LMA Loan Market Association

Fund Finance Insights

A Brief History and Evolution of Fund Finance – Middle East & Africa

February 2025

Introduction

Building on our previous exploration of the history of fund finance in Europe, we now shift our focus to the dynamic regions of the Middle East and Africa. The evolution of fund finance in these areas is a fascinating story of economic transformation, marked by a rich tapestry of historical and resource-driven growth.

From their origins as ancient trade centres to their current status as modern financial hubs, the Middle East and Africa have histories deeply interwoven with trade, commerce, and financial innovation. As these regions have progressed and become more integrated into the global economy, they have developed sophisticated financial systems that facilitate a diverse array of financing activities, including fund finance.

This paper delves into the historical financing practices and the development of fund finance in the Middle East and Africa, highlighting key milestones and opportunities that have shaped its integration into the modern financial landscape.

Part 1: Middle East

Early Financial Practices

To fully comprehend the development of fund finance in the Middle East, it is essential to understand the region's historical financial practices and how the later adoption of fund finance integrates with them.

The roots of finance in the Middle East can be traced back to ancient times when trade and commerce were the primary economic activities. For example, Ancient Mesopotamia (6500 BCE to 539 BCE), located in the region of the Tigris-Euphrates river system, had sophisticated systems of credit and banking (including regulations on loans, interest rates, and debt) that facilitated trade across the region, laying the groundwork for financial innovation.

During the Islamic Golden Age (8th to 13th centuries), the Middle East emerged as a vibrant hub of trade, with Islamic finance introducing innovative concepts such as مضاربة (*mudarabah*: profit-sharing) and مشاركة (*musharakah*: joint venture). These concepts have a number of parallels to modern investment fund structures, contributing to the later development and acceptance of Sharia-compliant fund finance products.

The Ottoman Empire (1299–1922) further advanced financial practices in the Middle East. The empire's vast trade networks necessitated sophisticated financial systems, contributing to the region's financial infrastructure and laying the groundwork for further innovation.

The discovery of oil in the early 20th century further transformed the Middle East's economies, leading to unprecedented wealth and economic development. This period saw the establishment of modern financial institutions and the integration of Middle Eastern economies into the global financial system. The need for investment vehicles to manage and grow this wealth led to the emergence of sovereign wealth funds **(SWFs)**, which became significant players in international markets and facilitated the development of fund finance in the region.

Emergence of Fund Finance Facilities

In the late 20th and early 21st centuries, the Middle East's growing wealth and economic diversification efforts led to increased interest in alternative investments. Private equity firms began to establish a presence in the region, targeting sectors such as real estate, infrastructure, and technology.

MENA/Gulf Cooperation Council **(GCC)** SWFs and pension funds have become significant Limited Partners **(LPs)** in the global finance and investment management landscape. The resources they have available to invest as LPs have been accumulated not only from oil revenue but also from monetisations and capital market liberalisation during the past decade. Additionally, GCC investors benefit from USD-pegged economies, making investments in General Partners **(GPs)** and funds more accessible. The high investment-grade rating of GCC economies further enhances their attractiveness as LPs.

Consequently, a range of innovative fund finance products emerged (including a large number of SMA structures), underscoring the Middle East's commitment to financial innovation and its ability to adapt to the demands of a dynamic global market.

Development of Facilities

Key developments in this area include the following:

Subscription facilities

These began to gain traction in the mid-2000s as private equity and investment funds sought efficient ways to manage liquidity and capitalise on investment opportunities. These facilities allow funds to borrow against the capital commitments of their investors, providing the liquidity needed to make investments quickly and efficiently.

Net Asset Value (NAV) facilities

These emerged in the early 2010s, allowing funds to borrow against the value of their existing portfolio of investments, offering additional flexibility and liquidity management options.

Hybrid facilities

These began to gain prominence in the mid-2010s, combining elements of both Subscription and NAV facilities, allowing funds to use both uncalled capital commitments and the value of their existing investments.

GP financing

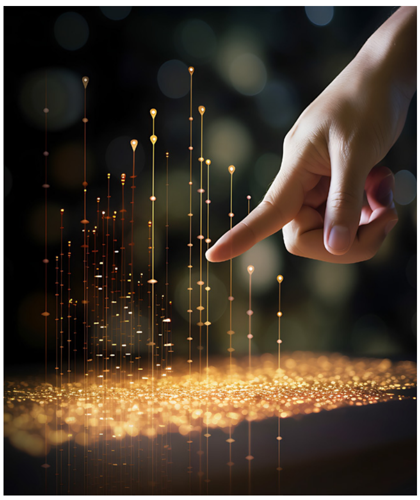
This gained traction in the mid to late 2010s, providing financing secured on the assets of the GP, including fee streams and/or the GPs share of fund assets to support GP co-investment, M&A or other strategic actions.

While the emergence of fund finance is a general development, regional fund finance facilities are still in the process of developing (with NAV, hybrid and GP financing in earlier stages of development). Nevertheless, these collective advances are a modern example of the region's dynamic approach to financial innovation and its commitment to meeting the evolving needs of its markets.

