

Part one of a three-part series

Making capital markets
work for Africa



Why capital market development matters and where the focus should be

May 2026

About this series

Making capital markets work for Africa is a three-part knowledge series from FSD Africa exploring the role of capital markets in financing Africa's long-term economic transformation.

At a time of tightening aid budgets, rising climate and infrastructure financing needs, and growing pressure on governments to mobilise domestic private capital, the series examines how African economies can build stronger, deeper, and more resilient capital markets.

Drawing on international experience and practical examples from Africa and other emerging markets, the series is intended to support policymakers, regulators, development finance institutions, institutional investors, and market practitioners working to strengthen domestic financial systems and mobilise long-term capital.

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About FSD Africa

FSD Africa is a specialist development agency making finance work for Africa's future.

Headquartered in Nairobi, it works with governments, regulators, financial institutions, and market actors to strengthen financial systems, mobilise capital, and support sustainable economic development across Africa. Learn more at FSDAfrica.org.

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Preface

Against the backdrop of tightening aid budgets and growing pressure on African economies to mobilise domestic private capital, capital market development has become increasingly important to Africa's long-term economic transformation.

This paper is the first in a three-part FSD Africa series examining the role of capital markets in financing development in emerging economies. The first paper focuses on why capital markets matter and where efforts should be concentrated. The second paper will examine how capital markets can be built and deepened, while the third will focus on the role of liquidity and secondary markets.

The paper draws on international experience and South-South learning to examine the conditions required to mobilise larger pools of domestic capital. It explores the role of pension reforms, institutional investors, equity and bond markets, hybrid public-private financing structures, and project preparation mechanisms in supporting long-term investment.

The publication also comes at a timely moment. The paper is intended to contribute to ongoing discussions on capital market development at the Global Partnership Conference, hosted by the UK Government in May 2026, and to support wider dialogue on how African economies can mobilise domestic capital at scale.

Executive summary

This paper presents the arguments for why domestic capital market development is becoming ever more important for emerging markets in Africa and makes the case for where to appropriately focus efforts to develop domestic capital markets. As strengthening the savings base is core to capital market development, establishing the foundation for enhanced savings through macro financial stability and pension reforms is crucial. While public equity markets have traditionally been regarded as core to capital market development, international experience demonstrates that their role in capital market development is limited. Early stages of capital market development are characterized by information asymmetries and high agency costs posing challenges for development of public equity markets. Corporate bond markets have been successfully developed in emerging markets but require broad-based commitment to institutional capacity development over an extended period.

African economies may be best served by hybrid markets that combine features of private and public markets by building on the upsides associated with a public approval process and disclosures while benefitting from regulatory accommodations that encourage investment in alternative assets by institutional investors. To encourage development of hybrid markets it will be important to (a) increase the confidence of institutional investors, e.g., through the use of guarantees and first loss arrangements, (b) establish suitable investment vehicles that engender collaboration among investors with a view to harnessing scale economies, and (c) build capacity in the preparation and development of bankable projects in infrastructure, housing and MSMEs sectors.

Key messages

1. Capital markets are no longer optional for African economies; they are central to mobilising long-term domestic finance.
2. Stronger pension and institutional savings systems are foundational to capital market development.
3. Public equity markets matter, but they are unlikely to be the main route for many smaller or frontier African markets.
4. Hybrid structures, guarantees, pooled vehicles, and project preparation platforms may offer a more practical pathway for mobilising institutional capital into infrastructure, housing, and micro, small and medium-sized enterprises (MSMEs).

Why has development of capital markets in emerging markets taken center stage?¹

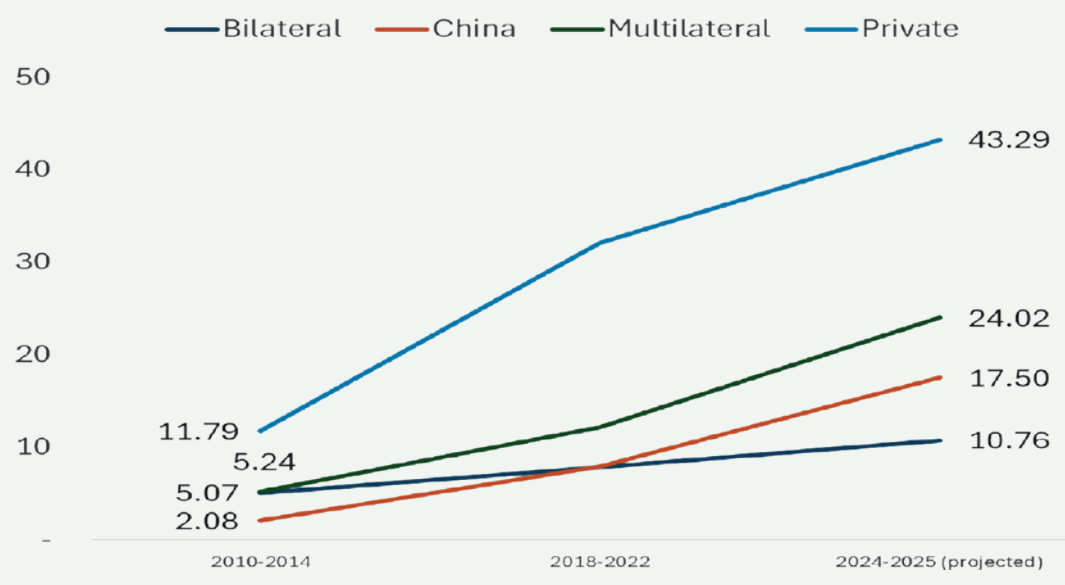
Need for capital market development accentuated by recent developments

