FINANCING START-UPS TO BUILD TOMORROW’S AFRICAN ECONOMIES

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With some USD 560m raised by over 120 African start-ups in the new technologies sector, 2017 broke a new record for venture capital investments on the continent. This marked increase compared to 2016 (+53%) not only gives us a glimpse of the huge potential for investors in Africa, it also allows us to see venture capital as an essential and credible driver to meet the development challenges on the continent.

Africa is a land with many opportunities: investment funds and international financial institutions have made no mistake about this. Despite the fact that physical and digital infrastructure is still underdeveloped and that there is a certain volatility on markets, the increase in its population (+25% between 2007 and 2016), combined with its constantly rising gross domestic product (GDP), brings the promise of a bright future. Countries such as Kenya, South Africa and Nigeria are already considered as hubs conducive to the emergence of start-ups. How could we fail to mention here the M-Pesa mobile money platform in Kenya, a real success story for the entire continent? While there has been a big boom in African e-commerce and fintech start-ups and the related venture capital investment, other sectors are also attracting more and more attention from investors (i.e., connecting the most remote populations to solar power, e-health, e-education, etc.).

Consequently, can we see start-ups as new tools for development in Africa? We think so! It has been proved that start-ups can serve as building blocks for job creation and new economic models, and that they can meet needs which are still served little or not at all. However, entrepreneurship, which is often seen as an alternative to unemployment and low wages, can create false vocations in light of the media and operational success of certain start-ups.

Devoting an issue of Private Sector & Development to venture capital and the world of start-ups in Africa means looking at a booming market, understanding the main components and discussing the potential negative externalities which can stem from this. Consequently, we wanted to give a voice to experts and avid players, who tell us about their experience. When reading the articles in this issue, we see that the common thread is that development finance institutions (DFIs), which include Proparco, undoubtedly have a crucial role to play. For Agence Française de Développement (AFD) Group, this involves a complementarity of operations. Thanks to the work conducted upstream by AFD to establish an ecosystem conducive to the emergence of start-ups (through the creation of incubators, accelerators, etc.), Proparco, for its part, can actively participate in financing these future “tech” champions in Africa.
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Venture capital in Africa: the long-term opportunity for investors

Andrea Traversone, Partner at Amadeus Capital Partners

With a high population growth rate and a significantly rising GDP between 2007 and 2016, Africa undoubtedly represents a strong potential for investors. And despite some gaps, the venture capital market has a bright future on the continent.

"Cape Town, Nairobi and Lagos [are] seeing the first significant generation of growing start-ups."

Ten years ago it was easier to pay for groceries via a mobile device in Nairobi than it was in New York. M-Pesa, the mobile money system set up by Vodafone for Kenyan telecoms group Safaricom and its Tanzanian peer Vodacom in 2007 revolutionised small money transfers in Africa and put the continent at the cutting edge of mobile payments processing. Within six months, 1 million Kenyans were using M-Pesa – and today 30 million people across Africa make over 10 million transactions per day.

It takes much more than one clever idea to create a tech culture. Since M-Pesa, few ideas or businesses have enjoyed similar success. A shortage of funding and support networks for entrepreneurs, as well as relatively shallow pools of people with spending power, has historically held back new tech businesses in Africa. But the situation is improving as start-up clusters develop and the middle class grows. Today, Amadeus Capital Partners is having discussions with entrepreneurs in Cape Town, Nairobi and Lagos that resemble the talks it had with business people in London, Berlin, and Stockholm two decades ago. And it is seeing the first significant generation of growing start-ups (those achieving later stage Series B funding) emerging from those cities ready to take on the rest of Africa and beyond.
HUGE OPPORTUNITIES WITH SIGNIFICANT CHALLENGES

Africa presents a huge long-term opportunity for investors. Its population grew by about 25% between 2007 and 2016 to 1.2 billion while GDP expanded at over twice that rate to $2.3 trillion, according to African Development Bank (ADB) statistics. ADB estimated that the continent’s middle class – those earning between $2 and $10 a day – numbered nearly 350 million as far back as 2011 (although critics have questioned those figures). Today, more than 60% of the population has a mobile phone, from which they frequently access the internet. But there are significant challenges too, such as weak physical and digital infrastructure, as well as volatile currency markets that can take a significant chunk out of investor returns.

