

## Rich World – Poor World London, Abidjan, Accra, Nairobi & Doha

July 2010

By Larry Speidell & Thea Jamison



*Food market, Abidjan, Cote d'Ivoire*

London, Cote d'Ivoire, Ghana, Kenya, Qatar and Bahrain - A study of contrasts: rich and poor, optimistic and pessimistic, happy and unhappy - which provides an opportunity to reflect on whether those dimensions relate to investment opportunity.

Larry and Thea started the trip by attending an Africa conference in London. Larry hobbled by a broken foot, soon discovered that the corridors at Heathrow Airport seem miles long. And London traffic will run you over quickly if you don't jump out of the way fast enough. One of our clients, Issac, joined us in London, and then we picked up another team member, Bob, a friend and consultant, on our flight to Cote d'Ivoire. In the frontier countries, we found bright, energetic, cooperative people in everywhere. In Abidjan, Cote d'Ivoire, Issac remarked: "There are more happy people on the streets here than you'll ever find in New York City."

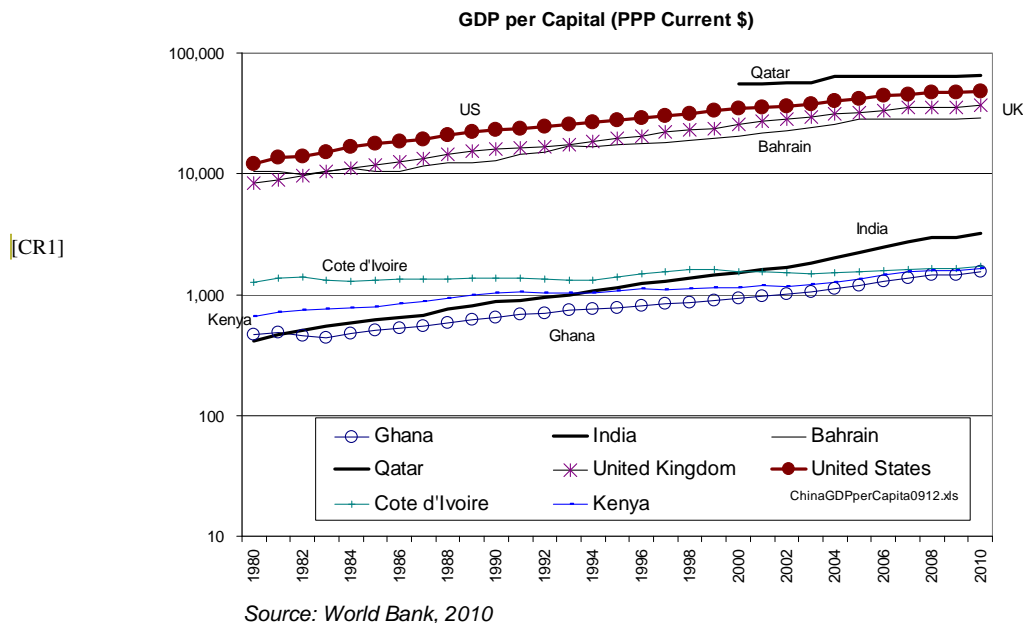
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Like George Clooney in “Up in the Air”, we settled into our frontier travel routine: passport in one pocket, Blackberry in another, shoes that slip off quickly for security and a wrinkle free suit you can sleep in on a night flight (check it in your luggage, and you might do meetings in borrowed clothes - as happened in Karachi one time). Also be sure to bring your yellow fever shot certificate, otherwise in Cote d’Ivoire, they’ll give you another shot in a dingy room outside passport control. Another tip: bring enough snack bars and nuts to survive for a couple of days in case the local food is inedible or simply uneatable.. Your stash can be supplemented along the way with packs of cookies or chips from business class lounges. Thus prepared, you breeze through the airport (except when the check-in computers are down), throw your wheelie bags through the x-ray scanners, assume the position for regular pat-downs by security and shake off the crowds of locals who might be porters, pickpockets, kidnappers or thieves. Have a hotel car pick you up unless you’re certain the taxis are safe, and change \$40 into local currency for tips and sundries. At your hotel, remember to keep your mouth closed in the shower, brush your teeth with bottled water and keep earplugs handy in case of noisy air conditioners or noisy neighbors. Most of the time, these precautions are overkill. Then again sometimes they can be lifesavers, or at least they can save your sanity. You know you’re in the frontier when you’ve spent more money on your visa to get into a country than on food while you were actually there.

