# The beef with Africa

BY BRUCE WHITFIELD

"Africa is full of opportunities, but also rife with bribery, bureaucracy – like import-control regulations that are different everywhere – and logistical problems like frightfully expensive fuel, a lack of tarred roads, and ports where activity can be frozen for up to six weeks so your cargo can't be offloaded. It's all quite terrifying until you've mastered it, built your network and have managed to construct your warehouses and to understand the workings of informal markets. Meanwhile you have to stay in the most expensive hotels in the world and you have to know how to deal with a mountain of cash in countries with underdeveloped banking systems," PSG Founder Jannie Mouton tells author Carié Maas in his 2011 biography *And then they fired me.*

**You would be hard pressed to find a CEO of a top 200 company in South Africa not at least paying lip service to an "Africa strategy". Jannie Mouton's words, however, ring true. Investment in some of the fastest growing markets on the African continent comes with a severe health warning. African investments tend to make up such a small portion of an average company's capital outlay as managers tentatively assess not only their own risk appetite but also just how long it will take to deliver sustainable returns to shareholders.**

The theme is gathering momentum, but not necessarily because it's the next sure thing in terms of investment returns. The story cannot be seen in isolation.

Appetite for the Africa investment theme comes against the backdrop of soggy global growth as many Western economies teeter on the brink of another recession. By contrast, emerging market growth is appealing, and African growth rates, from their current low base, are enough to tempt even the most ardent Afro-sceptic.

Is it best to have been an early mover whose persistence will be rewarded by market dominance over time or is it more sensible to let others make the early mistakes? The market is firmly polarised between early movers who have established their operations and are paying stiff school fees and those who are content to learn from other's mistakes along the way.

"Anyone embarking on an Africa strategy now has left it too late," says Grant Pattisson, CEO of Massmart. The world's biggest retailer Walmart acquired a controlling stake in Massmart earlier this year as part of its own global strategy of investing in regional champions to further its own international footprint. "Walmart has the advantage that we already have a strong presence in many African markets, which would have taken them a long time to set up themselves."

But according to a recent report from Accenture, it's not too late to start on an Africa expansion drive. The consultancy group however cautions investors against being overzealous with their profit forecasts.

Turning opportunity into profit, warns Grant Hatch, senior executive: strat-egy at Accenture South Africa, invariably takes much longer than companies' own often overly optimistic forecasts suggest. Hatch argues strongly for investment into the potentially lucrative sub-Saharan region, which has experienced rapid growth in consumer spending over the past decade. That, accompanied with rapid improvements in income levels, infrastructure and a business environment that's increasingly benefiting from a growing consumer market, make the continent a tempting investment destination.

Investec Asset Management Africa specialist Roelof Horne argues South African companies that are failing to invest "in spite of this high-growth, high-margin opportunity on their doorstep" will regret it later.

Horne questions the motivation of executives who focus their attention on highly competitive, low margin "nice to visit" countries and says corporate leaders do need to be more adventurous in their approach.

In a recent report, *The Dynamic African Consumer Market*, Accenture concluded sub-Saharan Africa has a rapidly growing consumer population that will reach 1.3bn by 2030.

Also:

- Average growth rates in sub-Saharan Africa will be between 5%-6% up to 2020 whereas most developed markets will struggle to achieve 2%-3%.
- Consumer expenditure in 2010 equalled \$600bn – estimated to reach \$1tr by 2020.
- Poverty rates are declining rapidly – from 40% in 1980 to 30% in 2008 and 20% in 2020.
- By 2050 an estimated 60% of the region's people will be urbanised.
- By 2012, 50% of all Africans, more than 500m people, will own a cellphone, growing to 56% by 2014.

"The data around Africa demographics and the opportunities available are very sexy," says one fund manager. "They can get you so excited that once you have finished reading them you do feel the need to take a shower afterwards."

Demographic arguments are compelling.

The Department of Economic and Social Affairs at the UNDP says Africa's population growth will outpace that of other developing markets such as India and China by 2030.

Its project-ions suggest Africa will have a population nearly 50% bigger than it was in 2010 with 1.5bn people, surpassing the numbers of people in each of the globe's two most populous nations.

