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Africa Auditions For A Leading Role

With a stunning twist of fate, companies that are looking for a refuge from the turmoil of recent years in developed markets are turning their attention to the continent that for much of the past century was considered suitable only for the bravest—or perhaps rashest—investors. Extractive businesses such as mining and oil and gas companies have been there for decades, for obvious reasons, but recent years have seen global consumer goods companies, banks and IT and telecoms companies also looking for opportunities in Africa. And opportunity is exactly what they are finding.

As they explore these hitherto underappreciated markets, they are discovering not only that the costs associated with setting up shop in Africa are often lower than they anticipate, but that the markets themselves are showing the sort of growth potential that is rarely seen elsewhere in the world.

At the same time, Africa is becoming a source of inspiration and innovation, particularly in the use of mobile technology. In West Africa, for example, cocoa farmers are using their mobile phones to share weather and pest alerts and to gather information that can dramatically increase their crop yields. Across sub-Saharan Africa, phone-based money management is becoming increasingly prevalent, particularly among those without bank accounts, upending traditional financial services models.

Although it is currently generating a great deal of interest and attracting a flood of investment, Africa still faces considerable challenges. Its infrastructure is woefully inadequate, even by the standards of developing markets. Many countries have neglected their education systems in recent years—meaning that even as investors eye Africa, they cannot find enough skilled or educated local people to help build the countries' economies. And although the continent is blessed with abundant natural resources, in many cases it lacks the expertise even to map those resources, let alone to take advantage of them.

One of the biggest issues Africa has to overcome is the perception that it is a dangerous, corrupt and difficult place to do business. There is no doubt that it is challenging, particularly for new entrants, but companies and investors are reporting that the risks of operating in Africa have been, in many instances, overstated. "The general perception of risk in Africa is changing," says Orli Arav, head of project finance at Frontier Markets Fund Managers. "But we've been there for a long time and never thought it was as risky as people thought."

Dan Keeler
Editor-at-large
Global Finance

Power To The People

Innovative financing techniques and growing investor sophistication are prompting a surge of interest in sub-Saharan infrastructure projects.

By Dan Keeler

Sub-Saharan Africa is rapidly turning into the growth and investment story of the decade. With a substantial youthful population, increasingly stable democratic governments and a growing desire for economic advancement, the region is already making tremendous progress. Inadequate infrastructure, particularly in the power sector, is hampering that development, however. Even in the more economically advanced countries, such as South Africa, Kenya and Nigeria, power shortages are common and transportation, sanitation and telecommunications infrastructure is seriously lacking—especially away from main urban areas.

In less-developed countries within the region, particularly those emerging from years—or in some cases decades—of turmoil, there is a tremendous infrastructure deficit. Across the continent, there is a need for new ports, airports, roads and rail networks, and for massive investment in power, water, sanitation and communications.

Because of the scale of the challenge, the numbers are mind-boggling. A commonly quoted statistic is that, simply to meet its development goals and bring its infrastructure up to the levels of other emerging markets, Africa will need some $93 billion in infrastructure investment every year for the next decade. Much of that investment will go into transportation, telecommunications and water projects, but a vast chunk of it will be swallowed up by the power sector.

According to the International Energy Agency, sub-Saharan Africa needs more than $300 billion in investment to achieve universal access to electricity by 2030. Currently, around 85% of people living in rural areas have no access at all to electricity, and many of those living in urban settings suffer regular power outages.

The lack of power generation capacity is costing Africa dearly, not only in purely financial terms but also in lost opportunities for social and economic development, says Nnena Nkongho, an emerging

VanNiekerk, Standard Chartered: There is fresh interest in investing in Africa

Arav, Frontier Markets: Infrastructure funding mechanisms have developed considerably

markets investment professional who splits her time between Lagos, Nigeria, and New York. "The lack of infrastructure, in particular power, makes many businesses here in Nigeria less competitive than their global peers in a wide range of sectors." The difference in pure cost terms is substantial, but the social cost is far greater. Producing more power domestically would generate jobs and help diversify the economy while strengthening the case for improving other infrastructure, such as transportation and telecommunications systems.

In the Democratic Republic of Congo, power shortages are thwarting the government's efforts to push its copper mining industry up the value chain. The government has repeatedly tried to force miners to stop exporting copper concentrate and instead export only finished copper, but many producers say they cannot process the ore in-country because they don't have access to reliable electricity supplies.