In recent years the rationale for capital market development in Africa has become much stronger. Where capital markets could previously be regarded as an optional feature of financial systems in emerging markets, recent years' developments have accentuated their centrality.

Among the primary motivations are the additional

financing burdens associated with investments in climate change, in preservation and restoration of natural capital and in accommodating the impact of demographic change on the labor market. Emerging markets are confronted by the need to make significant investments, both in adapting to climate challenges, mitigating climate-related risks and in building resilient infrastructure. A growing youthful population implies that African markets must create growth-inducing job opportunities, including in the green economy. These investments add to already overstretched external indebtedness² (Figure 1) and place increased burdens on local project sponsors in terms of building capacity to prepare investment programs and develop appropriate funding strategies.

Figure 1: Average annual debt service by countries in Sub Saharan Africa (US\$ billion)



Source: International Debt Statistics, World Bank.

Compounding the impact of climate change is the reduction (withdrawal in the case of the United States) of bilateral development assistance and the decline in private foreign direct investment. In addition to funding from donors, African countries placed significant reliance on foreign direct investment (FDIs) as a source of private

capital, but since 2018 FDI flows into Africa have declined (Figure 2). Both reduction in donor flows and FDI accentuate the need to leverage available fiscal resources and remaining donor funding with capital provided by the private sector.

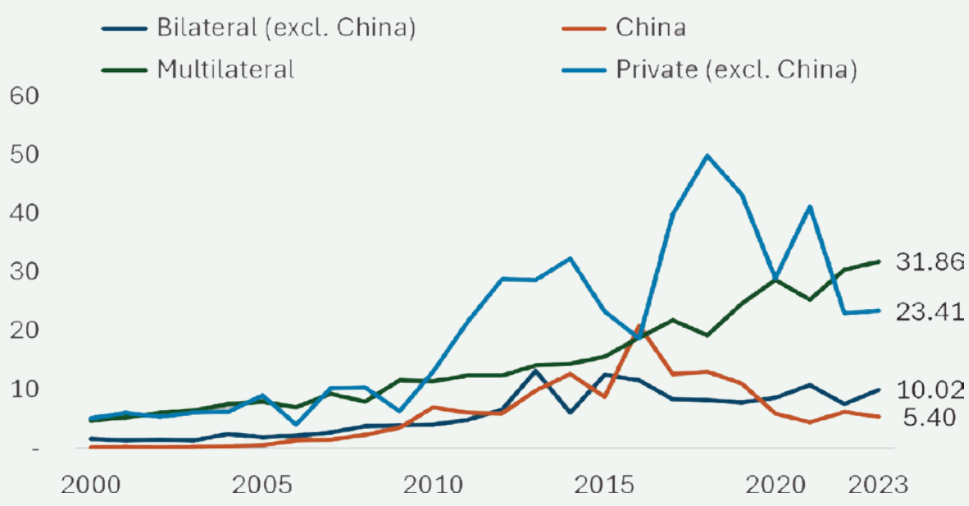
¹Studies motivating capital market development are Laeven, L. "The Development of local capital markets: Rationale and Challenges", International Monetary Fund, 2014; Carvajal, A., R. Bebczuk, A. C. Silva, and A. G. Mora. "Capital Markets Development: Causes, Effects, and Sequencing", World Bank, 2019; and the World Bank's Global Financial Development Report 2015/2016 on "Long-Term Finance".
²According to the World Bank's International Debt Statistics (2025) 75 percent of external debt of countries in Sub-Saharan Africa as of end 2024 was contracted by the public sector.

Enhanced domestic saving and investment depends on macro financial stability

Due to the size of the required investments, going forward much greater emphasis will need to be placed on stable, long-term domestic investment resources. Domestic investment in increased resilience and self-sufficiency in terms of energy, water and food security will contribute to reducing exposure to both foreign exchange, climate and geopolitical risks.

