Public Savings in Africa: Do Sovereign Wealth Funds serve Development?

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Overview

<table>
<thead>
<tr>
<th>Number of SWFs</th>
<th>&gt;100</th>
<th>19 (20%)</th>
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<tbody>
<tr>
<td>Asset Capitalisation (as of 2021)</td>
<td>$8 trillion</td>
<td>$70 billion (0.1%)</td>
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Why ask this question now?

- **Time horizon:** Half of Africa’s SWFs were created in the 2000s.

- **Usefulness:** Despite their small share of the global SWF capitalisation, the value of African SWFs is not insignificant compared to the continent’s financing needs & could contribute to financing the SDGs.

- **Depleting fossil fuel reserves & reducing demand:** Much of the capital base of SWFs derived from taxes, royalties, dividends, and licences from oil and gas (O&G) and, to a lesser extent, mining.

- **Rising demand for metals as part of the global energy transition**, which may imply higher public revenues for critical minerals exports in Africa, & raises questions on the suitability of SWFs in the near future.

  ➢ Given these events and trends, now is a good time to reassess the current role and future potential of SWFs in Africa.
Sovereign Wealth funds in Africa: (shrinking) size

- The 19 SWFs in Africa have a total estimated capitalisation of US$72.9 billion in 2020, which is a staggering 67% decline compared to 2013 ($226 billion).

- In 2013, Africa’s largest SWFs were those in Algeria, Libya and Angola (totalling 90% of assets).

- The only large fund that remains today is that of Libya (US$60 billion), followed – at some considerable distance– by Botswana’s Pula fund (around US$ 5 billion).

- The close of the 2000s commodities super-cycle is the main driver of the substantial fall (and the COVID-19 pandemic is likely to have seen a further decline).
### Sovereign Wealth funds in Africa: Types

<table>
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<tr>
<th>Fund Type</th>
<th>Objectives</th>
<th>Asset types</th>
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| **Stabilisation Fund**                 | • Provide a fiscal buffer in the case of a shock, to avoid increasing debt, or at least cushion the impact  
• Dampen the exchange rate volatility associated with shocks  
• Aims to prevent the ‘resource curse’ and the Dutch disease more specifically | Liquid & low yielding (e.g. sovereign bonds)                                                                                                          |
| **Intergenerational savings fund**     | • Transfer some of the current resource wealth to future generations  
• Potentially meet future liabilities (e.g. pensions)                                                                                                                                                       | Illiquid (investment-grade bonds of long duration, sovereign debt, commercial property)       |
| **Development Fund**                   | • Encourage national development by investing in domestic infrastructure & equity of companies with growth potential  
• Transfer and manage ‘privatised’ assets  
• Invest in equity abroad to foster technology transfer and JVs with domestic partners | Relatively illiquid (e.g. equity in unlisted start-ups)                                                                                             |
Sovereign Wealth funds in Africa: Types

- **Algeria**: Fond de regulation des recettes (2000)
- **Rwanda**: Agaciro Development Fund (2012)
- **Botswana**: Pula Fund (1994)
- **Sudan**: Oil Revenue Stabilisation Account (2012)
- **Uganda**: Petroleum Investment Fund (2015)
- **Angola**: Fondo Soberano de Angola (2012)
- **Gabon**: Strategic Investment Fund (1998/2012)
- **Equatorial Guinea**: Fund for future generations (2004)
- **Mauritania**: National Fund for Hydrocarbon reserves (2006)
- **Libya**: Libyan Investment Authority (2006)
- **Senegal**: FONSIS (2012)
- **Chad**: Oil Revenue Management Plan (2006)
- **Nigeria**: Sovereign Investment Authority (2008/2012)
- **Tanzania**: Draft Legislation
- **Mozambique**: Draft Legislation
- **Ghana**: Stabilisation Fund (2011)
- **Infrastructure Investment Fund (1998)
Overlaps

• Distinctions between funds are not watertight and a fund set up for one purpose may over time take on another.

• Governments can establish more than one fund, each with its own objective.
  ➢ The Ghana Stabilisation Fund is intended to cushion public spending during periods of unanticipated petroleum revenue shortfall, the Ghana Heritage Fund is an intergenerational investment fund, and the Ghana Infrastructure Investment Fund is an SDF.
  ➢ Nigeria’s Sovereign Investment Authority likewise has three funds: stabilization, infrastructure, & a ‘Future Generations’ fund.

