



**Cross Border Investments &
Diversification Strategies**
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Einstein Kihanda

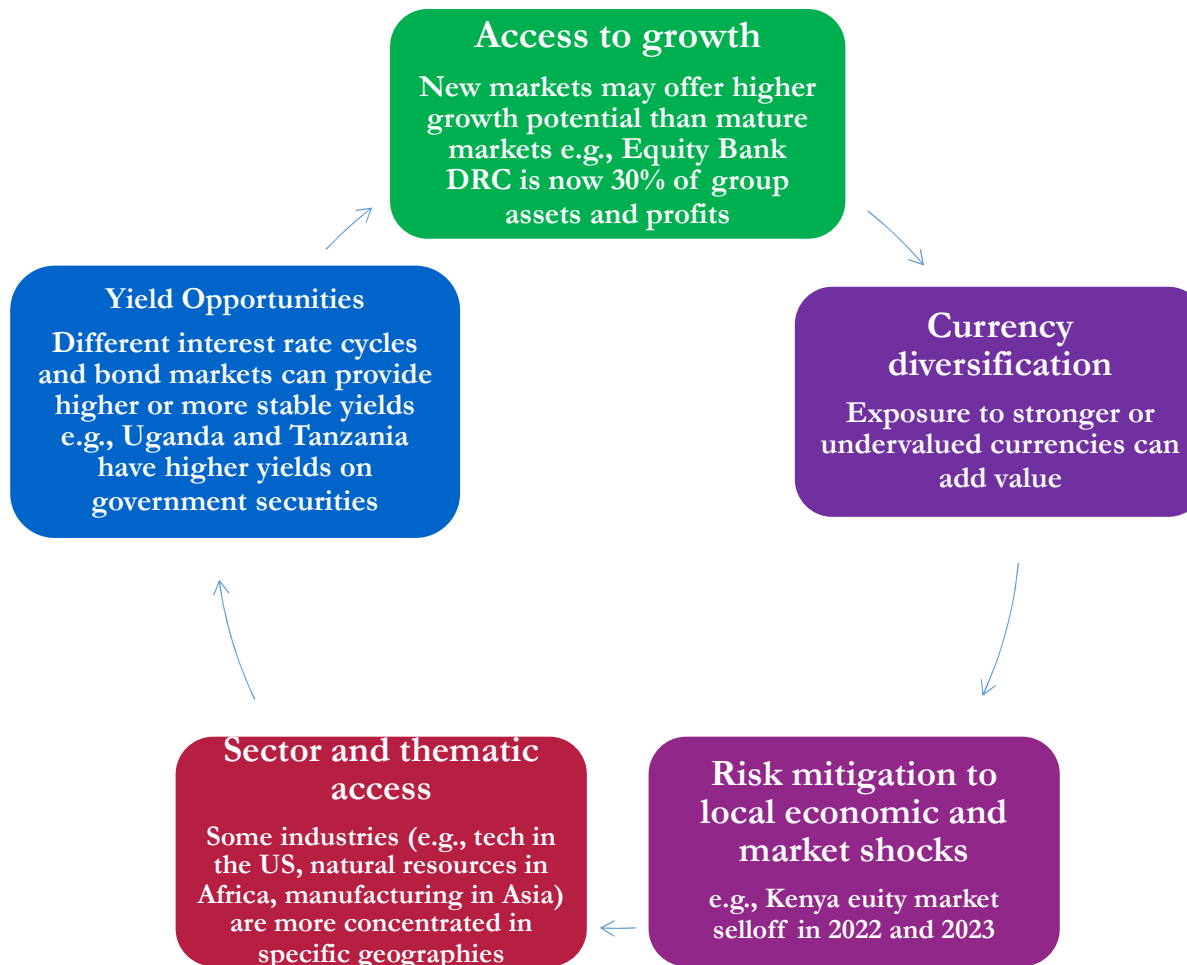


What are cross border investments?

