focuses on building a reserve or saving to provide for future generations when the resource has been depleted. They aim to transform non-renewable assets into diversified financial assets for future generations, thereby achieving inter-generational equity. Wealth diversification reflects the desire to minimize economic risks from volatile natural resource rents and prudent management of the country's assets. It aims to limit the adverse effects of a high degree of dependence on natural resources and represents some kind of self-insurance, capital preservation and liquidity concerns and is associated with a short to medium term investment horizon (Griffith-Jones and Ocampo, 2010).

The economic development motive is concerned about setting funds to support strategic economic projects, infrastructure and industrial development, which drives productivity, structural transformation and long-term economic development. For example, Ghana, Nigeria and Angola have established sub-funds within their SWFs to develop infrastructure and drive industrial development and structural transformation. These funds usually have long investment horizons and illiquid assets, such as infrastructure and private equity. Most African SWFs have an umbrella model of SWFs, which covers stabilization, funding future generations and economic development. Some selected SWFs in Africa are elaborated upon below.

Lybian Investment Authority

US$67 billion

The Libyan sovereign wealth fund, called the Libyan Investment Authority (LIA), has an asset base of US$67 billion, sourced from oil revenues. The fund is composed of the Future Generation Fund, Local Development Fund and Budget Stabilization Fund. Its purpose is to create a diverse wealth portfolio for Libya's future generations, provide stability against volatile oil prices, and stimulate the economy through major transformational private sector projects and infrastructure development. While the future generation fund and the local development fund are long–term in nature, the budget stabilization fund invests in short-term instruments. The LIA also invests in infrastructure projects, both in Libya and elsewhere in Africa (LIA, 2015).
Botswana's Pula Fund

**US$6.9 billion**

Botswana’s Pula Fund was created in 1994 and now boasts assets amounting to $6.9 billion. It aims to preserve part of the income from diamonds for future generations. Excess reserves are transferred to the Pula Fund and are largely invested in foreign currency denominated assets, especially public equity and fixed income instruments in developed countries (Bank of Botswana, 2015). The objectives of the fund include a short-term stabilization objective and a long-term investment objective aimed at ensuring that assets are available for future generations in a situation where Botswana’s natural resources (predominantly diamonds) are depleted. The Pula Fund cannot be used in any quasi-fiscal/off-budget operation to finance investment or the purchase of goods and services outside the government budget framework. If the need arises to enable the Government to pursue agreed national development objectives, the Pula Fund could be drawn down.

Fundo Soberano de Angola

**US$5 billion**

Angola’s SWF was established in 2012 with an asset base of US$5 billion. It aims to achieve capital preservation, maximize investment returns, develop infrastructure and provide support to certain strategic sectors such as agriculture, mining, hospitality, healthcare and timber in Angola and the SSA region. It targets investments that generate long-term and socially enhancing financial returns, while promoting Angola’s social and economic development and generating wealth for its population. The FSDEA is an ‘umbrella fund’ with multiple goals with a broad objective of pursuing investments that generate long-term and sustainable financial returns to promote Angola’s social and economic development. It allocates 7.5 percent of its endowment to social development projects that are vital for the socioeconomic development of Angola (FSDEA, 2016). About US$1.1 billion so far has been dedicated to infrastructure development, which covers energy, transport and industrial development. The fund has about 50% of its resources in low-risk assets (sovereign or institutional bonds rated investment grade), while 50% of its funds are invested in emerging markets and priority investment sectors in Africa. The FSDEA intends to allocate approximately one-third of its initial endowment to interest bearing financial assets, the other-third to various investment vehicles and sectors mainly in emerging and frontier markets, and the others in investing in Angola and across other African markets in sectors such as agriculture, mining, infrastructure and real estate. In April 2015, the FSDEA entered the private equity asset class and has made subsequent investments to its five dedicated and self-created investment funds, focusing on mining, timber, agriculture, healthcare and structured capital through a separate mezzanine fund. Its investment policy seeks to build a diversified portfolio by both geographical spread, industries and asset classes, including global private and public stocks, bonds, foreign currencies, financial derivatives, commodities, treasury bills, and real estate and infrastructure funds, in accordance with its investment policy and guidelines. Over time, the fund can invest 55 percent of its investment portfolio in asset classes with higher potential returns over a long investment horizon, with recourse to a maximum financial leverage of three times its equity value (SWFI, 2017).

Rwanda’s Agaciro Development Fund

**US$41 million**

Rwanda’s Agaciro Development Fund (AGDF) was launched in 2012 and is not based on minerals. It is built from contributions from Rwandans at home and abroad and other partners and friends. Assets under management are currently estimated at US$41 million. The AGDF focuses on building a sustainable fund for current and future generations, maintaining self-reliance and stability in times of adverse shocks to the economy and accelerating the socio-economic development of Rwanda (AGACIRO, 2015). It currently invests largely in short term deposits and treasury bonds in the local market, but plans to diversify its portfolio in other sectors of the economy in the future.
The Nigeria Sovereign Investment Authority (NSIA) was established in 2012, with an asset base of US$1.4 billion and funded from oil and gas revenues. It has three priority areas, which include an Infrastructure Fund (40 percent), Future Generations Fund (40 percent), and Stabilization Fund (20 percent). The stabilization fund aims to provide support and a buffer against external shocks. This fund has a short investment horizon and is mainly managed in-house in a diversified portfolio of liquid, low risk products such as Treasury bills and liquid short term investment grade bonds. The Future Generations Fund was established to safeguard oil revenues for future generations. The Infrastructure Fund focuses on domestic infrastructure development, including power, gas, transport, agriculture and health care, housing and water resources, etc. The objective of the Infrastructure Fund is to invest in domestic infrastructure projects either directly or as a leverage to attract private capital in a public–private sector partnership in order to stimulate economic diversification, job creation and ultimately growth. The NSIA has partnered with other financial institutions and investors such as the International Finance Corporation (IFC), General Electric (energy) and Julius Berger (bridge construction) to develop, finance and implement infrastructure projects that will stimulate job creation, economic growth and social development in Nigeria.

