

Three of a Kind: Senegal, Botswana and Ghana

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We are optimistic about Africa.

From a macro standpoint, we believe the continent is entering a period of better government, fewer conflicts and more enlightened economic policies. In addition, investment flows to the region are rising, coming from at least four sources:

- 1) Raw materials development spending by direct investors worldwide.
- 2) Infrastructure spending from petro-dollar flows from the Mid-East.
- 3) Investment flows from China as the Chinese seek long term friends in the region to bolster their raw material supplies.
- 4) Portfolio investment flows, such as ours.

If these trends continue, the current attractive valuations of equities in Africa should lead to good returns in coming years.

To look at things from a micro standpoint, we traveled to Senegal, Botswana and Ghana at the end of March with a small group of clients and friends. Each of these countries is unique: One is a popular French speaking tourist stop, another is near the top of the African income ladder and the last nation is cleared for progress as it celebrates 50 years of independence. That celebration is a reminder that not long ago this continent was seething with independence movements that ended in success but then sank into a morass of political corruption, violence, oppression and economic failure. Today, fortunately, things are much better. These countries provide strong evidence of the progress in Africa.

	Senegal	Botswana	Ghana	Emerging Mkts	USA	EAFE
RGDP Growth (2007e)	4.5%	4.5%	4.5%	4.4%	2.8%	2.0%
GDP/Capita	\$478	\$3,819	\$289	\$5,265	\$36,655	\$26,229
Inflation	0.2%	7.0%	8.0%	4.8%	2.0%	1.4%
Population (mil)	11.7	1.8	22.1	3549.1	296.5	582.2
Population % <15 years	43%	38%	39%	25%	21%	17%
Population % > 65 years	3%	3%	4%	8%	12%	15%
Corruption (10=best)	3.2	5.9	3.5	3.9	7.6	8.3
Market Cap (\$ mil)	\$1,980	\$5,900	\$1,375			
Float (S&P/IFC)	\$396	\$1,143	\$402			
PE	6.0	17.6	10.6	13.8	17.4	15.0
PB	1.9	8.6	7.5	2.1	2.8	2.3
ROE	31.7%	48.9%	71.0%	14.9%	16.3%	15.5%

Source: S&P/IFC & MSCI

Senegal



Delta Air Lines' flights from the U.S. to Johannesburg stop for fuel in Dakar, making it convenient to see this West Africa country with its spectacular coastline. Although the early morning drive from the airport across potholed streets is not impressive, a new road is under construction, and it will make the trip a quick one. Arriving in March, we were fortunate that the dusty, dry harmattan winds from the Sahara had ended, so the air was clear and comfortable. Enjoying a fish dish of yassa poisson over lunch in an elegant seafood restaurant on the beach, we spoke with local financial people about life in Senegal. As we looked at topless French tourists sunbathing on the sand, we heard that this is still a traditional Muslim country in many ways, with little consumption of alcohol and a common practice of taking up to four wives. Last year, the economy was hurt by the jump in oil prices and many power blackouts, but in 2007 things are expected to be better: 4-5% RGDP growth and 1.5% inflation.



Infrastructure, commercial and residential construction are all booming: A condo development rising by the sea offered 2000 square foot units with a good view for \$250,000 and was quickly sold out. It is probably a bargain compared with the Mediterranean or California. With rising prosperity, Dakar now boasts world class traffic jams, partly because much of its rolling stock of decrepit taxis are prone to breaking down anywhere, anytime.



Senegal is a stable democracy with 12 million people, 20% of whom live in Dakar. President Wade, now 80 years old, was reelected in February for another five year term. He hopes to continue reforms, expand the economy and reduce unemployment, which is 40% for urban youth. The Senegalese are nothing if not entrepreneurial, and this is reflected in the persistence of street merchants who tag along after visitors for a block or more offering deals at lower and lower prices. If this energy could be channeled into the formal economy, growth would explode. In fact, the quoted GDP per Capita of \$478 significantly understates the level of the economy since 70% of economic activity is said to be "informal". Presently agriculture employs 77% of the labor force but contributes only 18% of GDP, while industry is 19% and services 63%. The regional stock exchange is located in Cote d'Ivoire, but Senegal's quasi-monopoly telecom is one of the biggest stocks traded there.