Financial stability is a prerequisite for expanding reliance on financial resources sourced from the domestic capital market. Financing made available through capital markets, where investors are willing to take risks and have longer time horizons, can provide a stabilizing alternative to bank financing. However, financial stability is core to enhancing the predictability of longer-term asset valuations on which reliance will need to be placed in making investment decisions.

Figure 2: Financing flows into Sub-Saharan Africa (US\$ billion)



Source: International Debt Statistics, World Bank.

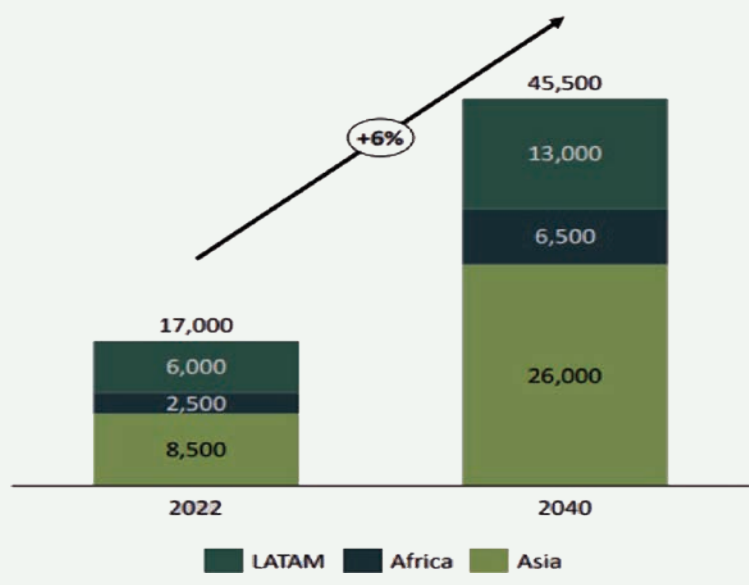
In pricing commitments of both shorter and longer maturities the domestic market for Government securities plays a crucial role as a benchmark. Assembling the issuance of Government securities in specific benchmark maturities across the yield curve serves the function of facilitating efficient pricing of funding provided to the Government and of setting a reference price for risk across the yield curve as defined by the maturities of the issued securities. Credibility in macroeconomic management, particularly in containing the size of fiscal deficits and adopting appropriate debt management policies, will be fundamental to establishing a liquid domestic yield curve for Government securities. At the short end of the yield curve money markets play an important role in recycling liquidity and setting a baseline yield for those investing in longer-term securities.

By facilitating more liquidity on money markets authorities can contribute to reducing the cost of capital.

The core role of institutional investors

Pension savings are gaining in importance in line with the transition common to most African countries from defined benefit pay as you go schemes to funded defined contribution schemes. Assets under management in Africa are expected to reach US\$6.5 trillion by 2040, Figure 3. However, given the large informal sector, coverage remains low as does the adequacy of the compensation provided by pension systems. Insurance penetration is also low in most countries, except South Africa.

Figure 3: Private domestic assets under management in Emerging and Developing Economies (excl. China) [US\$ billion 2022 (actual) and 2040 (forecast)]



Source: Systemiq and FSD Africa, Mobilizing domestic capital to drive climate-positive growth, 2024.

Traditionally funded pension schemes in Africa have invested in government securities, bank deposits, and real estate. Capital markets provide institutional investors – whether pension funds, insurance companies or sovereign wealth funds – with the potential to diversify their risk across a broader selection of more liquid asset classes with tenors that match the long-term nature of their commitments.

Competition with the banking system

Capital markets have an important role to play in enhancing competition within the financial system to ensure that scarce economic resources are allocated efficiently. By connecting issuers/borrowers directly with investors/lenders capital market instruments disintermediate the banking system, potentially reducing the cost of accessing funding provided by third parties. More fundamentally, capital markets can provide funding with a maturity commensurate with the payback period of investments being financed, thus avoiding the maturity mismatch risk and resulting limited tenors associated with bank financing.

Bolstering domestic savings on a sustainable basis

Among the core prerequisites for development of domestic capital markets is strengthening the availability of domestic savings. In emerging African economies pension funds are the primary repository of such savings with other institutional investors, such as insurance companies, mutual funds and sovereign wealth funds, potentially also playing an important role.

Institutional investors can play an important role in influencing market development by promoting improved governance, stronger market infrastructure and innovation in the use of financial products. By pooling risks and transacting in larger volumes, they can also put pressure on intermediation costs.

Empirical findings confirm the role of pension reforms as drivers of capital market development, revealing that in the years following pension reforms, countries experience more than a quadrupling of domestic net issuance activity (equity and bond issuances minus bonds matured) as a percentage of GDP, thus allowing firms to benefit from the increasing pool of locally available capital³.