Venture capitalists have seen this movie before and know how the story goes. It is known that economic progress is no guarantee of venture capital (VC) success, nor is economic development a smooth path. Take India as an example. On paper, it ticks many of the right boxes. The World Bank predicts it will be the world’s third largest economy within 10 years and its population of 1.3 billion is expected to overtake China’s by 2024, according to UN estimates. It too has a burgeoning middle class, which Indian think tank National Council of Applied Economic Research (NCAER) believes could hit 547 million people in 2025-26. Add to the mix its university pedigree in engineering and its recent history as an outsourcing destination for global technology firms and there are clear attractions for VC investors.

As a result, more venture capital was invested in start-ups in India than in the UK in 2017. Success is coming too. A number of companies have achieved multi-billion-dollar valuations, including ecommerce marketplace Flipkart, as well as mobile payments group Paytm, and these are attracting large technology investors like Japan’s SoftBank into the market.

Yet the reality is complicated. The country’s middle income bracket is not growing as quickly as previously forecast, nor is the term “middle class” a clear indicator of prosperity – NCAER reported in 2014 that only 40% of the middle class had a piped water connection. In fact, it’s the wealthiest that have been capturing the lion’s share of economic progress, with the top 10% of earners now accounting for 55% of national income, versus 40% at the turn of the millennium, according to the 2018 World Inequality Report. That is ultimately holding back consumption growth – ecommerce sales were virtually flat in 2016 and just a little better than the global average of about 20% in 2017, data compiled by The Economist showed. There are undoubtedly opportunities to invest, but the market is competitive and valuations in some sectors can be high.

So might venture capital dollars be better invested elsewhere?

As a region, Latin America is probably the wealthiest and most developed of the emerging markets. From a VC perspective, it’s so far the only region to have created technology start-ups that have grown to be very large scale businesses, eventually exited successfully via IPOs or M&As. Brazilian online travel agency Despegar.com, marketplace Mercado Libre and Argentinian IT and cloud computing firm Globant are among those to have gone public on the Nasdaq and NYSE exchanges.

Today, more than 60% of the population has a mobile phone, from which they frequently access the internet.
Southeast Asia is also coming up rapidly on the rails. The region does have its challenges, such as logistics in Indonesia, which has more than 17,000 islands, as many as half of which are inhabited. But it is producing a very strong pipeline of start-ups, mainly in Singapore and Kuala Lumpur, and the net is widening. And there is a growing cohort of early-stage funds, as well as interest from corporate investors particularly the large Chinese internet players. As yet, there are no large-scale exit successes that prove the market, but they are expected to emerge in the next three to five years.

OVERVIEW OF AFRICAN VENTURE CAPITAL HUBS

So where does that leave Africa? The continent is starting from a lower base but is catching up in terms of economic development and start-up culture. When Amadeus set up the Digital Prosperity Fund, it established a presence in Cape Town to capture opportunities in Africa’s largest tech hub. The Silicon Cape, as it is affectionately known, is responsible for more than 400 start-ups, over 60% of the continent’s total. Moreover, the Universities of Cape Town and Stellenbosch are world-class institutions that are breeding grounds for plenty more bright ideas.

The companies being created in Cape Town have a strong entrepreneurial pedigree and international ambitions. Travelstart, into which Amadeus invested $40 million alongside MTN in 2016, was founded by Stephan Eckbergh, who previously built and sold a leading Swedish online travel agency before turning his attention to South Africa. The capital injection Amadeus made is enabling the company to consolidate in South Africa and build scale in countries such as Nigeria, Kenya and Egypt.

Other African markets show potential but lag behind. Some 150 companies have emerged from Silicon Savanah, centred on the Kenyan capital of Nairobi, but none have yet replicated the success of M-Pesa. There are entrepreneurs and active investors, but the local market is relatively small, which makes it hard for companies to reach scale quickly. And without scale in their home market, businesses struggle to secure the funding needed to become pan-African players.

