

Africa: Tapping
into Growth
Opportunities,
challenges
and strategies
for consumer
products



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Africa: one of the world's fastest growing economic hubs

As the growth outlook for the Euro zone area and other developed economies remains weak – GDP growth for the Euro zone for 2012 down to -0.5% and for the US¹ to 1.8% - and consumer confidence has fallen to the lowest levels in the past three years, companies are increasingly targeting (second tier) emerging markets to secure their next level of growth.

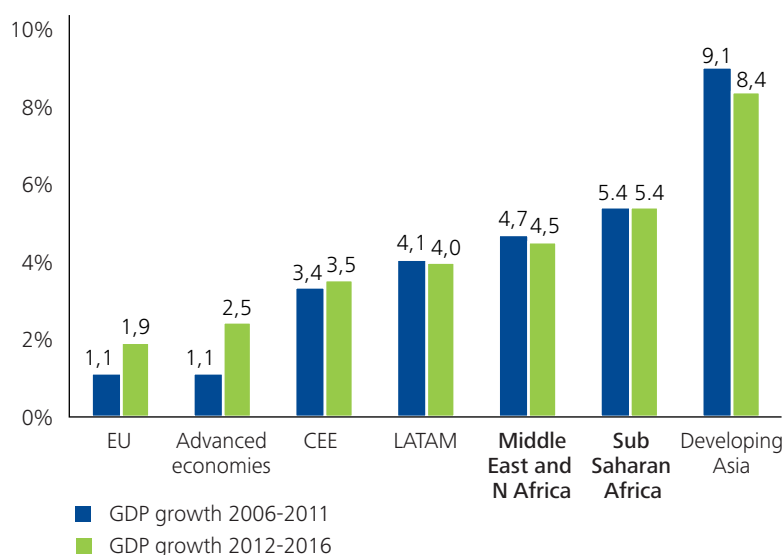
For years, growth for consumer products in Africa has been overshadowed by other markets as Asia, Eastern Europe, the Middle East and Latin America. However, despite the global impact of the Euro zone crisis, Africa came through reasonably unscathed, partly driven by the benefits they receive through close economic ties with China, and specific countries have started to impose themselves as viable investment opportunities. African GDP has outpaced world growth in the past and is foreseen to continue growing at an average rate of 5.4% until 2016². Additionally, nine of the world's 20 fastest-growing economies are from the African continent: The fastest growing countries Mozambique, Zambia, Niger and Ghana each have GDP growth of over 7% per annum between 2011 and 2016 as is illustrated in Figure 1.

While growth in Africa remains closely linked to the growing demand for oil, gas and minerals, which have been the cornerstones of the continent's economic boom, other economic segments are beginning to develop. Increased urbanization levels, the emergence of a middle class with higher purchasing power and an increased consumption of goods and services will drive growth for retailers and consumer product companies.

Africa's development shows characteristics that represent ample opportunity for the future and six major trends have been reshaping African economies and turning them into promising investment opportunities for the world's largest consumer business companies:

- **A larger, younger and more affluent population:** Today, Africa has the fastest expanding labour force in the world, expected to reach 1.1 bn and surpass India and China by 2040³. Demographic trends are extremely favourable with approximately 62% of Africa's inhabitants under the age of 25 and a population growing at an average rate of 2.2% which is twice as high as the growth in Asia (0.9%).
- **Increased urbanization levels:** Currently, around 40% of Africans live in cities; by 2050, 63% of Africa's population is expected to be urban and countries like Nigeria, Ghana or Angola will see urbanization levels of around 80%⁴
- **Increased spending power:** Africa's steadily growing per capita income drives the emergence of consumer markets with a surprising level of sophistication and growing spending power. EIU forecasts⁵ that by 2030, the continent's top 18 cities could have a combined spending power of US\$1.3 trillion. According to the EIU, Africa's urban consumers can be divided into three main tiers:
 - The first tier is the rising and the future middle-class market of 350m-500m, similar to the segments in India and China
 - The second tier is the number of consumers at the bottom of the pyramid, the growth of which is highlighted by the ascent of the mobile phone
 - The third is the challenge for firms to move from basic goods to affordable products
 Businesses will need to take this customer segmentation into account and build their market entry and growth strategies accordingly.