In 1981 Chile was the first country to adopt a mandatory, privately managed, defined-contribution (DC) pension fund model which replaced the public, defined-benefit (DB) pension system. Relatively early on Chile established a broad institutional investor base. By 2005, mutual funds, pension funds, and insurance companies collectively had assets under management equivalent to 84 percent of gross domestic product (GDP), with the share of assets managed by pension funds and life insurance companies being equivalent to 56 percent and 18 percent of GDP respectively.

There are some important lessons that can be drawn from the Chilean experience. The first relates to adopting a suitable regulatory approach. In the case of Chilean open-end pension and mutual funds, fund managers were subject to short term monitoring both by the underlying investors, the regulators, and asset

management companies. This short-run monitoring, combined with the risk profile of available investment instruments, generated incentives for managers to be averse to investments that are profitable over longer horizons (like longer-term bonds) but that can have poor short-term performance.

By contrast, insurance companies adopted longer-term investment strategies, as their assets could not be withdrawn at short notice and were not subject to the same kind of short-run monitoring⁴. In this context investment guidelines can also play an important role: while it is desirable that institutional investors invest their funds domestically, the extent to which domestic markets offer adequate risk diversification opportunities needs to be borne in mind.

The second lesson relates to ensuring that pension reforms are undertaken in a resilient economic context. In Chile, following the Covid pandemic, three rounds of legislative approvals were introduced enabling early withdrawal of pension fund savings resulting in a fall in the size of assets managed by pension funds from 87 percent of GDP in 2019 to 61 percent in 2022⁵. While it would have been difficult to anticipate the social consequences of Covid pandemic when designing the Chilean pension reforms, the Chilean experience suggests that introducing pension reforms in a context, where broader types of social security measures – e.g. relating to the coverage of health care and unemployment risks – are inadequate or have yet to be introduced, can result in fragility.

An alternative approach is taken by Asian provident funds, which in addition to managing pension savings to provide old-age support, also channel savings into investment in areas such as housing and medical expenses⁶. In effect these funds manage the broader social needs of their participants, expanding their role beyond being ‘fortresses of savings’ of those in formal employment, and as a result, such pension funds may be less susceptible to government intervention (financial repression) during times of economic stress.

³Measured across a sample of 30 low and middle income countries that introduced mandatory funded pension programs between 1990 and 2022 against a control group of 117 countries that did not implement major pension reforms, it was found that net capital issuance (CNI) rose from an average of 0.7 percent of GDP in the year before implementing these pension reforms to an average of 3.2 percent within four years of implementing the reforms. Source: Meh, C.A. and S.L. Schmukler, “Financing Firm Growth, The Role of capital Markets in Low- and Middle-Income Countries”, World Bank Group, 2025.

⁴See Opazo, Raddatz, and Schmukler, “Institutional Investors and Long-Term Investment: Evidence from Chile”, The World Bank Economic Review, 2015. For further discussion see “Long-Term Finance”. Global Financial Development Report, World Bank, 2015

⁵Sources: Alejandro Jara and Alberto Naudon, “The changing nature of the financial system: the Chilean experience”, Central Bank of Chile, 2024, and Tatsushi Okuda, “Post-Pandemic Changes to Chile’s financial markets”, IMF, 2025.

⁶In addition to Malaysia’s Employees Provident Fund (EPF), examples of such funds are India’s Employees’ Provident Fund (EPF) and Indonesia’s Jaminan Hari Tua (JHT).

Equity markets play a limited role

One core function of capital markets as traditionally conceived is to provide the fulcrum for trade in enterprise ownership rights. Empirical studies confirm that enterprises that issue equity grow faster both prior to and after equity issuance than non-issuing firms, showing a significant growth differential in sales, assets, and productive capability for issuers relative to non-issuers, accumulating to around 19 percentage points in growth differential over a 5-year window following equity issuance⁷.

China and India provide examples of two countries where stock market capitalization increased rapidly following financial market reforms initiated in the early 1990's. Stock market capitalization in China and India rose from 4 percent and 22 percent of GDP, respectively, in 1992 to 80 percent and 95 percent of GDP in 2010. Moreover, in both countries financial systems transitioned from being mostly bank-based to being capital (equity and bond) market-based. For example, capital markets in China expanded from an average of 11 percent of the financial system in 1990-1994 to an average of 53 percent in 2005-2010. Comparing the same periods capital markets in India expanded from 57 percent to 65 percent of the financial system⁸.

