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Private Equity: An Eye for Investment under African Skies?

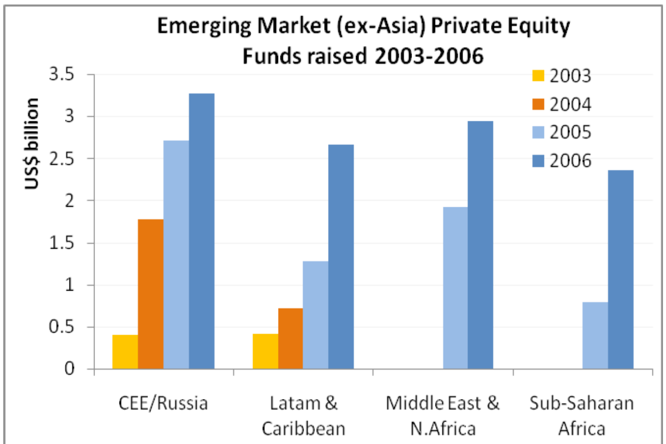
(based on the *African Economic Outlook 2008**)

by Thomas Dickinson

- Private equity is the African investment story to watch.
- African countries have made serious efforts to attract foreign investment.
- Global downturn may yet put successes at risk.

Private equity is not a new phenomenon in Africa but it is drawing increasing attention as a nimble and innovative vehicle for private-sector development on the continent. Improvements in African investment environments and a series of spectacular African business successes (such as the private-equity backed African telecommunications pioneer Celtel's USD3.4 billion buyout in 2006) have fuelled an unprecedented boom in the size and breadth of African private equity funds.

A huge increase in mergers and acquisitions (M&A) in 2006, notably in African banking and telecoms, brought high exposure to the dynamism of the continent's private sector and boosted investment to record figures: foreign direct investment flows reached USD 36 billion in 2006, twice their level of 2004[1].



Source: EMEA, 2007.

Private Equity from Emerging Markets

The sharp increase in private-equity investment from global emerging markets was mirrored in sub-Saharan Africa, which saw funds raised shoot up nearly 200 per cent[2] in 2006, to USD 2.3 billion. This brought sub-Saharan Africa's share of emerging market private equity funds to 7 per cent, which although well behind Asia (58 per cent), held up well compared to other emerging regions (Latin America: 8 per cent; Middle East/North Africa: 8 per cent; CEE/Russia: 10 per cent). Funds focusing on North Africa/Middle East grew by 50 per cent over the period.

1. Source: UNCTAD (2007) World Investment Report, Geneva and UNCTAD (2007) Global Investment Propects Assessment 2007-2009, Geneva.
2. African Venture Capital Association, South African Venture Capital Association, 2007

African funds, while still small by international standards, have been rapidly increasing in both size and reach: Pamodzi, a South African private-equity firm, launched the continent's largest, USD1.3 billion, pan-African fund in 2007. International financial institutions have also developed their own vehicles: Citigroup launched a USD200 million fund early that same year.

South Africa

The South African private-equity industry, mirroring the country's financial predominance, is the largest on the continent, at 1.7 per cent of GDP — a figure comparable to that of many developed markets (Europe: 1.5 per cent; UK: 3.7 per cent; North America: 2.8 per cent)[3] , and 17th in the world in terms of investment activity (2005). South Africa saw a 409 per cent increase in managed funds in 2006, to 11.2 billion rand (USD1.6 billion). South African funds manage over 80 per cent of total SSA private-equity capital, followed by Nigeria with 10 per cent.

3. Funds under management at 12/2006 for South Africa, 12/2005 for Europe/USA.

Channel for Investment

Developed economies, particularly the United States, remain the major source of capital, accounting for 50 per cent of total funds raised for African investment in 2006 (Europe 9 per cent). A quarter of the funds raised for the continent are South African, continuing a trend of growing local sourcing of capital. For the first time, a third of the capital raised in South Africa was also sourced through foreign pension and endowment funds, revealing institutional investors' growing appetite for, and confidence in, African assets.

Public funds, particularly from European development finance institutions are also important sources of capital. Seeking to foster private-sector activity, these government-backed agencies have historically been important guarantors of private investment funds on the continent. Representative of this field is France's Proparco, Dutch FMO and Britain's CDC (formerly Colonial Development Corporation), with USD845 million commited in Africa since 2004 through twelve African fund managers.

Openness to Foreign Investment

Over recent years, African governments have made serious progress in adopting market-friendly policies, improving investment environments and taking energetic steps to stimulate foreign involvement. New measures promoting foreign investment were introduced by 40 African countries in 2006. Foreign participation in the telecoms industry was allowed in Botswana, Burkina Faso, Burundi, Cape Verde, Ghana and Namibia. Important reforms of the banking sector took place in Congo, Egypt and Nigeria. Morocco legalised foreign ownership of large tracts of land. Several countries eased registration and taxation constraints on new businesses and established special investment zones.

A Source of Diversified Financing

The global boom of recent years pushed demand for African assets to new heights. Low correlations with global markets, high liquidity and the commodities boom all fuelled investment, but also contributed to pushing non-primary sector opportunities into the background.

Private equity, on the other hand, has tended to work against the grain of international investment, focusing its attentions on consumer-related and communications sectors[4]. Such investments have an arguably stronger impact on Africans' daily lives than the largest of extractive mega-projects, and bring private equity to stand out as a dynamic and diversified counterpoint to classic sources of foreign investment in Africa.

4. African Venture Capital Association, South African Venture Capital Association, 2007.

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