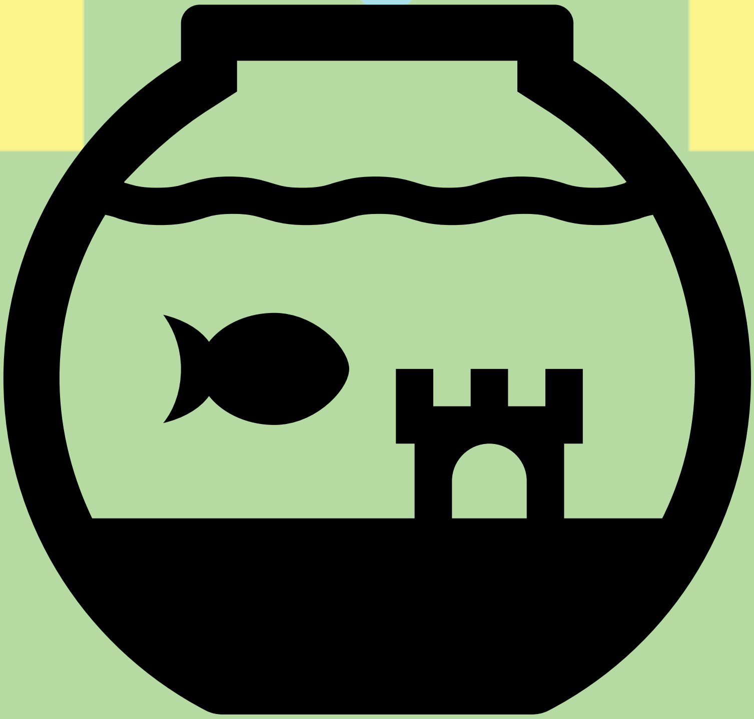
Centre for Development Finance Studies



In Search of a Rising Tide:
Can African Capital Markets Lift the Continent's Futures?

The CDFS Slightly Longer Read – November 2025

Local Capital Markets Development – Chapter 1

This CDFS Slightly Longer Read in Brief

As the development finance system seeks to address the local currency issue, the role it must play to catalyse the development of local capital markets is increasingly recognised. As the OECD's February 2025 report suggests, local pools of capital are inherently better positioned to match local currency liabilities with local currency assets. But to do so they must have local capital markets capable of delivering the necessary intermediation. Local capital markets are not a silver bullet for economic development, but rather serve a specific but crucial function: enabling local pools of capital to gain exposure to their own economic growth while naturally matching local currency assets and liabilities. This Slightly Longer Read sets out to identify the barriers that prevent capital markets in Kenya and Nigeria from fulfilling this foundational role and to formulate solutions for their removal.

The current situation should not, and cannot, be explained away by a lack of demand, by restrictive regulation or by technological backwardness. Pension funds and insurers in both countries are aware of the dangers of excessive concentration in government debt and have expressed willingness to diversify. Retail investor demand was demonstrated during the KenGen and Safaricom IPOs in Kenya. Both countries already run advanced trading and settlement platforms on a par with those in developed markets. The binding constraints are instead structural and stem from three mutually reinforcing dynamics: fiscal crowding out, supply shortages and institutional conservatism.

Government securities absorb the bulk of institutional savings. Sovereign yields crowd out private financing and deter firms from issuing bonds.

The supply of investable companies on public equity markets remains thin, with just over sixty listings in Kenya and around one hundred and seventy in Nigeria. Many promising firms are held by private equity funds significantly backed by development finance, but the mechanism through which this translates into listings appears to be broken and public capital markets are not construed as a natural and competitive exit route.

Institutional investors themselves are fragmented, under-resourced and at times governed by fiduciary interpretations that privilege capital preservation over the long-term returns needed to match liabilities. The result is a self-reinforcing cycle in which markets fail to deepen, institutional investors cannot diversify, and private firms cannot raise long-term growth capital. Pensioners and policyholders are left over-exposed to inflation and capital markets fail to support job creation and economic growth.

Breaking this vicious cycle requires coordinated intervention across three fronts, with timing and synchronisation essential to success.

A Grand Bargain is necessary to relieve the fiscal pressure on domestic institutional capital, allowing its custodians to reallocate towards equities and corporate bonds. This would require coordination with governments to ensure that the reallocation strengthens markets. Development finance stakeholders and eventually global investors should assume sovereign risk they can absorb, while domestic institutions take on the equity risk they need to secure long-term returns. Governments would thus maintain access to local financing whilst creating the fiscal and market conditions for private growth. This process may in addition compress government bond yields, making private sector assets relatively more attractive and creating fiscal space.

Development finance actors should seek to address the supply issue, redirecting capital through local markets by anchoring domestic bond and equity offerings, supporting secondary-market liquidity, and pressing private equity portfolio companies to list publicly. Governments can further broaden supply through carefully structured privatisations of viable state-owned enterprises.

Pension funds and insurers should pursue consolidation to achieve the scale necessary for sophisticated investment management, clarify fiduciary duties to recognise that prudent long-term investment necessarily includes equity allocation, and build the expertise required for more sophisticated investment strategies.

The potential benefits are substantial. A reallocation of just one and a half billion dollars from Kenyan pension funds into equities would lift the market's capitalisation by nearly ten per cent.

With strategic coordination, existing development finance resources could be channelled through rather than around capital markets, creating financial systems capable of supporting sustainable growth and providing domestic savers the financial security that developed economies take for granted.

1. **Shallow, Narrow, Hollow Waters.** Public capital markets in Kenya and Nigeria

A sad but inevitable feature of development finance research is that it must often begin with a sobering account of the current state of affairs.

There should be no doubt that no sustainable solution to the local currency issue, that no just financing of sustainable development can be found without the development of fit-for-purpose financial systems.

While our 'For whom the banks roll' series focusses on the dynamics affecting the commercial banking systems of Kenya and Nigeria, this Slightly Longer Read is the first episode of a series in turn examining their public capital markets. This dual track does not mean to ignore the role of private capital markets, but is derived from a recognition of their much smaller global scale, and does in any case incorporate how they impact the development of their bigger equivalents.

It is to the stock and bond markets of these two countries that we therefore turn our attention, again acknowledging both the important role that derivatives markets must eventually play and the fact that their nascent nature makes them all but unobservable.

This is not the place for exhaustive statistics, but the numbers do paint a sobering, if not frightening picture.

On the equity front, Kenyan and Nigerian stock markets are small, whether in absolute or relative terms. Nigeria's NGX market capitalisation stands at the time of writing at USD 57 billion, or 23% of GDP, while Kenya's NSE has a market capitalisation of USD 17 billion, accounting for an even lower 13% of the country's GDP.

The Johannesburg Stock Exchange has a market capitalisation of USD 1 trillion, a multiple of the South Africa's GDP. The market capitalisation ratio to GDP of the London Stock Exchange is 110%. The EU average is somewhere between 50 and 60%.

Size is not the only matter. Nigerian and Kenyan public equity capital markets are highly concentrated, illiquid and they are not growing.

Figure 1: NSE, NGX and JSE statistics

As illustrated in Figure 1, Kenya's NSE is home to just over 60 companies, while Nigeria's NGX manages just over 150. The top 5 listings in the former account for 66% of aggregate market capitalisation, while they add up to 41% of the latter. Safaricom PLC alone contributes in excess of 40% of the NSE's total market capitalisation.

And things are not looking up. No IPOs have taken place on the NSE over the last decade. Zero. There have admittedly been two or three listings through introductions, most recently that of SKOL on the SME segment, but these transactions did not raise new capital.

Few stocks to choose from mean few reasons to trade in and out. Trading numbers are no more impressive, with the NSE providing the scene for USD 74 million worth of trading per month, and the NGX for USD 166 million. The JSE sees over USD 25 billion of trading per month.