Resilience and Stability

Today, the key centres in the Middle East have become hubs for financial activity, attracting global banks and financial institutions. Their integration into the global financial system has led to increased collaboration and innovation. Regional financial institutions are partnering with international banks to develop new products and services, leveraging technology and expertise to enhance their offerings. As a result, these centres are increasingly offering a range of fund finance products and services, catering to both conventional and Islamic investment funds.

While the fund finance market in the Middle East faces challenges such as political instability, regulatory differences, and economic volatility, these challenges also present opportunities for innovation and growth. Political instability can drive the need for financial products that can withstand uncertain environments, while regulatory differences across the region encourage financial institutions to foster a culture of innovation as they tailor products to meet diverse legal frameworks. And economic volatility, while posing risks, also creates opportunities for financial institutions to offer specialised services that help clients navigate fluctuating markets. By addressing these challenges, the fund finance market can better position itself as a resilient and dynamic sector.



Future Outlook

The region's commitment to economic diversification and development, as seen in initiatives like Saudi Arabia's Vision 2030, is driving demand for investment and fund finance. As Middle Eastern economies continue to diversify and integrate into the global economy, the demand for this form of financing is expected to grow.

The region's financial centres are also well-positioned to continue attracting global investment, with the ongoing development of Sharia-compliant products further enhancing the region's appeal. As the Middle East continues to integrate into the global financial system, it will play an increasingly important role in the global fund finance landscape.

Part 2: Africa

Early Financial Practices

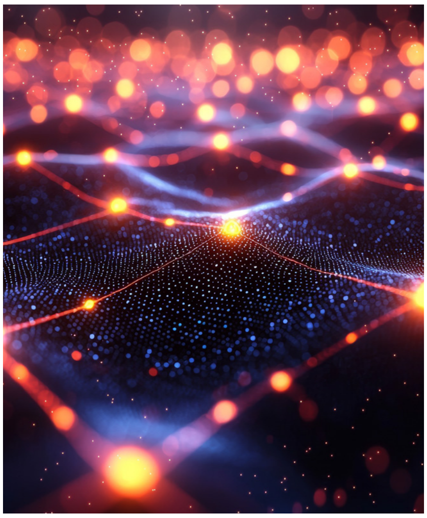
The history of fund finance in Africa is a complex and multifaceted narrative that reflects the continent's diverse economic landscapes, cultural influences, and evolving integration into the global financial system. The rise of private equity and investment funds, supported by development finance institutions, has played a crucial role in unlocking the continent's vast potential.

Africa's financial history dates back to ancient times, with early financial practices emerging in various regions across the continent. In West Africa, the trans-Saharan trade routes connected the region to North Africa and beyond, fostering the exchange of goods and the development of financial practices. The concept of pooling resources for collective investment, a precursor to modern investment funds, can be seen in various traditional practices across the continent, such as the "susu" system in West Africa and "stokvels" in Southern Africa.

These practices conceptually laid the foundation for financial innovation and the development of more complex financial instruments in the region.

The late 19th and early 20th centuries saw the introduction of modern banking systems, bringing significant changes to Africa's financial landscape. These systems were initially established to support economic activities, particularly in resource extraction and trade. Banks were set up in major cities, providing financial services to enterprises and settlers. During this period, the focus was primarily on commercial banking, with little emphasis on investment funds. However, the establishment of modern banking infrastructure laid the foundation for the development of more sophisticated financial systems in later years.

Following the independence movements in the mid-20th century, African countries faced the challenge of building their economies and financial systems. Many nations embarked on ambitious development plans, focusing on industrialisation, infrastructure, and social development. This period saw the establishment of national development banks and financial institutions aimed at mobilising resources for economic growth. The concept of investment funds began to take root during this time, with governments and development agencies establishing funds to support specific sectors, such as agriculture, industry, and infrastructure.



> *"Many of the LPs investing in African funds are Development Finance Institutions (DFIs), Multilateral Development Banks (MDBs), and philanthropic foundations. These entities bring a robust and attractive credit risk profile to the table..."*

Emergence of Fund Finance Facilities

In the late 20th and early 21st centuries, Africa saw a significant increase in private equity and investment fund activity. The continent's growing economies, expanding middle class, and abundant natural resources attracted global investors. Private equity firms started establishing a presence in Africa, focusing on sectors like telecommunications, financial services, consumer goods, and infrastructure (including digital infrastructure).

Many of the LPs investing in African funds are Development Finance Institutions (DFIs), Multilateral Development Banks (MDBs), and philanthropic foundations. These entities bring a robust and attractive credit risk profile to the table, making them highly appealing to banks involved in fund financing structures. Their participation not only enhances the credibility and stability of the funds but also provides banks with a level of assurance and confidence in the financial backing of these investment vehicles.

Development of Facilities

As a result of the above, fund finance products have begun to emerge, with key developments in this area including the following:

Subscription facilities

These emerged in the late 2000s as the private equity market in Africa matured, driven by the need for funds to efficiently manage liquidity and swiftly capitalise on burgeoning investment opportunities in a rapidly growing economic landscape.

