Africa in 2017:
Shaping the continent’s future
Summary report of the conference held on
25 January 2017 in Johannesburg
Welcome and Context

Africa’s future should not be left to chance and should be actively shaped by both businesses and policy makers. According to Deloitte Africa CEO, Lwazi Bam, Africa now needs a clear future and one that’s grounded in reality.

With vast untapped resources and favourable demographics, Africa’s potential has been highlighted many times. For instance the African Development Bank (AfDB) states that Africa has just over 30% of the world’s mineral resources and half of the continent’s one billion people will be of working age by 2020. However, major gaps still remain between the continent’s resource abundance and its achievements.

Relying on unprocessed raw materials for revenue and growth is not enough or as renowned Harvard economist, Michael Porter, pointed out “a nation’s prosperity is created and not inherited.”

These words hold true across the continent as countries that took initiative to diversify their economies are showing a more stable growth performance as opposed to those that continue to depend on a single raw commodity.

Beyond diversifying and creating wealth, another question that needs to be addressed is inequality and redistribution of wealth created from Africa’s resources. Businesses across the continent should strive to make an impact that matters and part of this is improving their communities.

By developing a common purpose and vision, African governments and businesses can work together to create and redistribute wealth more equally. This can actively shape a brighter future for the continent.
Presentation: Trends for Africa in 2017

2016 was a rather challenging year for a number of African economies. The prevailing question for the year ahead will be “what does 2017 hold for Africa?”

The six key forces that are likely to shape Africa in 2017 are:
1. Structural reforms,
2. “Repricing” of economies,
3. Privatisation of state-owned assets,
4. GDP growth recovery,
5. Gross fixed capital formation spend, and
6. External forces outside of emerging markets.

A brief review of major historic events such as the fall of the Berlin Wall, the Asian Crisis or the collapse of Lehman Brothers reveals that reforms, be it structural, economic or political, are often the direct result of crises or economic shocks to an economy. More often than not, these reforms have led to considerable socioeconomic improvements. This raises two important questions: What shocks or crises could cause such reforms to take place on the African continent? And, could the recent commodity price shock force governments to carry out much-needed growth-oriented structural reforms?

One of the key drivers of foreign direct investment (FDI) is the ease and cost of doing business in a country. Unfortunately, most African countries are known as costly and challenging investment destinations. This may be changing due to the current “repricing” taking place in some countries, particularly oil-propelled ones.

The repricing trend especially of previously overvalued assets makes it more affordable to invest in Africa, and this is likely to attract higher levels of FDI going forward.

Poor growth and a lack of revenue may result in “fire sales” of state-owned entities and assets in African countries. This is expected to take place in fiscally-challenged economies, which are struggling to raise revenues from commodity exports. These often inefficient state-owned entities may be described as handbrakes on development across the continent, largely in the infrastructure, utilities and transportation sectors. Privatisation could potentially address these issues.

A fourth force that will shape Africa in 2017 is the recovery of GDP growth rates. In 2016, Africa south of the Sahara saw its lowest growth in the past decade. Although growth is expected to have “bottomed out” in 2016 and improve slightly into 2017, it will take rigid policy interventions to steer Africa off a low-growth path.

As a rule of thumb, gross fixed capital formation (GFCF) should stand between 25% and 35% of GDP to ensure steady growth in an economy. While the sub-Saharan African (SSA) level of GFCF has hovered around the 20% mark for the last decade, countries like Ethiopia and Botswana have managed to maintain levels of investment in the 30–35% of GDP region. What are the forces that will drive other African countries to mimic the investment patterns of these countries in 2017?

There is reasonable concern surrounding the controversial stance US President Donald Trump has taken regarding international trade, and the ramifications this presents for Africa at large. Through the African Growth and Opportunity Act (AGOA), Africa, more specifically South Africa, has secured a sizable US market for exports - a market which now seems at risk. Similar to the Western financial crisis triggered by the collapse of Lehman Brothers, Africa faces a growing risk, not from emerging markets, but from the developed world.

On a more positive note, the United Kingdom’s (UK) decision to exit from the European Union (EU) is likely to see a far more assertive and independent UK, and possibly improved foreign trade and aid policies toward Africa.

Keynote: How Business must respond to the New Dynamics of the African Economy

Good governance and increased growth must form the pillars of how businesses think about both policy and execution. Bad governance leads to long-term decline and policy decline.

For businesses to address the challenges brought about by bad governance, inequality, and poor interregional trade they need to recognise the peculiarities of different territories across the continent.

A large portion of Africa’s population still survives on less than US$2 a day, and 60-70% of all goods are sold through informal or open-air markets. Therefore, fast moving consumer goods (FMCG) companies struggle to pass on price increases of products to their low income consumers as this is likely to be unsustainable. Pricing power in markets where income is low and the quality of products or services do not always give companies the ability to price up, forces businesses to rethink their business models and their approach to individual markets.