Power shortages and interruptions also impose less-obvious costs on business because they make Africa a challenging place to live, raising costs for employing expatriates and locals alike and forcing people to spend a considerable amount of time dealing with energy shortages rather than being productive.

BREAKING OUT OF A VICIOUS CYCLE

There is no question that the lack of infrastructure across sub-Saharan Africa is impeding the region's development, but it is also inhibiting the flow of investment needed to fund the construction of infrastructure. Historically, Africa has looked to donors, predominantly from the West, to square the circle, but new models of infrastructure financing are now appearing that are helping channel private funds into much-needed projects in Africa.

The changes taking place are timely: As much of the world wakes up to Africa's economic potential, there is no shortage of available funding, much of it coming from other emerging markets, such as Brazil and China. Just in the past year, for example, China pledged up to $20 billion in funding for projects in Africa. Japan promised to stump up $32 billion, and US president Barack Obama, at the conclusion of a three-nation trip to Africa, announced the Power Africa initiative, a multiyear plan backed by $7 billion in US funding aimed at helping reduce the continent's power infrastructure deficit. Private investors are keen to put money to work in Africa, too. With investment returns from other regions dwindling, Africa, with its rapid population growth, burgeoning economies and vast, untapped resources, is proving a tempting target.

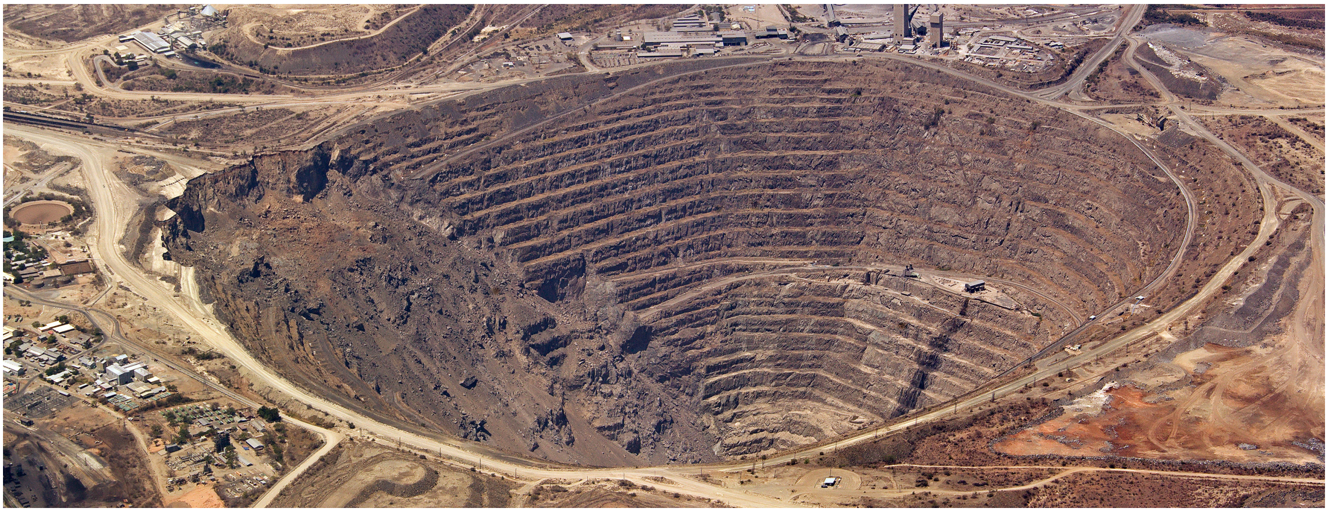
A number of funds are working to harness that enthusiasm. The African Development Bank, which already has $17 billion invested in infrastructure-related projects, recently launched its Africa50 fund with the hope of drawing up to $50 billion from private investors, sovereign wealth funds and, significantly, African savings and pension funds. Private investors are also the targets of a swath of recently launched, Africa-focused private equity funds—including one from Brazilian investment bank BTG Pactual, which aims to reach $1 billion.

Having access to funding is only half the battle, however. "The capital is available to fund infrastructure projects in Africa—there is no shortage of investors," notes Emile Du Toit, South Africa–based head of the Pan African Infrastructure Development Fund (PAIDF) and head of infrastructure investments at Harith Fund Managers. But, he cautions, "there are not enough well-crafted projects that are investable." There are two key problems, according to Du Toit. "In perceived high-risk areas like Africa, you have to go the project finance route for infrastructure, and you have to have strong government support. Many governments in Africa are not strong enough from a financial or regulatory standpoint, and project finance takes too long for most private-sector players."

