AFRICA PREBRIEF

On The J.P. Morgan NEXGEM Report

The new **JP Morgan 'Next Generation' Emerging Markets Index (NEXGEM) (http://www.thestreet.com/story/11343617/1/jp-morgan-launches-the-first-fixed-income-frontier-markets-index-the-nexgem8480-jp-morgan-next-generation-markets-index.html)** which seeks to establish an index for 'smaller, less liquid,' emerging markets individually covers 6 **Sub-Saharan African** nations: **Gabon, Ghana**, **Ivory Coast**, **Kenya, Nigeria** and **Zambia**. It provides a decent snapshot outline of some of the factors impacting economic growth, macro-policy and currency stability in each country. Below is a brief mention of aspects of the 1-sheet country outlooks for 2012 that caught our attention, and our comment:

Gabon – JP Morgan writes of a 'growth boost' it expects to accrue to the country due to its hosting of the 2012 **Africa Cup**. Some have doubted this but we agree with the thinking that 'sport mega events' contribute to economic growth in a measurable way [see ***APB*** **August 18, 2010, "South African Retail Sales Climb Due To World Cup"** for estimates of 1% growth due to the tournament and "Mega Events Impact On Economic Growth" published in ***African Journal of Business Management*** Vol. 5 (16) http://www.academicjournals.org/AJBM/PDF/pdf2011/18Aug/Anton%20et%20al.pdf]. The report doesn't specify the infrastructure investments associated with the Africa Cup nor with the nation's 50-year independence celebration which could generate 50,000 jobs over 3 years financed by **China**, **Singapore** and **India** (http://www.africaneconomicoutlook.org/en/countries/central-africa/gabon/).

Ghana – The report is spot on to point to the cedi's significant weakness since September and notes that the much celebrated Jubilee oil find is not producing the expected 120,000 bbl/d level (http://af.reuters.com/article/idAFJOE7B800W20111209) but does not envision either of these factors influencing the upcoming elections in 2012 which it expects to 'be a close call, but peaceful.' We are not so sure. The inflation is the worst in years 4 years and headlines like Monday's "Cedi Drops Faster Under Mills Than Kufuor" (http://www.thestatesmanonline.com/pages/news_detail.php?newsid=10849&section=1) in *The Statesmen* are warning signs. Decreased purchasing power and the expected decline in GDP from 13% this year (half of which comes from oil) to 8% in 2012 will matter to an electorate that has patiently waited for increased oil revenue to begin to address wealth distribution problems. This is no small matter with the government's accounting of oil barrels and revenues hotly challenged (see "NDC Gov't Is Lying About The Missing 4.58 Million Barrel Crude Oil" http://www.ghanamma.com/2011/12/ndc-govt-is-lying-about-the-missing-4-58-million-barrel-crude-oil/). We aren't sure the country's political environment can withstand the scenario the *Economists Intelligence Unit (EIU)* points to: "Recent opinion polls in Ghana are putting the current president, John Atta Mills of the ruling National

Democratic Congress (NDC), in a close race with Nana Akufo Addo, presidential candidate of their main rival, the New Patriotic Party (NPP). A local market research company, Synovate, conducted a poll in September that put Mr Akufo Addo ahead, with 48% of those surveyed intending to vote for him compared with 41% for Mr Atta Mills. This national figure masked regional variations. For example, Mr Akufo Addo was behind Mr Atta Mills in the Greater Accra Region (the capital area), with support of 37% to Mr Atta Mills' 46%. Greater Accra is a key region in any presidential poll, given the size of the population. Although these numbers point in different directions, one thing they have in common is that neither man enjoyed support of over 50%, which, if occurring at the 2012 election itself, would necessitate a second round of voting, as it did in 2008. Indeed, more and more the 2012 election looks to be a repeat of the 2008 election, where Mr Atta Mills defeated Mr Akufo Addo by less than 1% of the vote after going to a second round."

Ivory Coast – We feel NEXGEM exaggerates the positive contribution to national unity that recent parliamentary elections may have, "*They ran peacefully but saw a low turnout as people avoided polling areas fearing violence. The opposition was divided. While former President Gbagbo's, the FPI, did not participate, some of its members did independently and so did three smaller break-away parties. This should help guarantee some representation of the 46% of the population that voted for Gbagbo at last year's elections, thus helping the process of national reconciliation, in our view. The FPI had announced that it would boycott elections because it feared irregularities and in protest against the transfer of its leader to The Hague. The ICC said that it will continue its investigations and confirm only next June whether Gbagbo will be tried on different counts for crimes against humanity.*" Our conversations with Ivorians in the country and in the diaspora convince us that no election matters as much as the ICC handling of Gbagbo (*hundreds* of his supporters have gone as far as to protest the ICC directly outside its headquarters in the ***Netherlands***: http://www.cbsnews.com/8301-501714_162-57340774/gbagbo-supporters-protest-outside-icc/). There can be no national unity until that matter is resolved and the FPI's (Ivorian Popular Front) grievances – including allegations of French manipulation (http://www.news24.com/Africa/News/Gbagbo-blames-France-20111205) – are addressed. No amount of Western largesse can serve as balm for these wounds. Ironically, the NEXGEM report seems to give the ICC variable and its repercussions more weight in Kenya than in the Ivory Coast, where it is much more potentially explosive.