The World Bank believes growth rates on the African continent are rising while those in India and China cannot be sustained at the high rates achieved in the first decade of this cen-

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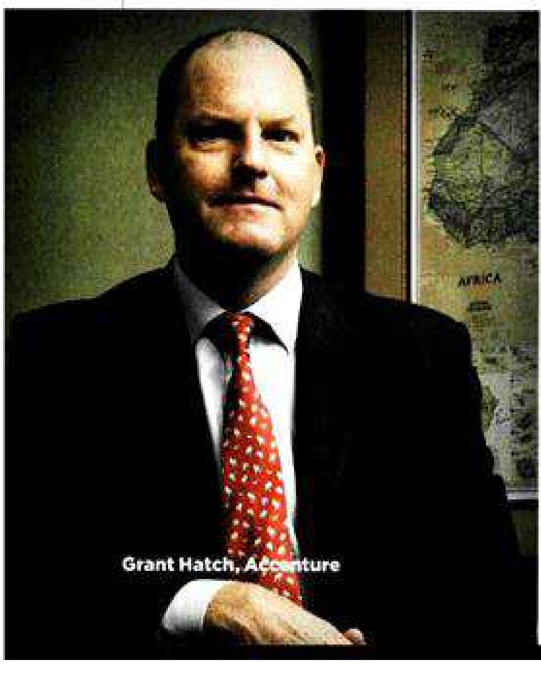
tury. African inflation rates have, on average, been contained to single digits and government borrowing as a percentage of GDP has declined from the mid-sixties 10 years ago to average levels below 30%.

The consensus growth forecast for the African continent puts countries like Angola, Uganda and Ethiopia north of 7% - more than twice the expectation for the South African economy.

Investment, however, is not about demographics. Averages are dangerous and making bald statements about prospects for a continent that in pre-colonial times was made up of an estimated 1 000 states, is downright dangerous. There are huge differences in the histories, cultures and demographics of the 47 countries that now make up mainland Africa.

"There's a window of opportunity open at the moment. Plenty of businesses are being set up. The big question for anyone going into the continent is the amount of time it takes between establishing a presence and delivering a profit," says Hatch. "The advantage the early movers have is that in many cases they are able to make the market."

A shortage of reliable data means that it's very difficult to do a desk-top analysis of many African countries. "South Africa has masses of data and you can sit anywhere in the world and can make a fairly accurate assessment of risks and opportunities in the market. The problem is that lots of companies do not do enough on-the-ground research," says Hatch.


Grant Hatch, Accenture

Certainly, Tiger Brands' CEO Peter Matlare is famed for encouraging his board to walk the streets and markets of countries into which the South African food producer wanted to invest.

Tiger Brands has been acquisitive during 2011 and others like MTN and SABMiller are among the more notable long-term success stories and continue to pour billions in investments into existing and newer operations.

"Other than MTN and SABMiller, Shoprite has been by far the most successful South African investor outside its home market on the African continent. It has been persistent, understanding the individual markets in which it operates and as a result makes good money in its operations," says Peter Leger at Coronation Fund Managers. "The implementation risk for new entrants is high. It's not too late to embark on an Africa strategy but if you're a food retailer looking to take on Shoprite in tough markets like Lagos, Kinshasa or Luanda, you need to be aware that returns will not come overnight."

For most South African companies invested on the African continent, the strong rand in recent years has led to earnings pressure when profits have been converted into local currency. MTN is probably South Africa's most geographically diverse company with operations in nearly 20 of the continent's most prominent economies. The strength of the rand until about June this year wiped R4.7bn off MTN's top line.

Growth instead was driven by gains in South Africa and Iran while several of its more promising African investments underperformed. Key operations tended to perform well in local currency: Nigeria up 13.1% and Ghana 11.9%, for example. Translated to rand, however, Nigeria, which is facing increasing competition was flat and in Ghana where the company has more than 50% market share, its profit contribution declined. More than two thirds of MTN's revenues are now generated outside South Africa, and CEO Sifiso Dabengwa described the group's results as being "damned" by the strong reporting currency.