Contrast that with the most youthful hub, Yaba in Lagos. While home to a relatively modest 50 start-ups, the sheer size of the Nigerian market, combined with locals’ hunger to consume and adopt technology, has propelled some companies far a very short time. Jumia, founded in 2012 and which spans ecommerce, jobs and finance, was the first to pass the $1 billion valuation mark. Within ten years – the lifespan of a typical venture capital fund – Lagos is likely to become another leading technology hub in Africa.
AFRICA, ONE OF THE FINAL FRONTIERS FOR VENTURE CAPITAL INVESTMENT

Although ecommerce, fintechs and online marketplaces are prevalent investment themes and reflect global technology trends, there are startups that address uniquely African issues. “Solar as a service” is giving millions of Africans in remote locations access to electricity via portable solar panels, controlled – and paid for – via mobile phones. M-Kopa, backed by the entrepreneurs behind M-Pesa, has connected more than 600,000 homes across East Africa to solar power and placed an order with a domestic manufacturer for 500,000 photovoltaic panels to help meet demand over the next two years. It’s one of about a dozen companies in the space already generating significant revenues.

The opportunity for financial investors will be in potentially consolidating the market to create a leader with the scale to appeal to a large strategic acquirer or float on a stock market, in turn paving the way for the next generation of startups in the sector.

Where there are opportunities, there are also challenges. Often the delivery infrastructure for ecommerce does not exist, so successful online retailers need to establish their own networks. Moreover, in many emerging markets, items that are considered small purchases by developed market standards – like training shoes – are paid for over 12 months. Where people don’t have credit cards or bank accounts then cash payments need to be collected in person at time of delivery. Investors also need to be aware of the macro risks. Sharp local currency movements are capable of wiping out a significant portion of annual earnings when translated back into dollars or euros. Over the typical five-year investment term, double-digit annual earnings growth should more than compensate for currency fluctuations, but shorter term investments may be disproportionately affected.

“Where there are opportunities, there are also challenges. Often the delivery infrastructure for ecommerce does not exist.”

For investors like Amadeus, it is a question of balancing the risks with the undoubted long-term opportunities. Africa is beginning to produce world-class start-ups and its growing population is hungry to adopt technology and consume – often bypassing fixed-line internet and going direct to mobile. Yet the evolution will take time, and there will be setbacks and challenges along the way. Nevertheless, Africa represents one of the final frontiers for venture capital investment and that’s why we are getting ready now for what promises to be a very large, long-term opportunity.

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Why are there so few unicorns in Africa and what are the key factors for success to help them emerge?

Maurizio Caio, Founder and Managing Partner, TLcom Capital

VC-backed African companies have just completed their first life cycle. The prospect of Africa generating unicorns is optimistic but achievable: it offers giant underserved markets, its companies and entrepreneurs are comparable to their peers worldwide, and the supply of capital and related business-building support is increasing. Unicorns need sufficient local capital and business-building capacity, which come with VC. The imperative is to invest capital and discipline to create a sizeable and professional local VC industry.

FOCUS

TLCOM CAPITAL

Launched in 1999, TLcom Capital is a VC firm based in Nairobi, Lagos and London investing in technology-enabled fast-growth businesses across Europe, Israel and Africa. Recent investments on the Continent include Upstream (acquired by Actis), Movirtu (acquired by BlackBerry), Andela, Terragon and mSurvey.

Many factors are conspiring to establish a vigorous venture capital (VC) market in Sub-Saharan Africa. A growing number of venture capital teams have recognized investment opportunities, driven by large underserved African markets, the ability of entrepreneurs to design innovative business models that leverage the high penetration of mobile technology, a lack of legacy infrastructure and increasing spending power. Development finance institutions (DFIs) and private capital, including family offices and high net worth individuals (HNWIs), have started to support this asset class. A maturing technology and entrepreneurial ecosystem is emerging in Nairobi, Lagos and Cape Town, fuelled by mobile money, growing demand for products and services, and the innovative solutions African entrepreneurs are bringing to vast, underserved markets.

Yet, is mobile technology the key to solving Africa’s problems? Will start-ups scale up fast enough to serve local markets? Is there enough talent? Do investors, entrepreneurs and VC investment teams have realistic return and time horizon expectations? And why the lack of African unicorns – VC-backed start-ups that reach a valuation of $1 billion in a financing round or exit – for many the evidence of a quality, functioning VC market?

The answers require a data-driven perspective of African VC markets and a knowledge of the key factors and behaviours of stakeholders that are most conducive to generating value for VCs.