- Cross-border investments involve allocating capital beyond the home market, either in developed or emerging economies
- Cross-border investments, also known as international investments, are a fundamental strategy for diversifying an investment portfolio. By putting money into assets, companies, or ventures in foreign markets, investors can reduce their reliance on a single domestic economy and potentially access new opportunities for growth



Why cross-border investments?



Cross-border investment vehicles

- **ETFs and Mutual Funds:** Low-cost, diversified exposure to global markets (e.g., Vanguard FTSE All-World ETF). These can be availed by the likes of Franklin Templeton and Blackrock. Locally we have the NewGold ETF provided on the NSE by Absa Securities
- **Direct Investments:** Purchase foreign stocks or bonds through international brokers like Franklin Templeton and Blackrock
- **ADRs/Depository Receipts:** Invest in foreign companies listed on domestic exchanges (e.g., Alibaba ADRs in the U.S.)
- **Hedge Funds/Private Equity:** For accredited investors, these offer tailored cross-border strategies
- **Digital Platforms:** Fintech platforms like Interactive Brokers or eToro simplify access to global markets.

Over the last six years, NSE has low correlation with offshore markets

Index Performance	2020	2021	2022	2023	2024	YTD Oct 9th	CORR
S&P 500	16%	27%	-19%	24%	23%	9.0%	0.3
Nasdaq	44%	21%	-33%	43%	29%	10%	0.1
FTSE 100	-14%	14%	0.9%	3.8%	5.7%	12%	0.5
MSCI (World)	14%	20%	-19%	22%	17%	12%	0.3
MSCI (EM)	16%	-4.6%	-22%	7.0%	5.0%	18%	0.4
NASI	-8.6%	9.4%	-23%	-28%	34%	35%	1.0

- This makes global markets an excellent diversification play in years when NSE underperforms

Cross-border investment risks

- **Currency Risk:** Fluctuations in exchange rates can significantly impact your returns. Even if a foreign asset performs well in its local currency, a drop in that currency's value against your own can wipe out your gains. Example is Safaricom Ethiopia and birr devaluation. Another example is the naira
- **Political and Geopolitical Risk:** Political instability, government policy changes, or geopolitical conflicts in a foreign country can negatively affect investments. This includes risks like expropriation, trade wars, or changes to regulations e.g., termination of Umeme concession in Uganda, KCB and Equity potentially forced to reduce ownership of DRC banks
- **Regulatory and Legal Differences:** Different countries have different legal frameworks, tax laws, and market regulations. Navigating these complexities can be challenging and may require professional advice to ensure compliance and avoid unexpected costs
- **Information Asymmetry and Transparency:** It can be more difficult for foreign investors to get reliable information on companies or markets in other countries. Accounting standards and corporate governance practices may also differ, making due diligence more complex
- **Liquidity Risk:** Some foreign markets, especially smaller or emerging ones, may have lower liquidity, making it difficult to buy or sell assets quickly without a significant price impact. Naira devaluation locked in foreign investors for several years



Geography
Regional allocation
Country selection

Currency
Hard currency &
Local currency



Diversification strategies

Sector & Theme

Defensive sectors &
cyclical sectors
Thematic opportunities e.g.,
infra, fintech

Asset Class
Fixed income
Equities
Alternatives

Manager & Strategy
Multiple external managers
Blend active and passive strategies

ASSET ALLOCATION



■ STOCK
■ BONDS
■ REAL ESTATE
■ CASH

Best practices in cross-border diversification

- **Strategic Asset Allocation (SAA):** Establish long-term targets for asset classes and geographies. Define long-term weights by asset class, region, and currency
- **Tactical Adjustments:** Make short-term shifts to capture market opportunities or reduce risks. Adjust based on market cycles and opportunities
- **Risk Management:** Use hedging instruments (currency forwards, derivatives) and set country or sector limits. Undertake manager due diligence
- **Governance and Oversight:** Implement clear investment policies, benchmarks, and regular portfolio reviews
- **Local Expertise:** Partner with experienced managers who have on-the-ground knowledge of specific markets.