"The lack of infrastructure makes many businesses here in Nigeria less competitive."

— Nnena Nkongho, emerging markets investment professional

Funds such as the PAIDF attempt to address these problems by devising agreements tailored to potential investors' risk tolerance and using a creative mix of dollar and local-currency structures. Two key factors are helping to support such efforts, says Orli Arav, head of project finance at Frontier Markets Fund Managers, which manages the $753 million Emerging Africa Infrastructure Fund: "A number of successful projects backed by private equity



have shown that companies can be comfortable with the risk," she says. The second key factor is that investors are receiving lower returns elsewhere, so the yield from a sub-Saharan African power project, for example, can suddenly look exceedingly attractive to a long-term investor.

Arav, whose fund tends to be involved in arranging or participating in financing for African infrastructure projects, says funding structures have developed considerably recently, but she still sees scope for innovation. One of the key issues, she notes, is that developers need to ensure there is an exit strategy. "Currently the exits are very limited," she says. "We are seeing some progress in that the new players might decide to buy some of the assets during development, but it's not enough. What could sharply change the pace of development is to have a market where you can sell projects later on. That will only happen when you have a lot of big players looking to buy assets."

"In perceived high-risk areas like Africa, you have to go the project finance route for infrastructure and you have to have strong government support."

— Emile Du Toit, Harith Fund Managers

LOOKING BEYOND LOCAL

One of the commercial banks that committed financing to Obama's Power Africa initiative is Standard Chartered, which pledged to fund more than $2 billion in energy projects. The bank's director of project and export finance for Africa, Neil VanNiekerk, says he is optimistic about changes taking place in the infrastructure funding space that are encouraging local banks to become more involved. "Different structures appearing now, including some that incorporate a soft-currency element, are encouraging local banks to participate. That is proving important in concession-based projects in the power and infrastructure space particularly, because the income the projects generate is almost certainly in local currency." Some of the new structures are also enabling domestic banks to take part in longer-term financings by including shorter-tenor, local-currency tranches that can be partially refinanced.

Dubai-based VanNiekerk is also seeing fresh interest in investing in Africa, particularly from private equity funds and asset managers, and believes the Power Africa initiative will bring new players into the market. "They are sitting on a lot of capital, and there is a strong chance they will start directing it into Africa," he asserts.

Changes in the way infrastructure development plans are being implemented may also enhance their effectiveness. Adonis Seka, Central Africa cluster head for Ecobank Capital—the investment banking arm of Ecobank Group, involved in infrastructure financing across Africa—says many countries in Africa are taking a more regional approach. "When you build roads, for example, it's not just about getting the network set up in this country, it's about connecting with the border countries and improving economic and social activities across the entire region," he explains. "It's about opening up trade to make sure you expand exports and the movement of goods regionally."

There is clearly a long way to go to bring Africa's infrastructure up to even a basic standard, but there is a high degree of optimism around recent developments. "The catalysts for a sustained productivity boost and a structural transformation of African economies are starting to fall into place," says Razia Khan, head of regional research Africa at Standard Chartered. Du Toit sums up the change in mood: "Suddenly there is more momentum. You can get meetings in a week or two, rather than a month—it's top of mind." If the momentum is sustained, perhaps Obama's hope that all Africans will have access to electricity by 2030 will be realized. ■

Boom Or Bust?

Africa's mobile-banking boom is a complicated tale of East versus West. But who's approach will prove right in the end? By Erik Heinrich

Mobile banking is a force for social and economic change in Africa unlike anything seen before. Of the world's 81.8 million mobile-money customers, 56.9 million are in sub-Saharan Africa, according to the GSMA, a London trade association representing some 800 wireless carriers.

But there are troubling signs that not all regions are benefiting equally from this financial boom. Increasingly, the deployment of mobile-money and mobile-banking services on the continent has become a tale of two Africas, with a great divide separating East and West. According to the most recent GSMA study of global mobile-money adoption, there are 48.5 million subscribers in Eastern Africa compared to just 7.8 million in Western Africa.

"There are now more mobile-money accounts than bank accounts in Kenya, Madagascar, Tanzania and Uganda," says Claire Penicaud, author of the GSMA study. "But while there is an increasing number of sprinters, there is also a persistent number of slow-growers who have not reached commercial scale. The reality is that mobile money remains a complicated business."