Figure 1: Average Annual real GDP growth

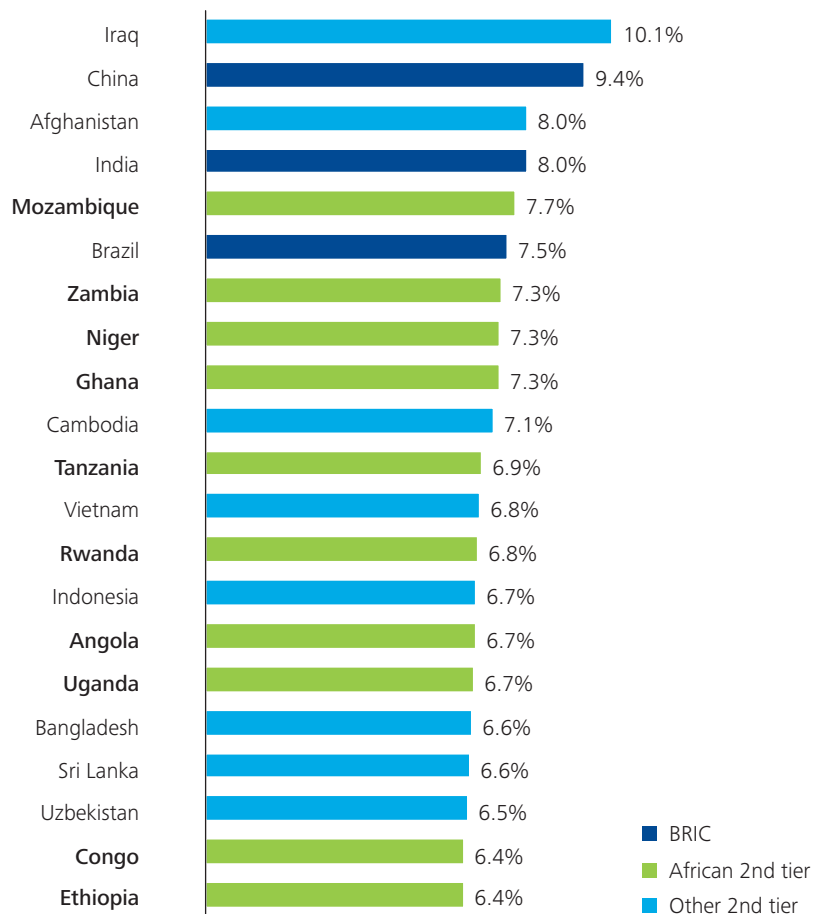


- **Higher internet and mobile phone penetration rates:** Africa is the fastest growing mobile telecom market in the world. With over 620 million mobile connections as of September 2011, Africa has overtaken Latin America to become the second largest mobile market in the world after Asia. Over the past 10 years, the number of mobile connections in Africa has grown by 30% per year (average growth) and is forecast to reach 735 million by the end of 2012. ⁶
- **Increased stability of the regulatory and financial sector:** African governments are keen on improving infrastructure and ensuring the right economic and regulatory environment to attract FDI (e.g. foreign investment grants, adopting programmes targeted at industrial development and beneficial to both local and foreign businesses ⁷, adoption of policies related to the granting of construction permits, lifting of various import restrictions or improving investor protection legislation). Today, several African countries compare favourably to many more developed economies on ease of doing business, investor protection or political risk.

These developments support an increasing focus on more sophisticated products and services, thus creating unique opportunities for consumer product companies as part of their strategies for growth. The African Development Bank estimates retail, manufacturing, financial services and telecommunications to account for approximately 2/3 of Africa's GDP growth. Also, since 2004, Africa has had the highest growth rate of private foreign direct investment (FDI) into emerging markets ⁸ and the profitability of foreign companies in Africa has been consistently higher than in most other regions in the world.