The reality is that, such as they are, market capitalisation numbers still paint too rosy a picture. Average free floats on the NSE and the NGX are around the 40% mark, compared to developed markets where they are consistently – and in places significantly – in excess of 60%. And this yet again fails to provide the real picture. While Nigerian and African banking stocks tend to have high free floats (78% for KCB Group in Kenya, 84% for Zenith Bank in Nigeria), top listings like Safaricom or MTN Nigeria hover around the 25% mark, as a result of strategic stakes jealously held by their foreign parents or indeed national governments.

Our conversations with Nigerian stakeholders indicated that many companies only list minimal stakes, and often do so at all for political rather than financial reasons, leaving little in the way of shares to trade.

Bond markets arguably present an even more striking imbalance. Government debt securities make up respectively 98% and 94% of the bonds outstanding in Kenya and Nigeria. Corporate bond markets are, for all intents and purposes, non-existent.

The "Africa Rising" investment bubble of the early 2010s exemplifies the structural limitations of capital markets across the continent. During this period, hundreds of millions in northern hemisphere capital flowed into African public equity markets, driven by institutional enthusiasm and fear-of-missing-out marketing tactics.

However, the combination of low public floats and limited liquidity meant that the narrow selection of available stocks experienced unsustainable valuation increases, with companies such as Nigerian Breweries trading at sixty times earnings. Crucially, when excess demand should have prompted investment banks and corporates to expand market supply through new listings and capital raising activities, this market response failed to materialise.

The subsequent market correction demonstrated the inherent fragility of these underdeveloped capital markets. When investor sentiment shifted and capital began to exit, the absence of sufficient liquidity and market depth resulted in a precipitous collapse across African equity markets.

The aftermath proved particularly damaging to local institutional investors, whose heavy losses increased risk aversion and stunted organic market development. This cycle of boom and bust left African capital markets, including those in Nigeria and Kenya, essentially unchanged from their pre-bubble state.

They remain shallow in terms of available instruments and narrow in terms of market participation, thereby limiting their capacity to support long-term economic growth and provide adequate financial security for domestic investors.

Glimmers of hope

The recent performance of both the Nigerian and Kenyan stock markets may present an opportunity that must be seized upon.

Kenya's capital markets have for instance experienced notable momentum in recent months, with the Central Bank's reduction of the policy rate from 13.0% to 9.25% compressing government securities yields and catalysing a shift in investor interest towards equities. The Nairobi All Share Index rose 15.2% in Q3 2025, whilst equity turnover surged 55.34% quarter-on-quarter and an impressive 165.79% year-on-year, accompanied by two new listings that expanded investment options. However, this resurgence must be viewed in proper perspective: the NSE has merely recovered to its 2021 high-water mark rather than charting new territory, and whilst trading volumes have improved, they remain modest by comparative standards. The year-on-year compression of Treasury bill yields has created precisely the conditions where alternative investments become more attractive to institutional allocators, yet this window of opportunity risks closing without a meaningful expansion of investable supply. The question facing Kenya's capital markets is whether the corporate sector and development finance stakeholders can respond with sufficient pace and scale to capitalise on this favourable alignment of monetary conditions, shifting investor appetite, and nascent market momentum before the tide turns once more.

2. **Small pond, one big fish.** Inevitable Institutional Asset (mis-) Allocation

No matter how short the report, it is at this stage important to ensure that a significant number of readers do not leave us full of righteous indignation. There is here no suggestion that the suboptimal allocation of institutional assets in Nigeria and Kenya is anything other than the logical result of a set of factors their custodians do not control.

If there is little for sale, it may not be completely surprising for little buying to take place.

The resulting institutional investor behaviour systematically perpetuates the lack of productive capital formation. Pension funds and insurance companies, which should serve as the backbone of domestic capital markets, instead effectively function as captive buyers of government debt. The asset allocations of Kenyan and Nigerian pension funds are illustrated in Figure 2, as are the corresponding regulatory limits that will be discussed later.

Kenyan institutional investors demonstrate allocation patterns that directly contradict their role as long-term capital providers. Pension funds, managing approximately seventeen billion dollars in assets representing 14% of GDP, allocate 50-60% to government bonds and 20% to guaranteed funds that in turn mostly hold government debt, while dedicating less than 12% to equities. This equity allocation has declined from 19% in 2019, indicating movement away from rather than toward productive investment.

Corporate bonds allocations remain below half a per cent in Kenya.

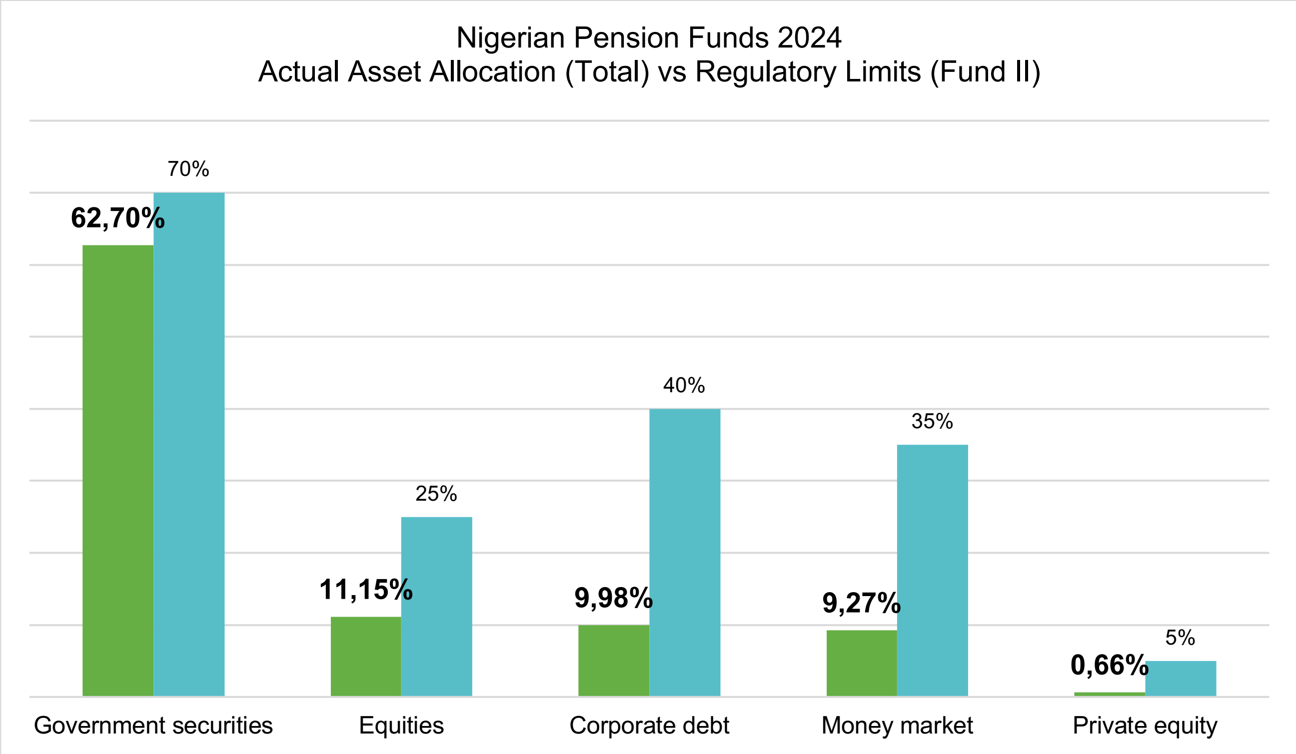
Kenyan Insurance companies, controlling eight and a half billion dollars in assets, exhibit even more conservative patterns with 75% allocated to government securities and only 5% to equities, with this allocation decreasing since 2021.

