Fifteen years
Fifteen lessons from Africa

Chapter 2: Market Lessons

IP INVESTISSEURS & PARTENAIRES

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2 *Market Lessons: (r)evolutions*

The last fifteen years have been characterized by profound changes in the sub-Saharan economy. According to the World Bank, sub-Saharan Africa's GDP has increased from $350 billion in 2000 to $1,500 billion in 2016, and the Gross National Income per capita from $485 to $1,500 over the same period. It has been accompanied by dramatic societal transformations (urbanization, the emergence of the middle class, etc.) and cultural and environmental changes (notably in the energy and agriculture sectors). These transformations are shaping new markets and are key determining factors of economic activity. They explain the deadlocks that some companies face, as well as the success of others, regardless of the quality of entrepreneurs.

I&P has experienced and followed developments that have directly impacted transformations the structure of our portfolio. three of them in particular stand out: Africa's shift from an imitation-based to an innovation-based economy; the crucial nature of the issue of nutrition and the strategic development of the agribusiness sector; and questions of market access issues through a reflection on marketing strategies and distribution patterns in the African context.

4 Lesson n°4 : The African economy: Moving from imitation to innovation

In the years 2000 to 2010, the entrepreneurial component of African growth was characterized mainly by the creation and development of companies in traditional sectors. African growth was seen as "catching up" with the industrial and service fabric of so-called advanced countries.

During this decade, the entrepreneurial fabric supported by I&P was characterized both by this perception and this reality: conventional service companies, including microfinance institutions, an under-representation of manufacturing and agribusiness, and a small share of firms engaged in technological innovation. Even the microfinance sector, which is more in which is more specific to poor countries than in industrial countries, could not be claimed as an African innovation. It is difficult to draw specific conclusions on the expected returns of these investments because even these traditional companies, often launched without competition at their onset, brought significant transformations to local economies. They generated significant productivity or quality of life gains for customers, leading to rapid growth in sales and earnings in a sketchy, difficult, and risky economic environment characterized by numerous operational obstacles. Expecting gross actuarial returns above 20%, however, seemed possible albeit difficult.

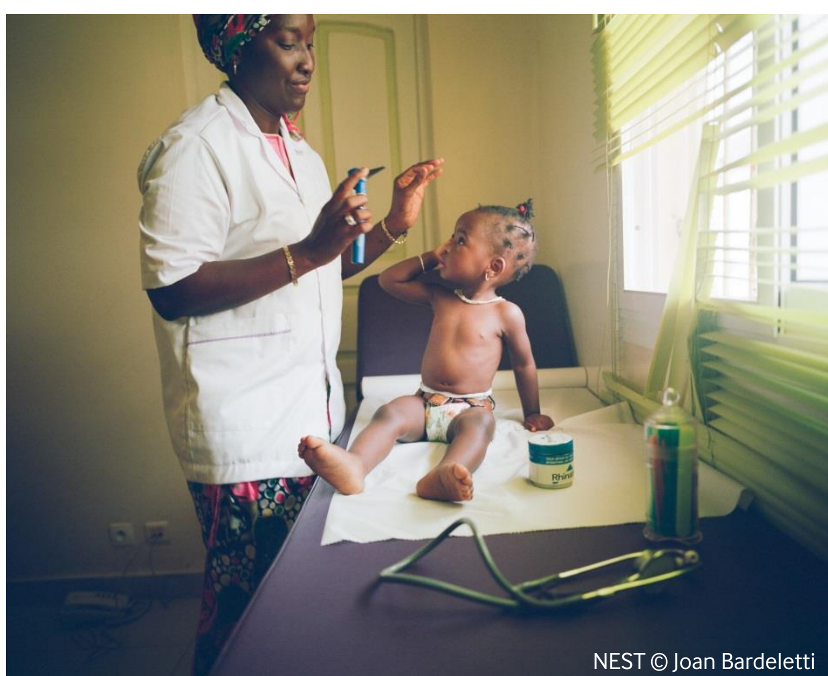
The last few years have seen this situation change in two distinct ways.

On the one hand, important technological innovations have emerged in the wake of information technology revolution. The widespread use of mobile telephony in itself has generated significant productivity gains and accelerated African growth. This phenomenon has been fueled not only by the major global telecom players (Orange, Vodafone, etc.) but also by African operators (MTN and many local and regional operators that have either been newly created or have emerged from the privatization of former public monopolies, as in Madagascar). As an extension of mobile telephony, "mobile money" appeared, constituting the first truly African technological revolution and radically changing life and business in Africa. New mobile money innovations are multiplying globally and in countless domains, creating unique services throughout the world and specifically adapted to the needs of Africans, the most spectacular of which is in the energy sector, with the creation of SHS or domestic "pay-as-you-go" solar kits.

> *"Mobile money" appeared, constituting the first truly African technological revolution*

Many African-owned or expatriate-led start-ups (often created in North America or by people of the African diaspora) are being born across the continent, particularly in East Africa, but also in West Africa, as evidenced by PEG Africa, a company that we invested in and aided when it was founded in Ghana and that now operates in several countries in the sub-region.

At the same time, without involving technological innovation, the social sectors are also attracting investment (above all the healthcare sector) by the African private sector at a heightened scale and pace unique to the African continent. This is also the case for essential services such as energy and water. Our investments in companies such as Enko (private education), Nest (network of care centers dedicated to mother and child in Dakar) and CDS (a Mauritanian company that promotes access to electricity and water in rural areas) perfectly illustrate this trend. We come back to this point, which is linked to the emergence of a middle class in Africa, is the lesson number 3.



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Africa's economic landscape is in the process of perpetual transformation, resulting in two major consequences for investors.

The first is the partial loss of historical benchmarks and the ability to replicate the experience gained in OECD countries. Until recently, support for enterprise development was perceived to be based on the transfer of technologies, methodologies and capabilities built in industrialized countries and sometimes "adapted" or "tropicalized" for the African context. The new dynamic involves figuring out how to support entrepreneurs who invent their model every day without reference to pre-existing models.

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The second is related to returns. The rapid growth of companies implementing new technologies is multiplied in the African case by the growth rate and the partial relief of physical constraints related to failing infrastructure. Some subsectors can thus generate two-digit gross return-on-investment (IRR) rates. Many new-technology companies also justify a "venture" approach and methodologies rather than "private equity," and many investors have developed a growing interest in this approach. Unlike most of the African SMEs and start-ups we have talked about, some areas, such as decentralized green energy, are heavily financed by international capital, especially from the United States. Nevertheless, all of these technological sectors are inherently risky and sometimes over-valued, as the African context is more difficult than that of OECD countries. Delusions arise and in some country/sector pairs, such as SHS in East Africa, there is reason to fear the appearance of market bubbles, with excessive valuations based on unrealistic assessments of the future performance of companies.

This is our fourth lesson from Africa. Africa's (rapid) evolution towards an innovation economy should not overshadow the basic precautions of capital investment in rudimentary, unstable and vulnerable economies. Nevertheless, a "venture" sector should be established to meet the needs of African technology and innovation companies, particularly in the energy and telecommunications sectors. Such venture capital could reasonably expect high returns, even with small investments, but at the cost of higher risks than in OECD countries. To better reduce these risks, a strong and deeply-rooted local presence seems essential, combined with an excellent knowledge of the technologies being used while investor should be prepared to support the rapid growth of these companies by engaging in numerous, ongoing and important financing rounds.