These factors embolden consumer product companies and lead them to reassess the risks they are prepared to take to capitalise on the obvious growth potential and expand their presence on the African continent.

Figure 2: Average Annual real GDP growth per country



Clients need to balance risks and rewards when selecting the appropriate market to enter

If growth opportunities are significant, so too are the risks associated with expansion in Africa. However, the degree and nature of these opportunities and risks vary significantly from one country to the next.

Looking at only one indicator can give a wrong image of the market potential of particular markets. For example, when evaluating African total GDP, South Africa is still seen as the economic powerhouse of Africa, with a GDP valued at US\$378 billion and making up nearly a quarter (22.7%) of the continent's total. This compares favourably to the position of Nigeria (7.4%). However, when comparing FDI into African countries, Nigeria attracted US\$6 billion in 2011 compared to South Africa's US\$1.5 billion.

This illustrates that a broad view has to be taken on African economies and a detailed analysis is required to select appropriate growth markets. The high divergence in indicators makes expanding operations in African markets a challenging endeavour. The size and diversity of the continent's economies makes it difficult for companies to use the strategies they have successfully applied in other parts of the world. Lack of proper market and risk analysis can lead many companies to either under-achieve or fail in their expansion strategy.

A first step towards a successful market entry strategy is determining where the greatest growth opportunities are and carefully evaluating expected benefits against the risks of doing business in these countries.

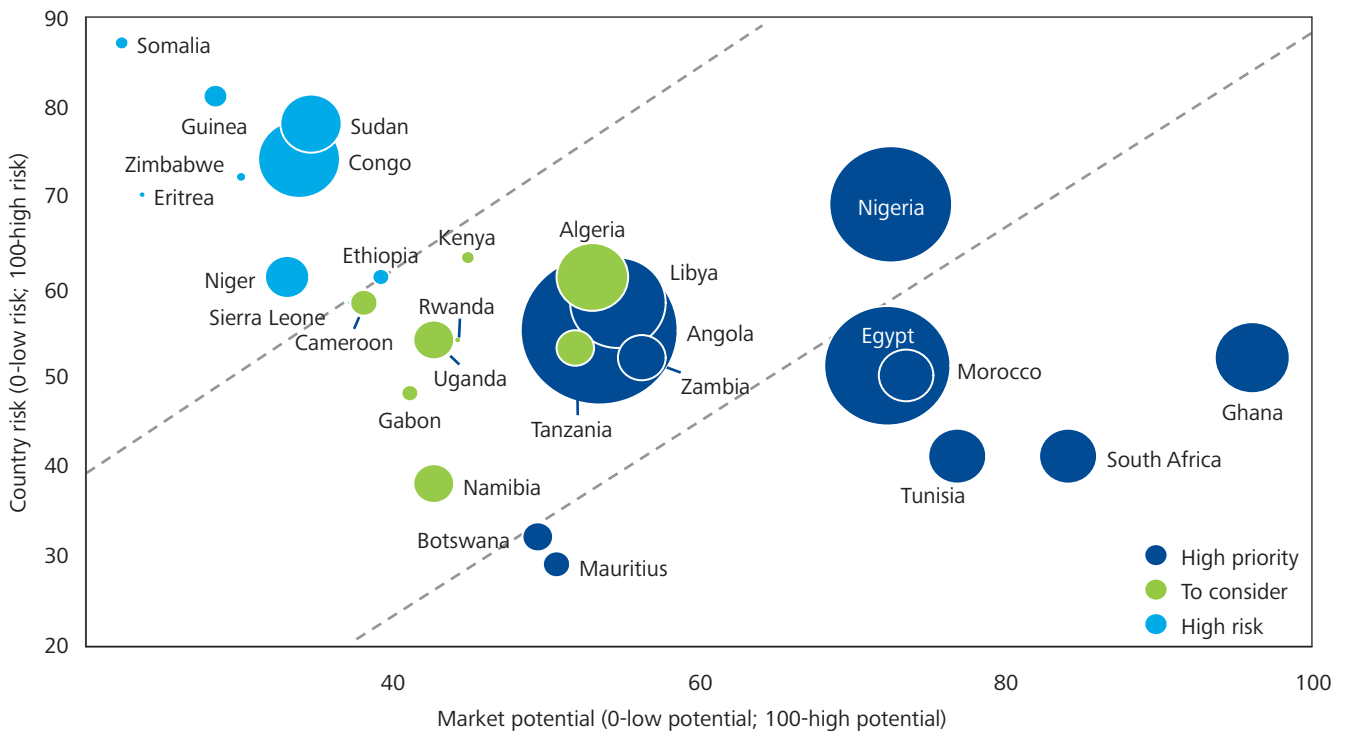
The Deloitte Emerging Markets team has analysed all African countries based on 10 macro-economic and social indicators⁹ to identify the markets that offer most potential for Consumer Business companies. The analysis considered both economic indicators for market potential (GDP growth; household expenditure; FDI levels) and indicators reflecting the level of risk in the country (economic and political stability, ease of doing business, investor protection legislation, corruption perception index). Combining these indicators and led to interesting insights, showing Ghana, S. Africa, Tunisia, Morocco, Nigeria and Egypt as the most interesting markets.