For Telkom, hardly a stellar performer at home, its operations outside South Africa have been a disaster zone. The group remains keen to invest in other African markets despite the failure of its Nigerian business Multi-Links. Chairman Lazarus Zim can hardly be accused of overstating the issue, describing the lessons learned from the R7bn losses incurred in Nigeria as "expensive and important". Telkom failed on two fronts – it bought into a business using one kind of technology, CDMA, while the rest of the market used GSM. Arguably its failings were managerial rather than as a result of a difficult or hostile environment in Nigeria.

Tiger Brands has recently been raising its cross-border exposure on the continent. Until recently it had a physical presence in eight African countries and has created hubs in both East (Ethiopia and Kenya) and West Africa (Nigeria and Cameroon). It also has export markets all the way from South Africa as far north as Sudan. Its R1.35bn February acquisition of unlisted beverage maker Davita Trading gave it a presence in 28 African and Middle Eastern countries, with a particularly strong expansion in West Africa. Late last year it bought 49% of the food business of a domestic entity called UAC in Nigeria for R417m and spent a further R275.8m on unlisted biscuit maker Deli Foods Nigeria, while entering into a joint venture with Ethiopia's East African Group into which it invested nearly R113m.

According to Euromonitor, the top 50 packaged food companies in Africa and the Middle East increased market share from 25% to 34%. But that growth has come at a price. Nestlé and Unilever, leading companies on

Source: Riscura

## Not for the faint-hearted

Riscura is the only consulting company that produces a survey of Pan Africa ex-South Africa funds. The products in its survey represent those funds that invest in companies that are either listed on African markets or that generate more than 50% of their revenues on the continent. The funds exclude exposure to South Africa.

The table below uses data from the Riscview Pan Africa ex-SA Survey - September 2011. Performance is in US dollars and is net of fees.

| Product | Benchmark | Market Value (USD) | Sept 2011 | Qtr 3 2011 | 2011 (Jan to Sept) | 1 year | 3 years |
|---|---|---|---|---|---|---|---|
| Africa Sustainability Fund | MSCI EFM Africa ex SA Index | 19 | -8.56% | -16.33% | -22.39% | -18.04% | - |
| African Alliance Africa Pioneer Fund | MSCI EFM Africa ex SA Index | 24 | -8.70% | -16.98% | -22.31% | -16.70% | -11.83% |
| Coronation Africa Frontiers | 3M USD Libor + 5% | 148 | -7.45% | -16.57% | -18.89% | -13.19% | 8.17% |
| Investec Africa Fund 1 | 1M USD Libor + 4% | 638 | -9.42% | -21.19% | -26.80% | -18.10% | -10.03% |
| Momentum AM SICAV Africa Equity Fund | MSCI EFM Africa ex SA Index | 7 | -7.70% | -16.08% | -20.12% | -16.51% | -8.10% |
| Sanlam African Frontier Markets Fund | MSCI EFM Africa ex SA Index | 31 | -8.14% | -20.17% | -28.07% | -24.10% | - |
| Standard Africa Equity Fund | All Africa Top 100 (excl. SA) | 74 | -9.74% | -23.27% | -30.01% | -22.79% | -21.83% |
| STANLIB Africa Equity Fund | All Africa Top 100 (excl. SA) | 62 | -9.75% | -23.54% | -31.67% | -24.86% | - |
| **Benchmarks** | | | | | | | |
| USD Libor + 4% (one month) | | | 0.35% | 1.04% | 3.20% | 4.31% | 4.59% |
| USD Libor + 5% (three months) | | | 0.45% | 0.45% | 4.04% | 5.42% | 5.76% |
| All Africa Top 100 (excl SA) | | | -10.43% | -10.43% | -28.49% | -24.54% | -20.86% |
| MSCI EFM Africa ex SA | | | -8.43% | -8.43% | -30.04% | -25.55% | -17.93% |

the African continent, are sacrificing margin for growth as their customers simply cannot afford the prices of products, which have been developed for wealthier consumers. Despite its status as Africa's second biggest economy, research by Tiger Brands puts average annual disposable income per capita in Nigeria at R3 100 versus South Africa's R16 200. Multinationals therefore focus on volume growth over margin expansion.