Gabon's SWF

US$2.4 billion

Gabon's Sovereign Wealth Fund (SWF) was established in 1998 and has an asset base of US$2.4 billion. It aims to increase the capture of revenue from the country's natural resources; support the growth of small and medium-sized local enterprises through direct investment; diversify government revenues and mitigate risk from volatile commodity prices. It also aims to support long-term investments in strategic projects that drive economic diversification in Gabon, including agriculture, forestry, energy and other infrastructures, hospitality and tourism, telecommunications and banking. The SWF is funded from a 10 percent levy on government oil revenues. Like most other African SWFs, the Gabon SWF includes stabilization, intergenerational savings and economic development objectives. The fund aims to follow Norway's SWF in using a portion of investment proceeds to fund the budget. Gabon's SWF has provided capital for the €301 million Infrastructure Public-Private Partnership (PPP) Africa Fund, which focuses on greenfield infrastructure projects and PPPs; and the €200m Agriland Fund, which targets processing and supply-chain activities. Among Agriland's investments is an industrial chicken-processing facility in Gabon. The SWF also owns a port development company, Société de Developpement des Ports (SDP), which was established in 2012 to upgrade port facilities throughout the country. It is also investing in South African SFM Group's multi-use Grande Mayumba Project, has taken a stake in the Port Mole redevelopment project in Libreville and partnered with France's Telespazio to establish a cartographic data and environmental monitoring station in Gabon known as Earthlab. Furthermore, it is working on a feasibility study for a greenfield rail line.

Senegal's FONSIS

US$1 billion

Senegal’s Fonds Souverain d’Investissements Stratégiques (FONSIS) was established in 2012 and has an asset base of US$1 billion. It focuses on managing and growing state assets, and setting aside financial reserves for future generations, while distributing regular dividends to the state (FONSIS, 2015). It also aims to boost the use of the country’s assets in productive investments for jobs and wealth creation for present and future generations. FONSIS will initially invest in Senegal only, and later invest abroad, as assets grow. It aims to attract institutional investors to Senegal, generate financial returns for current and future generations and optimize state-owned assets.

Ghana's SWF

US$540 million

Ghana’s sovereign wealth fund, the Ghana Petroleum Fund, was formed in 2011, initially with two sub-funds: the Ghana Heritage Fund and the Ghana Stabilization Fund. The Heritage fund is an investment for future generations, while the stabilization fund aims to cushion the impact of revenue shortfalls in times of economic stress. The Infrastructure Investment Fund was later established in 2014 and provides financial resources to a diversified portfolio of infrastructure projects within Ghana. The infrastructure fund focuses on developing strategic infrastructure, to be developed through partnerships with the private sector and other financiers. Total assets under management are about US$540 million.
ASSET ALLOCATION AND INVESTMENT STRATEGIES OF AFRICAN SOVEREIGN WEALTH FUNDS

Asset allocations of African SWFs vary widely, depending on their specific investment objectives and mandates, and the complexity of the funds. For instance, SWFs that focus more on fiscal stabilization have a higher weight on more liquid assets such as fixed income instruments and hedge funds. Their investment horizon is fairly short as they have the specific goal of managing macroeconomic shocks and providing stability to a government’s revenue stream. These funds are allocated to low-risk and low-return assets as their need to provide a stable income stream and have a greater need for liquidity.

Funds for future generations whose liability profiles are multi-generational in nature have usually had long investment horizons with higher target returns. They favour relatively diversified and low-risk portfolios and illiquid assets such as infrastructure, public equity and private equity, and real estate. Development funds are characterized by long-term investments, especially in infrastructure. Development Funds invest in illiquid and strategic assets which can stimulate economic development. Funds for development purposes place greater emphasis on target returns and allocate more of their capital to infrastructure and private equity.

Asset allocation of SWFs is also driven by the economic outlook, fiscal situations, market trends, investment beliefs, regulation and risk appetite and liability considerations (Croce, and Yermo, 2013). In the past decade, SWFs have been largely investing in external financial assets, especially securities traded in major markets. But now the trend is changing, as they seek to diversify their portfolios in terms of both asset class and geographic focus (Banque de France, 2012). SWFs are shifting from traditional asset classes (bonds and equities) to alternative assets such as real estate and infrastructure in search of higher yields. Alternative assets help to increase diversification and balance portfolios, while offering potentially higher returns and meeting institutional investors’ long-term investment objectives. African SWFs are also increasing investments at home to cover some pressing development needs.
The recent global economic uncertainty and decline in commodity prices has increased the need to draw down on assets to support government budget gaps, and slowed down capital injections into SWFs. The prolonged low oil prices and widening fiscal gaps will continue to drive SWF redemptions to cover fiscal deficits, reduce exposure to volatile equity markets and shift towards other assets such as infrastructure and real estate. The search for higher returns in the context of the low interest rate environment on traditional assets will continue to generate interest in non-traditional assets. The ability of SWFs to access asset classes that require long-term investment horizons, and the need to balance risk and return also remain important factors in shaping asset allocation dynamics of African SWFs.