Not only should businesses in Africa adopt a low-cost model, they must also adopt a flexible model especially in a market where challenges change over time. Adopting a flexible model will prevent stagnancy and will allow businesses to address opportunities when there is a change in ideas and models.

For Mr Matlare, the road to success is always under construction. Businesses should continue to retool their business models in order to adjust to unpredictable challenges and practice good governance to achieve desired goals and successes.
Panel Discussion: Africa’s new Winning Companies

In 2016, Africa recorded its lowest growth in over a decade. Despite this record low, a number of companies continue to succeed. The success of these winning companies is often based on careful due diligence and planning prior to entering new markets as well as investments and attempts to localise operations once the new market has been entered.

Choosing the appropriate market to enter in itself can be challenging and requires careful planning. Often it is wise to analyse regional opportunities, instead of focusing on a single country. By strategically targeting a regional market it is possible to develop regional supply chains and to expand distribution to a wider market, and by doing so reap the benefits of scale. Additionally, regional targeting can help mitigate the risk of volatility within a single country by spreading the risk across a larger region.

An additional important aspect of the planning process is to make an effort to understand the legal and regulatory environment of the target market prior to entry as emphasised by Mr Whitfield. The AAAM – the African Association of Automotive Manufacturers, of which he is the vice chair – works to partner with government bodies across SSA to promote the expansion of the automotive industry on the continent. Industry initiatives such as the AAAM will go a long way in reducing risk across Africa by shaping the legislative environment for first-movers and attracting FDI from across the world.

It is important to note that the benefits of being a first-mover are at times limited on the African continent. Nigeria and Angola, for instance, attracted a lot of attention from investors during their high-growth boom years. Companies sometimes rushed into these markets without appropriate planning in order to be first-movers.

However, due to the lack of planning and not understanding the market, some of these first-movers faced serious challenges. Early entrants into a new market often have to do the heavy-lifting as they are breaking new ground for their respective sectors or industries. Later entrants experience a much smoother entry as most of the initial groundwork, including shaping the legislative framework, has been done by the first-mover. Companies considering entry into new markets also have to be prepared to adopt a highly flexible approach to mitigate risks stemming from volatilities in many African markets. It is difficult to enter foreign markets with rigid preconceived ideas. Instead, a highly adaptive approach should be applied.

For Mr Werth, establishing strong local teams is one of the key success factors when entering a new market. Local partners are not enough. Mr Williams emphasised that it is important to invest in local directors and management. Additionally, it is important to develop a strong relationship with this team, as they play a key role in understanding the subtleties and nuances of the local marketplace.

Adopting a “copy-paste” approach – where a foreign company attempts to replicate its home strategy in Africa – does not always work, stressed Mr Mwaniki. Local management is usually more effective than using expatriates, as locals better understand the market dynamics and cultural nuances, which is very important to build local networks.

While building local teams is crucial, the shortage of required skills may be challenging at first. Certain skills can increasingly be accessed in local labour markets, yet it remains important for companies to invest in shaping these skills to meet their specific requirements. This also enables companies to integrate themselves into their host communities, illustrating a commitment to socioeconomic development as opposed to pure profit-seeking.

While there is no single recipe for success in Africa, investing in market research, local teams and skills development as well as adopting flexible business strategies increases the likelihood for success especially in the uncertain times ahead.

Panel Discussion: Investment Trends and Private Equity Opportunities in Africa

Private equity (PE) is increasingly playing an important role in economic and social development on the African continent. While PE activity in the last few years has been growing, the question is whether this upward trend can be sustained in the near future.

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Mike Whitfield, Managing Director, Nissan Africa Group
Joshua Mwaniki, Country Director, Andela
Victor Williams, Head, CIB, Rest of Africa, Standard Bank Group
Heinie Werth, Financial Director, Sanlam Group
Moderated by Alisheia Seckam, Business News Anchor, BusinessDayTV

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Mr Ntoi voiced concern that African PE funds may not be able to allocate as much capital to private equity when compared with their international counterparts. This may lead to crowding out of African players.

For both African and non-African PE investors, the relatively small size and low liquidity of local stock markets remains a challenge for executing a swift and profitable exit. The success of exit might also be compromised by the current economic uncertainties and the volatile currency markets.

Despite these possible challenges, Mr Fischer highlighted the importance of building companies that will contribute to social and economic development in the region. In fact, the exit strategy often depends heavily on what value PE investors can add to these companies. By ensuring high standards of governance, environmental and regulatory compliance in a company, the exit process tends to be much smoother and the value of the company higher.

While the PE market is expected to remain a challenging space in 2017, attractive opportunities persist in Africa. From a sector perspective, non-banking financial services, health care, infrastructure and consumer goods have been highlighted as attractive sectors for PE.