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Despite this dramatic shift towards capital market-based funding and the benefits associated with equity issuance, the realm of enterprises taking advantage of equity market deepening remains quite small. While the average amount of capital raised through the issuance of equities on the domestic market doubled in China (from 0.5 to 1 percent of GDP per year) between 2000-2004 and 2005-2010, the average number of firms annually raising capital on the equity market only increased by 20 percent (from 87 to 105 out of 1,621 listed firms) comparing the same periods. The high fixed costs associated with equity issuance may act as a deterrent. These include disclosure costs (financial reporting and governance), investment bank fees (typically the highest costs), legal fees, taxes, rating agency fees, and marketing and publishing costs⁹. Partly due to the role of economies of scale in defraying these high fixed costs, the approach to equity market development adopted by China and India is more feasible in countries with large, relatively diversified economies. Developing equity markets is much more challenging in emerging market financial systems, let alone in frontier markets.

Efforts have been made to tailor investment by private equity (PE) limited partnerships to reach smaller, fast-growing, innovative enterprises, such as firms in high-tech sector or with high research and development expenditures. Equity financing, rather than debt, is better suited to funding innovation, which is usually associated with uncertain cash-flows and value generated largely taking the form of intangible assets, ill-suited as collateral for lending by banks.

Despite financial support designed to defray the additional costs associated with assessing and monitoring equity investments in many smaller

⁷These observations are based on firm-level analysis of the relation between firms issuing securities and changes in their productivity and overall growth rates using a comprehensive dataset of 150,165 firm-level issuances of equities and bonds in domestic and international markets over the period 1991-2016, see T. Didier, T. R. Levine, R. Llovet Montanes and S. Schmukler, "Capital Market Financing and Firm Growth", World Bank, 2019.
⁸More recently, since 2017, the relative importance of the banking sector has increased slightly (IMF/World Bank Financial Sector Assessment (April 2025)). Regulatory and reform measures have stalled the growth of the nonbank sector, especially NBFIs. Notably, the 2018 reform of the asset management sector—which sought to align the regulatory framework across different products and address other problems such as implicit guarantees on investment returns, asset pooling practices and opaque multi-layer investments—played a crucial role in reducing the linkages between NBFIs and the banking sector. In 2025 total assets under management were estimated at 95 percent of GDP (down from 130 percent of GDP in 2017), but still positioning China as one of the four largest asset management markets in the world.
⁹Source of comparison of India and China: Didier, T., R. Levine, and S. Schmukler, "Capital Market Financing, Firm Growth, and Firm Size Distribution." Policy Research Working Paper 7353, 2015, World Bank, Washington, DC.

enterprises¹⁰, PE partnerships – even when set up to focus on servicing SMEs – have tended to gravitate towards financing relatively large and mature firms, an outcome that can largely be attributed to structural impediments. On the demand side, SME owners are reluctant to (even partially) dilute the ‘sweat equity’ and control they have assembled in the enterprises they have created. On the supply side PE partnerships, which operate with a fixed investment period, find it difficult to realize an appropriate market price for their investments at the time of exit, and often the only option available to them is trade sales¹¹.

Given the scale economies associated with listed equity markets, their limited outreach, and the relatively low level of funding deployed via private equity markets, smaller emerging African economies will need to adopt a more focused, strategic approach to capital market deepening. This is borne out by the experience of a significant number of countries across Africa which in recent years have prioritized establishment of equity markets touting their existence as a measure of achievement. Most equity markets in Sub-Saharan Africa (other than in larger economies such as Kenya, Nigeria and South Africa) are small, illiquid, and concentrated compared to the vast, high-growth markets of China and India.

African equity markets have generally underperformed, often showing lower, more volatile returns driven by commodity dependence, political instability, and limited liquidity. Unfortunately, too often equity markets remain underutilized, and adoption of measures designed to support capital market development (as described in section 5 below) that require broader political commitment over the longer term may not enjoy the required sustained strategic focus. ommitment over the longer term may not enjoy the required sustained strategic focus.

Opportunities associated with developing corporate debt markets

An alternative approach is for countries to focus on developing the market for corporate debt. Focusing on the fixed income market with payment streams similar to bank loans provides more immediate competition to the banking system, the largest provider of financial services in emerging markets. Corporate securities markets benefit from the presence of benchmark yields on government securities which can be used in pricing corporate securities. As noted above a key prerequisite for establishing benchmark yields in government securities is that country authorities pursue sound macroeconomic policies. This is illustrated in the case of Malaysia discussed below.

As in the case in many emerging economies today, until the early 1990’s Malaysia financial services were almost exclusively provided by the banking system. But since then, Malaysia adopted a focused, strategic approach to developing its domestic bond market to (a) diversify credit risks beyond the banking industry, (b) alleviate currency and maturity mismatches risks, and (c) facilitate the use of domestic savings to finance the real economy. Having a deep domestic bond market has also helped Malaysia mitigate the impact of capital-flow volatility, reduce reliance on foreign debt, and increase resilience to weathering economic and banking system crises¹².

