



Sea Meadow House
PO Box 116
Road Town, Tortola VG-1110
British Virgin Islands

Oyster Bay,
Dar es Salaam
7 November 2023

Dear Investor,

The Fund has been doing extremely well in the first three quarters of this year, and this trend is set to continue.

Year to date, through September 30, we are up 6.95%. To put that in perspective, our hurdle index is down -7.11%.

September was a particularly strong month, with gains of 2.73% for the Lead Series.

I estimate we gave back about 0.6% points of that in October, but that is subject to final numbers from the administrator.

"Day 1" African Lions Fund investors are enjoying 13.45% compound annual growth

The Fund has now been in existence for 3 years. Over that time, if you were with me from day one, you've seen gains of 46.03%, after all fees and expenses, in US dollar terms. That's 13.45% compound annual growth per year.

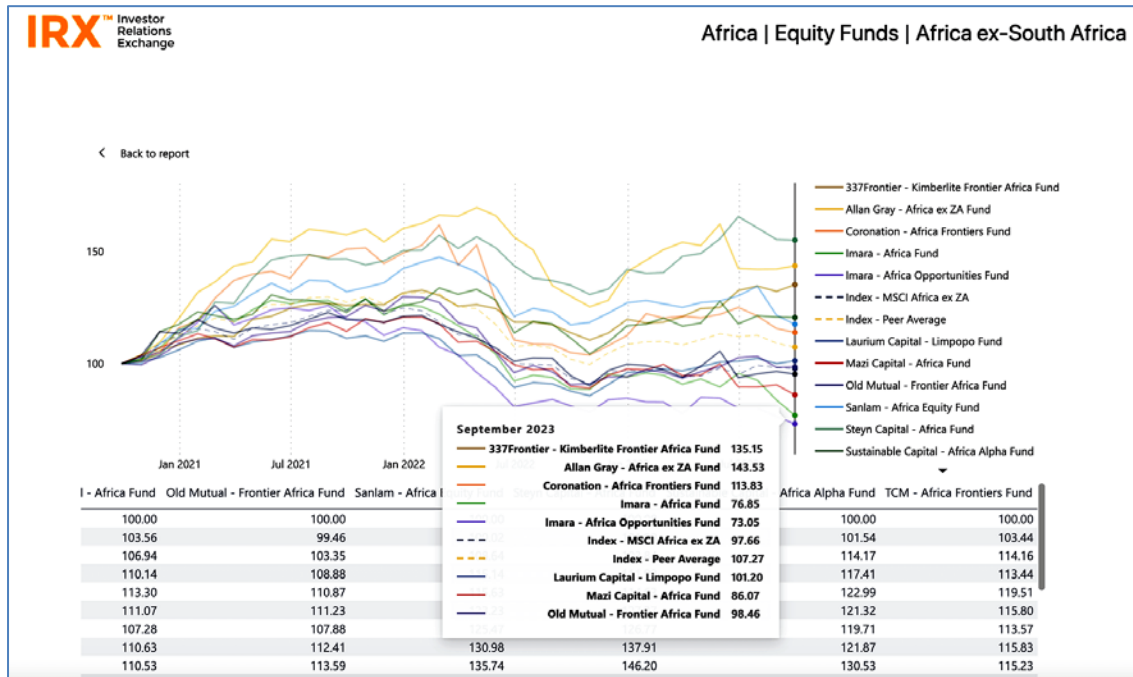
If you are based in a country where your home currency has weakened against the US dollar over the course of the past 3 years, which applies nearly everywhere, you will be even further ahead in local currency terms. The Euro, British pound, Aussie, Kiwi and Singapore dollars have all weakened considerably over the past 3 years.

While this absolute performance is satisfying, our relative performance has also been excellent.

Though not an exact comparison, as many of the funds listed in the graphic below also invest in north African countries, our performance has been ahead of the entire "Africa ex-South Africa" pack, except for one fund, the Steyn Capital Africa Alpha Fund, which has gained an impressive 55% in the past 3 years:



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The MSCI Africa ex-South Africa Index, over the same 3-year period, was down 2.3%. The average performance of the 12 actively managed funds in the above peer group was +7.3% in the last 3 years. So, you can also see clearly what a huge difference good, active stock selection makes in these markets. Passive investing in this part of the world, unlike in developed markets, cannot hold a candle to active funds, which clearly earn their fees.