Given its robust growth and low dependency on commodities, East Africa has been singled out as the region with the highest potential for PE investors, and growth in value-added industry has attracted much attention from PE investors recently.

In order to succeed, PE investors have to have the right strategies in place to ensure the creation of value in the companies they invest in.

Michael Fischer, Director Regional Office: Southern Africa, KPMG
Fredre Meiring, Partner, Corporate Finance Leader: Africa, Deloitte Africa
Moderated by Alisheia Seckam, Business News Anchor, BusinessDayTV

David Cooke, Partner, Actis
Vuyo Ntsi, Investment Director: Head of Southern & Central Africa, African Infrastructure Investment Managers (AIIM)

Panel Discussion: Investment Trends and Private Equity Opportunities in Africa

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Panel Discussion: Africa’s Repricing after the Commodity Boom

Weak global demand for raw materials triggered a rapid decline in economic activities and decelerated economic growth in SSA from 3.4% in 2015 to 1.6% in 2016.

Lower commodity prices have been a key driver of Africa’s slower growth trajectory, given the (often single) resource-dependence of a number of economies in the region. It is in this regard that economies have to have a strategy for when challenges, such as weakening commodity prices, arise in order to lower the negative impact this may have on economic performance.

Oil is the most important commodity in Africa. Nigeria produces about US$36bn a year from its oil sector accounting for more than 90% of its export earnings. When oil prices declined in the second half of 2014, Nigeria’s foreign exchange reserves fell by 50% and within one year pushed Nigeria into recession.

However, investors base investment decisions on policy first, then infrastructure and only thereafter commodity prices, argued Mr Major. Governments that had initiated positive policy changes such as Chile in Latin America drastically increased mining production. Despite an increase in gold prices, South Africa, which has not seen policy changes since 1994, has seen a decline in production.

Mr Sturgess echoed that policies stimulate production. Issues surrounding the agriculture sector such as food security and production all goes back to implementing the correct policies which will allow for free trade and production stimulation.

While investors might be able to tolerate corruption to some extent, they cannot tolerate a loss of time. Time is needed when there are adjustments in policy or structural changes – time that investors do not have or want to lose. The internal rate of return (IRR) is even more so affected by time, rather than by policy, explained Mr de Vries.

Potential growth for soft commodities could centre on policy, infrastructure and the cost of production. Experienced management can also be a driver for potential growth as they possess a lot of skills and insight on how these markets have grown and how policy impacts on them.

Governments are starting to realise that there is a need for incentives and for reviewing regulations, especially in the mining sector. The problem is whether or not this realisation will find its way into policy.

In conclusion, governments need to balance policy and politics in order to stimulate growth and improve sectors that have the potential to contribute to economic growth and job creation.

According to Dr Moyo, most African countries struggle to align the various interests in their countries due to the lack of a common vision and identity. This makes it more difficult for countries to effectively tackle their specific challenges at a national level.

There are many structural challenges that countries need to address. These centre on institutional assessment, monetary assessment and issues such as economics, fiscal balances, debt and budgets. In order to evaluate the prospects for 2017, existing challenges have to be overlaid with new challenges such as political risks and other risks that might materialise over the course of the year.

According to Mr Dutiro, as Africa is very commodity dependent, the topic of diversification is only discussed at the weakest point, which is when commodity prices drop or are at their lowest. However, commodity dependent economies should think of diversification at the start of commodity cycles, not at the end.

Given the risks linked to the overreliance on resources, the focus in Africa should be shifted towards creating ideas-driven economies. Economies that have achieved rapid and sustained growth in recent years – such as China - are often resource poor and have largely relied on industrialisation and innovation.

Interactive Dialogue: Looking Ahead - What is in store for Africa in 2017?

Some of the factors that are likely to shape the continent’s future include the industrial capacity developed in Africa and the infrastructure that is needed in order to be able to produce and deliver products and services to consumers.

Slow diversification of economies will have an impact on countries’ ratings in 2017 and might therefore undermine the growth outlook of these economies, stressed Mr Reuss. In addition, the subdued GDP growth outlook and weak fiscal performance in sectors such as mining and agriculture, the impact of the uncertain global policy frameworks, as well as pressure on the fiscal position of countries emanating from state-owned enterprises weigh down on the ratings outlook.

As state-owned assets are often the cause of slow development in Africa, privatisation programmes will provide opportunity for more competent private-owned companies to drive countries’ economies which in turn will advance development efficiently.

Mr Ntuli noted that governments that are truly interested in development, should not be wavered by commodity prices. Instead governments should look at creating partnerships with global investors in areas such as telecoms, logistics and power, shifting away from a dependence on resources and being more innovative in different industries to drive and diversify the economy. This will ensure a more positive growth outlook for the continent.

Some of the factors that are likely to shape the continent’s future include the industrial capacity developed in Africa and the infrastructure that is needed in order to be able to produce and deliver products and services to consumers.
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