In the frontier, investment opportunities can exist whether or not a country is doing well, but our bottom-up approach doesn’t rule out awareness of country level macro impressions. Last fall, we went to Nigeria with low expectations, and they were fully met. On this trip, we were cautious about Cote d’Ivoire, and optimistic about Ghana, Kenya and Qatar. In every case, we were pleasantly surprised. We met with more than a dozen companies including Letshego, Banque Internationale pour le Commerce et l’Industrie (BICICI), Societe Africaine de Plantations d’Heveas (SAPH), Palmci, Bank of Africa – Cote d’Ivoire, Standard Chartered Bank – Ghana, Ghana Commercial Bank, Cal Bank, British American Tobacco – Kenya, Centum, Commercial Bank of Qatar, Qatar Electricity and Water, Qatar National Bank and Vodafone Qatar. Not only were we impressed with these companies, but we were impressed with the talent of almost all the management teams we met.



|                                       | Cote d'Ivoire | Ghana   | Kenya   | Qatar    | Emerging Mkts | United States | EAFE     |
|---------------------------------------|---------------|---------|---------|----------|---------------|---------------|----------|
| RGDP Growth 2010e                     | 4%            | 7%      | 6%      | 9%       | 4%            | 3%            | 2%       |
| GDP per capita, PPP (current intl \$) | \$1,651       | \$1,452 | \$1,590 | \$63,588 | \$12,481      | \$46,716      | \$38,830 |
| Inflation                             | 3%            | 14%     | 10%     | 4%       | 5%            | 2%            | 2%       |
| Population (mil)                      | 20.6          | 23.4    | 38.5    | 1.7      | 4,757         | 304.1         | 582.2    |
| % Rural                               | 52%           | 51%     | 79%     | 4%       | 29%           | 19%           | 17%      |
| % Literate                            | 80%           | 80%     | 80%     | 80%      | 87%           | 80%           | 100%     |
| Electricity (kWh/capita)              | 170           | 266     | 138     | 16,801   | 2,902         | 13,648        | 9,822    |
| Corruption (10=best)                  | 2.1           | 3.7     | 2.1     | 6.0      | 4.1           | 7.2           | 8.2      |
| Market Cap (\$ Bil)                   | \$7.1         | \$3.4   | \$10.9  | \$76.3   | NA            | \$11,737.6    | NA       |

Source: World Bank, S&P, MSCI, Transparency Int'l & Frontier Market Asset Management, 2010

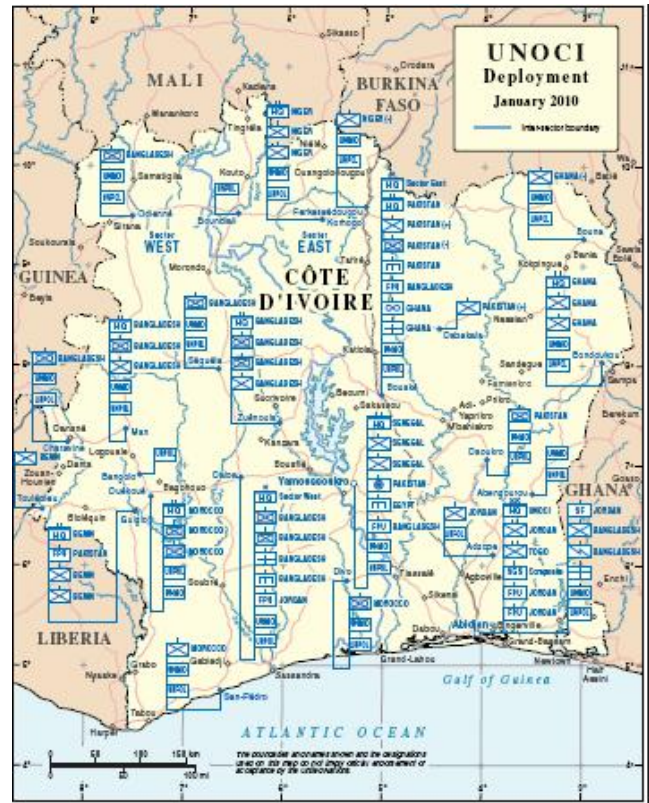


## COTE D'IVOIRE (Ivory Coast)

Cote d'Ivoire has some of the best French restaurants south of Paris, but it is also home to several thousand UN troops to keep the peace in advance of much postponed elections due later this year.