Fixed income investments comprise the largest proportion of most portfolios. Recent data from Preqin (2015) shows that about 78 percent of African SWF investors invest in fixed income instruments, which reflects the dominance of the stabilization role in African sovereign wealth funds (Figure 2).

African SWFs are increasing their allocation to private equity as they seek higher returns, especially in the low-yield environment. Private equity investments offer portfolio diversification and potentially generate higher returns in the long term and benefit from an illiquidity premium. They are also less volatile compared with public equities. They are important in driving innovation, promoting economic development and creating employment – important facets in Africa’s economic development (Miceli et al. 2015). Technological breakthroughs and increasing productive potential are creating new industries and increasing opportunities for private equity. About 22% of African SWF investors invested in private equity in 2015 (Figure 2), reflecting a shift from traditional assets. Co-investments and direct investments are the preferred strategies for private equity among sovereign wealth funds seeking opportunities in Africa. The FSDEA invests about 39% of its assets in private equity, while the Libyan investment authority invests about 37% (Figure 3). NSIA’s portfolio in private equity is still low, at about 5%, but is poised to increase as it invests more in strategic economic sectors such as agriculture and telecommunications.
About \textbf{22 percent} of African SWF investors invested in \textbf{private equity} in 2015. Co-investments and direct investments are the preferred strategies for private equity among sovereign wealth funds seeking opportunities in Africa.

In the coming years, asset growth of SWFs together with the gradual shift to alternatives will generate more capital flows towards private equity, and SWFs will continue to utilize co-investments given their long-term investment horizons and ability to fund large investment tickets.

Public equities are still favourable, with a proportion of 44 percent of SWF investors investing in these assets. Sovereign wealth fund investments in public equities are driven by the desire to complement the long-term allocation to illiquid assets. Investments in public equities also serve as a way to support national policies by backing national development plans (Preqin, 2017). Public equities are likely to remain a key part of African sovereign wealth fund portfolios going forward, as many will look to rebalance their portfolios and diversify against macroeconomic shocks in their domestic economy.

Infrastructure seems to be gaining prominence among SWFs, with about 33 percent of African SWF investors having invested in infrastructure in 2015 (Figure 2). SWFs favor infrastructure investments for many reasons. First, infrastructure investments align very well with SWFs long investment horizon, coupled with limited or sometimes no explicit liabilities. Second, infrastructure assets provide potential stable, higher and inflation-protected long-term yields, coupled with lower correlation to other financial assets, which implies lower risk, which is ideal for SWF investments and risk profile (Croce, and Yermo, 2013). Infrastructure, together with other illiquid assets, benefits from liquidity premiums.

Figure 3: \textbf{Sovereign Wealth Fund Asset Allocation} of selected African SWF (2016)
Third, infrastructure allows SWFs to maximize investments’ risk-adjusted returns and accumulate resources for future generations. This is because once constructed, infrastructure assets are less vulnerable to economic downturns and can hedge against inflation, compared with other assets which are more cyclical, and making it more attractive to SWFs. Fourth, infrastructure offers strong portfolio diversification benefits, especially if combined with more traditional asset classes such as public equities and/or bonds. Fifth, infrastructure can help sovereign wealth funds to achieve economic objectives. Given Africa’s demographics and infrastructure financing gaps, channeling SWF resources towards infrastructure is a positive step towards building above-ground assets for future generations, while improving the productivity of businesses. Infrastructure can be a catalyst for economic diversification. With their long-term investment horizon, SWFs are better positioned to provide long-term capital for long term infrastructure projects in different sectors to support economic diversification. This is important given the scarcity of long-term finance on the continent and constrained liquidity of African financial institutions.

SWFs gain access to infrastructure assets’ direct investments, co-investments, joint ventures or public private partnerships (PPPs), listed funds, and indirect financing. Infrastructure investments will continue to attract institutional investors due to their solid fundamentals, including strong returns and perceived low risk and stable long-term cash flows. The FSDEA currently allocates about 23 percent to infrastructure, covering transport (deep water port) and energy which are key to its economic diversification and structural transformation. NSIA allocates about 40 percent to infrastructure, targeting transport, power, and telecommunications and water resources (Figure 3).

Public equities are still favourable, with a proportion of 44 percent of SWF investors investing in these assets. The proportion of SWFs with investments in hedge funds is low (22 percent), reflecting their complexity and short term volatility in the view of SWFs that seek investments with higher returns over a longer cycle.

In terms of sectoral allocations, a significant part of SWF investments in sub-Saharan Africa are in hotels, extractives and industrial development. Of a selected set of global sovereign wealth funds by Triki and Faye (2011), about 27 investments are in real estate and hotels, while 7 were in infrastructure (Figure 4). Most investments are in sub-Saharan Africa (21 for real estate and hotels and five for infrastructure), compared with North Africa (six for real estate and hotels and two for infrastructure). Investment in extractive industries and industrial development is higher than infrastructure in SSA, reflecting a skewed appetite for resource sectors. Investments in infrastructure have focused more on bankable projects, especially high-return existing infrastructure, rather than greenfield investments, suggesting that there is still room to allocate more funds into the infrastructure sector.
According to Turkisch (2011), SWF investments in Africa have recently focused on natural resources (hydrocarbons and minerals) and infrastructure linked with their extraction (ports and roads) in order to secure energy supplies and other strategic sectors which can help to diversify the economy. The allocation towards banking and financial sectors is lower in SSA than in North Africa, possibly because of risk concerns.