It is interesting to note that the major Northern African countries (Egypt, Morocco, Tunisia) are represented in the top 10. Many of these markets have been targeted by larger retailers in the past, albeit that investment has simmered as of late due to political unrest (Arab Spring). However, despite these events, we believe these countries will continue to show high growth in the coming period as their young and increasingly outspoken population demands more economic stability and higher global integration in the region.

What companies' management needs to bear in mind is that all these countries have their own challenges that make doing business difficult: the aforementioned Arab Spring, oil crises in Nigeria, local content laws requiring to have a certain % of indigenous employees, high income tax rates, unusual withholding taxes on foreigners or foreign companies, recent developments in union strife and the list goes on. A macroeconomic analysis is a first step when considering expanding your operations in an African economy, but it is by no means the only one. It needs to be complemented by an in-depth market and risk analysis that needs to include the following key factors:

- Competition and market concentration: Market fragmentation; supplier over-dependency; anticompetitive practices
- Customers and sales channels: Dependence on traditional sales channels in specific countries; client segmentation; cultural disconnect; different needs to Western societies
- Third Party / Joint Venture Requirements: Finding the right partners and stakeholders; Inadequate structures to facilitate identification of JV partners; Inadequate structured contractual arrangements
- Geopolitical: lack of cross-border agreements; excessive trade embargos; corruption risks; lack of free market mechanisms; political instability (local, state, country) suspension of country concessions; expropriation by country governments; lack of adequate infrastructure
- Laws and regulation: laws inhibiting foreign ownership; adverse legal/regulatory changes; inappropriate lobbying; tax implications
- Credit access: access to capital; maturity and integrity of the financial sector

Figure 3: Market prioritization framework



Note: Size of the bubble indicates FDI inflows (2011)
 Source: World Bank; UNCTAD; African Development Bank; EIU; Deloitte analysis

Despite these considerations, it is becoming increasingly clear that the business case for entering African markets is favourable. Many companies have entered the African market over the last years and are expanding their presence on the continent.

There are many case examples of companies entering the African market

Over the years there are multiple success stories of companies either entering or expanding in African markets. Companies enter markets at their own pace and in their own manner, but generally successful entry strategies in Africa tend to have two aspects in common:

- 1) The company adapts its product or services to the needs of the local customer
- 2) The company bonds with and invests in the community and the local government

Two clear examples of successful entry strategies are Coca-Cola and Unilever.