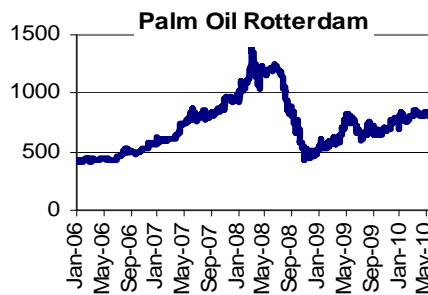
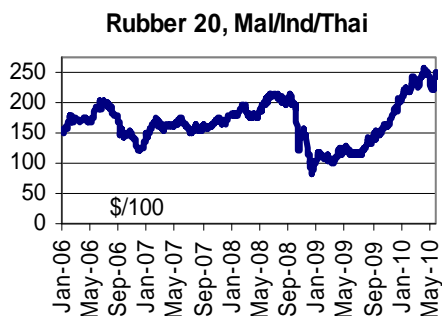
Sincer our last visit two years ago, conditions overall have hardly changed. In the interim, Cote d'Ivoire has seen food riots during the commodity price bubble and then a sharp fall in farmers' income as prices of cacao, palm oil and rubber plunged. Now those prices are headed higher and the outlook for exporters is good. Rubber prices may be headed even higher, as Vietnam appears likely to join the International Rubber Consortium (Thailand, Indonesia and Malaysia), which will then control 84% of the world output of natural rubber.

On the other hand, Cote d'Ivoire's electric power situation has deteriorated due to neglect and non-payment of bills by the government. From being a power exporter ten years ago, the country now sees blackouts of up to eight hours in Abidjan and as much as two days in rural villages. Despite this, the food markets are filled with rich produce, and if election uncertainty ends there will be a big gain in confidence. Patrick Hornecker, Directeur Administratif et Financier of Society Africaine de Plantations d'Heveas (SAPH), the big rubber producer, has just moved here after many years in Nigeria, and calls Cote d'Ivoire a "holiday camp" by comparison.



United Nations Operations in Cote d'Ivoire  
Source: <http://www.un.org/en/peacekeeping/missions/unoci/>

President Gbagbo recently disbanded the electoral commission and reconstituted it, resulting in violence and suspicion. In fact, however, voter roles are very hard to determine in this country. For years the northern border was fuzzy, and families would hire workers to come in from Mali to help with the crops. Many of them have stayed for generations. Should they now be considered Ivoirian citizens? Whatever is decided, it will be best if elections come sooner rather than later.



Source: Bloomberg May 2010

A similar issue affects property rights, not just in Cote d'Ivoire, but throughout the frontier. This is important because farmers need to borrow money to buy fertilizer, and currently they cannot get credit. Thus in palm oil, the crop yields of "outgrowers" are only seven tons per hectare (roughly 2.5 acres) compared with twenty tons on company owned plantations where fertilizer is used. The process of granting property rights is slow, as the country needs to set up special offices in the villages with a local committee to decide who owns what. This is a bit like tracing the ownership of goats that roam free in city streets; they don't have tags, but everyone knows whose goat is whose.



Abidjan, Cote d'Ivoire

Clearly, the establishment of property rights will help more than just the farmers. Currently, consumers can only get unsecured personal loans at high rates. These are generally limited to employees of companies where the banks already have a lending relationship.

Work ethic in Africa is misunderstood by outsiders. Official unemployment in Cote d'Ivoire is 40%, but roughly 50% of economic activity is "informal" or underground. These are the workers in the open air food market in Abidjan, and also the many who risk their lives selling CDs, sunglasses and bags of water in between the lanes of heavy traffic. People here know hard work. What they need is formal jobs. For example, at PALMCI, Clovis Kacou, the Finance Director, leaves home at 6:45 am, drops his kids at school, and works a twelve hour day. He personifies the high quality of top management in many African companies.

While we had hoped that Cote d'Ivoire would be farther along in its democratic process, we believe that external pressure and internal pragmatism will maintain the peace and continue the democratic process. Meanwhile, we are being paid to wait: the stocks are cheap, and several have dividend yields more than 10%.



## GHANA

### *The Tiger of Africa?*

Ghana is on the cusp of change. ("Cusp: a point of transition, as from one historical period to the next," *Merriam-Webster*).