Angola’s FSDEA is targeting strategic economic sectors which can drive economic diversification, productivity and structural transformation in Angola and SSA, with higher return potential. It established seven funds for some strategic sectors: (i) the **Infrastructure Fund**, which targets investments in PPPs, privatizations and large industrial developments (ii) the **Hotel Fund**, aiming to invest in hotels and related assets in Angola and sub-Saharan Africa (iii) the **Timber Fund**, targeting investments in timber (iv) the **Mining Fund**, targeting mining investments (v) the **Agriculture Fund**, targeting agricultural investments (vi) the **Health Care Fund**, for health care related investments focusing on countries with the highest return potential and favorable government support for healthcare, including Angola and other SSA countries such as Cameroon, Ghana, Kenya, Mozambique, Nigeria, and South Africa; (iv) the **Mezzanine Investment Fund** targeting other emerging opportunities, including startups and venture financing. The mezzanine financing offering is positioned to meet the needs in sectors that are predominantly entrepreneur driven, a critical element that drives Angola’s prosperity.

**Figure 4**: Selected global SWF investments in Africa by sector and region

According to the SWF Institute, in considering areas to invest, SWFs seek out sectors where they have expertise, can navigate, find reliable local partners (government or private) and cherry pick at the right price (Sovereign Wealth Quarterly, Q4, 2015). As such, co-investment deals have increased recently, with African SWFs teaming up among themselves or with global SWFs or private partners, especially in private equity and infrastructure projects. This has largely been driven by the need to leverage investment partners’ knowledge and information and spread capital outlay and risks. The Ghana Infrastructure Investment Fund has partnered with Morocco’s Ithmar Capital to invest in various economic sectors. Ithmar capital has also partnered with Nigeria Sovereign Investment Fund to develop the Trans-African Pipeline project—a new regional gas pipeline connecting Nigeria and Morocco.
With many joint venture/co-investment deals among African SWFs, there is likely to be an increase in the number of joint venture entities targeting private equity in different sectors, including real estate and infrastructure in sub-Saharan Africa. SWFs from Asia and the Middle East are also showing great interest in Africa, and setting bases, targeting the African market and sourcing proprietary deals and lucrative opportunities. For example, China has set a fund (China–Africa Development Fund [CADFUND]) which is dedicated to the African region. By 2012, CADFUND had co-financed and supported 60 projects across 30 African countries (Fattah, 2015). Abu Dhabi’s Mubadala, Qatar Investment Authority, ACWA Power (Saudi Arabia), TAQA (Abu Dhabi) and QEWC (Qatar) invested significantly in Africa. According to the Dubai Chamber of Commerce report, the Gulf entities together have invested more than US$30 billion in African infrastructure in the last decade. The Seychelles’ huge wind power project and Algeria’s power plant were financed by Abu Dhabi’s US$60.9 billion fund.

Other SWFs in Africa are establishing small venture capital funds within their investment structures to support startups, small and medium enterprises. This is very important in the African context, since startups including those in the informal sector perform best when they are supported. For instance, Gabon’s Okoume Capital and Angola’s FSDEA are supporting entrepreneurial startups and innovation ecosystems. The FSDEA has allocated 7.5% to the Social Charter, which directs resources to viable projects that create sustainable wealth generation through entrepreneurial development. This trend is aligned with the rejuvenation of Venture Capital, which is becoming a common vehicle among global sovereign wealth funds.

**ROLE OF SOVEREIGN WEALTH FUNDS IN AFRICA’S DEVELOPMENT**

*Africa’s development challenges are numerous and quite unique. So are opportunities, which investors such as SWFs can tap to foster economic development. Africa continues to face high unemployment rates, with the current industrial structure not able to absorb all the available labour force, leaving millions of young people unemployed. The World Bank estimates youth unemployment at 29 percent of the population in North Africa and 13 percent of the population in Sub-Saharan Africa. There is, therefore, a great need for economic activities and industrial structure which creates jobs.*

Despite the fact that Africa boasts abundant natural resources, which have arguably been driving strong growth rates in recent years, poverty and inequality levels still remain elevated. About 41 percent of the population in SSA live on less than US$1.90 a day, compared with 15 percent in South Asia and 5.4 percent in Latin America (World Bank, 2016). Thus, African governments must implement policies that ensure that natural resource wealth fosters more inclusive growth and equity.
Can SWFs steer development to reduce poverty and inequality in Africa? The infrastructure needs are also huge. About 19 percent of roads in sub-Saharan Africa are paved, compared to 43 percent in South Asia, while less than 40 percent of the population have access to electricity. Physical and social infrastructure stocks in SSA are among the lowest in the world, with significant deficits in energy, transport and water resources. The poor state of infrastructure reduces growth by two percentage points every year and cuts business productivity by as much as 40 percent (World Bank, 2010). About US$93 billion is required annually to cover infrastructure needs, but only about half of this amount is being met. Hence, there is a need for new sources of infrastructure financing, as the traditional instruments are failing to cope with the huge funding gap. SWFs can certainly help.

On the corporate front, financing remains limited, as financial sectors are shallow and banks are liquidity-constrained, providing short-term funding. This has been worsened by the global financial crises. Short-term bank financing is not suitable for longer-term corporate financing, which raises the need for alternative financing schemes especially for long-term projects.

While many countries are endowed with natural resources, they mostly export unprocessed products, resulting in high commodity dependence, which leads to countries experiencing significant macroeconomic volatility and cyclical budgets. This calls for concerted efforts to design policies that help to stabilize economies. The size of informal sectors in Africa is also very large, with estimates of more than 50 percent of GDP for a number of countries. High levels of informality pose a challenge for fiscal revenue collections and, in most cases, is a sign of extensive unemployment and poverty.