Coca-Cola is currently present in 56 countries and territories across Africa, running 160 bottling plants on the continent. The African continent is a major contributor to their global sales and of all the markets that Coca-Cola has entered in Africa; it has not pulled out of a single one. It therefore has tremendous experience in the market and the success of the company in Africa has been due to its savvy advertising, distribution techniques, product adaption and its abundant involvement in local community life. Several examples illustrate this:

- In the late 90s Coca-Cola collaborated with the South African advertising organization SMLB to promote the brand to the local population by linking Coke to Africa’s greatest passion: soccer.

- The company has slightly modified its business concept to make it available to the poorer population. When consumers drink their beverage on the premises of a local store, they only have to pay for the contents of the bottle which significantly minimizes costs. By partnering with a local distribution company it can sell its drinks in returnable bottles.
- The company has found new ways to get its products delivered to even the most remote corners of Africa. Where trucking stops, a small army of entrepreneurs takes over, that transports the product the last few miles (by bike or foot) to the most isolated points of Africa.

Unilever has been active on the continent for more than a century. The company's annual African sales are over 5 billion and they employ around 40,000 people in the offices and factories spread out in 40 locations. Like Coca-Cola, Unilever has tailored its products towards the needs of African customer and invested heavily in bonding with the local community:

- Unilever has developed a low-cost, climate stable margarine that does not require refrigeration
- It has been aggressively pushing a low-price packaging strategy to cut costs. With these initiatives, Unilever has created several brands of varying affordability levels
- To distribute its products Unilever cooperates with small local retailers, often with stores no bigger than a large appliance box. With a rural sales force distributing products to isolated villages, Unilever is able to reach 80% of the population
- In 2007, the company was the first large tea company to commit to sustainable sourcing of tea on a large scale. In Kenya 250,000 farmers have now been trained in so called farmer field schools on sustainable tea agriculture

Product modifications and investing in the local population have made Unilever a trusted brand in Africa. Frank Braeken, Unilever executive VP for Africa confirms this: "Our strategy is to increase our social impact by ensuring that our products meet the needs of people everywhere for balanced nutrition, good hygiene and the confidence which comes from having clean clothes, clean hair and healthy skin". Braeken stresses that Unilever is devoted to serve the "Base of the Pyramid" (BoP) in Africa.

Market Entry strategies

While there is no one size fits all entry strategy, several key elements need to be considered when considering expanding operations in African markets:

- Building local presence
- Leveraging first mover advantage
- Taking a long-term view
- Building relationships & working together with governments
- Taking a holistic view (market, financial, legislative, tax, culture)
- Investing in local talent

Aligning your ambitions to these aspects as well as developing a detailed and quantitatively solid framework, growth strategy and implementation plan is crucial to successfully expanding operations. Deloitte generally breaks down the challenges into three concrete phases of expansion, each focused on specific questions and requiring a different set of service offerings. The approach is depicted in Figure 4.

Figure 4: Emerging market growth framework



¹ IMF estimates for 2012; GDP growth estimates for 2013 have also been lowered down to 0.8% for the Eurozone area and to 2.2% for the US

² IMF World Economic Outlook 2012; World Bank Databank

³ United Nations, Department of Economic and Social Affairs, World Population Prospects

⁴ United Nations, Department of Economic and Social Affairs, World Urbanization Prospects, 2012

⁵ EIU and the Economist - Africa: Open for business, 2011

⁶ African Mobile Observatory, 2011

⁷ E.g. the clothing and textile competitiveness improvement programme, the manufacturing improvement programme, the food, beverage and agro industries improvement programmes

⁸ UNCTAD

⁹ GDP growth past and future, population size, level of urbanization, mobile phone penetration, FDI, Ease of doing business, Household consumption, Corruption perception, Investor protection

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Interested in discussing how Deloitte can help your company leverage new growth opportunities in African markets? Just contact:



Randy Jagt
Director Deloitte Consulting, Emerging Markets Taskforce leader
+31 6 1098 0178
rjagt@deloitte.nl



Eric Damoiseaux
Senior Consultant Deloitte Strategy & Operations
+31 6 1004 2870
edamoiseaux@deloitte.nl

www.deloitte.nl/emergingmarkets

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