Net Asset Value (NAV) facilities

These gained traction in the early 2010s as African private equity funds began to amass substantial portfolios, necessitating a mechanism to unlock the value of existing investments for enhanced liquidity and strategic capital management.

Hybrid facilities

These began to emerge in the mid-2010s as funds sought versatile financing solutions that could address both immediate liquidity needs and long-term capital optimisation, reflecting the increasing complexity and sophistication of the African investment environment.

GP financing

This became prominent in the mid to late 2010s as GPs in Africa sought to align their interests with LPs through co-investment, while also gaining the financial flexibility to pursue strategic growth initiatives in an expanding market.

These facilities play a pivotal role in facilitating access to capital and supporting the growth of investment opportunities across the African continent.

Local Fund Managers and Thematic Funds

In recent years, there has been a notable increase in the number of local fund managers operating in Africa. These managers bring valuable local knowledge and expertise, enabling them to identify and capitalise on investment opportunities that may be overlooked by international investors. The growth of local fund managers has contributed to the diversification and deepening of Africa's financial markets.

Local fund managers have also played a key role in promoting sustainable and impact investing, aligning their investment strategies with the continent's development goals. This focus on sustainability has led to the creation of thematic funds that target sectors and themes such as renewable energy, agriculture, healthcare, and financial inclusion, which are critical to Africa's long-term development.

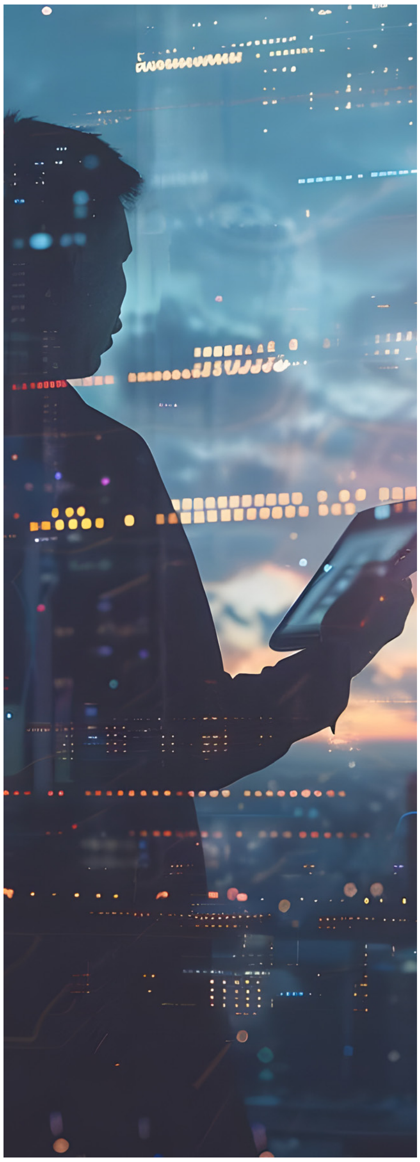
Resilience and Stability

Despite its growth, the fund finance market in Africa faces several challenges, including political instability, regulatory differences, economic volatility, and long-term local currency depreciation. However, these challenges also present opportunities for innovation and growth. Africa's young and dynamic population, coupled with its abundant natural resources and growing consumer markets, offer significant potential for investment. As African economies continue to develop and integrate into the global economy, the demand for sophisticated financial products and services is expected to grow.

Future Outlook

Africa is a dynamic and rapidly evolving market for fund finance. The continent's financial centres, such as Johannesburg, Lagos, Nairobi, and Cairo, have become hubs for fund finance activity, attracting global banks and financial institutions. These centres offer a range of fund finance products and services, catering to both local and international investment funds.

The integration of African economies into the global financial system has also led to increased collaboration and innovation in fund finance. Regional financial institutions are partnering with international banks to develop new products and services, leveraging technology and expertise to enhance their offerings.



Conclusion

The history of fund finance in both the Middle East and Africa reflects the unique economic, cultural, and historical contexts of these regions. From ancient financial practices to modern innovations, both regions have demonstrated remarkable adaptability in the face of changing global dynamics.

In the Middle East, the integration of traditional Islamic finance principles with modern fund finance products has created a unique and thriving market. Meanwhile, Africa's dynamic economic landscape and growing private equity presence have fostered a vibrant fund finance sector.

As the Middle East and Africa continue to integrate into the global financial system, the future of fund finance in these regions is positive. The demand for investment and financial services is expected to grow, driven by economic diversification, technological advancements, and a focus on sustainable development.

Together, the Middle East and Africa are poised to play an increasingly important role in the global fund finance landscape, offering further opportunities for growth, innovation, and collaboration.

As fund finance in the Middle East and Africa continues to evolve and expand, the need for a unified and influential voice in the EMEA loan markets has never been more critical. We invite you to engage with the Loan Market Association (LMA) to help drive efficiency, liquidity, transparency, and sustainability across the region. By collaborating with the LMA, you can play a pivotal role in shaping the future of fund finance, ensuring that it meets the highest standards and adapts to the changing needs of the market. Join us in our mission to foster innovation and growth, and be part of a community that is committed to advancing the EMEA loan markets for the benefit of all stakeholders.

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