At the same time, Africa is endowed with natural resources, which is the source of funds for most of the SWFs. It boasts over 10 percent of world reserves of oil, 40 percent of gold, 80–90 percent of chromium and the platinum group of minerals, over 50 percent of diamonds, over 85 percent of phosphate reserves, and many other minerals. It has about half of the world’s arable land, extensive fisheries and forests, abundant renewable and non-renewable energy resources and vast tourism potential. According to the IMF, about 32 countries in Africa are resource-rich, with 28 in SSA and 4 in North Africa. Clearly, the continent’s massive mineral wealth can be a catalyst for its development.

Africa’s population is booming. The continent’s population is set to double to 2.4 billion by 2050, with the percentage of the population living in urban areas expected to increase from 36 percent to 60 percent. At the same time, the growing population will be in need of jobs, infrastructure and other goods and services. This clearly presents an opportunity for institutional investors such as SWFs to tap into, while steering the development of the continent.
The continent is also undergoing rapid urbanization and its relatively young labour force and growing middle class makes it a new emerging market and destination for investment. The number of middle-class (defined as those earning between US$2 to US$20 per day) households in the region has tripled in the last 30 years, representing a growth rate of 3.1 percent (African Development Bank, 2011). The middle class is projected to continue to grow and reach 1.1 billion by 2060, representing 42 percent of the population (Ncube and Lufumpa, 2014). McKinsey (2010) projects that by 2030, the overall purchasing power of the populations of 18 of the largest cities in Africa could amount to USD 1.3 trillion. This represents a growing level of future demand for infrastructure and other consumer goods and services such as food, housing, telecommunications, energy, water and sanitation – with potential for high returns for SWFs and important drivers of economic growth.

SWFs can play a vital role in driving Africa’s development. Considering the huge infrastructure funding gap, estimates suggest that allocating 20 percent of SWF assets can cover Africa’s infrastructure funding gap for at least a year (Hove, 2016). In order to secure intergenerational equity, it is important for the SWF to invest in long-term assets such as infrastructure, whose benefits can be enjoyed across generations. This ensures that underground and finite resources such as oil, gold, copper and other minerals for example, are transformed into above-ground, long-term inter-generational assets like infrastructure. For example, Angola’s SWF is investing in large infrastructure projects such as the deep-water port in Cabinda and power plants. Nigeria’s SWF is investing in energy, roads and bridges and water resources, while Gabon’s SWF is investing in ports and railway lines. By investing in infrastructure, SWFs spread risk, reduce capital outlays and have an opportunity to earn higher returns. Investing in infrastructure could also boost non-resource growth and create a virtuous cycle of increased fiscal space (World Bank 2014).

**SWFs** can play an important role in reducing macroeconomic volatility, by utilizing stabilization funds as countercyclical fiscal tools.

While African SWFs can invest in the continent’s infrastructure, they are also in a position to attract other external SWFs to invest in infrastructure through co-investments and partnerships. SWFs can act as reliable partners to foreign SWFs/investors searching for low-risk opportunities in Africa. This means that African SWFs are strategically positioned to act as catalysts to attract more investments in the infrastructure and other industrial sectors and to reduce risk. They know the local terrain well, and understand risks in the local economy. Countries such as Nigeria, Ghana, and Morocco are partnering with foreign investors and financiers to develop infrastructure in their countries.
Africa's industrial development is lagging behind other regions of the world, as most economies still depend on commodities. There is an urgent need to diversify economic bases and insulate them from boom-bust cycles. Natural resource funds in the form of SWFs could help in steering industrial development and speed up economic development by strategically investing in projects that contribute to economic diversification and structural transformation. High-growth industries such as agriculture, manufacturing, hospitality, and telecommunications provide SWFs with high-return opportunities that contribute to job creation and the development of sustainable industries. Countries such as Malaysia and Indonesia have succeeded in using natural resources to industrialize and diversify their economies. Malaysia used endowments in oil, rubber and tin to develop infrastructure and technology, while Indonesia used abundant oil resources to develop the agriculture and manufacturing sectors, which contributed to economic growth, employment and poverty reduction.

Botswana has used diamond resources to finance human capital development and support economic development, which has helped to reduce poverty over the years. Today, 19 percent of Botswana's population are poor, compared with 60% in Zambia. The Angolan, Nigerian and Moroccan SWFs are doing the right thing by investing in economic sectors that support economic diversification and boost productivity, such as the hotel sector, mining sector, infrastructure, agriculture and timber.

SWFs allow the accumulation of capital from natural resources for future generations. According to the Hartwick rule, if natural resources are exhaustible, the best way of sustaining development from their use is to reinvest resource rents into some form of capital, which in turn generates some return over time. Thus, the achievement of 'inter-generational equity' is an important part of the African SWF strategy. SWFs can therefore act as long-term investors for future generations, accumulating resources for future generations, which contributes to intergenerational equity, while maximizing investments' risk-adjusted