In a recent presentation, Tiger Brands highlighted some of the difficulties it faces in doing business in several of the new African markets which it has entered. Among those problems are an abscence or slow evolution of democratic institutions, currency instability, lack of infrastructure, acute local skills shortages, corruption, counterfeiting, low disposable income levels and demand constraints in countries where access to credit remains a big problem.

Standard Bank, which is regularly named as "top bank in Africa", has been investing heavily in its network across the 16 African countries in which it operates outside South Africa. "The strategy we are executing right now goes back to the Eighties", says Standard Bank Deputy CEO Sim Tshabalala. That work was done by then chairman Conrad Strauss and ex-CEO Eddie Theron. "We are not discovering the opportunities in Africa for the first time." This is a big issue for Standard Bank, which announced this year that it would be stepping back from its ambitious global strategy that saw it buy stakes in banks as far afield as Argentina and Russia – but is undoing all of that now and intends channelling its energy into doing most of its business on the continent. It has the additional pressure of course of having the world's biggest bank, China's ICBC as a 20% shareholder. It will be wanting to ratchet up its own strategy of taking a stake in a business it plans to use as a conduit into other parts of Africa.

FirstRand has taken its Africa growth strategy back to the drawing board following a decision by the new Zambian government to overturn its acquisition of that country's Finance Bank. Earlier this year, it walked away from a pricey deal in Nigeria, concerned that the asking price was too high relative to the quality of asset it was seeking to acquire.

"There's a risk of overpaying for assets," says Coronation's Leger. "Arguably Standard Bank did that in Nigeria."

Shoprite made its first Africa foray in 1990 when it opened its first store in Windhoek, Pick n Pay instead chose to enter Australia twice and has now put the continent as one of its key future building blocks. Spar, which operates six distribution centres in South Africa serving a network of independent retailers across the country, is looking to Nigeria as its first port of call outside South Africa.

Clothing retailers are also increasingly interested in the opportunities the continent can provide. Woolworths earlier this year stated its interest but said it would not be pursuing its highly successful South African foods model in a continent where it can take three months to receive product. Mr Price, which has nearly 50 stores predom-

# Vulture funds circle

## Secretive groups are claiming $1.5bn from Africa

**The African continent is not only the target of long-term investors in infrastructure, retail and banking. The UK government is being urged to shut a legal loophole that allows purchasers of debt from war-ridden countries to claim many multiples of the value of that debt from the world's poorest countries.**

Exactly how many of these so-called "vulture funds" are in operation and the extent of their claims are unknown, but NGOs, including Oxfam, the Jubilee Debt Campaign and Christian Aid maintain one of these funds is on the cusp of claiming $100m from the DRC on an original debt of $3.3m. The IMF has estimated that vulture funds have claims as high as $1.5bn against some of the world's poorest countries.

The DRC debt was originally owed to the former Yugoslav government for a powerline project. The Bosnian government now maintains the debt was sold illegally and argues financier Peter Grossman, who runs FG Hemisphere, has no legal right to it. Grossman, who has previously failed to seize the DRC embassy in Washington DC as part payment for the debt, insists he is doing nothing wrong. As far as he is concerned he is the legal holder of the debt and is entitled to demand payment.

The secretive nature of the industry lends itself to conspiracy theories. Vulture funds take considerable risk. They buy debt cheaply when countries are in chaos and are at risk of default. They wait until the state in question stabilises – until aid and investment recovers – before seeking to cash in on what is owed to them.

Among some of the industry's more colourful and public faces is Michael Sheehan, a lawyer who likes to be known as Goldfinger. Sheehan has worked in both Kinshasa and in the US. He runs Donegal International, which owns a $15m Zambian debt instrument dating back to 1979. Sheehan bought the debt from Romania for $3m in 1999. Formerly a lawyer to a debt relief NGO, he has now turned to collections to make his living. Grossman, also a lawyer, was a consultant to Morgan Stanley before founding FG Hemisphere as an advisory firm for investors into developed markets. Paul Singer is best known for buying $20m of Peruvian debt and successfully suing for $58m. Singer has also managed to claim $39m of DRC oil sales for payment on a $30m DRC debt.

