PRIVATE EQUITY AND VENTURE CAPITAL INVESTMENT CAN ALLEVIATE POVERTY IN AFRICA

Prior to working in investments, I naively thought that I could help Africa by working for the United Nations and, coming from a family of civil servants and politicians, it was the obvious choice to navigate towards the UN and “non-profit” world. However, I soon realised that the world of multilateralism and “non-profit” was more about the talk than the actual walk.

Disappointed, I pivoted my career and went into the corporate world. I am grateful to have been accepted in one of the best schools (University College London) where I read my LLM in trade and finance law. Equipped fort the corporate work, I discovered private equity when I was a trainee at Hogan and Hartson (now Hogan and Lovells) in Geneva. I had no idea about private equity, but working on the PE project was when I got my first “aha moment”. Private equity could be the answer that Africa needed to get out of poverty and develop. I remember the chills and the excitement I felt.

A pool of capital supported by expertise and competence, investing into companies in Africa, building brands, services and products and empowering people to be financially independent and create wealth seemed more impactful than sitting in a room with Heads of State and NGOs and discussing endlessly the same problems about poverty and the need for alleviation but never quite committing to any action because of politics and lack of consensus.

From that point on, I decided to pursue this area of work and gained experience by working with several GPs, family offices, investors that have been looking for investment opportunities and very eager to invest in Africa.

From the time I started working in PE that is in 2007, the industry was mainly concerned about developed markets, especially the US and European markets. However, since 2012 I have worked increasingly with GPS, family offices and investors from Europe and the USA who have been increasingly scouting for and investing in opportunities in Africa. This is due to the significant growth of emerging markets and the increasing importance that Africa is playing as a key driver for global growth.

Although the continent is booming with opportunities, foreign private capital in PE and VC investments are largely concentrated in four (4) countries in Africa out of 54 countries on the continent: South Africa, Nigeria, Egypt and Kenya.

The Big 4 receive a bigger share of private capital due to several factors namely:

* the more conducive environment that these countries have for PE investments in terms of fiscal regime and legal investment structures available for funds, limited partners and general partners;
* the liquidity of the markets;
* the existence for exit strategies from portfolio companies within a time span of 5 to 7 years;
* maturity of the markets in terms of capital markets and more developed asset classes
* GDP and population size

Analysis of the sectors where investments are made in these Big 4, we see that the leading sectors are Fintech, technology infrastructure, the digital economy are receiving most of the private capital. This is not surprising considering private capital is from the US and Europe, which remain the dominant players PE on the African continent, and the priority sectors in these markets are sectors aligned with the 5th industrial revolution. The Big 4 are taking lead on the continent to be crucial players in the 5th industrial revolution.

The Africa Venture Capital Association report of 2022, Industry Quarter review Q3 reveals the following data between 2016 and 2022:

* **South Africa** has closed 325 private capital deals with the total value of USD 3.5 billion. South Africa is known as Africa’s data center capital with the likes of Google wanting to establish Google Cloud in the region, which has ignited the interest and growth of the Information Technology sector in South Africa where the technology ecosystem has been receiving the largest amounts of private capital in terms of deal volume since 2019.
* **Nigeria** has closed 318 private capital deals with the total value of USD 3.9 billion. Despite the complex macro-economic environment in Nigeria, the engine for Nigeria’s strong performance largely lies in the rise of FinTech. Nigeria is the undisputed leader in digital financial payments in Africa and Venture Capital has played a role in igniting this sector since 34 of the 35 deals that place in the financial sector in Q1 of 2022 where Fintech and comprised of Venture Capital investment. In addition, Information Technology contributes to 14% of the GDP in Nigeria, outperforming the oil revenue.
* **Egypt** closed 199 private capital deals with a total reported value of US$2.4 billion. Egypt was intentional in diversifying its economy and put in place policies and frameworks to enable growth agriculture, manufacturing and information and communication technology. The result of this is that most of the private capital from venture capital flows to Consumer Discretionary, Financial Sectors including Fintech, and Industrials.
* **Kenya** closed 192 private capital deals with a total reported value of US$2.2 billion. Kenya’s growing digital ecosystem is changing the future of traditional retail in the country, where retailers and consumer discretionary traders and companies are using digital technology to deliver their goods and services. A bulk of investment is therefore going into consumer discretionary which is digitalised and Fintech. Kenya is also a leader in Africa in clean energy development and therefore impact investors from Europe and the US have been channelling private capital in that sector too.

So, what about the other 50 counties in Africa that do not seem to be getting the private capital that the Big 4 receive?

A significant number of African countries are having sizeable yearly growth in the range of 6% to 8% such as Tanzania, South Sudan, Rwanda, Cote d’Ivoire, Ethiopia, and Senegal. While these countries and others may not be at the forefront drivers of the 5th industrial revolution, there are several countries in Africa that are showing strong economic and political reforms, a growing middle class that is driving consumption, and a relatively high return on investment rate for portfolios with investments in the region which are all key factors making African countries more attractive targets for private equity investments.

The reality is that most of Africa focused PE and VC funds are all chasing the same deals which are scarce. They are chasing the diversified African companies with a “sophisticated” management team and deemed “high quality”, but these are thin on the ground. Furthermore, the ticket size that they are willing to invest is at a minimum of USD 2 million to make it worth their time and the management fees.

There are about 4,000 companies in Africa that generate over USD 50 million and these are all distributed in the Big 4 countries. The reality though is that small enterprises with less than 10 employees are the drivers of 80% of Africa’s GDP, contribute to 97 percent of business volume and employ more than 80% of the population. The greatest growth potential is in the small enterprise market sector which remains to be under served when it comes to PE and VC deals.

PE firms when investing in Africa should venture outside their comfort zone and search for investments in small or medium enterprises where the ticket size is between 50,000 to 1,000,000. The needs of small enterprises though is not only capital. The most important part of PE and VC is the expert competence and knowledge that comes with the capital. This coupled with a different investment strategy which requires a more hands on approach, working with local partners (which has its benefits as the costs may be reduced) and therefore yielding more control on the management would see an increase in the chances of success. The truth is just because there are companies that do not reflect “success” as it is known and appreciated in the US and European markets, it does not mean that there are no investment opportunities at all. Instead, the companies that are successful in many African markets tend to look different than the ones in the west. Foreign Investors need to understand that they would more likely need to play a proactive role in building financial controls of the portfolio company or improve them, improve governance and operational efficiency as well as human capital, but that the upside of this may be worth a lot more since Africa is an emerging market and the returns are great and even greater than in developed countries.

That being said, perhaps the saviour of the continent should be private capital from Africa, specifically PE and VC funds in Africa. There is less than 1% of funds that are in Africa since most High Net worth Individuals and institutional investors in Africa are still of the mindset of investing in real estate and land rather than in companies. There is a real opportunity for Africa to create more players in this sector. So many countries in Africa have a vibrant and youthful population that are motivated and creative because of the circumstances they find themselves in. Imagine if we could empower these people through knowledge and capital to grow businesses. Imagine if we could alleviate poverty through creation of enterprises and value. I think the answer is there.