Due to high commodity dependence, most African resource-rich countries periodically experience macroeconomic volatility, especially export revenues and fiscal budgets, which significantly limit economic growth. SWFs can play an important role in reducing macroeconomic volatility, by utilizing stabilization funds as countercyclical fiscal tools. Empirical evidence suggests that countries with sovereign wealth funds have responded better to large external shocks and reduced macroeconomic volatility during turbulent times (see e.g Mehrara, et al 2012). Norway's fiscal policy and the management of its oil wealth have played an important role in stabilizing the economy, especially during the global financial crisis in 2008 and the recent oil price slump of 2014. Algeria has used its sovereign wealth fund to fund fiscal deficits, while Mauritania withdrew about US$45 million from its sovereign wealth fund to stimulate the economy during the financial crisis in 2009.
SWF resources can also be used to balance large capital inflows and outflows and prevent asset price bubbles and exchange rate fluctuations. In this way, they help to mitigate against the Dutch Disease. The ‘Dutch Disease’ occurs when large inflows of foreign exchange earnings relative to the size of the economy result in increased real exchange rates, which negatively affects non-resource sectors. The investment of excess revenue offshore helps to obviate this artificial strengthening of the domestic currency, which helps to preserve the competitiveness of non-resource industrial sectors. The SWF of Botswana has played an important role in mitigating the Dutch Disease.

SWFs can be used as tools for fiscal discipline. This is important in resource-rich countries which have tendencies to increase expenditures during booms, only to drastically reduce expenditures or borrow heavily during slumps. A government setting funds for use during periods of economic stress clearly demonstrates fiscal discipline. This setting aside of funds also grows the investment, which could support economic growth and development. Norway uses a rule where real returns of the SWF assets are used to fund the budget, which is quite an effective fiscal disciplinary instrument.

Africa’s financial markets are less developed compared to other regions. SWFs can play an important role by participating in the markets as investors (bond purchases) or shoring up the banking sector. Because of their huge financial resources, they can serve as stabilizing instruments for the financial systems’ depth, investing during financial stress and providing support to non-bank financial institutions such as insurance and leasing companies, and private equity funds. They can strengthen the capital base of Africa’s financial institutions. They can provide valuable liquidity and stable long-term funding especially in an environment where banks are faced with liquidity challenges and mostly require short term financing. For instance, Gabon’s SWF has subscribed to the six-year, €22.5bn bond launched in late 2013 by the Orabank, while the Botswana SWF has been used to mitigate the effects of the recent global financial crisis. In some cases, the participation of SWFs has boosted credit ratings of countries which lowered the cost of borrowing. For example, Angola and Nigeria had their credit ratings upgraded after establishing sovereign wealth funds.

One of the important contributions of SWFs in the African context is the support of entrepreneurship, startups and innovation. A number of SWFs in Africa, such as the FSDEA and Gabon’s SWF, are supporting start-ups as part of their social charters. Angola’s FSDEA allocates 7.5% of its SWF assets towards activities that support socio economic development through its Social Charter. Similarly, the Kuwait Investment Authority (KIA), through its venture unit Impulse International, has invested in Careem, an online taxi startup servicing the Middle East and North African regions (Sovereign Wealth Quarterly, Jan 2016).
BEST PRACTICES: ENHANCING THE EFFECTIVENESS OF SOVEREIGN WEALTH FUNDS IN AFRICA

Some sovereign wealth funds have succeeded in supporting economic activity, enhancing productivity and fostering structural transformation of their economies. There are important lessons and best practices to learn from such experiences for African governments and SWF investors.

Following the establishment of the Santiago Principles, some countries have embraced them to enhance the effectiveness and impact of their investments on the economy. The Santiago principles are a set of guidelines that seek to instill best practices for SWFs. They aim to develop practices that promote appropriate governance, accountability and transparency of SWFs that foster adequate operational controls, manage risk, ensure accountability, improve the conduct of investment practices by SWFs, ensure management of SWFs consistent with sound macroeconomic policy framework, bring economic and financial benefits to home and recipient countries, and the international financial system, contribute to the stability of the global financial system, reduce protectionist pressures, and help maintain an open and stable investment climate. Embracing SPs can help SWFs deliver on their objectives and help contribute to economic development.

The effectiveness of SWFs in driving economic development can also be enhanced by setting clear objectives. Some countries hold a unique SWF that executes the international investments while others have preferred to establish several vehicles with distinct purposes. But, whichever the case may be, the objectives of the fund must be clear. Abu Dhabi owns five Sovereign Investment Funds, two of which have recently merged into a $125bn powerhouse and have a clear objective. Norway’s SWF also provides an example of a SWF with a clearly defined mandate and objectives, which has been instrumental in supporting Norway’s economic development. Its fund serves a multipurpose role, contributes to intergenerational equity, and has development funds to support socio economic activity and a stabilization role to stabilize the budget against the cyclicality of oil prices. It is the institutional framework, the underlying social consensus and the political incentives facing policy makers that make the Norwegian model work. Most African SWFs have clear objectives, but implementation is sometimes a challenge.

1. The Santiago Principles describes 24 principles which broadly focus on three main areas that is the (i) legal framework, objectives, and coordination with macroeconomic policies; (ii) Institutional framework and governance structure (iii) Investment and risk management framework.
A SWF must be set up in a context of good governance and independence. The characteristics of good governance involve demonstrating that the fund’s investment processes are independent of government control and potential conflicts of interest. This can be achieved through structuring the right review committees, appointing independent committee members and instituting a clear investment mandate. For example, Angola’s FSDEA is managed by an autonomous executive committee and the organizational structure ensures adequate review mechanisms through the adoption of global best practices, such as the appointment of independent auditors, while the Board of Directors defines the investment strategy. The success of some SWFs, such as the Norwegian SWF, has been partly attributed to their strong governance frameworks. The lack of governance, operating structures and control frameworks, and independence from political pressures and changes, can result in a failure to achieve set objectives and a rapid depletion of capital, as in the case of Venezuela’s SWF.