The NGOs claim that the demands from the funds are many times higher than the original debts and put considerable financial pressure on already heavily burdened economies. As a purely capitalist principle, it makes complete sense, but does it make sense then to be pouring billions in aid and investment in the front door when the money is destined to leave out the back just as quickly to pay off legacy debts?

The IMF and the World Bank warn several African countries are facing demands from vulture funds. Among them: Cameroon, Ethiopia, Sudan and Uganda. According to the World Bank, more than a third of the countries that have qualified for debt relief programmes face legal action from more than 20 vulture funds. As the countries try to rebuild themselves, in some cases after decades of civil war and political unrest, they find themselves facing substantial financial demands. While many developed countries have banned the vulture funds from using their courts to claim the funds – there is a loophole that the financiers use in tax havens such as the British Virgin Islands and Jersey,which permits such claims. The British government is expected to implement new regulations next month that will prevent it occurring in future. ■

inantly in Kenya, Ghana, Zambia and Tanzania plans to open its first Nigerian store in Lagos in March next year.

The investment by South African companies into other parts of Africa has made them attractive in turn to bigger global investors. Walmart this year concluded its takeover of Massmart, following the 2010 acquisition by Vodafone of 75% of Vodacom, despite the fact that it is a minnow in the African ICT space relative to MTN. Standard Chartered, which already has African operations, left Nedbank standing at the altar in 2010 in a deal that looked similar to that done by China's ICBC, which took a 20% stake in Standard Bank in 2008. Barclays bought control of Absa in 2005 but it was only this year that it made Maria Ramos, the CEO of the local group, head of its Africa operations. She has formed a committee to look at growth opportunities. Judging, however, by the recent experience of FNB in Zambia where it had its acquisition of Finance Bank overturned by the new government, which cited its unhappiness over the purchase process and the fact that in recent years banks have decided against pricey acquisitions, growth for financial sector players is likely to remain muted. But with merger and acquisition activity under pressure elsewhere – investment banks in particular are trawling the continent looking for business. And many countries on the continent – more stable politically and economically now than at any point in the past 30 years – are opening up for business.

SABMiller has brewing and beverage operations across 16 countries in sub-Saharan Africa, while a further 19 economies are covered via its strategic alliance by the family-owned French brewing group Castel. It has dominant market share in most of the countries in which it operates and bottles Coca Cola-company products in 20 of those markets as well. Like Standard Bank, its involvement in other parts of the continent has not occurred overnight. Its first investment in a neighbouring state was in the then Rhodesia in 1910 with the formation of Rhodesia Breweries, which in turn expanded its own sphere of influence into Zambia in the Fifties, but the rate of expansion became accentuated from the early Seventies when the company expanded into Botswana and Angola. Earlier this month the group said it was making $260m available for investment in Uganda, Ghana, Zambia and Tanzania as its volumes on the continent outside a more mature South African market soared 15%. The fresh cash injection is in addition to some $1.5bn invested in projects across the continent over the past five years. The group's Africa operations outside South Africa have seen a steady increase in production in recent years and its contribution to EBITA has grown to 13% of group earnings and is still growing. The region contributes almost as much for its parent as the US operations do – the difference being that the contribution from Africa is growing while the Miller Coors joint venture in North America continues to struggle in that massively competitive market.

"No company can afford to ignore the opportunities the region represents," says Accenture's Hatch. "The new African consumer is a force to contend with. Despite current low per capita incomes in Africa, average income is growing, giving rise to an emerging middle class that will become more demanding as income levels and spending increase."

Plenty of South African companies burned their fingers investing in other African economies in the Nineties. In many ways these were no different to the early forays into the US, Australia, and Asia where executives, corporate rockstars in their own environments, made blanket assumptions not only about their own goods and services but also the requirments of the markets they anticipated serving.

"Nowadays the approach is more subtle and partnerships are more likely than previously. The key is in finding the right model and how you apply that model from a South African perspective when we tend to have a very Anglo-Saxon style of conducting business," says Hatch. ■

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# How to do it

**So, you have a high risk appetite and are prepared to wait to harvest the returns corporate investors believe will follow as a result of their investment into new markets. The reality is that in order to invest into the Africa growth story, you probably are best off doing it yourself – building a portfolio of shares doing business across the continent. There simply are not the retail funds through which to do it.**

Unless you are a member of the Oppenheimer dynasty, which will have up to $5bn at its disposal for investment once the sale of its De Beers stake to Anglo American is concluded, you will have to consider the alternatives.