Nigeria's pension sector, managing approximately fifteen billion dollars in assets, representing approximately 7% of GDP, shows similar misallocation patterns. Federal Government of Nigeria bonds absorb over 60% of pension fund assets, while domestic equity allocation remain inscribed in the 5 to 10% range. Short-term treasury bills attract an additional 5 to 15%, meaning that government securities claim the vast majority of institutional capital that could otherwise fund private sector growth and development.

While the assets under management among Kenya’s and Nigeria’s pension sectors represent a comparatively small but still significant portion of the GDP in the respective countries, their capital is not allocated to assets providing impetus for the long-term growth and prosperity of their respective local capital markets.

This allocation pattern represents a systemic failure in capital intermediation with far-reaching economic consequences. Private sector companies face severe constraints in accessing long-term capital for growth and expansion, leading to stunted corporate development and limited public market participation.

The shortage of viable public listed companies creates extreme market concentration as illustrated above. The lack of institutional participation curbs market depth and increases volatility, creating adverse conditions that discourage new listings and further concentrate trading activity. The overall effect constrains economic growth by limiting private sector investment and reducing the efficiency of capital allocation across the economy.



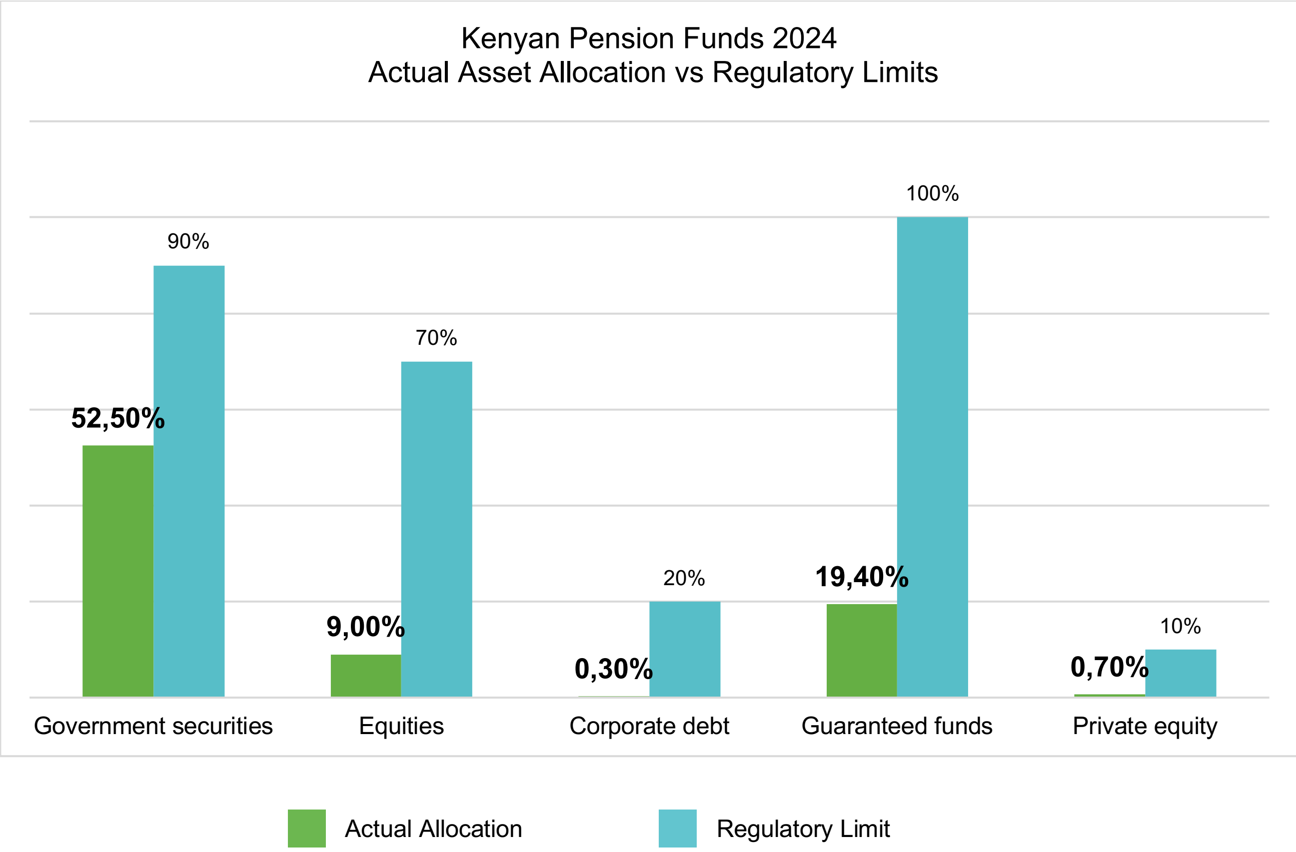


Figure 2: Nigerian & Kenyan Pension Funds Asset Allocation vs Regulatory Limits

3. **Red Herrings.** Where not to look for the causes of stalled market development

It's not the regulator.
As clearly illustrated by Figure 2, the limits put by regulatory or prudential frameworks on the proportion of their assets pension funds in Nigeria and Kenya are allowed to allocate to risk assets are not a credible constraint.

Regulatory frameworks for example allow for much higher allocations by pension funds towards public and private equity. There are in fact more granular categories than displayed here where the introduction of permissible allocations has yet to result in any observable investments.

A case can, and later will, be made that it may not be sufficient for regulatory bodies to allow for diversification and that they should do more to drive institutional assets towards riskier asset classes better able to meet their long-term liabilities and to shelter their members against the worst of inflation.

There simply however cannot be any suggestion that pension funds in Kenya or Nigeria are forbidden from investing in a manner that would both fuel and secure the rewards of their domestic economic growth.

It's not demand.
Direct engagement with the senior management teams of pension industry bodies in both countries further indicate that Kenyan and Nigerian pension funds are fully aware of the systemic risk their inadequate diversification levels present and are keen to reallocate assets to public equity.

The demand is there, the issue they identify is the absence of supply of investment opportunities, from both the quantitative and qualitative standpoint.

Retail demand for quality equity offerings has been conclusively demonstrated in both countries. Kenya's experience with the Initial Public Offerings (IPOs) of KenGen in 2006 and Safaricom in 2008 generated approximately one million new retail accounts, proving substantial local appetite for attractive investment opportunities.

A very large portion of these accounts are today inactive due to a large extent to poor performance and failures in the equity and debt markets[1]. Nigeria maintains 30 to 40% retail participation by volume, with domestic investors, institutional and retail accounting for 80 to 90% of equity flows in recent years. These figures contradict assumptions about insufficient local demand and suggest that the constraint lies elsewhere[2].

It certainly is not technology.
Both countries have successfully implemented sophisticated technological infrastructure that functions effectively. Kenya operates the Millennium Exchange platform. An ultra-low latency platform solution, allowing for advanced order types and high output. The situation is the same in Nigeria with the exchange running on Nasdaq's X-Gen platform. The securities platforms in Nigeria and Kenya allow for real-time settlement, electronic custody and clearing mechanisms, and innovative mobile-enabled bond platforms like M-Akiba. Without doubt, these systems

[1] "1.5 million accounts inactive as IPO drought bites", Business Daily, 10 Sept 2024 (www.businessdailyafrica.com/bd/markets/capital-markets/1-5m-idle-nse-accounts-frozen-as-ipo-drought-bites-4756976)

[2] https://ngxgroup.com/exchange/data/foreign-portfolio-investment-report/

process transactions efficiently and provide the technological foundation necessary for any modern capital markets. Table 1 provides the basis for comparison against the more developed JSE and NASDAQ Stockholm.

Arguments around the potential of Artificial Intelligence (AI) to provide a path towards vibrant local capital markets should be met with a healthy dose of scepticism, considering the underwhelming results from implementing state of the art technology systems in Nigeria and Kenya. Despite these capabilities, market performance continues to deteriorate rather than improve.