Unlike many emerging markets, that depend on offshore bond markets for dollar-denominated financing of infrastructure investments, Malaysia’s domestic market for project bonds stands out. Local currency corporate bond issuance swelled from just RM2.1 billion (US\$ 840 million) as at the end of 1990 (equivalent to 20 percent of the corporate sector’s capital market financing needs) to RM40.9 billion (US\$ 10 billion) at the end of 2019 (equivalent to 88 percent of the corporate sector’s financing needs). By 2019 the Malaysian bond market represented an equal mix between government securities (51.5 percent of GDP) and corporate bonds (49.5 percent of GDP)¹³.

The steps taken and scope of efforts required to develop the Malaysian bond market go back some 40 years¹⁴. Throughout this period the authorities maintained strong

¹⁰Such supplemental funding to PE funds seeks to compensate General Partners for the additional costs associated with assessing and monitoring a larger number of small investments as provided, for example, by the IFC SME Ventures program.
¹¹Sixty percent of participating PFAs in a survey undertaken by the Africa Venture Capital Association (AVCA) and PenOp cited a limited number of established GPs and perceptions of weak exit climate/unpredictable exit windows as the largest challenges to Nigerian PFAs investing in PE, see AVCA and PenOp, “Pension Funds and Private Equity in Nigeria”, December 2021.
¹²Unlike most other emerging economies, Malaysia already had institutional investors (pension and provident funds, insurance companies, and asset management companies) seeking diversification into a new asset class.
¹³Source: “Malaysia’s Domestic Bond Market: A Success Story”, World Bank, 2020.
¹⁴The scope of these efforts is summarized in Annex 1.

political commitment to the core pillars of financial sector development: maintaining macroeconomic stability (a high savings rate supported by low and stable inflation generally below 5 percent); prudent fiscal policy (leaving room for domestic savings to be used to develop the private sector); a conducive enabling environment (efficient, transparent, and reliable methods for debt recovery); and commitment to maintaining a stable and robust banking system (including at the time of the Asian financial crisis of 1997). The central bank, Bank Negara Malaysia (BNM), was committed to building a sound, stable, and resilient banking system that was a vital precondition for the growth of the domestic bond market. BNM has consistently led and collaborated with the government and other agencies on efforts to support the growth of the Malaysian capital market.

Following the Asian Financial Crisis the authorities supported the revival of the corporate bond market by creating the National Bond Market Committee (NBMC), a high-level committee comprised of representatives from key government agencies and market regulators with broad executive authority to provide policy direction in support of bond market development. Bond market development was also a core aspect of capital market masterplans adopted for the periods 2000-2010 and 2010-2020. The plans conceived by Securities Commission (SC) in close collaboration with the Ministry of Finance and BNM sought to sequence implementation based on fulfillment of predefined preconditions and the absorptive capacity of domestic markets and institutions. For example, the need for reliable and efficient market infrastructure for trading and settlement was addressed very early on and systems were continually enhanced; and innovation was supported by easing of regulations in a manner that reflected the level of market and investor maturity.

Tailoring the agenda for capital market development to emerging markets

Due to the limited outreach associated with equity market development and the institutional capacity-building efforts required to develop corporate bond markets, the

question arises whether alternative, more targeted approaches could be adopted to foster capital market development in emerging markets. While development of liquid, listed corporate bonds markets may lie within scope for larger emerging economies, such as Nigeria and Kenya, developing such markets lies beyond the scope of smaller and frontier capital markets.

The investment portfolios of institutional investors have traditionally concentrated on investment in low-risk government debt, bank deposits and real estate. To more effectively leverage domestic savings to address the investment needs of African economies, it will be important to diversify the portfolios of institutional investors beyond current investment choices.

Such portfolio diversification will need to be addressed from a multifaceted perspective involving, (a) greater focus on sustained macroeconomic stability, leading governments to issue less debt and leaving space for alternative investment by asset managers, (b) adoption of effective regulatory frameworks encompassing development of hybrid markets that provide greater comfort to asset managers in terms of governance and transparency than private markets, and encourage investment in alternative asset classes; (c) development of an adequate supply of investible assets and suitable investment vehicles, such as debt funds or special purpose vehicles, and (d) adoption of strengthened governance practices by institutional investors so they are better equipped to build the capacity required to manage the risks associated with diversification into new asset classes.

Success in diversifying fund manager portfolios depends on investing in the development of bankable projects, building an environment that fosters robust governance of investment decisions, efficient resource management (technology and skilled, fit-for-purpose human capital) and transparent measurement of both success and failure¹⁵. Efforts undertaken to address this multifaceted agenda have hitherto been insufficient. While regulators have provided institutional investors with limits within which they are authorized to invest in “alternative assets”, investment by institutional investors in such assets so far constitutes only very small proportion of their portfolio allocations¹⁶.

¹⁵“Innovations in Long-Term Capital Management: The Practitioner’s Perspective”, World Economic Forum, White Paper, 2016.