A maturing technology and entrepreneurial ecosystem is emerging in Nairobi, Lagos and Cape Town, fuelled by mobile money.
to $277 million of capital was invested in 55 to 125 start-ups (Disrupt Africa, 2016).

Estimates of the size of VCs in Africa in 2017 varied between $195 million and $560 million of capital invested in 128 to 160 deals (Partech Ventures, 2018). In the same period, the US VC market generated $72 billion invested in over 5,000 deals; China, $71 billion in over 2,800 deals; Europe, $18 billion in about 2,500 deals.

The average holding period of a VC investment in the developed world is between five and seven years, often longer for investments resulting in high returns. VC-backed African companies have just started to complete their first life cycle from seed to exit. Hence, the African VC ecosystem is young and small, and it is unsurprising that it has not yet resulted in a string of positive exits, the basis for predictable returns.

AFRICA’S YET-TO-BE-GENERATED UNICORNS

Unicorns indicate a VC ecosystem that is ripe for investment. In Q4 of 2017, CB Insights (2017) published its most recent report on unicorns, recording a global total of 214, with 106 outside the US: 52% were in China, 9% in India, 8% in the UK, 4% in Germany, 3% in South Korea, with the remaining 24% in other countries.

Africa has generated three unicorns: in e-commerce, Nigeria-based Africa Internet Group; in food and beverages, South Africa-based Promasidor; and in telecom services, South Africa-based Cell C.

Compared with their US, Asian and European counterparts, these companies have not followed traditional VC paths: funding has come primarily from public companies and private sponsors, which tend to back mature companies, with typical private equity expectations.

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Key drivers of value for VCs

What is the basis for the expectations of the African VC ecosystem, and how can it support the development of unicorns on the Continent? And what are the common features of value generation in the global VC industry?

Unicorns are world-class companies that scale up quickly in large, underserved markets, based on competitive advantages that translate into high margins, high growth and that generate significant cash flow, with financing and business-building support from competitive VCs. When valuations and minority protection rights are aligned with global standards, normalized for the stage of the company, the result is value generated for founders and management, VC teams and their fund partners.

When evaluating companies for investment and assessing their unicorn potential, VCs should ask the following. First, is the market underserved and attractive in terms of size and growth?; could technology and innovative business models enable success?; are the capital requirements aligned with those typical of VCs; does the market indicate material prospects of exits? Second, is the company comprised of a world-class team?; is it based on solid business fundamentals and a unique competitive advantage? Third, is the investment attractive in terms of valuation and key terms relative to the expected exit scenarios? VC teams should invest only where the answers to all these questions are yes.
AFRICAN UNICORNS ARE POSSIBLE

“[In Africa] entrepreneurs live in a less mature and supportive ecosystem, resulting in longer times to financing.”

With these questions as a framework, the prospect of Africa generating unicorns is optimistic. There are three reasons for this.

First, Africa offers gigantic underserved markets. Most of the demand is low-income, necessitating business models based on low-cost positions. Technology can enable these. A similar opportunity exists in the B2B space. Low-productivity SMEs need affordable technology solutions, while value chains can also benefit from technology-enabled solutions. Consumer-facing corporates also need mobile-based enterprise software to better segment, serve and increase their customers.

Second, African companies and entrepreneurs are comparable to other countries. The ratio of investable companies to the total deal flow in Africa is similar to other regions. However, entrepreneurs live in a less mature and supportive ecosystem, resulting in longer times to financing, or to adjusting or giving up on their business models. Also, less guidance from angels, VCs, consultants and repeat entrepreneurs can result in business models that are less market-driven and business fundamentals-oriented, and more focused on brilliant tech. Management and technology talent is also scarce. However, these obstacles are balanced by advantages peculiar to Africa. The technology risk is lower because entrepreneurs tend to create business models that leverage proven technologies and there is a more predictable exit path associated with large private equity funds.

Third, there is a growing supply of early stage and growth capital, and related business-building support. Sources of capital for African entrepreneurs include seed-stage financing rounds of up to a few hundred thousand dollars; for mature companies looking for growth/expansion, rounds of $10 million or more are typically served by mid-market and private equity funds. The gap is in the $500,000 to $10 million range, which is typical of series A and B venture capital financing. Companies such as Andela and Twiga demonstrate that fast growth in large, underserved markets via tech-enabled business models is taking root in Africa. But these companies have tapped the global VC market in the series A to B range.