What accounts for the great disparity between East and West on the African continent, and can it be bridged anytime soon? Much of the success that Eastern Africa has experienced is thanks to Kenyan mobile carrier Safaricom and its M-Pesa mobile wallet, which launched in 2007 and today has 15 million users conducting more than 2 million daily transactions.

The GSMA estimates that over 60% of Kenya's GDP moves across the M-Pesa platform each year. In Tanzania and Uganda, where M-Pesa has satellite services, that figure is 30% and 20% respectively, signifying impressive levels of penetration far exceeding anything in North America or Europe for mobile money.

PARTNERING FOR BANK SERVICES

M-Pesa has recently begun partnering with financial institutions to become what is, in effect, a full-service bank branch. South Africa's Standard Bank, a pan-African financial institution, is a typical Safaricom partner. "Our mobile services are seamlessly integrated into M-Pesa," says Gustav Vermaas, head of mobile and

Internet banking for the lender's operations outside its home territory. "A big driver for our digital strategy is the ability to easily move funds between bank accounts and mobile wallets," he adds.

Apart from offering basic banking, Standard Bank is working toward making its mobile wallet, which in all cases is linked to an account, the primary payment mechanism for clients and a distribution channel for a variety of financial products, including investment and insurance.

Nearly 2,000 miles from Nairobi on the Atlantic coast of Africa, Nigeria has also jumped aboard the mobile juggernaut sweeping Africa. With a population of 162.5 million, Nigeria is nearly four times the size of Kenya, and its annual GDP of $244 billion is seven times bigger. Yet despite its size and stated goal of becoming a cashless society, Africa's most populous country is far behind Kenya in the mobile-money race.

REGULATORY FRAMEWORK

Kenya's four-year head start partly explains the difference in adoption rates. But some industry analysts point to another reason. The two countries, both pillars of sub-Saharan Africa, have dissimilar regulatory regimes for mobile money and mobile banking.

"The reality is that mobile money remains a complicated business."

—Claire Penicaud, GSMA

While Kenya's mobile revolution in financial services is being driven by Safaricom, a wireless carrier, in Nigeria it's the banks who have taken a leadership role. In fact Nigeria's powerful bank lobby has created a regulatory environment where telecommunications companies are prohibited from applying for mobile-banking licenses. Their role is limited to supplying the technical infrastructure that makes mobile banking possible.

Vermaas, Standard Bank: A big digital strategy driver is the ability to easily move funds between bank accounts and mobile wallets

Adedeji, UBA: Once the banks in Kenya agree to have a central national switch, the monopoly of M-Pesa will be broken

Why did Nigeria and many other West African countries choose a different route than Kenya? "The lack of a central switch has made interoperability very difficult in Kenya," says Yinka Adedeji, director of e-banking at the United Bank for Africa (UBA) in Lagos. "The transfer of money between banks has not readily been an option. Other countries in Africa have seen this weakness and decided not to replicate the Kenyan model of mobile money."

UBA has acquired a modest 200,000 customers for its U-Mobile banking service since launching at the beginning of this year. The service can be self-activated with a debit or credit card by people with existing accounts; the unbanked can activate it with a prepaid card.

About 90% of the customers of U-Mobile—whose functionality will soon include money transfers from countries where UBA has operations—were already doing business with the bank. "People with bank accounts will adopt mobile banking first, and the unbanked will follow in adoption," says Adedeji.

But whether this proves true is debatable. "The vast majority of fast-growing deployments are from mobile-network operators rather than banks," says Penicaud of the international wireless trade association GSMA. "This highlights the importance of creating regulatory environments which allow MNOs to offer mobile-money services along with banks."

Togo-based Ecobank, the continent's biggest pan-African bank by reach, with operations in 34 countries including Equatorial Guinea and South Sudan, is taking a hybrid approach to mobile banking. "Ecobank Mobile is working with a number of leading telco partners, together with our own technology platform, depending on the country and transaction requirements," says Patrick Akinwuntan, Ecobank's group executive director and head of domestic banking, representing the group's retail, local corporate, public sector and microfinance businesses. "We're committed to making financial services available to the underbanked and unbanked in Africa that are convenient, accessible and secure."