¹⁶“Gauging Appetite of African Institutional Investors for New Asset Classes”, joint study by IFC, AfDB and Making Finance Work for Africa, 2022.

Recently several innovative funds have been designed to use blended finance structures (with DFIs participating as anchor investors) to establish public, listed placements suitable for mobilization of funding by domestic institutional investors to the advantage of infrastructure investments and MSMEs. From the perspective of deepening capital markets the value added associated with these fund structures is that they leverage a hybrid public/private funding structure: (a) they benefit from the governance and public approval process associated with listing on public stock exchanges to attract investment by domestic institutional investors, and (b) the assembled funds can be used to provide liquidity to investments, both in the form of loans and private equity, thereby contributing to filling an important funding gap.

Finally, attention needs to be paid to various forms of risk-mitigation. Risk mitigation can take the form of first-loss arrangements tailored to the issuance of specific corporate bonds. Such risk-mitigation can be offered by donors both directly to specific projects or through the entities benefiting from first loss guarantees, such as InfraCredit in Nigeria and Dhamana in Kenya. From a capital market development perspective, the advantage of guarantees is that they provide a flexible instrument that can be built into transactions where they are needed to support the delivery of financing in local currency. GuarantCo, initially funded and set up by the U.K. Government, provides local currency guarantees that bridge the gap between the financial requirements of a project and the financial terms available from the local market, thus crowding in longer-term local private institutional capital. Due to GuarantCo's high credit rating GuarantCo's credit risk is equivalent to, or lower than, sovereign risk in emerging economies and GuarantCo's currency exposure is limited as – other than payment of guarantee premiums – cash flows are only exchanged in the case of default¹⁷.

While guarantees can be used to facilitate the issuance of corporate bonds in local currency, their role is best understood less as a stand-alone product and more as one layer within a broader operating system¹⁸. To work effectively guarantees are instruments available to project development facilities established with a view to fostering a suitable pipeline of implementation-ready bankable projects. If used strategically, utilization of guarantees by development facilities can standardize replicable project

preparation processes that reduce project due diligence costs and thereby support issuance of listed corporate securities that allow domestic institutional investors to diversify their investment risks and reduce the cost of capital for project sponsors¹⁹. The result is not merely leverage, but a more investable ecosystem that leverages the capacity of the local capital market, and once tested and proven viable, sets a precedent for further expansion of financing without the need for guarantees.

However, the costs associated with establishing development facilities, as described above, is high as they are a PE-based solution²⁰. Alternative, less costly forms of collaboration designed to streamline the process of project development could range from (a) informal sharing of information about investment opportunities, (b) a more formal platform organized as a company with permanent staff, where services are contracted in from a third party, and members pay for management, (c) a platform where the management function is conducted in-house, or (d) collaboration through an independent fund manager who takes responsibility for investment decisions²¹.

Several examples exist of institutional arrangements that (aim to) use issuance of capital market instruments to mobilize institutional capital to fund investment programs:

- **Using collaborative investment platforms:** In early 2026 the Nigerian Pension Industry Investment Consortium, a common platform among pension fund managers, was established on the initiative of the National Pension Commission (PenCom) to boost infrastructure and alternative asset investments. The platform aims to channel long-term pension capital into bankable infrastructure projects, while ensuring adequate risk management and sustainable returns for contributors.
- **Fund structures targeting domestic institutional investors:** The Nigeria Infrastructure Debt Fund (established in 2017), which benefited from an investment by the African Development Bank, is an example of a independently managed fund which attracts investment by pension. The IFC's Managed Co-Lending Portfolio

¹⁷GuarantCo mitigates its exposure to local currency exchange rate risks via diversification, being aware that "right-way risk" will likely play in its favor, i.e., in situations where the local currency depreciates, and it is more likely that local borrowers will come under pressure and may not be able to amortize their borrowing, a default on a local currency loan will have a smaller impact in US\$ terms leading to a smaller loss. Given the contingent nature of its exposures and the relatively limited extent of its currency exposure, GuarantCo does not hedge against currency risk.

¹⁸For further discussion see Claessens, S. and Kapoor, S.: "Bending the Climate Change Curve by Blending Finance", Finance for Development Lab. Policy Note, 2026.

¹⁹The Private Infrastructure Development Group, initially sponsored by the U.K. government, has invested in several project development facilities which were assembled into InfraCo Africa and InfraCo Asia in 2025, described in <https://pidg.org/our-solutions/project-development/>

²⁰As is normally the case in private equity funds, the GP earns management fee of 2% of the assets under management as compensation for establishing and running the fund. In addition, the GP earns 20% as an incentive-based fee or 'carried interest', which is charged on profits achieved from the fund above a certain pre-agreed level.