Africa has attractive markets and companies that can scale, but unicorns need sufficient local capital and business-building capacity, which come with VC.
INCREASING THE ODDS FOR AFRICAN UNICORNS?

The imperative is to invest capital and discipline to create a sizeable and professional local commercial VC industry. This is the responsibility of limited partners who recognize the Africa VC opportunity or who have room for a less-proven asset class in their global allocations, and VC teams who need to build high-risk, high-return portfolios validated by subsequent financing rounds at growing valuations, and by value-generating exits.

Also, a business fundamentals culture driven by an understanding of industry dynamics must be embraced by VC teams and entrepreneurs. African entrepreneurs and their start-ups must be held to the same rigorous standards as their worldwide counterparts. Declining an investment in – or unplugging from – a failing company is as critical as supporting a winner. Attracting more capital to African VC involves generating success stories. Even with investment only in potential winners, there will still be failed investments.

Business fundamentals should be adopted early in the lives of companies, creating realistic expectations in young teams about the availability of capital, investment requirements and valuations. Local governments can also make a difference by creating a supportive environment through regulation, tax incentives for VC investment, and building economic stability to attract more capital.

Ultimately, the key value generator is the entrepreneur. It is up to VC teams to fulfil capital market expectations by serving the needs of the entrepreneur for business building, talent support, and guidance, from financing to exit. If we can nurture a new generation of African VCs focused on these values, Africa will generate her share of unicorns.

“Africa has attractive markets and companies that can scale, but unicorns need sufficient local capital and business-building capacity, which come with VC.”

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The transitions currently spearheading change – with the digital transition in the vanguard – are leading to a global paradigm shift. The world is entering a different era and Africa is no exception. The Continent has surprised everyone with the spread of mobile phone technology, the deployment of broadband and the emergence of a multitude of start-ups that help unlock all of the untapped creativity of its young people. All over the world and especially in Africa, the transforming power of new technologies is revolutionising how we live, work and interact. The sea changes taking place at all levels (i.e., technological, economic and social) raise questions concerning the conditions that are most conducive to fostering the emergence of innovative start-ups in Africa today, particularly in the digital sector. What trajectory has been followed by these business leaders who frequently harness innovation to a specific need or context for the benefit of the greater good and the development of the Continent?

Start-ups and digital innovation: fertile ground for social transformation in Africa

Karim Sy, Founder of Jokkolabs

Social innovation in Africa is currently closely bound up with the digital revolution. To generate economic development that benefits as many people as possible, the digital sector must conserve all of its innovation potential – especially prevalent among FOSS communities. Innovation spaces help young entrepreneurs to structure their approach while keeping all of their social transformation potential intact.

FOCUS JOKKOLABS

Jokkolabs is a network of innovation spaces created by Karim Sy in 2010 in Dakar to foster the emergence of start-ups. At the time, it was the first network of its kind in French-speaking Africa and it has grown around a community of independent hackers and free and open source software (FOSS) advocates that now covers around a dozen spaces in nine different countries (Côte d’Ivoire, Cameroon, Mali, Morocco, Burkina Faso, Benin, Gambia, France and Senegal).

All over the world and especially in Africa, the transforming power of new technologies is revolutionising how we live, work and interact. The sea changes taking place at all levels (i.e., technological, economic and social) raise questions concerning the conditions that are most conducive to fostering the emergence of innovative start-ups in Africa today, particularly in the digital sector. What trajectory has been followed by these business leaders who frequently harness innovation to a specific need or context for the benefit of the greater good and the development of the Continent?

“...”
YOUTH AND MOBILE PHONES: FERTILE TERRITORY

In terms of innovation, Africa has two key advantages: its young population and high mobile phone penetration: by 2050, it will count close on one billion, well-connected young people under 18 years old. This young population is helping to drive the transformations that are gradually changing the face of Africa, particularly through the creation of digital start-ups. For example, in Niger, one of the world’s poorest agrarian countries, farmers are being connected by an e-irrigation and e-assistance system set up by Abdou Mamane Kane’s Tech-Innov enterprise. This young entrepreneur, winner of several awards (Orange Social Business, the Hassan II water award, 3rd prize for young African start-ups), has designed an irrigation system that can be switched on remotely via a mobile phone.