Transparency is also critical for the success of a SWF. It entails disclosures of various aspects of the SWF, systematic and clear reporting of investments, broad communication of the investment strategies and risks. Transparency also comes with disclosures of various aspects of the SWF (asset classes invested in, financial performance, benchmarks considered, investment objectives, risk tolerance, investment horizon, and investment constraints).

Table 2: Transparency Indicators of African SWFs

<table>
<thead>
<tr>
<th>Country</th>
<th>Name of SWF</th>
<th>Linaburg-Maduell Transparency Index</th>
<th>IFSWF Membership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Algeria</td>
<td>Fonds des Regulation des Recettes</td>
<td>1</td>
<td>No</td>
</tr>
<tr>
<td>Libya</td>
<td>Libyan Investment Authority</td>
<td>1</td>
<td>Yes</td>
</tr>
<tr>
<td>Botswana</td>
<td>Pula Fund</td>
<td>6</td>
<td>Yes</td>
</tr>
<tr>
<td>Angola</td>
<td>Fundo Soberano de Angola</td>
<td>8</td>
<td>Yes</td>
</tr>
<tr>
<td>Gabon</td>
<td>Gabon Sovereign Wealth Fund</td>
<td>N/A</td>
<td>No</td>
</tr>
<tr>
<td>Congo Republic</td>
<td>Fonds de Stabilisation de Recettes Budgetaries</td>
<td>N/A</td>
<td>No</td>
</tr>
<tr>
<td>Nigeria</td>
<td>Nigeria Sovereign Investment Authority</td>
<td>9</td>
<td>Yes</td>
</tr>
<tr>
<td>Morocco</td>
<td>Morocco Sovereign Wealth Fund (Ithmar Capital)</td>
<td>N/A</td>
<td>Yes</td>
</tr>
<tr>
<td>Senegal</td>
<td>Senegal Fonsis</td>
<td>N/A</td>
<td>No</td>
</tr>
<tr>
<td>Ghana</td>
<td>Ghana Petroleum Funds</td>
<td>N/A</td>
<td>No</td>
</tr>
<tr>
<td>Mauritania</td>
<td>National Funds for Hydrocarbon Reserves</td>
<td>1</td>
<td>No</td>
</tr>
<tr>
<td>Equatorial Guinea</td>
<td>Future Funds for Generations</td>
<td>N/A</td>
<td>No</td>
</tr>
<tr>
<td>Chad</td>
<td>Fonds de Stabilisation de Recettes Budgetaries</td>
<td>N/A</td>
<td>No</td>
</tr>
<tr>
<td>São Tomé and Príncipe</td>
<td>National Oil Account</td>
<td>N/A</td>
<td>No</td>
</tr>
<tr>
<td>Sudan</td>
<td>Oil Revenue Stabilisation Fund</td>
<td>N/A</td>
<td>No</td>
</tr>
<tr>
<td>Rwanda</td>
<td>Agaciro Development Fund</td>
<td>N/A</td>
<td>Yes</td>
</tr>
<tr>
<td>Tanzania</td>
<td>Natural Gas Reserve</td>
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<td>No</td>
</tr>
<tr>
<td>Kenya</td>
<td>Kenya Sovereign Wealth Fund</td>
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<td>No</td>
</tr>
<tr>
<td>South Sudan</td>
<td>Oil Revenue Stabilization and Future Generations Fund</td>
<td>N/A</td>
<td>No</td>
</tr>
<tr>
<td>Zimbabwe</td>
<td>Zimbabwe Sovereign Wealth Fund</td>
<td>N/A</td>
<td>No</td>
</tr>
</tbody>
</table>

Source: IFSWF is the International Forum of Sovereign Wealth Funds.
Transparency is crucial to building trust and confidence in the management of the Fund – both domestically and internationally. The Alaska SWF (USA), Alberta (Canada), Azerbaijan, Chile, Pula Fund (Botswana) and Norway have high levels of transparency and make detailed disclosures about their funds. For Botswana, the spending of resource rents is well reported and transparent, with benefits of resource windfalls visible. This helps to manage citizens’ expectations, while ensuring checks and balances on the government’s use of natural resource rents. NSIA has a score of 9/10 transparency rating from the SWF Institute and is on par with South Korea, Malaysia and Alaska in the USA, while Angola scores 8, reflecting high transparency. Algerian, Libyan and Mauritanian SWFs have a score of 1, indicating low levels of transparency (Table 2). Transparency is expected to increase gradually among African SWFs in the next few years as more SWFs move to publish their annual reports.

One question which has often been raised in policy circles relates to whether African SWFs should invest at home or invest abroad, in light of their unique challenges such as capital constraints. Investing in both external and domestic assets is probably best for African SWFs, as it ensures diversification of incomes. Considering the multiple objectives of most SWFs, the best practice could be to establish an ‘umbrella’ sovereign wealth fund with different components/mandates such as stabilization fund, fund for future generations and domestic economic development (Amoako-Tuffour, 2016).

On investment strategy, African SWFs could consider co-investments or co-financing with other SWF or private investors. This helps to bring expertise in the projects, spread capital outlays, reduce share risks and increase credibility of the investments. The NSIA has partnered with General Electric, Julius Berger and Power China in energy development, road and bridge construction, and with Africa Finance Corporation and International Finance Corporation to finance infrastructure projects.