Kenya – The report astutely notes the enormous level of support the IMF has provided Kenya this year, "*Kenya requested additional financing from the IMF, which granted it an extra US$252 million on top of the US$509 million facility already in place*." As we have previously commented these amounts almost perfectly (and not coincidentally) match the dollar reserves lost in the struggle to prop up the shilling and provide drought-humanitarian relief (see ***APB* August 1, 2011, "Kenya: Post-MPC Meeting – Opaqueness Not Inflation The Problem"**). We were struck that in assessing risks for Kenya in 2012 an ICC case is mentioned ("*Some questions remain, instead over the potential repercussions of the ICC case against six key government officials – one of which is a likely presidential candidate. This remains a risk to watch."*) while the greater geopolitical risk to economic growth stemming from Kenya's invasion of Somalia in response to al-Shabab and increased U.S. militarization (see ***APB* October 18, 2011, "U.S.**

Foreign Policy: The Greatest Threat To East African Economic Growth") does not receive a word of attention.

Nigeria – The NEXGEM report is right on naira weakness ("…*we are not highly confident that further naira weakness will be avoided in 2012*") and justified in its positive outlook on reforms due to the "appointment of a strong cabinet" (see **APB September 15, 2011, "Nigeria: A Top-Down Dream Team?"**). But a team is often only as good as its manager and Nigeria will only rise as high as its commitment to infrastructure - as we wrote in September, "The combined dream team of **Security and Exchange Commission Director General Arunmah Oteh**; incoming **Finance and Economic Coordinating Minister Ngozi Okonjo-Iweala**; **Central Bank Governor Sanusi Lamido Sanusi**, and **Assets Management Corporation (AMCON) head Mustafa Chike-Obi** is a delightful sign of Nigeria's growing ability to nurture, retain and attract its best minds. But the likelihood is that the foursome will be hard for **President Goodluck Jonathan** to manage as a cohesive unit. We expect the sum of their efforts to be net positive but too top-down in orientation and possibly – with the exception of Mr. Sanusi - not focused or radical enough to address the fundamental concern of infrastructure, perhaps the only consensus issue among the country's electorate. While **Oteh/Okonjo-Iweala/Sanusi/Chike-Obi** is perhaps the most formidable economic team Nigeria has *ever* assembled we aren't convinced that the foursome will be able to resist turf wars and the temptation to assume too broad of a portfolio, too soon. But if they can collaborate and Nigeria can simply get infrastructure finance right, everything else will fall into place." While hopes for the 'dream team' are high (http://www.ghanamma.com/2011/12/ndc-govt-is-lying-about-the-missing-4-58-million-barrel-crude-oil/) the new 2012 budget raises as many questions as it answers (http://blogs.ft.com/beyond-brics/2011/12/13/nigerias-budget-only-surface-deep/#axzz1gWHJv9uW).

Zambia – The report notes an important detail left out of many assessments of growth prospects in Zambia - **President Sata**'s pulling on the fiscal lever by reducing Pay-As-You-Earn (NEXGEM: "…*the budget increases the tax exempt income threshold from ZMK12 million to ZMK 24 million per year*") in a way that will increase disposable income (**Finance Minister Alexander Chkwanda** advertises "*The PAYE restructuring increases disposable incomes of the workforce by about K1 trillion which can only be salutary for the economy*" http://postzambia.com/post-read_article.php?articleId=23716&highlight=income%20threshold) and capital formation from the ground up and serve as a potential buffer against bracket creep due to inflation. JP Morgan also advocates a wise strategy relative to the Zambian kwacha, juxtaposed to risk and uncertainty "*In FX we are sidelined: The kwacha is likely to remain weak into year-end, while the outlook for next year is less clear given opposing forces at play – an expected rise in tax receipts and FX inflows on one hand, lax fiscals (with a focus on infrastructure spending), easing monetary policy and softer copper prices on the other. Coupling this with BoZ likely to intervene only to smoothen volatility makes us stay sidelined the ZMK.*"

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