• SWFs with more than one simultaneous objective for a single fund are also quite common:
  ➢ Botswana’s Pula Fund & Mozambique’s proposed SWF have both stabilization and intergenerational savings objectives.
  ➢ Running several funds entails additional administration, but has the merit of only one objective against which to match assets.
  ➢ If a single fund has several objectives then its portfolio should reflect the relative weight of each objective to policymakers. When the purpose of the fund is unclear, its governance becomes harder.
Sovereign Wealth funds in Africa: governance issues

• SWFs are vulnerable to mismanagement & corruption.

• Examples illustrate governance challenges of SWFs:
  ➢ Angola FSDEA
  ➢ Equatorial Guinea’s Fonds de Réserves pour Générations Futures
  ➢ Libyan Investment Authority
  ➢ Algeria’s FRR

• Nigeria is highest ranking African country in the 2019 SWF transparency scoreboard and the only country above the SWF scoreboard average.

<table>
<thead>
<tr>
<th>Table 1: Results of the 2019 SWF scoreboard (African countries)</th>
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</thead>
<tbody>
<tr>
<td><strong>Country</strong></td>
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<tr>
<td>Nigeria</td>
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<tr>
<td>Angola</td>
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<tr>
<td>Botswana</td>
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<tr>
<td>Rwanda</td>
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<td>Senegal</td>
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<td>Ghana</td>
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<td>Morocco</td>
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<td>Kiribati</td>
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<tr>
<td>Algeria</td>
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<tr>
<td>Libya</td>
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<tr>
<td>Equatorial Guinea</td>
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<tr>
<td>Global Average (64 funds)</td>
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Source: Maire et al. (2021)
* Member of IFSWF.
Which SWFs offer a better use of resource revenues in Africa? Is it even desirable for African countries to set up SWFs, in contrast to alternatives such as paying off public debt, setting up a national development bank?
If sold, risks that asset prices turns against sellers (e.g. GFC).

If assets are intended for future public liabilities (e.g. pensions), crisis sales could endanger the capital base & require recapitalisation.

High opportunity costs for current generations and for wealth transfer through productive development and improving living conditions.

If the country has no access to financial reserves and support in case of external shock.

If the interest rate on sovereign debt exceeds returns on investments of the SWFs.

If the needs of current generation in terms of living conditions are already met.

If institutional capacity exists (or is expected to be built within a reasonable time frame) to contain state failures.

Helps deal with unanticipated external shocks.

Unlikely that LIC or MIC would have a fund of sufficient scale to cushion effects of a large shock (e.g. Nigeria with COVID or oil price shock).

Need an international monetary system that provides adequate help.

Short-dated liquid assets may have low returns (US treasury bonds).

reduce the cost of sovereign borrowing by improving credit ratings, which, in many African countries, is in excess of what they can earn on liquid financial instruments:

- reduce the current debt service

Assumption that capital markets remain open to African economies in case of a shock (esp. global shocks).

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Assumption that capital markets remain open to African economies in case of a shock (esp. global shocks).

Can support intergenerational equity for non-renewable resource revenues.

Could be sold down in cases of emergencies.

If sold, risks that asset prices turns against sellers (e.g. GFC).

If assets are intended for future public liabilities (e.g. pensions), crisis sales could endanger the capital base & require recapitalisation.

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High opportunity costs for current generations and for wealth transfer through productive development and improving living conditions.

Can draw on private capital by issuing bonds, and partner with foreign investors.

Helps overcome market failures prevent investments in productive capacity development.

NDBs face more scrutiny than SDFs as the former have commercial credit ratings if they issue bonds.

Success depends on containing state failure & political capture, building the requisite institutional capacity to evaluate prospective investments and loans together with the necessary transparency & oversight.
Are SWFs really a good way to use resource revenues in Africa?

Figure 7: Infant mortality rate in relation to SWFs capitalization per capita

Source: authors’ construction using their own calculations and data from the World Development Indicators
If the country has no access to financial reserves and support in case of external shock

If the interest rate on sovereign debt exceeds returns on investments of the SWFs

If the needs of current generation in terms of living conditions are already met.