Furthermore, SWFs should be governed by a set of detailed investment rules that inform investment decisions, including target asset class allocation (percentage of investments in cash, fixed income, equities and alternative assets), guidelines on domestic investment, rules on risky asset purchases, and restrictions on the use of natural resource funds as collateral to guarantee public debt. Investment rules could, for instance, require an asset allocation that mixes safer, lower-return investments with higher-risk, higher-return investments, while prohibiting the riskiest types of investments (e.g., derivatives).
Investing abroad helps to diversify income, maximises financial returns, lowers the volatility of government revenue, helps to avoid the Dutch Disease, and minimises the absorption capacity problems. At the same time investing domestically helps to boost the local economy, cover infrastructure financing gaps, create jobs, and help to cover pressing economic development needs of the current generation and future generations.
While some SWFs lost large sums of money during the global financial crisis, others including Azerbaijan’s State Oil Fund, Chile’s SWF and Trinidad and Tobago’s SWF made positive returns during the global financial crisis due to their clear, conservative and low-risk investment approaches.

The investment strategy must match its objectives. For instance, a stabilization fund would need to invest in more liquid assets than a long-term savings fund, while an infrastructure fund could invest in long-term illiquid assets. While some SWFs lost large sums of money during the global financial crisis, others including Azerbaijan’s State Oil Fund, Chile’s SWF and Trinidad and Tobago’s SWF made positive returns during the crisis due to their clear, conservative and low-risk investment approaches. Norway’s SWF targets a maximum allocation of 5 percent of the overall portfolio to real estate, while Botswana’s Pula Fund makes fixed income investments denominated in only convertible currencies, mainly the U.S. dollar, the Euro, pound sterling and yen.

One practice that enhanced the effectiveness of SWFs in Chile, Norway and Saud Arabia is fiscal rules. It is important for African SWFs to institute fiscal rules. Fiscal rules determine how much resource revenue is saved, spent, and withdrawn, hence helping to stabilize budgets. This is important in managing resources, especially in Africa where resource windfall revenues are often large enough to destabilize the economy. Fiscal rules can also help to overcome the Dutch disease by sterilizing capital inflows. The Norwegian SWF withdraws no more than the real return on the SWF annually to support the budget. Its fiscal policy has effective revenue instruments, fiscal rules to limit discretion, rules outlining operation of natural funds, and effective public investment management. The fund has helped to delink the economy from oil price fluctuations, minimize the potential corrosive power of oil dependency and foster Norway’s economic development. According to Asafah (2007), most African SWFs do not have clear fiscal rules which define how they should cover fiscal deficits during economic downturns.

The best practice in asset allocation is to develop a medium- to long-term decision based on extensive research and consultation with key stakeholders, which is in line with objectives. The asset allocation needs to be reviewed from time to time, and be rebalanced to remain consistent with the long term.
objectives in line with economic developments, fiscal situation, market trends, and risk tolerance. For example, if stabilization is the overarching objective, more funds would be invested in liquid assets. Long-term savings funds are able to afford some degree of volatility and illiquidity and could therefore adopt a more diversified, higher-risk portfolio. A SWF investor who is more risk averse, with shorter investment horizons and a high preference for liquid assets, could favor a relatively higher allocation to bonds and money market instruments. Over time, the divergent performance of the various asset classes in the SWF portfolio may imply that its effective asset allocation drifts away from its strategic asset allocation and will need to be rebalanced. The process of rebalancing ensures that the fund’s overall portfolio is periodically returned to its target long-term strategic asset allocation.

One way of ensuring that investment managers manage well within the constraints imposed on them by the asset class allocation is to select a series of benchmarks for each asset class.

The benchmark is usually an index that reflects market performance so that the government and oversight bodies can measure investment manager performance against a market average, thus improving manager accountability. Benchmark indexes can help explain why returns are high or low for any given period. Chile and Norway’s SWFs effectively use benchmarks in their portfolios. The Chilean SWF is not allowed to deviate from the benchmark by more than 0.5 percent on its sovereign bond portfolio, 0.3 percent on its equity portfolio and 0.5 percent on its corporate bond portfolio.

It is important for SWFs to have a well-functioning risk management framework to ensure that it is able to identify, assess, and manage its risks to protect its assets and stay within the tolerance levels as set in its investment policy. Adherence to high standards of risk management with sound operational controls and systems helps to preserve assets, while earning decent returns on the portfolio. Risks should be managed on a multi-dimensional framework, including asset class, individual fund, and risk types.
CONCLUSION

Sovereign wealth funds are becoming important sources of development finance in many countries. A lot of African countries have established sovereign wealth funds in recent years, and many others are preparing to join the international trend amidst a number of Africa’s unique development challenges. This paper analyses the role of SWF’s in promoting development in Africa. The paper notes that SWFs can play a more active role and be game changers in Africa’s development. The rise of SWFs is a clear opportunity for African governments to tap the full potential of these resources to achieve greater economic growth and development, and ensure that they benefit from their rich natural resources. Sovereign wealth funds can help to bridge the infrastructure funding gap, support strategic economic sectors, drive industrial development and economic diversification, help to reduce macroeconomic volatility, ensure wealth diversification, and enhance intergenerational equity by accumulating assets for future generations.

For SWFs to be effective in delivering their mandates and support economic development, they need to have clear goals and objectives, and improve their governance and transparency frameworks. Their medium to long-term strategic asset allocation should be linked to their objectives. SWFs should invest both at home and abroad to diversify their incomes. Moreover, they should embrace the Santiago Principles which sets out guidelines for best practices. African governments also need to develop more attractive frameworks for SWFs and to encourage them to invest in sectors that contribute more directly to addressing Africa’s development needs, while operating with strong corporate governance structures and ensuring that resources are adequately managed.
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