Our niche, sub-Saharan Africa Frontier, also makes African Lions Fund different from most other Africa-centric funds. We offer pure exposure to the fast-growing frontier markets. Egypt, Morocco, and other north African markets are a different proposition for investing in as far as I am concerned.

What is the “secret sauce” for generating such outperformance?

Someone recently asked me, what makes a good investment for African Lions Fund. I replied, with no hesitation:

We invest in profitable, listed companies, in sub-Saharan Africa, outside South Africa, typically number 1 or number 2 in their sector or industry, with strongly entrenched franchises, generating at least 15% unlevered returns on invested capital, run by honest and competent management teams which treat minority shareholders well.



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And that really is it, in a nutshell. It sounds simple... and it is. But it is not *easy*.

If we can find businesses which fit the above description, we can generally achieve our aim of investing in companies that can double their sales and profits on a horizon of 5 to 10 years. If you recall, we also want to buy these on valuations so low that they too have the potential to double on a 5- to 10-year horizon.

For our current portfolio, earnings growth (in USD terms) has been 11.3% per year for the last three years. To double in 5 years, it needs to be about 14.9% a year. To double in 10 years 7.2% will do it. Our portfolio is on track to double earnings in about 6.5 years if the historical growth continues. So, I feel comfortable we have selected the right stocks.

However, the skill of a fund manager does not stop at stock selection. How much capital to allocate to each potential investment, once identified, is every bit as important for the overall results achieved. To do well, you need to have more capital in your best ideas than in your lower conviction ideas. And I am confident that we do.

We run a concentrated portfolio. Although we aim to own 10 to 20 stocks, we are not shy to hold large weightings in just a handful of those. Indeed, NMB Bank, Tanzania Breweries Limited, and Twiga Cement, our three biggest holdings, together account for 48% of the entire fund (on a current price basis).

With the benefit of hindsight, I should perhaps have been EVEN MORE concentrated in Tanzania. I set a 50% limit for the fund to allocate to any one country (on a cost basis). But, had we put ALL our money in our top 3 or 4 Tanzanian company choices, we'd have made a lot more money to date.

We have made nearly all our profits in Tanzania, along with some small gains in Senegal and Rwanda. In Kenya, Ghana, and Nigeria we lost money so far, though I am quite confident that in time, our substantial allocation to Kenya, which I have recently increased by over US\$1 million, after taking some profits in Tanzania, will bear fruit.

Kenya accounts for a significant part of the overall portfolio now, at almost 15%. Ghana at 4.6%, and Nigeria at 4%, are small in comparison. Nigeria holds potential.

I will be visiting Nigeria, both Lagos, and Abuja, from November 11 to 18. I will have more to say about the lay of the land there, after my trip. For now we hold only a small portfolio there.

It is clear that the new government, led by President Tinubu has bitten the bullet and decided on significant policy reforms. Unfortunately, in the short-term that is causing lots of economic upheaval, in the form of inflation, and drastic currency weakness. But there is usually no