Botswana



Botswana is Africa's success story. Since independence from the British in 1966, Botswana has enjoyed scheduled elections, peaceful transitions of power and a multiparty nonracial government. Part of this good fortune is the result of significant diamond deposits discovered in the 1960s that now contribute a third of the country's GDP and represent a third of the world's production. Botswana is now integrating downstream in the business. Several diamond cutting firms are setting up business in a large building under construction between the capital and the airport. Tourism is another key sector of the economy, with luxurious safari lodges in the Kalahari Desert and the Okavango Delta, where the Okavango River from Angola and Namibia spreads out in vast lagoons before being absorbed in the Kalahari sands. Driving around Gaborone (Ga-bo-RO-nay), one sees

a city of 200,000 people that sprawls without much of a center, but it has a sense of peace and cleanliness that is lacking in many Frontier Markets. Unfortunately, Botswana has the highest HIV prevalence according to the World Health Organization Survey (24.1% in 2005 versus 18.8% in South Africa, 2.3% in Ghana and 0.9% in Senegal), but in contrast to South Africa, the government is extremely proactive in education and treatment, so prevalence is now stable.

Beginning as one of the poorest countries in the 1960s, Botswana has invested its diamond wealth wisely and has grown at 5-10%. It has avoided the corruption that often curses resource-rich countries, and it now has GDP per capita of \$3,819. Although economic policy is enlightened with respect to taxes (a low 25% maximum rate), there has been difficulty with inflation which was 11.5% last year, partly the result of a misguided 12% devaluation of the Pula. Things are improving though, with growth around 5% and inflation around 7% in 2007. More important, the government is shifting from attempts to subsidize industrial development to encouraging more production of the country's natural resources that include coal, gold and copper (a venture with Malaysia's Pula auto manufacturer tried producing parts here before going bankrupt in 2000). These new policies should reduce unemployment from its current 20% level.



We watched a typical trading "day" (30 minutes long) at The Botswana Stock Exchange

We met with five companies, ranging from insurance and micro-finance to property, retailing and food production. We were pleased to find that the managements were all smart, energetic and knowledgeable. They are using tight controls and thoughtful planning to turn around old businesses and create new ones, often with innovative business models. One diversified conglomerate, for example, has shed an unwanted joint venture partner, streamlined its food processing operation and trimmed staff to focus on higher shareholder returns.

Trading is not exactly heavy on the Botswana Stock Exchange, with a typical day's volume amounting to \$200,000 for the 16 listed domestic stocks. Things are changing, however, with pressure on the government to release some of its holdings as IPOs, and with modernization of the exchange by its CEO, Hiran Mendis, who is copying many of the developments in his native Sri Lanka. The stock market, with a capitalization of \$8 billion, trades at a PE ratio of over 20x, dominated by the big banks, but there are smaller stocks selling at attractive prices for patient buyers.

		Mkt Cap \$	P/E	ROE	P/BV
		mil			
Sechaba Investment Trust Company Ltd.	Brewers	\$288	8.4	174%	14.6
Letshego	Consumer Finance	\$185	12.6	39%	5.0
Botswana Insurance Holdings Ltd.	Multi-line Insurance	\$362	19.8	18%	3.5
Barclays Bank of Botswana Ltd.	Diversified Banks	\$856	23.5	55%	12.8
Standard Charter Bank Botswana	Diversified Banks	\$717	23.3	70%	16.3
First National Bank of Botswana Ltd.	Diversified Banks	\$848	27.9	43%	11.9

Source: S&P/IFC

Ghana



Akwaaba means "welcome" in Ghana, and that sentiment is abundant everywhere in the country. From banners draped in and on buildings in the colors of Ghana's flag to the smiles of people you meet, one quickly discovers that Ghanaians are among the friendliest people in the world. Although the poorest country on our trip, with GDP

per capital of \$289 (versus \$478 in Senegal and \$3819 in Botswana), Ghana feels safe, and there is an attitude of optimism among the country's 22 million population, 10% of whom live the Accra, the capital.



Our five days in Ghana included a dozen visits with companies and local organizations, but first we drove three hours southwest along the Gulf of Guinea to see forts built over three hundred years ago by the British, Dutch, French and Portuguese to control the slave trade. This grim chapter in the history of mankind is brought alive by walking through in the dark, hot dungeons where victims were imprisoned before either dying or being shipped out to the Americas. Thankfully, the world needs different exports from Ghana today such as cocoa, gold, bauxite and timber.

Apart from its sad history, the coast is blessed today with a beautiful shoreline, teeming villages, active fishing fleets and the rich rain forests in Kakum National Park.

The story of bauxite is an interesting example of Frontier Market economic management...or mis-management. Forty years ago, Valco, part of Kaiser Aluminum, decided it could capitalize on Ghana's bauxite deposits by financing a dam to produce hydro-electric power for an aluminum smelter. The dam flooded 7% of the country and created Lake Volta, the largest artificial lake in the world, stretching 300 miles. Valco got 2/3 of the power for its smelter but never built a refinery to turn bauxite into alumina. So today, the bauxite is exported to Jamaica, refined there, and the alumina is then imported to Ghana to make aluminum.

