

**Semi-scientific**

# Diversifying without Africa is not real diversification

*Pension funds and their asset managers still barely invest in the 54 countries of Africa, despite the continent's attractive demographic and economic growth prospects and its urgent development needs.*



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**The illusion of global diversification**

Anyone investing passively on a global scale assumes they are well diversified. But appearances can be deceiving. The MSCI All Country World Index (ACWI) consists of approximately 64% U.S. equities. The ten largest companies now account for more than 21% of the index, while the IT sector alone represents 25%.<sup>1</sup>

So, those who believe they are broadly diversified are in reality investing a substantial share of their assets in a single country and a single sector.

**“In broad indices, the continent generally accounts for less than 1%”**

And where is Africa? In broad indices, the continent generally accounts for less than 1%. As a result, investors largely overlook a region with a young and rapidly growing demographic profile, abundant natural resources, and relatively low debt levels.

**Africa as a blind spot**

Africa is the youngest continent in the world: more than 60% of its population is under the age of 25.<sup>2</sup> This demographic dividend forms a powerful engine for future

consumption, labor market growth, and innovation. In addition, the continent possesses abundant natural resources that are indispensable for the energy transition, such as cobalt, copper, and lithium. Absolute debt levels are also significantly lower than in many Western economies, making the macroeconomic starting position less vulnerable than is often assumed.

Therefore, anyone who truly wants to diversify their portfolio cannot ignore Africa. The continent offers unique opportunities to spread risk and gain exposure to growth markets that are barely represented in traditional indices. But Africa is more than just another investment destination: it is precisely here that investors can achieve not only financial returns, but also the greatest social impact.

For pension funds, this directly relates to their fiduciary duty. That duty is not solely about securing sufficient returns, but also about ensuring that pensions can be paid out in a livable world. Investments in Africa, particularly impact investments, contribute to this by strengthening both long-term financial value creation and the social stability and sustainable development needed for future generations.

Moreover, both the financial and social marginal returns in Africa are much greater than in developed markets. Whereas in

Western countries the marginal impact of an investment may be limited, an investment in Africa can genuinely make a difference in access to basic needs such as electricity, healthcare, or education. These investments therefore directly contribute to achieving the Sustainable Development Goals (SDGs).

### What still holds investors back?

Despite all these opportunities, the continent remains a blind spot for pension funds and their asset managers. Most investments remain concentrated in a limited number of developed countries. Several factors explain this.

First, risk perceptions and cognitive biases play an important role. Political instability, currency volatility, and operational challenges are often overestimated. From an ethnocentric bias, Western norms and institutions are treated as the benchmark, causing African contexts to be more quickly labeled as risky. In addition, attribution bias leads investors to attribute negative events to structural flaws within the region, while dismissing positive developments as exceptions.

Secondly, modern portfolio theory leaves little room for smaller and less conventional allocations. Pension funds are strongly focused on scale and benchmarks, meaning African impact projects simply do not fit within existing frameworks. Strict return requirements and the emphasis on minimizing risk further discourage investments in new or less liquid markets. Under the supervision of the Dutch Central Bank (DNB), this results in a strong preference for established markets, even though frontier markets may offer opportunities for diversification and long-term value creation.

Finally, investors place too much weight on credit ratings, which often fail to reflect

reality adequately. These assessments are backward-looking and biased against frontier markets with future potential. Low sovereign credit ratings are particularly restrictive: through the so-called “sovereign ceiling,” companies within a country can rarely obtain a higher rating than the state itself. As a result, investments in Africa are frequently excluded automatically, regardless of their actual risk-return profile. Passive allocations through indices such as the MSCI ACWI reinforce this pattern.

### The way forward

The key to investing in Africa lies in a more forward-looking investment approach. Rather than relying on historical data, ratings, and benchmarks, Africa requires a broader long-term perspective. Exploring future scenarios and strategic options helps break through biases and unjustified risk perceptions, making opportunities more visible. Scenario thinking also reveals that the absence of investment not only undermines stability in Africa, but in the long term also increases pressure on developed countries through rising migration flows, climate challenges, and geopolitical tensions.

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In addition to a future-oriented approach, it is essential to make the actual risks more visible and manageable. The overestimation of risks in Africa can be countered through the expertise of development banks and impact investors, as well as through tools such as the GEMs Risk Database, which provide transparency regarding performance and risk profiles. These

sources are a valuable complement to traditional information sources such as credit ratings and indices. They help create a more realistic picture of actual risks and returns.

Risks can also be actively mitigated through innovative financing structures. Blended finance, in which development banks or governments take first-loss positions, lowers the threshold for institutional investors. B-loans, where development banks carry the senior debt portion and pension funds can co-finance alongside them, offer similar protection. By collaborating with specialized parties such as ILX Fund, pension funds can limit risks while gaining access to new markets with high growth potential.

To fully utilize these financing structures, adjustments in governance and portfolio management are also necessary. Through a total portfolio approach, investments in Africa should no longer be viewed as niche investments, but as an integral part of a globally diversified portfolio. Where traditional mandates remain too rigid, emerging market or impact mandates offer the flexibility to capitalize on the continent's opportunities.

**“It is now up to pension funds and their asset managers to overcome their hesitation”**

Anyone who truly wants diversification can therefore no longer afford to overlook Africa. It is the missing puzzle piece that helps mitigate long-term risks, unlock structural growth opportunities, and generate real impact. It is now up to pension funds and their asset managers to overcome their hesitation and finally lay this piece of the puzzle.

**In short**

- Global investments are highly concentrated: approximately 64% is invested in the United States, while Africa accounts for less than 1%.
- Africa offers opportunities through its young and growing population, critical resources for the energy transition, and relatively low debt levels.
- Biases, return requirements, traditional governance structures, and credit ratings continue to hinder investments in Africa.
- Forward-looking investing, better data tools (such as GEMs), innovative financing structures, and flexible mandates can help overcome these barriers.
- Africa is the missing puzzle piece for diversification, returns, and impact.

**References**

1. <https://www.msci.com/documents/10199/255599/msci-acwi-imi.pdf>
2. <https://www.unicef.org/executiveboard/stories/UNICEF-Board-turns-the-spotlight-on-children-and-young-people-in-Africa-srs-2023>

**Disclaimer**

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