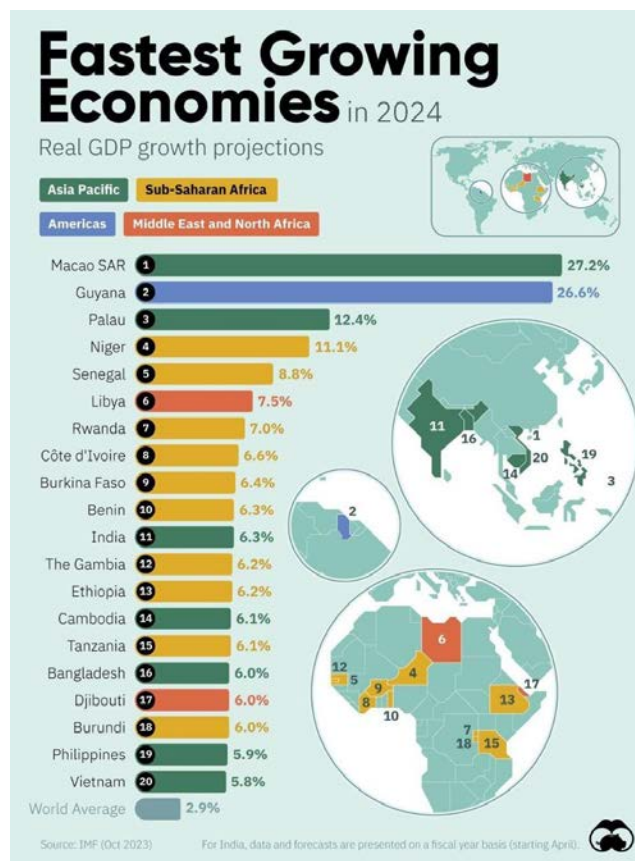


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gain without pain. And, for the medium and long-term future, I think what has happened is good news. Time will tell.

Can our portfolio's earnings growth continue at 11.3% per annum, in USD?

Looking ahead, African Frontier markets still have some of the fastest economic growth on the planet. That provides tailwinds, even if it doesn't always directly correlate with stock market performance.



6.1% forecast GDP growth for Tanzania in 2024 squares with what I am observing on the ground. The economy remains strong. Private sector credit growth is in the high 20% range. There is concern that import growth, in particular fuel, capital goods, and manufactured consumption goods, is outpacing export growth. That will mean a continued scarcity of foreign exchange and keep downward pressure on the exchange rate.



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On the flipside, a recent government agreement signed with Dubai Ports World to operate and invest in the modernization of the Dar es Salaam port, strong tourism growth figures, and a recent up-tick in gold prices, should all provide positive momentum for Tanzania. We are also experiencing above average rainfall, which is a blessing for agriculture and food production.

In Kenya, meanwhile, the economic forecasts are worse. But an adjustment is underway. The exchange rate has already slid by 19% in 2023, from 122.40 Kenyan Shillings per dollar at the start of the year to 151 now.

The pressure to depreciate was partly a result of the excessive interest burden that Kenya's foreign borrowings have imposed on the country's budget. The economy has also been struggling with rising bills for imported fuel and food greatly exceeding rising proceeds from exports.

The government has had to resort to hiking taxes and levies to try and raise the required money for its on-going expenses, and looming debt repayments. A US\$2-billion maturing Eurobond that must be rolled over, partly repaid, or fully repaid, by June 2024 is the immediate priority.

Kenya's government has also been forced to borrow heavily on the domestic bond market, forcing up interest rates. The government is now paying over 15% on its short-term 91, 180 and 364-day Treasury Bills.

Having visited Kenya last in May, and followed it very closely since, it is my assessment that the market is overly pessimistic. Yes, times are very tough. High prices for basic goods and services, combined with higher taxes, and a weaker exchange rate is causing economic hardship among the masses.

Even so, **I don't think the country will miss its Eurobond payment and default.** They have seen the dire consequences in places such as Zambia and Ghana, which defaulted, and instead are taking the pain NOW, in order to be able to repay.

Not everyone agrees with me or wants to stick around to find out. The wholesale exodus by foreign investors from the Kenyan market has been relentless. 2023 will be the fourth year in a row that the Nairobi Stock Exchange sees a foreign investment outflow.

For the 10 months year to date, net selling by foreign investors has been KES 19.5bn. That is US\$129.1 million at current exchange rates. But that is actually an improvement. In 2022, at then-prevailing exchange rates, for the same 10 months, the selling was worse. It came to KES 21.bn, or about US\$175.8 million.



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However, the number of foreigners exiting is even bigger this year. For the first 9 months, 6,256 foreign investors closed their Kenyan brokerage accounts, leaving 42% fewer foreign accounts than the 14,877 which existed at the start of the year.

This is a proper bear market!