If institutional capacity exists (or is expected to be built within a reasonable time frame) to contain state failures

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**Stabilization Fund**

- Helps deal with unanticipated external shocks
- Unlikely that LIC or MIC would have a fund of sufficient scale to cushion effects of a large shock (e.g. Nigeria with COVID or oil price shock)
- Need an international monetary system that provides adequate help.
- Short-dated liquid assets may have low returns (US treasury bonds)

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**Paying down debt**

- reduce the cost of sovereign borrowing by improving credit ratings, which, in many African countries, is in excess of what they can earn on liquid financial instruments:
  - reduce the current debt service
- Assumption that capital markets remain open to African economies in case of a shock (esp. global shocks)

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**Intergenerational Fund**

- Can support intergenerational equity for non-renewable resource revenues.
- Can be sold down in cases of emergencies
- If sold, risks that asset prices turns against sellers (e.g. GFC).
- If assets are intended for future public liabilities (e.g. pensions), crisis sales could endanger the capital base & require recapitalisation
- High opportunity costs for current generations and for wealth transfer through productive development and improving living conditions

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**Development Finance fund (SDF & NDB)**

- Can draw on private capital by issuing bonds, and partner with foreign investors.
- Helps overcome market failures prevent investments in productive capacity development
- NDBs face more scrutiny than SDFs as the former have commercial credit ratings if they issue bonds
- Success depends on containing state failure & political capture, building the requisite institutional capacity to evaluate prospective investments and loans together with the necessary transparency & oversight
The implications of the climate crisis for the role of SWFs

• The climate crisis also affects the best use of public savings in Africa, where high commodity-dependence makes countries exceptionally vulnerable to adverse effects of climate stress as well as global decarbonisation.

• Climate risks: Agriculture and food security.

• Transition risks: Fossil fuels represent around 40% of African exports, with countries such as Algeria, Angola, Chad, Nigeria and Sudan being highly dependent on them as a source of revenue.

➢ Orienting sovereign wealth towards productive investments for economic diversification.
Overview

- Although many African countries have NDBs, most are quite small, with limited access to finance (average mean asset size of $1.8 billion)

- The capitalisation of African NDBs varies tremendously

NDBs in Africa by size of assets (in USD thousands)
Total: 38.8 USD billion

South Africa - IDC, 10000

Development Bank of Southern Africa (DBSA), 5800

Bank of Industry (Nigeria), 3400

South Africa - Land and Agricultural Development Bank, 3055

Egypt-Indu... Dev... and Wor... Bank, 597.6

Angola Banco de Poupança e Crédito, 2300
How do NDBs compare with SWFs in Africa?

- The paucity of the data on their capitalization makes the comparison a rough one.
- In total, the capital base of SWFs is larger, but their assets have shrunk at a very fast pace compared to the capital of Africa’s NDBs.
- There is therefore considerable scope for rethinking the transfer of public savings from SWFs to NDBs.

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<th>SWFs</th>
<th>19 in Africa</th>
<th>73.6 USD billion (2020)</th>
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<tr>
<td>NDBs</td>
<td>23 in Africa</td>
<td>38.8 USD billion (2011-2015)</td>
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How do NDBs compare with SWFs in Africa?

- The paucity of the data on their capitalization makes the comparison a rough one.
- In total, the capital base of SWFs is larger (more countries have them), but their assets have shrunk at a very fast pace compared to the capital of Africa’s NDBs.
- There is therefore considerable scope for rethinking the transfer of public savings from SWFs to NDBs.
Takeaways and concluding remarks

• **SWFs have stalled in Africa**, and their capital base is in decline. Nevertheless, SWFs are still on the policy agenda of O&G and/or mineral-rich economies.

• Fiscal stabilization funds are useful and necessary but entail **considerable opportunity costs**, & a stronger framework of multilateral financial assistance would reduce such ‘self-insurance need’.

• Returns on **investments in human capital and critical infrastructure** far exceed those on financial investments and offer superior intergenerational wealth transfer in addition to benefiting the current generation (many of whom live in dire poverty).

• The case for an **intergenerational savings SWF is generally weak**, except for middle-income countries with very large revenues.

• There is a stronger case for a **Sovereign Development Fund (SDF) and/or a National Development Bank (NDB)** to fund productive investments, provided that they have clear mandates, strong governance and legislative oversight.

• **Recognising political realities:** It is difficult for governments to pursue a consistent public savings strategy. Political expediency can win out, especially around election time and fiscal rules introduced with the best intentions often break down.
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Tony Addison¹ and Amir Lebdioui²

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