Furthermore, Ghana's electricity needs have grown, and it has renegotiated Valco's contract. Unfortunately the water level in the lake has fallen due to a drought, so the government has required the smelter to suspend operations. Scheduled power outages began last August. There is talk of building another dam, but a more immediate is the prospect of receiving gas from a Nigeria-Cote d'Ivoire pipeline being completed. Also, some regional power grid problems are being solved...and fortunately rainy season has just begun.

Businesses are coping, but there has been a cost to economic growth and to profitability. At the Golden Tulip Hotel, lights go out occasionally, but they quickly switch to three rail-car size diesel generators to keep lights and the kitchen running. On the other hand, Fan Milk, with 70 % of Ghana's dairy market, has lost production and had much spoilage, especially of ice cream at its many dealers.

Fortunately, Ghana celebrated its 50th anniversary of independence last month with many things turning in its favor. For example, the Millennium Challenge Corporation, funded by the U.S., gives grants based on good government and improved policies. It has decided to provide \$547 million for projects that include a cold storage unit at the airport, a road to speed agricultural products to the port, improving ferries on the lake and aid to farmers so they can shift to production of world class pineapples. Meanwhile, Standard Chartered Bank, with a long history in Asia, reports that Chinese public and private investments in the country are growing rapidly.

In all Frontier Markets, finance is a big growth area. Out of Ghana's 22 million people, for example, only 1.5 million have bank accounts, only have 400,000 debit cards and there are just a handful of credit cards. The banks have historically neglected the retail market, preferring to simply take deposits at low rates and either lend to government agencies or buy bonds. But this is changing. We met with seven financial organizations, ranging from sleepy (perhaps asleep) to extremely aggressive. All told the same story of new programs involving outreach and education to broaden the base of retail customers. ATMs in the country will probably double this year, to 400 or so, and point of sale terminals are being rolled out everywhere. Mobile phones also play a part, with prepaid phone cards being treated almost like currency.



At the bottom rung of the financial ladder, we visited Women's Trust, www.womenstrust.org, that makes micro-loans, starting at \$55, to groups of women. Although small, this organization is doing fine work in the village of Pokuase, just outside Accra. Visiting their cramped, humid office on a hot day, we were impressed with the enthusiasm of Gertie Ankrah and Alex Koomson, a board member who is with the Central Bank. Founder Dana Dakin and her colleague Susan Kraeger in the U.S. have created an outstanding organization providing important help to women in Ghana.

The capitalization of the Ghana Stock Exchange is roughly \$3 billion and the float is \$1.375 billion. Liquidity is low, but price earnings ratios are often under 10x and growth rates can be 20% or more.

		Mkt Cap \$	P/E	ROE	P/BV
		mil			
CAL Bank Limited	Diversified Banks	\$35			
Social Security Bank	Diversified Banks	\$44	3.0	81%	2.4
Ghana Commercial Bank	Diversified Banks	\$105	7.2	87%	6.3
FAN Milk Ltd.	Dairy	\$37	11.5	30%	3.4
Guinness Ghana Ltd.	Brewers	\$113	8.2	38%	3.2
Standard Chartered Bank	Diversified Banks	\$288	7.9	50%	3.9
Aluworks Limited	Aluminum	\$31	9.2	52%	4.8
Cocoa Processing Company	Agricultural Products	\$48	14.9	100%	14.9
Produce Buying Company	Agricultural Products	\$129	40.0	49%	19.4
Home Finance Company	Finance	\$45	46.1	28%	13.1

Source: S&P/IFC

Conclusion

Our ten day trip barely scratched the surface of Senegal, Botswana and Ghana. We endured aggressive street merchants in Senegal, temporarily "lost" luggage in South Africa (a credit card missing and electric shaver borrowed... it was quite heavily used!) and a stuck elevator in Ghana. We learned that hotel wake-up calls rarely happen, and that one should check for towels before stepping into the shower. We learned to carry snacks, so we could skip lunch and fight the traffic to the next meeting. But we also learned that people in these countries are both friendly and flexible. At the macro level, we learned that governments are improving and foreign investors are arriving. At the micro level, we saw many excellent companies, often with high quality management teams. They knew their companies inside and out, and they knew what we were looking for in terms of data and information. Their managerial skills are on par with those of businessmen in the developed world; and they have far more creativity and patience.

With similar creativity and patience, investors can participate in this segment of the Frontier Market world. Each country in Africa has its own unique flavor, but many of them combine improving growth prospects with excellent companies at attractive prices.



Aluworks, aluminum rolling mill, Tema, Ghana

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