But in my experience, this is when great opportunities to buy wonderful businesses at cheap prices arises. So, that's what we are doing.

I have been adding to our stake in Safaricom, Kenya's leading telecommunications, internet and payments processing company. Safaricom now trades on a single-digit P/E and yields more than 10%. Strip out the Ethiopian business, which is in the start-up phase and thus losing money, and the Kenyan business sells for only about 6 times earnings.

I have also bought more Jubilee Holdings, the leading insurance company in East Africa, at sub 0.3x book value and under 3 times earnings. We recently initiated a position in Kenya's largest banking group as well **at a price of just 1.5 times historical earnings.**

There are a lot of good things to buy. But somewhat disappointingly, the Fund just had its...

**First two consecutive months with no new money inflows
and we paid one redemption**

In the past quarter, the Fund experienced net outflows for the first time. We had no new subscriptions in August or September. As you are aware, we are a private fund, so we do not advertise to gain more investors, but even so, these have been the only two months since the Fund began, which saw no inflows.

Moreover, we also paid one redemption at quarter end.

While redemptions affect the Fund's ability to buy more investments and can even force us to sell existing positions from time to time, it's important to note that we have had no issues meeting three significant redemptions, and two or three smaller ones, thus far. Investors are able to redeem when they need to.

Pleasingly, this month, inflows have resumed, with three existing investors topping up their investments. But, with all the bargains available around the markets we invest in, **we could easily be deploying a lot more money.**



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Just today I learned of a golden opportunity in Zambia

If we can raise the capital, we have a shot at buying \$8 million worth of shares in one of the country's biggest companies, owner of some of the most iconic brands, in a **forced sale**.

The seller is not unhappy with its stake and would, according to my sources, happily own 100% of the business if it could. In fact, it has been busy spending tens of millions of dollars to add capacity in Zambia, given its bullish outlook on business prospects in the country. But it is being forced to sell down its stake by regulators.

I need to do some more numbers, but we'd get these shares for about 8 times this year's likely earnings at the price I was quoted. There may be room for more bargaining. But it's all hypothetical for me, unless I can attract more capital to African Lions Fund. That has unfortunately not been so easy this year.

And yet, while the fund has posted 46.03% gains since inception ...

Valuations for our portfolio are now more attractive than at any time since the fund began

I just finished updating my current year earnings forecasts for our portfolio. In short, valuations are as low as they've ever been. The portfolio is trading on an indicative P/E multiple, for 2023, of just 6.2x.

If we look back to when the fund first began investing, in 4Q2020, the same portfolio we own now was trading on an indicative 2020 P/E multiple of 8.8x. Of course, we didn't own exactly what we own now back then, but the comparison is valid.

The low valuation now is a function of:

- a) Significant earnings growth for many of our large holdings
- b) Me taking profits on some investments, and rotating into even cheaper stocks, as the opportunity has arisen due to sell-offs, such as that in Kenya
- c) Eliminating some of the underperforming positions we've had.

In short, there's been no better time to invest in the Fund, from a valuation standpoint, than right now. You are getting even more shares in high quality companies for your capital than you did at the inception of the Fund three years ago.



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Housekeeping, and upcoming travel schedule

This Wednesday afternoon, I will be participating in the NMB Bank PLC 3rd quarter earnings call organised by my friends at iTrust Financial, a new brokerage firm here in Tanzania. All investors are welcome to dial in and hear from top management. If you are interested, email me for a link. I sent it to some of you already.

On Thursday, Safaricom will be out with its half-year numbers, for the period 1 April to 30 September. A link to a webcast presentation will be available from the Safaricom website.

Saturday, I fly to Nairobi. I'll spend the night there before continuing to Lagos on Sunday morning. I'm in Lagos and Abuja all next week, arriving back in Dar es Salaam November 18.

Quarterly investor call

I'll host the quarterly Zoom call for investors after I return from Nigeria, in the week beginning November 20. Dial-in instructions will follow closer to the date.

As always, questions and feedback are welcome at tim@africanlionsfund.com

Until next time...

Good investing!

Tim Staermose
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