Oil was found offshore in mid-2007. Now, production will begin to flow in October 2010 at 60,000 barrels per day (bbls/day) scheduled to ramp up to 240,000 bbls/day in 2011. The world is watching to see if this will be a curse or a blessing. After a peaceful transfer of power following the close election votes in December of 2008, Ghana was singled out by President Obama for his visit to Africa in July 2009. Now Norway is helping Ghana's government with advice on setting up a sovereign wealth fund for some of the oil revenues.



*Repairing the nets, Cape Coast, Ghana*

An angry editorial in *The New York Times*, "Why Africa is Poor", (December 18, 2009), singled out Ghana for meddling in the proposed sale of oil rights in the off-shore Jubilee Field by Kosmos (an oil explorer backed by the Blackstone Group and Warburg Pincus) to Exxon. "Spooking new investors by repudiating contracts will rapidly ruin the country's prospects," said the editor. As with many stories in the media, the truth requires more digging. At Standard Chartered Bank Ghana, Hemen Shah, the bright Chief Executive Officer, explained that the government is being justly cautious. The deal includes a questionable provision whereby an individual with connections to the former president of the country would receive a 2% stake in the oil rights. Mr. Shah explains that it is better to have a fair transaction than a quick one, even if this means delaying payouts to the private equity investors in the oil development. This delay in the sale might actually work to Ghana's advantage by offering China more time to make a serious cash counter-offer.

Meanwhile the production schedule is still on track. As a result, Ghana's GDP is expected to grow 7% in 2010 and an astonishing 22% in 2011, according to the International Monetary Fund. This will turn around Ghana's fiscal problems, which were exacerbated when the government locked in future oil costs at \$140/bbl in mid-2008. These contracts are now running off, and inflation in the country is finally dropping from near 20% to 14% currently.

Officially, Ghana's unemployment rate is 9%, but, in fact, it is closer to the 40% rate in Cote d'Ivoire; and the informal economy is probably a similar at roughly half of total GDP. With growth, this will all change. Already there is pent up demand for consumer credit. Part of this is because residential rental properties require two years of rent paid in advance, and private school tuitions are due one year in advance. As a

result, the limited consumer lending that is done in Ghana, carries very high interest rates. UT Financial has banners around the city of Accra promoting its generous lending, but it charges 9% a month! And, we are told, they evidently use rather aggressive collection techniques.

Meanwhile, Standard Chartered charges consumers an annual rate of 35%, and it lends mostly to employees of their corporate customers. Their overall net interest margin (NIM) is an impressive 7%. In fact many of the banks in Africa have very impressive NIMs, compared to those around 1.5% in the much more competitive Middle Eastern banking markets.



*Bringing the fish to market, Elmina, Ghana*

With a boom on the way in Ghana, companies are getting prepared. One hotel owner received a booking from an oil company of fifty rooms -,for the next ten years! He took the deposit and used it to begin construction of another hotel.

Also, China is an active investor in Ghana. Standard Chartered Ghana is proud of the longstanding relationships of its parent company in Asia. They have two Chinese staff-members, and they hosted a massive Chinese New Year event. Mr. Shah says they “own the China space in Ghana”.



## KENYA

Another visit to Kenya, and yet the same thoughts come to mind. This is a wonderful country with plentiful resources. The people are educated, have one of the highest literacy rates in Africa (85.1%), and are hard working. From the company managers we met, to the staff at the Java Coffee house, to our car drivers – we were impressed with the hustle and pride in their work. There is little, if any presence of ex-pats, and most of the management positions are occupied by local talent. As in other frontier countries, Kenyans are returning back home after years of education and experience abroad. A Kenyan-born professional recently recruited from Goldman Sachs in New York said that there are “great opportunities as well as better living standards in Nairobi”.



*Nairobi's Famous Train Museum, Courtesy of Bob Bukowski*

Kenya is rich in other resources too. Nairobi, 5,500 ft above sea level, has one of the most benign climates in the world. Also the country has a great location -- neighboring Tanzania, Uganda, Sudan, Ethiopia and Somalia. Between the Indian Ocean and Lake Victoria, it is central in Eastern Africa. The country's human resources, geography and climate are important in making the country a regional hub in

Eastern Sub-Sahara. Add to that the beauty of the land and the wildlife; one can appreciate why Kenya has been an inspiration for many memorable, best selling biographies, such as *I dreamed of Africa*, *West with the Night*, and *Out of Africa*.