Kenya's equity turnover declined from approximately two billion dollars in 2016 to one billion dollars in 2024, indicating worsening liquidity conditions despite infrastructure improvements. Nigeria's trading velocity fell from 15 to 18% before 2008 to 8 to 12% by 2023, well below emerging market averages. Corporate bond markets remain virtually non-existent in both countries, suggesting that the problems lie in structural rather than technical constraints.

African exchanges' adoption of cutting-edge trading and clearing systems demonstrates a clear commitment to global best practice. But while these platforms are technically world-class, their high specification does not create a market; liquidity, active participation, and sufficient transaction volumes are required for an exchange to function effectively.

Some of the rapid adoption of advanced systems may be facilitated by donor support or partnerships with foreign technology vendors, making it financially feasible for nascent markets to deploy top-tier infrastructure. Nevertheless, these factors are secondary: the core constraints remain structural. No matter how modern the technology, African equity markets are limited by market width and depth, not by the sophistication of their trading or post-trade systems.

If the constraints are not regulatory, technological, or demand-related, then the causes of market stagnation must lie in the structural dynamics that govern how capital flows through these economies.

Exchange	Latency / Throughput	Advanced Order Types	CCP / Margining	CSD / Post-Trade Features	RTGS / Cash Settlement
Nairobi Securities Exchange (Kenya)	Sub-millisecond matching, high throughput (Millennium Exchange)	Limit, market, iceberg, IOC, FOK, pegged orders	NSE Clear provides CCP for derivatives, margining, daily mark-to-market	CDSC handles DVP settlement; securities immobilised; corporate actions managed	Cash settled via CBK RTGS ensuring finality in central bank money
Nigerian Exchange (Nigeria)	Low-latency matching (X-Stream), capable of >1M trades/day	Limit, market, stop, iceberg, pegged orders	CSCS as CCP & clearing house for derivatives & equities; netting, margining, daily MTM	DVP settlement for equities & bonds; securities dematerialised	Cash leg settled via banks, integrated with central bank oversight
Johannesburg Stock Exchange (South Africa)	Sub-millisecond matching, scalable throughput	Full suite of advanced orders, including auctions	JSE Clear manages derivatives CCP, margining, risk management, default fund	Equities & bonds settled via ECS & SALS; corporate actions processed; securities immobilised	Cash settled internally, integrated with South African RTGS system
Nasdaq Stockholm (Sweden)	Ultra-low latency INET Nordic / Genium INET; very high throughput	Market, limit, iceberg, pegged, stop, discretionary	EuroCCP (equities) & Nasdaq OMX Clearing (derivatives) provide margining, daily MTM, default fund	Euroclear Sweden provides DVP settlement, safekeeping, corporate actions, immobilisation	Cash leg settled via RIX (Swedish RTGS) in central bank money

Table 1: Comparative Systems Infrastructure

4. **Three Sheets to the Wind.** How Fiscal, Supply, and Institutional Issues Capsize Markets

4.1. Crowded Out and Taxed Away: The Fiscal Elephant in the Pool

The game is bonds, government bonds.

Perhaps the most widely acknowledged feature of institutional investment patterns in either country is the dominance of government securities across portfolios. Though the financing the public sector is of course a legitimate use of funds, it can when taken to extremes create structural impediments to capital market development.

Kenya's government debt-to-GDP ratio of approximately 70% creates substantial borrowing requirements that systematically absorb institutional capital that could otherwise fund private sector growth. Nigeria, despite maintaining a lower debt-to-GDP ratio of 50%, sees its financial sector adopt similar investment patterns.

Facing substantial fiscal deficits and limited access to concessional external financing, governments understandably prioritise immediate funding needs over longer-term market development objectives.

Government bonds flood every corner of both financial systems: pension funds holdings, insurance companies' asset portfolios, banks' balance sheets. There can be here no suggestion of foul play, it is purely a matter of supply, demand and resulting incentives.

Potential corporate debt issuers are bound to find the cost of compensating investors for a risk mechanically deemed higher than the 'risk free' government bonds off-putting. Attractive government bond yields thus risk drawing institutional capital away from productive private investment. Compounding this effect is the fact that liquidity is logically only to be found in government bond markets: corporate bond markets are virtually non-existent and equity markets are as observed above problematically shallow.

This directly constrains private sector debt market development, and more widely corporate growth funding, which in turn prevents any growth in equity market depth.

Tax vs mobilisation

In mid-2024 the Kenyan government proposed reintroducing withholding tax on interest from infrastructure and green bonds (5% for residents, 15% for non-residents), thereby threatening the tax-exempt status that these instruments had enjoyed since their debut in 2009. The proposal was however rejected by Parliament, preserving the exemption for the time being.

While capital gains tax changes have been implemented, these involve complex modifications including preferential rates for certain investment thresholds rather than across-the-board increases.

These policy shifts signal growing tensions between short-term fiscal revenue needs and long-term capital market development objectives.

Fishing for coherence

It is not the purpose of this paper to question the manner in which these two countries conduct the business of government, but merely to point at the very real choices they face.

Both countries exhibit misalignment between fiscal policy and capital market development objectives, with short-term revenue needs overriding long-term considerations. Tax policies discourage capital market participation while debt issuance strategies constrain corporate funding.

This fiscal pressure creates conditions where alternative supply simply cannot emerge.

4.2. Supply Draught: Water, water everywhere and not a drink to be had

Debt deserts and IPO droughts

There is one thing that trumps even the strongest incentives to over-allocate to government debt. The absence of any other options.

The persistent underdevelopment of Kenya and Nigeria's capital markets primarily reflects not demand-side constraints but a fundamental shortage of investable corporate opportunities that creates a self-reinforcing cycle of market stagnation.

Of the corporate bond markets in either country there is unfortunately little to say, other than the combination of the government debt dynamics discussed above and in the case of Kenya the unhealed wounds of historical bank defaults represent formidable obstacles to the advent of the issuance volumes required to diversify institutional portfolios.

Kenya's 60-odd listed companies represent a tiny fraction of the economy's corporate base, while Nigeria's tally, at just over 150 listed entities, is scarcely more impressive in the context of the country's 3.2 million registered companies. This represents a ratio of approximately 20,000 registered companies per listed company, compared to Europe's 7,500:1 ratio.

Admittedly many of these companies lack the scale, the growth prospects or the governance standards necessary to attract institutional investment.

The growth of private equity and venture capital markets, with Nigeria recording over 400 transactions worth USD 3 billion between 2020 and 2024, does however suggest that at least some do, that the investors they attract choose to deploy capital through private rather than public markets.

It is crucial to understand who these investors, are and even more importantly who they are not. Conversations with AVCA indicate that they are to a significant extent DFIs and MDBs, who are deemed to contribute in excess of 40% of private equity assets across the two countries. The asset allocation data discussed earlier establishes that they are neither Nigerian nor Kenyan pension funds. Local insurance companies are equally not involved.

Development finance stakeholders have historically deployed programmes to seek to address this vexing state of affairs and to 'educate' local pension funds into embracing private equity. This is however arguably misguidedly trying to bend asset allocations to meet the deployment preferences of development finance actors rather than to seek to meet local institutional investors where their developed economies colleagues are and have always overwhelmingly been: public capital markets.

Critically, in a context where the lack of exit routes yields a generation of zombie funds, the number of IPOs emerging from a private equity sector meaningfully capitalised by public development finance is either very close to zero, or actually zero.

And yet, when IPOs do take place, they are successful. The case of InfraCredit is particularly telling. Neither its limited size nor its admittedly niche business model deterred Nigerian pension funds to join development finance actors and the NSIA on the shareholder register.

Box 1: InfraCredit Case Study

The creation of InfraCredit in 2017 – set up to issue local currency guarantees to infrastructure assets – provided a catalyst for the emergence of a functioning local currency infrastructure bond market and a pathway for the participation of domestic institutional investor participation.