²¹For further discussion of these options, in addition to those cited in the text, see: Ekaterina Gratcheva, Aaron Levine, Jonathan Mirlrees-Black, Benjamin Osenius-Eite, Mark Brennan. "Co-Investment Options in Infrastructure: A Guide for Institutional Investors", IFC, 2021.

Platform Africa's MDB fund (under development) are examples of similar co-investments facilitated by independent fund managers. By specifically targeting domestic institutional investors FSDA's MDB fund focuses on local capital market development.

- o **Guarantees facilitating involvement of local institutional investors:** The South Africa Blended Finance Platform for Resilient Infrastructure Program, launched by the South African Government with international development partners in 2026, establishes a Credit Guarantee Vehicle (CGV) to help mobilize private capital for resilient infrastructure. The CGV will issue market-based credit guarantees that will help de-risk investment in infrastructure, crowd in private capital, and reduce reliance on sovereign guarantees. The objective in setting up the new platform is to attract domestic and global institutional investors by offering appropriate risk tranching and governance safeguards, thereby deepening local capital markets and supporting long-term financing for transformative infrastructure. As noted above, Infracredit in Nigeria and, more recently, Dhamana in Kenya similarly utilize first loss guarantees provided by Guarantco to crowd in investment in corporate securities by Nigerian and Kenyan pension fund managers.

- o **Tapping into domestic institutional capital using domestic listed vehicles:** FSD Africa is in the process of establishing a series of listed vehicles in Rwanda, Kenya and Ghana which use a hybrid structure to mobilize local currency financing to the advantage of MSMEs, see annex 2 for further description of these examples. The First of these vehicles has been in Rwanda in which the Rwanda Social Security Board (RSSB) alongside Enko Capital, announced in April 2026 the initial closing of its Rwanda-focused SME Growth Fund, with a commitment of US\$30 (RWF equivalent). The Fund, which aims to achieve a final close of US\$100 million, will be managed by Enko Capital. The fund will offer long-term, flexible growth capital in local currency to SMEs. FSD Africa played a crucial role in the successful structuring and implementation of this initiative and is developing an ancillary Risk Sharing

Facility, to incentivize the new fund to allocate capital of the fund to underserved SMEs (e.g.. women-owned, climate-focused).

- o **Securitizations increasing availability of credit to priority sectors:** Securitization is another example of an instrument that can mobilize domestic capital for MSME lending. In July 2025 the IFC announced its participation in the senior tranche of a securitization SPV established in the West Africa Economic and Monetary Union (WAEMU) by Banque Ouest Africaine de Développement (BOAD) PV. The SPV will issue asset-backed securities (for a value equivalent to US\$90 million) with a maturity of five years on the Bourse Régionale des Valeurs Mobilières (BRVM) and use the proceeds to acquire loans to MSMEs and individuals made by NSIA bank. IFC draws on the World Bank's private sector window to partially cover its currency risk in funding investments in local currency. A similar example is provided by Kaleidofin, an Indian Fintech company, which closed the first local currency farmer loan securitization in Kenya in 2026 with the support of FSD Africa. This securitization represents the first rating and the full set up of a structured capital financing vehicle (SPV) in Africa to unlock affordable, scalable local currency funding for smallholder farmers and MSMEs.

Such collaborative funding platforms are essential both to project sponsors in developing project pipelines and to asset managers in managing risk. Even the largest asset managers will be unable to viably assemble the specialized capacity required to prepare, develop, and manage the risks associated with investment in alternative assets targeting the infrastructure, housing and SMEs sectors. Without such collaborative efforts economies in Africa – even in the larger economies – will remain in a low-level equilibrium, as they will lack the capacity required to unleash economies of scale associated with development of capital markets. And by implication the imperative for developing similar but suitably tailored solutions that will suit the needs of smaller and fragile economies is that much stronger.

Conclusion

The growing financing needs associated with climate adaptation, infrastructure development, industrialisation, urbanisation, and demographic change mean that African economies can no longer rely primarily on external financing flows. Mobilising larger pools of domestic long-term capital is becoming increasingly important.

This paper argues that capital market development should not be approached narrowly as the creation of stock exchanges or the expansion of listed equity markets alone. International experience demonstrates that successful capital market development depends on a much broader ecosystem encompassing macroeconomic stability, pension reforms, institutional investor development, market infrastructure, governance, project preparation capacity, and suitable regulatory frameworks.

The paper also highlights that there is no single model for capital market development. Different countries have followed different pathways depending on the structure of their economies, institutional capacity, and domestic savings base. For many African economies — particularly smaller and frontier markets — hybrid approaches that combine elements of public and private markets may offer more practical and scalable solutions than attempts to replicate larger public equity markets.

Ultimately, capital market development is not only about expanding financial markets. It is about building financial systems capable of mobilising domestic savings into productive long-term investment that supports economic transformation, resilience, and sustainable development.

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