The Kenyan stock market (\$13 billion market cap) is the third largest in Sub-Saharan Africa, after South Africa and Nigeria. Compared to the stock markets in Cote d'Ivoire (\$6bil) and Ghana (\$4bil), this market has much more depth and liquidity. There are 56 listed companies and average daily trading volume of roughly \$1 million. The top stocks are institutional favorites for South African and domestic asset managers, and as such, they trade at premium valuations. To find compelling value, one has to dig deep. Some interesting stocks include the dominant regional airline, which is adding routes to more African countries, and a private equity company that is now making investments in less developed Ethiopia, Rwanda and South Sudan.

Visiting the vibrant Nairobi Stock Exchange, walking down the streets, driving through the newer neighborhoods and even just sipping coffee at the Java House - one cannot help but feel enthusiastic about the prospects of the rising Kenya, and even more, the rising East African region.



## QATAR

You can take a night flight from Ghana, change planes in Dubai, and arrive in Doha in time for a 10:30 meeting with Commercial Bank of Qatar. The country is like a thumb stuck out into the Arabian Gulf (better not call it the Persian Gulf here).

Only a third the size of Belgium, Qatar is becoming the second largest hydrocarbon producer in the world, as its huge Japanese financed liquefied natural gas (LNG) project comes on stream.



Source: The CIA Fact Book, [www.cia.gov](http://www.cia.gov)

Now, real GDP growth is forecast at 9.5% in 2010, more than 20% in 2011 and further growth of 15% annually through 2015. While LNG production is expected to level out in 2013, the moratorium on exploration and production projects ends in 2011, so this may prove conservative. At any rate, growth in the out-years is expected to settle around 8-10% as the country continues its diversification downstream.

### Natural Gas: Proved reserves

| Trillion cubic metres | 2008  | Rank |
|-----------------------|-------|------|
| Russian Federation    | 43.30 | 1    |
| Iran                  | 29.61 | 2    |
| Qatar                 | 25.46 | 3    |
| Turkmenistan          | 7.94  | 4    |
| Saudi Arabia          | 7.57  | 5    |
| US                    | 6.73  | 6    |

Source: BP Statistical Review, 2009

Already, in the downstream area, Qatar Industries is a leading petrochemical producer, based on its low feedstock costs. Now, the nation is planning to move into aluminum, and there is a gas to liquids (GTL)

project under development with Shell. Meanwhile, Qatar Electricity and Water has plans to “export” electricity by following LNG overseas and building power plants in places like Bangladesh.



*Qatar*

While much media commentary has generalized the bubble problems of Dubai to all of the rich oil states in the Gulf Cooperation council (GCC), Qatar is different, because they were late to the development party. And they have been cautious, restricting foreigner real estate purchases to only a few zones, such as The Pearl, an 8,000 unit residential development on an artificial island off the coast of the capital city of Doha. Thus, while high end properties in Dubai are down by 2/3 in price (versus 50% for the middle market), prices in Qatar are down far less.

The population profile of Qatar is much like the rest of the GCC. There are only 225,000 Qatari citizens, but the country holds another 1,475,000 people. Of these ex-pats, 200,000 are long term white collar workers; another 150,000 are short term white collar workers; and the remaining ex-pats are blue collar laborers, mostly from Asia. Out of more than 1.1 million, 300,000 are from Nepal, followed by Indians, Pakistanis, Filipinos and Sri Lankans. They may be poor (and often poorly treated), but their work ethic is high. My driver, from southern India, works a seven day week, with only a short day on Fridays, when he stops work at 2 pm. Once a year, he returns to India for a month to visit his wife and baby son, now one year old. His story is repeated by thousands of others in the GCC.

Recently, the government of Qatar has given a gift to these visitors by introducing competition into the mobile phone market. After paying \$2.1 billion for its license (in hindsight perhaps \$1 billion too much), Vodafone launched its service in mid-2009 and has gained 450,000 customers, or 20% of the market (penetration is 159% of the population as most people have several phones!). Vodafone began by offering international calls at the local rate. Then Qatar Telecom (QT, the previous monopoly, offered calls at 0.55 Qatar Reals (QR) per minute (\$0.15). Vodafone dropped to 0.50 QR. Recently, reason has returned to the market, with QT at 0.99 QR and Vodafone at 0.95 QR. This is still a huge benefit for foreign workers compared to their previous international calling rate of 2.5 QR per minute. Vodafone will hold at roughly a 5% discount while it builds network quality (with permanent towers rather than “cells on wheels” and wiring buildings for indoor coverage). While Vodafone is pleased with its progress, it didn’t expect such a high portion of international calls where its interconnect charges are high. Likewise, the response of customers has been interesting. A recent New Year promotion offered 2010 free minutes if you signed up by the end of January. Many illiterate workers did so, but then thought they had to use up all 2010 minutes by the end of the month. Vodafone had to struggle to keep up service at an unexpected 100% of system capacity!