Employing the GuarantCo model, InfraCredit's strong balance sheet and credit ratings enable it to issue guarantees that boost project creditworthiness, enticing pension funds and other local institutional allocators to diversify into infrastructure. To date, it has backed over 20 projects, mobilised 19 local pension funds, extended tenors to 20 years, and halved spreads relative to government bonds – lowering costs and making more projects bankable.

Historically, pension funds in Nigeria largely stuck to sovereign debt or occasional corporate issues. Key barriers were limited product variety and lack of familiarity with the infrastructure asset class. With technical assistance from its DFI partners, InfraCredit was deliberate in providing capacity-building programmes targeted at local investors and regulators, including the Nigerian Pensions Commission (PENCOM). This has been successful in supporting the core guarantee product offer. Interestingly, the market for local currency infrastructure bonds in Nigeria has since developed to the point where issuance without guarantees is possible. One such sign of maturation and future sustainability of the market is the successful issuance in recent years by Axxela and North South Power of unguaranteed NAIRA infrastructure bonds.

Beyond its success in fostering a local currency infrastructure debt market, InfraCredit is also an excellent example of a business using listed markets to attract local equity investors. Further to its establishment by the Nigerian Sovereign Investment Authority (NSIA) and GuarantCo, InfraCredit relied initially on DFIs such as Africa Finance Corporation, InfraCo Africa, KfW and AfDB to grow its capital base. The addition of LeadWay Assurance and AIICO Insurance as shareholders pointed to appetite on the part of local institutional investors.

However, in order to enable pension funds to invest InfraCredit had to structure itself as a PLC, something that it achieved with listing on Nigeria's NASD OTC Exchange in 2025. This listing, supported by the UK's government's MOBILIST programme and a cohort of Nigerian pension funds, resulted in NGN 27 billion in new share capital being raised.

InfraCredit is now firmly established as a domestic financial institution that both supports local currency infrastructure bond issuance and acts as an example for DFI-funded businesses in Africa seeking to diversify away from public funders and attract local institutional capital sources.

Of regulatory arbitrage

It should be added that regulatory compliance costs and ongoing disclosure requirements create prohibitive barriers, particularly for smaller enterprises, High-profile corporate failures and de-listings have in addition created reputational risks that discourage larger companies from pursuing public listings.

As is always the case in matters financial, it comes down to risk and reward. Where the promises of long-term financing at scale provide a fair reward for the added costs of transparency, public capital markets can and do thrive.

Where however businesses have readily available access to less demanding sources of capital, where private markets can provide for short-term needs under the comforting blanket of confidentiality, the temptation can be too strong.

In an environment where businesses are already reluctant to face the heightened scrutiny associated with public markets, the combination of overly demanding regulatory frameworks too often directly imported from far more mature markets and the comparatively ample provision of private equity capital creates a regulatory arbitrage opportunity. This may be a significant headwind for local capital markets, and a problematic side effect where development finance is a significant contributor.

If as conversations held with investors local and global, the lack of trust in corporate governance and an imperfect understanding of risk borne out of insufficient access to data are to blame for the underwhelming levels of private capital mobilisation, then perpetuating a cycle that encourages businesses to remain opaque is a grave if unintended error.

Box 2: Different hemispheres & common themes

The challenges of deteriorating public markets facing Kenya and Nigeria are not isolated phenomena but find echoes in broader global trends affecting public markets worldwide.

Understanding these international patterns provides crucial context for developing appropriate solutions and realistic expectations for reform outcomes.

The European Union's experience between 2010 and 2018 offers particularly relevant insights into the limitations of conventional capital market development approaches. Despite achieving 24% total GDP growth during this period, EU securities exchanges experienced a 12% decline in the number of listed companies, representing over one thousand corporations leaving public markets, while market capitalisation remained stagnant at 50 to 60% of GDP.

Most significantly for institutional investor analysis, the United Kingdom's pension industry decreased domestic public equity allocation from 35 to 40% to less than 10% between 2013 and 2023. This dramatic decline occurred across both defined contribution and defined benefit schemes, suggesting structural rather than regulatory causes. It should however be noted that while the UK pension industry has also decreased its exposure to international equities, it did not at all do so to the same extent.

The EU has implemented comprehensive policy measures to address market attractiveness challenges, including the 2024 EU Listing Act with simplified prospectus requirements, the European Capital Markets Union initiative promoting cross-border integration, and the 2025 Savings and Investments Union strategy focussing on retail investor engagement. However, these extensive reforms have not achieved significant increases in trading volumes or new listings, indicating that regulatory interventions alone cannot overcome fundamental structural constraints without addressing institutional investor behaviour.

Acknowledging that the sources of these phenomena are multiple, complex, and include at least some measure of idiosyncrasy, two factors could be relevant to decision making in development finance.

The first observation is that this shift did coincide with significant growth in allocations to private markets, providing an alternative source of capital to businesses across developed economies. It is crucial for development finance stakeholders to understand that although they can be complementary stages of the funding continuum, public and private markets are at least as often competing against each other.

The second is that, by the EU's own increasing admission, the regulatory burden imposed on publicly listed companies reached levels that weaken the attractiveness of its markets, and that of others like them.

The combination of these two factors contributes to the regulatory arbitrage that may be affecting public markets fortunes on either side of the north/south divide.

Break the dam

The scarcity of attractive investment opportunities predictably results in a rational response among institutional investors who retreat toward government securities because the public markets they can access fail to offer compelling corporate sector alternatives.

The message from the representatives of Kenyan and Nigerian institutional investors is clear. They understand the urgent need to diversify portfolios and take on equity risk. There is simply nothing – good – to buy.

4.3. Going with the Flow: Why Institutions Choose the Current of Least Resistance

Whilst it is therefore wrong to lay the blame at the door of local investors, they themselves transparently acknowledge that there is a need for continuous capacity building,

Current pension systems feature fragmented structures with numerous small funds that lack the scale and expertise necessary for sophisticated investment management. These smaller institutions can neither internally develop nor externally afford the professional capabilities required for complex investment decision making and instead rely on following the allocation decisions of larger, more sophisticated funds.

There exists a need for deepening and strengthening expertise among pension fund trustees and managers regarding equity investment strategies and long-term portfolio management. This knowledge deficit represents a fundamental constraint on institutional equity allocation by limiting decision-makers' confidence in implementing appropriate investment strategies.

Observed interpretations of fiduciary responsibility too often emphasise capital preservation over total return optimisation, leading to conservative allocation patterns that fail to serve beneficiaries' long-term interests.
Legal frameworks do not in fact explicitly recognise that fiduciary duty should include consideration of long-term economic growth and inflation protection rather than merely short-term capital preservation.

This suggests the welcome reforms that have led to risk taking being allowed now need to be followed by those leading to the level of risk taking needed to meet liabilities being placed at the core of fiduciary mandates.

There is little doubt that the need for capacity building is very real. This should not however mask a sobering reality. There are few skilled fishermen in the middle of the desert. There is little incentive to acquire the skills and expertise required to build diversified portfolios of assets matched to liabilities for investors confronted with a toxic mix of fiscal pressure and absent asset supply. And where these skills are absent, financial systems are unlikely to proactively seek diversification and stimulate supply. The nefarious cycle these three mutually reinforcing dynamics create can only be addressed by a coordinated approach addressing each of them. The development finance system can play a determining role in its delivery.

5. **Let it flow, let it flow, let it flow.** Plotting a course to fit-for-purpose markets

This section will serve as an introduction to future Short Reads that will in turn engage in a more granular reflection around each of the proposed solutions. We will address the three broad concerns detailed in the previous section.

5.1. Open the Floodgates: DFIs, Supply & Liquidity

Debt: Structure to distribute

Development finance actors risk hampering capital market development when providing capital to domestic banks that bypasses local capital markets entirely. This practice may achieve short-term development finance objectives but fails to build sustainable capital formation mechanisms that can support long-term economic growth.