Perhaps in the long run, West Africa's focus on a central clearing house for all players will prove to be a winner, as an increasing number of banks and wireless operators get into the game. Notes Adedeji of UBA: "Once the banks in Kenya agree to have a central national switch, the monopoly of M-Pesa will be broken."

Meantime Vermaas has advice for banks embracing mobile: "Design from the outside in. Too many banks allow suppliers or employees to dictate their strategy." He adds: "The cost of rolling out mobile financial services is always twice what you expect, and the uptake half." ■

Trading In Stability

Developed-markets watchers hope tightening trade ties and increasing foreign direct investment will help ease tensions in North Africa.

By Dan Keeler

Two years after the Arab Spring swept through North Africa and beyond, toppling entrenched regimes and spreading a sense of democracy, freedom and optimism, the region's prospects were beginning to look rosy. Early this year, economic growth was beginning to pick up and the efforts of those who had fought to depose dictators seemed to be bearing fruit.

But as *Global Finance* was going to press, North Africa was in turmoil. Two political assassinations in six months had triggered angry demonstrations in Tunisia and prompted the moderate Islamist government to agree to consider resigning in favor of a nonpartisan "national unity" government. In Egypt the brutal crackdown on demonstrators opposing the ouster of a democratically elected president, the military takeover of government and the demonizing of the Muslim Brotherhood were threatening to ignite widespread violence. Sandwiched between the two, Libya was dealing with its own crisis. Unrest and lawlessness were triggering disruption at the country's key ports, slashing oil exports to as low as a sixth of their normal level and raising questions about the stability of the country's government.

TRADE PACTS

Amid so much turmoil, Morocco and Algeria present relative oases of calm. Although they still have not reached agreement over the disputed territory of Western Sahara, after years of enmity the two countries appear to be heading for reconciliation. Morocco, in particular, has been pushing for greater regional cooperation and integration and has been working to build its trade links with Europe and other regions, such as West Africa.

It is through trade that the European Union is hoping to help North Africa's troubled fledgling states recover their poise and develop their economies. As part of its "neighborhood policy," the EU is working with countries around the bloc's periphery to create a more productive trading relationship. It has focused recent North African efforts on building a trade pact with Morocco.

EU negotiators are hoping the Morocco pact will become a model for other countries in the region. In a recent discussion of the progress of the neighborhood policy, the commissioner in charge of the project, Štefan Füle, said he was optimistic that Tunisia would begin talks that would mirror the EU's discussions with Morocco: "Tunisia offers good prospects of a successful democratic transition, and the EU must remain engaged to support this country," he commented.

Tunisia's trade with the EU illustrates the importance of Europe to the economies of North Africa. Of Tunisia's total of nearly €12 billion ($15.6 billion) in exports in 2011, almost €10 billion went to the EU. Four-fifths of the country's FDI originates in Europe. Morocco is also heavily reliant on Europe, with 60% of its FDI originating there.

The EU makes no secret of its hope that the countries of North Africa will eventually form part of the economic union. Noting that the pending trade agreement with Morocco would include a wide range of services and investments, the EU said it hoped the pact would lead to "the gradual integration of the Moroccan economy into the EU single market."

Over the past decade, trade between North Africa and the fast-growing emerging markets—particularly Brazil, Russia, India and China—has also deepened considerably: North Africa represents both a source of sorely needed commodities for the BRICs and a market of some 170 million people for their products.

Perhaps a more compelling reason for the BRICs to invest in North Africa is the fact that, through their trade links, North African countries present another channel of access to the lucrative consumer markets of Europe and beyond. Tempted by the region's free-trade agreements, not just with Europe but also with several countries in the Americas, companies from the BRICs have poured billions into factories across North Africa. China has been leading the charge. Brazil and India have also been highly active, as have such non-BRIC countries as Turkey and South Korea.

In its April 2013 report "Arab Countries in Transition," the International Monetary Fund noted that Arab Spring countries are struggling with an immensely difficult balancing act as they try to maintain political stability while fulfilling the economic and social hopes of their populations. A key part of the solution, the IMF believes, is promoting international trade, as well as attracting more FDI inflows to the countries of the Middle East and North Africa region. In order to do that, MENA countries must "deepen trade integration with the advanced economies, fast-growing emerging markets, and among countries within the region," the report asserts.

Whether growing trade and growing FDI will ease tensions in the region by boosting economic growth or add to unease by pushing out domestic businesses remains to be seen. But there is no doubt the region will be in transition for some time to come. ■