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Innovation as a New Driver of Growth in Africa

Summary of discussions:

Deloitte breakfast at the
World Economic Forum on Africa
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Sparking ideas for growth

Many African states require structural change for significant economic improvement. The impact of structural change is however only felt in the long term, taking up to a generation in order to see a turnaround, as was the case with Asia's development model. With complex socioeconomic challenges across the continent, questions about how long it will take African economies to structurally change and whether the required change can be fast-tracked through innovation were raised at the Deloitte breakfast during the World Economic Forum on Africa in Kigali earlier this year.

Thinking to transform a continent

> "Africa's future is dependent on minds and not on mines."

Looking at the resource sector, currently an investment in a commodity is in most cases an investment in an asset with a continuously dwindling rate of return. Conversely, an investment in innovation has the potential to yield a sustainable and ultimately scalable rate of return. Investing in innovation is an absolute and fundamental shift in the continent's traditional business model.

Besides structural change, another major issue for African economies is non-inclusive growth. Resource-driven African states continue to fail to equally redistribute returns from resources across their societies even in times of high commodity prices. Given the poor historical trend of resource returns supporting structural change, innovation provides a far greater opportunity to drive more inclusive growth than the traditional resource-based business models. In this regard, a memorable quote from the Economist magazine states that, "Africa's future is dependent on minds and not on mines". This statement means that capital is arguably more scalable through innovation than commodities. However, the question whether innovation is really suited to the developmental environmet and economic structure of African economies, remains.

A major contribution to structural imbalances on the continent is not just overdependence on commodities but also the major imbalances between the formal and informal economy. For example, the informal economy in Nigeria is estimated to be as large as 75% of the formal economy. This is almost as big as South Africa's GDP. If large informal sectors across the continent could be formalised through innovations such as electronic payments, the derived positive economic externalities from this could to some extent insulate the negative impact of volatile commodity prices on African countries.

While the continent may not have large innovation hubs like Silicon Valley, innovation is critical for economic development, and African public institutions need to play a greater role. Compared to Singapore and Korea and other emerging economies heavily investing in R&D at state level, African states are still not doing enough. R&D investment at state level remains insufficient and besides direct investment into R&D most African states still have a long way to go in developing the core infrastructure needed to stimulate innovation at a globally competitive level. In the context of innovation driving inclusion, the private sector is playing a major role. For instance in the financial sector, innovation in the Information Technology (IT) sector in recent years has enabled a large proportion of previously financially excluded people across the continent to join the formal financial sector.

Although agreeing with the importance of innovation for greater financial inclusion, companies such as those with a traditional insurance distribution model have limited their client base to employed and higher-income consumers. Consequently, to scale up distribution of their services and capture a wider client base, some companies are looking to partner with Telco's and Fintech companies, that can develop innovative, and also pragmatic digital insurance service solutions in the African markets context.

In the healthcare sector, the majority of Africans still do not have access to basic health services. However, this is changing and basic healthcare is improving with increasing mobility enabled by innovations in the telecommunications and transport space. For example, with innovations in mobile technology, people in need of medical care in remote areas can use a mobile device to send a distress signal. Soon enough in response to such distress signals, unmanned drones delivering medical supplies at lower costs than currently imagined, could become the norm.

Yet, as much as innovation is important, there needs to be more focus on the final outcome of innovative solutions. Innovations should be focused on large scale outcomes for faster structural change. For instance, as of 2013, non-communicable diseases killed more people in Africa than HIV but there is still minimal focus across most of the continent on innovations to mitigate the growing challenge. Non-communicable diseases will become a serious health challenge in Africa as most healthcare facilities on the continent are ill-equipped to deal with them and the end result could be further pressure on already constrained government budgets. For example, a technology, company has developed solutions that can provide early diagnosis and help mitigate the wide-scale impact of non-communicable diseases, but beyond the technology, countries also need to invest in the skills needed to implement these solutions effectively.

To add on to focusing on the final outcome, comparing healthcare services in African countries to those in India, business model innovation is needed to provide more cost-effective solutions to African consumers on a wider scale. The private healthcare sector in India has solved the healthcare for the masses cost equation and through innovating their business models expensive medical procedures in India are available at a fraction of the amount that consumers pay in Africa.

A view that often comes up when observing innovation trends in Africa, is that it seems more concentrated in some regions than others. However, across the continent Africans are faced with numerous challenges and tend to come up with informal innovations to address their challenges. The question is not necessarily a lack of innovation in some regions but rather how to formally capture and protect African innovations.

The challenges being dealt with on the continent are at times very basic and when they are formally solved, the solution can be applied in many contexts across the world. A good example is how M-Pesa and similar innovations are enabling ecommerce across the continent today. About 15 years ago ecommerce in Africa was a near unthinkable idea because internet payments traditionally needed credit cards and not enough consumers across the continent owned these.

Besides developing new technology, in many cases innovative solutions that can solve numerous challenges in Africa and the funding required to implement these solutions already exist but government policy, often not up to date with current and fast-changing technology trends, sometimes hinders their implementation. Furthermore getting different African states to act in unison in terms of policy is difficult. African governments need to be encouraged to abandon traditional policies to better enable economic development through innovation.

Another important part of the African innovation puzzle is Africa's growing unemployed youth population and the coinciding skills shortage. Substantive discussions on innovation on the continent therefore need to momentously involve the youth. Innovation has multiplier effects and can open up new opportunities for entrepreneurs and create new jobs for the continent's growing youth populations. However innovation needs to be accompanied by relevant skills development to enhance the impact it has on economic growth.

With a more cautious view about innovation driven growth in Africa, decision-makers should not get too ahead of themselves as impactful innovation requires some fundamental factors to be in place. Indeed, there are many examples of innovative solutions to African

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challenges including those mentioned here but most of these only have an impact on a microscale. Their dollar value impact on GDP in Africa as a whole is quite insignificant. They are small money investments with good returns but have a negligible macroscale impact. Big money investments in infrastructure projects including transport, water, and electricity among others are still the most critical for the type of structural change currently needed across the continent, ultimately unlocking the potential to innovate.

Innovation is undeniably an important component of economic development but has to be supplemented with enabling policies, relevant skills, and core infrastructure. On a broader scale, innovation should include local content and an element of public-private partnerships. In addition, the private sector needs to play a focused and sustained role in developing the accompanying factors needed for more impactful innovation.

All things considered, innovation has the ability to shorten the length of time needed for structural change across the continent and should be an extensive part of Africa's development strategy for inclusive and sustainable growth.

This article is based on the discussions at a thought leadership breakfast hosted by Deloitte at the World Economic Forum, Kigali, Rwanda in May 2016. The discussion was facilitated by Dr Martyn Davies, Managing Director: Emerging Markets & Africa, Frontier Advisory Deloitte and included the following experts:

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The views expressed in this document are those of the speakers and panelists and do not necessarily reflect the views of Deloitte, the World Economic Forum or its Partners and Members. The purpose of this report is to elicit comments and encourage further debate.

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