Wherever possible, a significant portion of development finance lending to domestic banks should by default be deployed through domestic capital market instruments.

In extenso, they should anchor bank-issued bonds rather than lend directly. This approach would ensure that development finance contributes to market development while achieving financing objectives. It will once again be argued that bonds may not offer the flexibility that development finance's banking 'clients' prefer. And it should once again be kept in mind that these beneficiaries of public funding must accept that capital markets development impact is part of the bargain.

Make a market

The provision of secondary market liquidity has hitherto too seldom been understood as a key instrument in the development finance toolkit. Without it, the primary markets that impact is more traditionally linked to cannot sustainably thrive.

There is a significant opportunity for DFIs and MDBs to provide capital and technical assistance for market making programmes that enhance liquidity and trading conditions. This support must be carefully structured to address the fundamental causes of illiquidity rather than creating temporary trading activity that may not be sustainable over the long term.

The primary challenge with market making in emerging markets stems from a combination of insufficient natural trading flow and limited institutional participation, creating conditions where market makers face significant inventory risk without adequate counterbalancing trading activity.

Development finance can address this structural problem by providing both capital support and demand generation that creates more balanced trading conditions for market makers to operate effectively.

Capital support for market making should take the form of risk-sharing mechanisms rather than direct funding that could create market distortions. DFIs and MDBs can provide partial guarantees or credit enhancements that enable market makers to maintain larger inventory positions and tighter bid-ask spreads during periods of market stress.

The design of DFI-supported market making programmes must include provisions that ensure market makers fulfil their obligations during periods when their services are most needed.

Performance requirements should specify minimum quote availability, maximum bid-ask spreads, and minimum trading volumes that market makers must maintain across different market conditions. Penalty mechanisms should be established for non-compliance, while incentive structures should reward market makers who provide consistent liquidity services that genuinely benefit other market participants.

Coordination with exchanges and regulators is essential for effective market making support programmes.

Market-making would in turn offer development finance a diversifying risk exposure with lasting capital market development impact.

Drop the anchor

Whether they are already shareholders through private investments or whether they invest for the first time DFIs and MDBs should support IPOs.

Anchor investment programmes should position them as cornerstone investors in domestic IPOs and corporate bond issuances, providing credibility and confidence that attracts broader institutional participation.

This approach addresses one of the fundamental barriers to successful public offerings in emerging markets: the chicken-and-egg problem whereby institutional investors hesitate to participate without evidence of strong demand and trust, while companies struggle to demonstrate such demand without institutional participation.

The anchor investment model would require them to commit meaningful capital allocations during the pre-marketing phase of offerings. This early commitment signals to the market institutional quality and due diligence validation to other investors, as DFIs and MDBs typically maintain rigorous investment standards and extensive due diligence processes. It does in addition provide price discovery guidance by establishing a credible valuation floor based on professional investor assessment.

DFIs should adopt investment criteria that emphasise market development potential alongside financial returns.

Investment terms should be structured to encourage rather than crowd out other institutional participation, for example by tapering commitments as local investor interest materialises. The selection criteria for anchor investments should prioritise companies and sectors that can catalyse broader market development by establishing precedents.

Priority should be given to issuances that demonstrate strong corporate governance standards and transparent financial reporting. Exit strategies for anchor investments must be carefully planned to avoid market disruption while achieving the objective of transferring ownership to broader institutional investors over time.

Equity: A developmental duty to list

Interviews with financial markets actors in Nairobi, Lagos and Abuja make it clear that for local capital markets to become relevant, investors must be presented with a fresh supply of opportunities to invest in the equity of well governed, profitable businesses. Nigeria's National Pension Commission specifically highlighted that the presence of development finance actors in a transaction can provide strong signalling to pension funds, reassuring them about the quality and suitability of an offering.

DFIs and MDBs, through their extensive support to African private equity funds, have helped create a significant pool of such companies in both countries. The integration of strong ESG frameworks into business operations is an inherent part of their investment mandates, and beyond the injection of capital the provision of technical assistance helps build stronger prospects.

Conversations held with African General Partners (GPs) over the years have confirmed that the role of DFIs/MDBs is so important to them that there is little these would ask that they could refuse.

Through their positions on fund advisory boards and their influence over follow-on funding decisions, DFIs and MDBs possess meaningful leverage to shape GP exit strategies. The challenges facing private equity exits are well documented globally, with investments-to-exits ratios reaching historic highs, and concerns about limited exit options are particularly acute in East Africa where approximately 100 exits have emerged from 255 private equity investments over the last decade[3]. Building reliable exit routes through public market listings is essential for the private equity ecosystem they have helped create to remain viable.

It is therefore in development finance actors' gift, in their long-term interest and arguably their duty to put pressure on GPs to exit positions through IPOs on public equity markets.

Some will reasonably question whether the valuations on offer are attractive enough and highlight that pushing GPs to seek listings when more lucrative options exist may drive private capital away from private equity funds supported by DFI/MDB capital.

Notwithstanding the modest levels of private capital mobilised, we should acknowledge that there may indeed be consequences for fund performance. Public funding support for private equity must however serve development policy objectives, and development finance investments in ever larger follow-on funds able to keep promising businesses private may bear a level of responsibility in the stunted growth of African public capital markets.

Conversations with the Nigerian Sovereign Investment Authority further highlighted that while Nigerian entrepreneurs may be reluctant to take on the increased transparency requirements of life on public markets, institutional investors can play a driving role in guiding companies to public markets that can bring long-term access to growth capital. This role DFIs and MDBs must play as responsible, strategic investors.

The recent InfraCredit listing on Nigeria's NASD OTC Exchange demonstrates this dynamic in practice, with DFI anchor investment providing the confidence that enabled local pension funds to participate in what might otherwise have been perceived as too small or too niche an opportunity.

And SOE forth…

The privatisation of state-owned enterprise (SOE) would provide opportunities for market breadth and depth enhancement. Viable SOE listings can demonstrate government commitment to capital market development while providing attractive investment opportunities for institutional investors. The privatisation process should be designed to encourage domestic institutional participation rather than focussing on international investors, for example through reserved allocations for local pension funds or preferential pricing mechanisms that prioritise domestic institutions in the offering structure.

5.2. The Grand Bargain: Relieving Fiscal Pressure to Unlock Local Capital

Stating the destination

Fiscal pressures facing Kenya and Nigeria are real and immediate. Governments need financing, and domestic institutional capital provides the most accessible source. The crowding-out dynamics this creates however

[3] https://jepaafrica.squarespace.com/insights/continuation-funds-east-africas-private-equity-exit-solution

risk systematically undermining capital market development.

It may be worth restating these dynamics. To attract local investors in a market where it competes with the private sector for finite if growing pools of capital, governments need to, and do, make their bonds attractive by offering high yields. This in turn makes financing the private sector comparatively unattractive. Corporate bond issuers struggle to provide the premium investors require to justify the additional risk, equity returns appear too low, particularly through a short-term lens. Relative illiquidity makes matters worse, but it is worth highlighting that this is both a capacity (demand) and a competitive (supply) issue.

This section explores how the development finance system can leverage its unique capabilities to address this structural tension through a coordinated approach. This is not about judging, let alone dictating sovereign policy choices, but rather offering partnerships that align fiscal sustainability with capital market development objectives.

The Grand Bargain

Building fit-for-purpose financial systems that provide local populations the same ability that citizens of developed economies enjoy to save and invest should be central to the development finance mission. Achieving this requires helping institutional investors reach asset allocations aligned with their long-term liabilities.

The Grand Bargain addresses the fiscal-crowding-out problem directly: external actors would purchase government bonds from local pension funds, enabling those pension funds to reallocate freed capital into the growing supply of public equity and corporate bonds described in 5.1. Whilst this paper does not prescribe which specific institutions should implement this mechanism - recognising for example that bilateral DFIs may lack either the mandate or capacity to hold local currency government bonds directly - it argues that someone must play this role. The critical point is not who holds these bonds, but that domestic institutional investors are freed from their current role as captive buyers of government debt.