Qatar is basically a family owned country, headed by Amir HAMAD, who deposed his father in 1995 to take over and begin reforms. As a result, many of the best companies are part of what is called the Q “Family”: Qatar Electricity and Water, Qatar Fuel, Qatar Industries etc. Typically, companies here understand what investor relations is all about because the country wants to encourage inbound investment. It is relatively easy to schedule meetings, and excellent roads make it quick to get from the new business center to the old city and back multiple times (as we did).

## The Markets

Cote d'Ivoire, Ghana, Kenya and Qatar are very different markets, but all have interesting stock opportunities. The economic and political backdrops are brightest in Ghana and Qatar, but the markets are cheap in the other two countries, offering upside if there is positive change.

As bottom-up stock-pickers, we will look anywhere as long as countries are investor friendly and transactions can be managed effectively. Comp sheets, listing stocks in the market, are our starting point. We compare PEs and yields, but like to focus on those that could benefit from our theme of rising consumer disposable income. We like what we call "sidecar" companies. These are the locally listed subsidiaries of global multinationals, where the parent typically holds 50-70% while the balance trades in the local stock market. In this camp in Cote d'Ivoire are BICICI (Banque Paribas), SGBCI (Societe Generale), Nestle, and even SAPH, a rubber producer (part owned by Societe Internationale de Plantation d'Heveas SA, based in France). In Ghana, we like companies such as SCB (Standard Chartered Bank), Unilever but also government controlled Ghana Commercial Bank (a turnaround with new management).



*Mariane Dollou Beugre, Head of Trading,  
Hudson & Cie, Cote d'Ivoire*

Unfortunately, in most of Africa, companies don't really understand what investor relations is all about; even though we are shareholders, our meeting with Unilever Ghana was abruptly cancelled, and Guinness Ghana refused to move a meeting from 2pm to the morning, despite a week's notice.

On the other hand, the stock exchanges themselves are all now modern. They use Central Depositories and trading is electronic. Gone is the white board for handwritten pricing that Ghana used as recently as 2008. Still, the ease of trading differs widely. Markets in the Middle East are extremely liquid, but in Sub-Saharan Africa, the situation varies from markets in liquid Nigeria and Kenya to places where one simply needs to be patient. In Cote d'Ivoire, the Bourse Regionale de Valeur Mobiliere (BVRM) is a regional market for francophone West Africa. The largest stock traded is Sonatel, the Senegalese mobile and fixed-line operator. Here, brokers can see depth on both sides of the bid-ask spread, which itself is sometimes wide at 5-8%, which allows the broker more information to use in judging how to cross a "block" of \$100,000 or so. By contrast, the Ghanaian exchange does not offer such information, and thus, small \$100 trades flow through while bigger amounts are simply stuck.

## Conclusion

There is no substitute for travel to confirm impressions and replace hunches with conviction. After traveling in frontier markets for more than three and a half years, we know our way around. Much of the novelty has worn off, but our understanding of the opportunities is greater. And our conviction is greater.

Over the past three years, the relative contrast between frontier countries and the developed world has changed dramatically. Previously it was assumed that in the developed world, financial conditions were stronger and political risk was lower than in the emerging and frontier countries. Now, those gaps have both narrowed, and in some cases may even have reversed. The strong banks we visited on this trip

provide examples of this. They are savoring the opportunity for expansion in the largely untapped consumer retail sector, where current debt levels are close to zero. It may take years for the developed world to recover from its burdens of public and private debt. Meanwhile, a growing middle class in the developing world is providing a new customer base for the many companies we find attractive in these overlooked frontier stock markets.



Food Market, Abidjan, Cote d'Ivoire

### About Frontier Market Asset Management

*Founded in 2006, Frontier Market Asset Management holds more than 35 years worth of investment experience including work in Emerging and Frontier Markets since 1987. For more information, please contact us at (858) 456-1440.*

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