So telephones are a constant in all of these transformations – nearly everyone uses one, even in the remotest areas – and telephone-internet convergence is increasingly important, especially since the advent of 3G and 4G broadband. Young African entrepreneurs have got the picture: digital is the new country from which they intend to conquer the world. Ulrich Sossou, a young entrepreneur from Benin is another example. He has launched an innovative and profitable real estate management solution that targets the US market – even though he’s never actually been to America!

LEARNING WITHIN DEVELOPER COMMUNITIES

Digital innovation – the lifeblood of solutions tailored to African problems – is the raison d’être of the communities that are developing these open source apps. These communities are therefore the structures in which future Pan-African entrepreneurs are learning their trade.

The communities are not hierarchical and function in a very informal manner. Consequently, recognition is conferred by merit and by one’s peers, and not by virtue of diplomas, social class or networks of influence – and this is a new thing for Africa. All members contribute to the greater good of the community and are only too willing to share their knowledge with others. The communities may have inspirational or charismatic leaders but they do not accept any hierarchy, especially one imposed from the outside.

INNOVATION UNDER THREAT?

At the same time, with the help of development institutions, especially within the scope of the World Bank-sponsored InfoDev programme,² the first digital incubator projects are beginning to come on stream. Enterprise support is starting to become more structured.

So community members are turning into project-focused entrepreneurs and they don’t share like they did before – they may even be in competition with other members. When incubation structures are designed in a too conventional way that disrupts digital community culture,
unfortunately, horizontal, peer-based learning dynamics can disappear leading to a depletion of expertise. In Africa, one of the trickiest places in the world to do business where informal practices are very important, it is vital for young entrepreneurs to maintain collaborative links that keep them in touch with peer-based learning dynamics.

Community leaders and young entrepreneurs are snapped up very quickly by businesses in need of scarce human capital. Multinationals are deploying programmes to acquire start-ups just to ensure their survival. This is often a hard-nosed, unsentimental process and if it is not properly regulated, innovation could suffer in the long run. For entrepreneurs, the “Holy Grail” no longer consists in building up a business but in selling off their start-up to a big corporation within a couple of years. Under this approach, instead of taking on a big group, the start-up seeks to integrate one. It is as if Uber tried to sell its structure to the big French group Taxis G7 instead of trying to completely revolutionise the sector.

INNOVATION SPACES FOR INVENTING THE FUTURE

But there is an alternative approach to getting bought out and merged into a big corporation: innovation spaces seek to provide young entrepreneurs with a forum in which they can meet and exchange experiences with their peers while preserving links and a similar mindset to FOSS communities (particularly in terms of peer-based learning). In a nutshell, these spaces are created specifically to maintain and reinforce their innovation potential.

Jokkolabs is an independent, not-for-profit organisation offering innovation facilities focused on social transformation. It has emerged out of hacker and FOSS communities and Jokkolabs’ philosophy is a naturally inclusive one. For its members, innovation is a bottom-up phenomenon and any local innovation – whether it comes from the North or South – can have a global impact. Jokkolabs’ members experiment with different approaches to try to come up with solutions to societal requirements in healthcare, agriculture, education, the new media and good governance. It is the first structure of this type in French-speaking Africa and has helped foster the emergence of numerous start-ups (Coin Afrique, Niokobok, Afri Malin, etc.).

Jokkolabs has also paved the way for a number of African “tech hubs” (i.e., these spaces that have been fostered by tech communities). In 2014, the World Bank estimated that there were 174 tech hubs (World Bank, 2014); in 2016, the GSM association identified 314 (GSMA, 2016) such spaces of various different types: coworking spaces, incubators, tech hubs, mobile labs, etc. All of these terms describe the same basic idea: spaces that were originally closely bound up with, and provided a forum for members of FOSS-type communities. These forums organise their own events: BarCamps (open, tech-focused and user-generated conferences), hackathons, bootcamps and other novel forms of exchange.