The critical constraint is a firm commitment from governments not to expand domestic bond issuance programmes opportunistically as space emerges. Without this commitment, freed pension fund capital would risk simply being absorbed by additional government borrowing, perpetuating the crowding-out cycle.

The high-level mechanics are straightforward: pension funds gradually reduce government bond holdings as development finance actors acquire them (either directly or through specifically mandated intermediation vehicles), simultaneously increasing equity and corporate bond allocations as new supply becomes available through the supply-side interventions outlined above.

Development finance takes on sovereign and currency risk it can absorb, while pension funds take on equity risk they need for long-term liability matching. For governments, the bargain offers continued access to local currency financing without the market development costs of domestic crowding-out. Development finance backed purchases maintain fiscal space while enabling the private sector growth that ultimately expands the tax base and reduces long-term aid dependency.

This is not debt relief or fiscal subsidy - it's a coordinated reallocation that aligns each party's comparative advantages toward capital market development objectives.

An Indirect Effect: Catalytic Yield Compression

The Grand Bargain's secondary effect may prove equally important. By introducing patient, comparatively price-insensitive demand for government securities, the intervention should compress sovereign bond yields, creating multiple reinforcing benefits. Lower government yields would make alternative assets relatively more attractive to institutional investors, shifting their risk-adjusted calculus toward private sector investment. Simultaneously, compressed sovereign yields would reduce the base rate for corporate borrowing, making debt financing more viable for companies that previously found it prohibitively expensive and stimulating supply of investable corporate securities. Lower risk-free rates would also improve equity valuations through reduced discount rates, supporting both existing listings and IPO pricing. For governments, yield compression would reduce debt service costs, creating fiscal space that reduces pressure for opportunistic borrowing expansion since, paradoxically, cheaper borrowing reduces the need to borrow. The magnitude of these effects would depend on the scale of intervention and broader market conditions, but the directional impact should create self-reinforcing dynamics: as pension funds reallocate toward equities and corporate bonds, corporate issuers respond to improved financing conditions by bringing new supply to market, which provides pension funds with the diversification opportunities they seek, whilst compressed sovereign yields tilt incentives away from government securities and toward private sector investment.

How much are we talking about?

Kenyan pension funds held Ksh 1 183.3 billion as of December 2024, equivalent to roughly USD 9 billion[4], to which a significant proportion of the Ksh 437.5 billion allocated to guaranteed funds (approximately USD 3.4 billion) should be added. Their Nigerian counterparts held NGN 13 468.16 billion of Federal Government of Nigeria securities as of September 2024, coincidentally also worth just over USD 9 billion.

Zooming in on Kenya for the purpose of illustration, doubling the pension industry's 9% (Ksh 202.3 billion / USD 1.5 billion) allocation to public equity, bringing it to just short of 20% would mean shifting USD 1.5 billion from local currency government bonds to the NSE. An amount equivalent to 8.8% of its current market capitalisation.

This magnitude of reallocation, combined with the yield compression effect on corporate borrowing costs, could prove transformational. The improved relative attractiveness of equities to pension funds, coupled with reduced issuance costs for corporates, could create conditions for sustained market development.

To put this into context, Kenya's external debt stock stood at Ksh 5 057.01 billion at the end of 2024[5]. Of this 54.9% was contributed by multilateral lenders. This is roughly USD 45 billion. Add to this the $10 billion in bilateral debt, and a USD 1.5 billion increase in exposure to a sovereign borrower – admittedly in its own currency - starts to look like a manageable price to pay for a transformational intervention that can generate economic growth, increased tax income and therefore reduced sovereign risk across the entire external debt portfolio.

Choppy waters

There is of course the small matter of where in the development finance system these local currency bonds should end. The Grand Bargain concept presented here is deliberately institutional-agnostic, acknowledging that MDBs and DFIs are, albeit for different reasons and to different extents, constrained in their ability to take on local currency exposure, as discussed in some detail in the OECD's 'Unlocking Local Currency Financing' report[6] written in cooperation with the CDFS.

[4] https://www.rba.go.ke/download/kenya-financial-sector-stability-report-august-2025/?wpdmdl=7723&refresh=68da2b6855f131759128424&ind=1758543489535&filename=Kenya%20Financial%20Sector%20Stability%20Report-%20August%202025.pdf

[5] https://newsite.treasury.go.ke/sites/default/files/Debt%20Monthly%20Bulletins/December%202024%20Monthly%20Bulletin.pdf

[6] https://www.oecd.org/content/dam/oecd/en/publications/reports/2025/02/unlocking-local-currency-financing-in-emerging-markets-and-developing-economies_af15df6a/bc84fde7-en.pdf

The sovereign nature of the assets concerned does at least in theory offer lower risk profiles. Precedents including the African Local Currency Bond Fund demonstrate that DFIs, MDBs, development agencies and impact investors alike can technically invest in funds holding local currency debt securities, and private sector fund managers including Record can help finance local currency positions. The potential for yield compression through this mechanism provides an additional risk-return rationale: if purchases demonstrably reduce sovereign yields, the resulting fiscal space and market development effects may reduce sovereign risk over time, improving the fundamental credit profile of the very assets being purchased. Specific implementation mechanisms will be reviewed in a future Short Read.

The critical distinction here concerns the nature of government commitment. The Grand Bargain does not seek to prevent governments from issuing bonds to meet genuine growing fiscal needs. Rather, it requires commitment not to opportunistically expand issuance simply to absorb newly available pension fund capacity as development finance substitutes for domestic institutional buyers. Without this discipline, the intervention merely replaces one source of government financing with another, achieving fiscal substitution but no capital market development.

The real implementation challenges lie in establishing credible monitoring mechanisms to distinguish legitimate fiscal expansion from opportunistic absorption of freed capacity, achieving effective syndication of bond purchases across multiple development finance institutions with varying mandates and risk appetites, and synchronising fiscal substitution with supply-side interventions so that pension funds can actually deploy freed capital into emerging equity and corporate bond opportunities rather than seeking alternative safe havens.

5.3. Steady the Ship

Shared responsibility

Whilst the Grand Bargain requires an understanding with the governments of the countries it seeks to support, the first two legs of this coordinated approach are primarily the responsibility of development finance stakeholders. Once their combined effects materialise, and the additional supply of investment opportunities is met by the freed up capacity of local investors, there will arise an opportunity for local institutions to accelerate and amplify the process through structural reform and capacity building.

The institutional assets reallocation process that this strategy seeks to deliver will only prove sustainable if fully integrated in the way asset owners conceive of their mission.

Pension system structure

Pension system transformation represents a key foundation for sustainable capital market development over the medium term. Current pension systems in both countries feature fragmented structures with numerous small funds that lack the scale and expertise necessary for sophisticated investment management.

Consolidation programmes should encourage mergers of smaller pension funds to achieve economies of scale and professional management capabilities that can support higher equity allocation. These larger institutions can then internally develop the professional capabilities required for complex investment decision making rather than simply following the allocation decisions of larger, more sophisticated funds.

Redefining fiduciary duty

Fiduciary duty frameworks require clarification to recognise that prudent long-term investment necessarily includes equity allocation for inflation protection and growth. This is even more important considering the demographic structure in Kenya and Nigeria with a high ratio of young individuals accumulating pensions.

Current interpretations often emphasise capital preservation over total return optimisation, leading to conservative allocation patterns that fail to serve beneficiaries' long-term interests.

Legal frameworks should explicitly recognise that fiduciary duty includes the necessary consideration of long-term economic growth and inflation protection, not merely short-term capital preservation.

Building investment expertise

Based on interviews held with market participants in the local capital markets of Kenya and Nigeria, there is a need for deepening and strengthening know how and expertise among pension fund trustees and managers with regards to equity investment strategies and long-term portfolio management.