Practical considerations when investing across borders

Research and due diligence

- Use reliable data sources (e.g., Bloomberg, IMF reports) and consult local experts to understand foreign markets

Tax implications

- Account for withholding taxes, double taxation treaties, and local capital gains taxes

Risk management

- Use hedging instruments (e.g., futures, options) to mitigate currency and market

Portfolio rebalancing:

- Regularly adjust allocations to maintain desired risk-return profiles

Cost management

- Minimize fees by choosing low-cost ETFs or brokers with competitive rates.

Regulatory limits

- Offshore exposure for pension schemes is capped by RBA at 15% of AUM

*Net return to investors

Sample Cross-Border Portfolio 1 : Moderately aggressive strategy

This portfolio is for an investor with a higher risk tolerance and a long-term horizon (e.g., a young professional saving for retirement). It is tilted toward growth assets, such as stocks, with a significant portion allocated to international and emerging markets

Equities (65%):

Domestic Stocks (30%): Large-cap, mid-cap, and small-cap companies in your home country.

International Developed Market Stocks (25%): Companies in established, stable economies like Europe, Japan, and Canada. This can be achieved through a broad international index fund or ETF.

Emerging Market Stocks (10%): Companies in rapidly growing economies like Brazil, India, or China. These offer higher growth potential but also come with greater volatility and risk.

Fixed Income (30%):

Domestic Bonds (15%): Government and corporate bonds from your home country.

International Bonds (15%): Bonds from foreign governments and corporations. This helps to diversify a fixed-income portfolio and can offer different interest rate exposures.

Alternative Investments & Cash (5%):

Real Estate/REITs (2%): A small allocation to international real estate through a Real Estate Investment Trust (REIT) or direct property investment.

Cash (3%): Held for liquidity and to take advantage of new opportunities.



Sample Cross-Border Portfolio 2 : Balanced strategy

This portfolio is suitable for an investor with a moderate risk tolerance, aiming for a mix of growth and stability. The allocation is more evenly split between stocks and bonds, with a balanced international component

Equities (50%):

Domestic Stocks (25%): A mix of large-cap and mid-cap companies.

International Developed Market Stocks (15%): Exposure to major global markets.

Emerging Market Stocks (10%): A smaller, but still meaningful, allocation to high-growth markets.

Fixed Income (45%):

Domestic Bonds (25%): Government and high-quality corporate bonds.

International Bonds (20%): Bonds from various developed and emerging countries.

Alternative Investments & Cash (5%):

Commodities (2%): Such as gold or other raw materials, which can act as a hedge against inflation.

Cash (3%): For short-term needs and market opportunities.



Sample Cross-Border Portfolio 3 : Conservative strategy

This portfolio is for a risk-averse investor, such as someone nearing retirement. The focus is on capital preservation and generating stable income.

Equities (30%):

Domestic Large-Cap Stocks (20%): A low-risk, stable equity allocation.

International Developed Market Stocks (10%): Limited exposure to international markets for some diversification.

Fixed Income (65%):

Domestic Government Bonds (40%): Considered a low-risk, stable asset class.

Domestic Corporate Bonds (15%): Higher-yielding but slightly riskier than government bonds.

International Developed Market Bonds (10%): Provides additional diversification and income.

Cash (5%): Held for immediate liquidity and to reduce volatility.



ILAM Offshore Investment Offering

Eurobonds



USD Fixed Income Fund



Global Equities



Private Equity Funds



Trade Funds



Summary

- Cross-border investing, when combined with thoughtful diversification strategies, provides investors with a broader opportunity set and reduces concentration risks inherent in single-market exposure
- While risks such as currency volatility, political uncertainty, and liquidity constraints exist, disciplined asset allocation and strong risk management practices can help mitigate them
- Ultimately, the combination of global reach and diversified exposure supports more resilient portfolios, better positioned to navigate market cycles and capture long-term growth
- Be cognizant of RBA maximum exposure limits