Beware – just because a fund manager sticks an "Africa" tag on to an investment product does not mean it is what you think it is.

There have been fund managers that have tried and failed to make non-South Africa retail funds available to private investors. Among them, the UK-based New Star Africa retail Africa fund which was forced to close when it ran into liquidity problems. There are funds that claim to be "African" but on closer inspection will have a high weighting to South Africa.

"There is very little retail opportunity for private investors who want to buy into frontier Africa. That is simply because most African markets don't have sufficient liquidity to allow private investors to be nimble," says Peter Leger, a portfolio manager at Coronation who focuses on investing in African companies. "If you try to change your mind about an investment too quickly it can be expensive. In Zimbabwe, for example, you have to pay brokerage fees to get in and out of a position plus an automatic capital gains charge whether you make or lose money – that process can cost you around 5% – plus there is no guarantee that you will match the price you paid. Changing your mind is expensive."

There are just 29 stock exchanges operating on the continent. Fewer than a third of those offer sufficient liquidity and trading activity to make them attractive to institutional investors. Mozambique has a fledgling stock market, but only one company listed on it, SABMiller. Rwanda has two stocks and Uganda has some, but limited liquidity. Outside of South Africa, Egypt is the most active but its liquidity since the Arab spring is down to between $30m and $60m a day. Morocco is active and Nigeria has fallen off dramatically from its peak of $100m/day.

Most daily traded Africa funds you see have up to 70% South Africa exposure, so you have to be careful about paying higher costs for a so-called Africa fund, where you're getting a mostly South African fund that tends to charge a lower fee given the size of the opportunity.

"The real risk when it comes to making investments on the African continent is that you do get caught up in the hype. The demographic argument is strong and there have been funds set up in the past aiming to capitalise on what looks like a no brainer. It's more complicated than that. As African economies outside South Africa better understand the role and the power of capital markets and take a longer-term view as to what their role is in the societies they serve, understanding this is a long-term game, so much the better, says Leger.

Courageous investors will be well rewarded," says Investec Asset Management's Roelof Horne, who believes that returns can be generated in a relatively short space of time if acquisitions are properly researched and executed.

If you do feel enticed to invest in South African companies for the Africa blue sky opportunity you think they might represent – go in with your eyes wide open. Just because you are a fan of Koo smooth peach jam does not mean the residents of Abuja or Addis Ababa will have the same brand affinity. Also never assume that South African companies are entering undertraded markets that are ripe for plucking. There are plenty of well-established, well-run local companies across the African continent. They tend to be unlisted, family controlled and many have connections to Greek, Italian or Lebanese expatriates.

The Accenture research suggests local operators understand the importance of the price point better than the multinationals, including those in South Africa, do. Often the quality may be inferior to what South African consumers are used to, but the product can be delivered at an acceptable level. Many foreign investors underestimate the power of established businesses in many markets.

Just because a product or a brand has resonance in South Africa does not mean that translates automatically in other markets. In countries where refrigeration is limited and wages are paid daily or weekly, shoppers prefer and trust markets more than they do foreign-owned chain stores. Markets provide pack sizes at price points they can afford. Trust is crucial. Early movers often have the advantage that their brands build up credibility and become established. Shoprite in many markets is a dominant player because it has become established over time, making its chairman Christo Wiese one of the continent's 10 richest people.

*Forbes* magazine, the American journal with a fixation for lists, has just issued its first African wealth rankings, listing the 40 richest people on the continent. The wealth of Africa's 10 richest individuals is centred on just six countries: Zimbabwe, Kenya, South Africa, Nigeria, Morocco and Egypt, where the wealth sits predominantly with two families, the Mansours and Sawiris.

The number one spot goes not to an Oppenheimer or a Rupert but to cement magnate Aliko Dangote, whose cement and other industrial interests mean he is worth about $10bn – 35% more than South Africa's diamond scion and considerably more than the luxury goods and cigarette entrepreneur. ■