This capacity building addresses one of the fundamental constraints on institutional equity allocation by ensuring that decision-makers possess the knowledge and confidence necessary to implement appropriate investment strategies.

Investment committee training represents a crucial intervention for improving institutional investment decision-making. Professional development programmes should focus on equity investment strategies, risk management techniques, and long-term portfolio optimisation methods that enable appropriate asset allocation decisions.

Risk management enhancement should develop sophisticated capabilities that support higher equity allocation while maintaining prudential standards. This capability building should include scenario analysis, stress testing, and portfolio optimisation techniques that demonstrate the risk-return benefits of diversified portfolios including significant equity allocation.

Performance measurement reform

Performance measurement systems should implement long-term, risk-adjusted metrics that properly evaluate institutional investment performance over appropriate time horizons. Considering local pension funds and insurance allocation of capital, it appears that the investors are over-emphasising short-term volatility over long-term returns. This increases the matching risk between assets and liabilities on the pension funds balance sheet given the long duration of the liabilities, i.e. the pension obligations.

Stakeholder engagement should educate beneficiaries about the importance of equity investment for long-term returns and inflation protection. This education process should explain the rationale for appropriate asset allocation and help beneficiaries understand the relationship between investment strategy and retirement security.

6. **Reach for the sextant.** Assessing progress and course correction

Performance Indicators and Success Metrics

Market development progress should be measured through specific indicators that reflect underlying changes in institutional behaviour and capital allocation patterns.

Market depth can be tracked through market capitalisation to GDP ratios and the breadth of listed companies, with meaningful improvement demonstrated by both increasing ratios and steady new listing activity. Trading velocity and liquidity measures would indicate whether markets are becoming more functional for institutional participation. Corporate bond market emergence would signal successful diversification of financing sources beyond government securities and banking credit.

Institutional investor metrics should focus on core behavioural changes. Pension fund equity allocation increases, insurance company portfolio diversification, and declining concentration in government securities would demonstrate the reallocation strategy's effectiveness. The pace and sustainability of these shifts matter more than hitting specific targets, as rapid forced changes could create instability.

Economic impact indicators measure broader effects on private sector development. Increased capital formation through equity and debt markets, employment growth in listed companies, and improved SME access to growth capital would validate that market development translates into real economic benefits rather than just financial sector activity.

Risk Management and Mitigation Strategies

Opposition to pension fund reform represents a significant implementation risk that requires careful management through gradual implementation approaches and clear demonstration of beneficiary protection and performance improvements. Reform initiatives should emphasise enhanced returns and retirement security rather than abstract market development objectives.

Market volatility during transition periods requires careful sequencing of reforms and maintenance of prudential standards throughout the implementation process. Risk management frameworks should be strengthened rather than relaxed during transition periods to maintain confidence and prevent adverse outcomes that could undermine reform efforts.

Regional economic instability could affect implementation timelines and outcomes, requiring flexible approaches and robust contingency planning. Implementation strategies should account for potential external shocks and maintain adaptability while pursuing core reform objectives.

Coordination challenges among multiple stakeholders require clear governance structures and communication protocols to ensure effective implementation. Regular monitoring and adjustment processes should maintain momentum while addressing emerging challenges and opportunities.

7. **Land!** In Conclusion

Prioritising the mobilisation of local pools of capital to develop financial systems and begin the long path towards solving the local currency issue can at first seem ungenerous. Why should limited local savings take on this burden when there is so much more liquidity in global markets?

In fact this is a necessary and justified course of action not only because local investors are comparatively better positioned to finance local assets in local currency, but also fundamentally because to deliver just and sustainable economic development, local savers need to be the first beneficiaries of their own economic growth, and increasingly own the assets that will drive it.

The evidence is clear: Kenya and Nigeria possess the technological infrastructure and investor appetite for vibrant capital markets. What they lack is coordinated intervention to break the three-way doom loop of fiscal crowding out, supply shortage, and rational institutional conservatism that this paper has documented. Each constraint reinforces the others, creating a vicious circle of market stagnation despite genuine demand for quality investment opportunities.

The difficulties ahead should not be underestimated. Redirecting development finance flows through rather than around local markets will face considerable friction and demand profound changes to operating models.

Driving assets towards public markets where they can be accessed by both institutional and retail investors will encounter entrenched reticence in business communities.

Much to the chagrin of the current if fading zeitgeist, the reallocation of local institutional assets away from government securities is in the short term a zero-sum game, requiring the Grand Bargain this paper proposes: development finance absorbing sovereign risk to free pension capital for productive investment.

Whilst capacity building should not seek to drive institutional investors towards what is convenient for the development finance system, there is a self-identified need for continued and a more profound reform and skill transfer to ensure they are equipped to increase exposure to what is right for them, and crucially for their clients.

This paper addresses but one facet of a complex problem. The banking sector plays a key role that we continue to reflect upon in our parallel For Whom the Banks Roll series. When confronted with this level of complexity, it is challenging to identify where the frontier lies that separates well-intended reflection from presumptuous recommendations.

The price of inaction for the populations we owe sustainable development to is however too high for the status quo to prevail.

Development finance stakeholders have the tools, relationships, and capital to catalyse a tangible and sustainable transformation. The question is whether we are ready to fundamentally shift from local market avoidance to local market development as the pathway to sustainable growth. The infrastructure exists, the demand exists, and the capital exists. What is needed now is the strategic coordination to channel existing resources through local markets rather than around them.

Sail on, silver researcher

This paper could not under its own steam provide an exhaustive assessment of all the relevant topics it raised. Three critical areas do specifically warrant dedicated examination in subsequent research.

First, the mechanics and implementation pathways for the Grand Bargain, specifically how development finance can effectively purchase government bonds from local pension funds using local currency financing. This involves designing credible commitment mechanisms to mitigate the risk of governments opportunistically expanding domestic issuance, and ensuring optimal sequencing so liberated institutional capital flows into emerging equity and corporate bond opportunities rather than alternative safe havens.

Second, pension fund consolidation and scaling deserves deeper exploration, examining how fragmented institutional structures in Kenya and Nigeria can be transformed through consolidation around entities with sufficient scale and expertise to manage sophisticated equity portfolios.

Third, the potential for regional market integration merits investigation. Could cross-border coordination across East and West Africa generate the depth and liquidity that individual markets cannot achieve alone? How might such regionalisation complement rather than undermine national market development while addressing sovereignty and regulatory harmonisation challenges?

As many short, and slightly longer reads to look forward to.

This CDFS Slightly Longer Read was composed by:

Magnus Billing, Senior Advisor

Magnus has over 20 years of experience in the international financial industry. He was previously the CEO of Nasdaq Nordic and, most recently, the CEO of Alecta, one of Europe's five largest pension funds. As CEO, he transformed the portfolio into a sustainable asset base by leveraging an active, in-house investment model to drive transitional growth. Magnus holds an LLM from Stockholm University and an Executive Management degree from the SSE.

Viola Kilel, Senior Advisor

Viola is a policy advisor at the Netherlands Embassy in Kenya and a senior advisor to the CDFS. She previously spent 8 years at the Capital Markets Authority, Kenya within the policy and market development directorate. Viola holds a MSc in Development Finance from Strathmore Business School and is a Chartered Development Finance Analyst with the CIDF in South Africa.

Thomas Venon, Executive Director

Thomas is the executive director of the CDFS and a founding partner at Eighteen East Capital. Thomas has 20 years' experience in the asset management industry including as head of institutional business at African Alliance, a director at S&P Fund Research, and senior positions at RBS/ABN Amro and Old Mutual. He holds an MBA from the University of Cape Town and a Master's in Applied Finance from the University of Melbourne.

Centre for Development Finance Studies

For more information:
Please contact the CDFS at info@thecdfs.org with any comments or questions about this Slightly Longer Read.