Some network members have launched social impact projects such as Ushahidi3 in Kenya or SIG Santé in Senegal, both of which are health
mapping initiatives. These types of projects are blurring the distinction between enterprise and social activism. So digital innovation can drive development but for this to happen, we need an approach underpinned by the notion of “digital commons” (Wikipedia is a good example), i.e., harnessing a resource (knowledge) to a community and a specific set of rules. Such innovative initiatives pave the way for a new approach to development.

THE ROLE OF POLICY MAKERS

Political decision-makers do not always fully appreciate the extent of the digital revolution. Indeed, only 40% of African countries have currently enacted legislation that protects digital data and there is a chronic shortage of statistics on the key aspects of the digital economy, all of which restricts the possibilities for devising appropriate public policies (CNUCED, 2017).

True, it is difficult to keep up with the sheer pace of this revolution, the paradigm shift and its systemic impact. We need to foster awareness among all stakeholders (public, private and those from civil society) of how the digital revolution actually works in practice along with all of its multiple facets, opportunities and risks (data protection, net neutrality, etc.). We also need to create a think tank that will reflect upon ways of controlling (and not just being subjected to) the digital revolution, and an action tank that will devise concrete solutions on the ground. Finally, we need platforms specialised in public–private partnerships and key resource persons within the communities themselves – powerful innovation drivers – focused on all of the major transitions currently in progress (i.e., energy, education, agriculture, etc.).

“So digital innovation can drive development but for this to happen, we need an approach underpinned by the notion of “digital commons”."

“Only 40% of African countries have currently enacted legislation that protects digital data and there is a chronic shortage of statistics on the key aspects of the digital economy."

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3 • https://ushahidi.workable.com/
The impacts of digital credit in Africa: beware of negative externalities

Isabelle Barrès, Vice President of the Center for Financial Inclusion at Accion, Global Director of the Smart Campaign

Demand for credit in Africa exceeds supply, despite the rise in mobile money. Yet start-ups, growing daily in number, are at risk of accelerating over-indebtedness, by supplying credit to clients without conducting appropriate repayment capacity analysis. Digital lenders need to understand the risks of over-indebtedness from a client perspective, and algorithms need to evolve to take this into account. Regulation also must guide good practice for fintech digital lenders.

If providers profit while clients are experiencing stress in repaying, defaults will catch up with the client or the institution, and the client will no longer be able to borrow.

Desplespite the rise in mobile money in Africa, and globally, the gap between supply and demand for credit in the region remains. Surprisingly, in this milieu start-ups are at risk of accelerating the pace of over-indebtedness in Africa. The number of start-ups reaching last mile clients is rising. The driver of this is fintechs taking advantage of a business opportunity, and the prospect that if you offer clients much-needed credit at a lower cost than the alternative, they will be better off.

But is this necessarily true? Are these start-ups offering solutions to the credit needs that many small and medium-sized African businesses have, and are clients better off with these solutions? Or is the fintech digital credit hype attracting lenders that offer credit in the wrong places – and for the wrong reasons? What is needed to ensure that digital credit is provided responsibly, for the benefit of clients?

Some estimate that digital technologies have cut the cost of providing financial services by 80-90 percent (McKinsey, 2016). Africa is taking the lead in the rise of mobile technology, and the opportunities are promising (figure opposite). Start-ups in this space are making big strides. Those involved in digital credit either deliver digital credit directly or enable its delivery through downstream product servicing. The number of fintechs – start-ups offering these services – in Africa is growing daily (Mesropyan, 2016).

Technology well used offers opportunities not previously available. However, two key issues need to be recognized and addressed in order to generate long-term benefits for both clients and providers. First, provider and client interests must be aligned. If providers profit while clients are experiencing stress in repaying, defaults will catch up with the client or the institution, and the client will no longer be able to borrow. Aligning interests requires providers to think of client benefits as well as their own from the start. Second, a well-designed loan should match the ability to repay. Well-designed loans are a blessing, for
Africa is taking the lead in the rise of mobile technology

example, helping a small business; yet loans that do not consider clients’ capacity to repay sets them up for failure. Even if they repay in the short term – which is often why default rates stay low – it can be at the cost of extreme hardship, making it a poor predictor of over-indebtedness. It may take some time before the debt stress of clients affects providers.

‘INSTANT’: AN OPPORTUNITY AND A RISK FOR CONSUMERS

A key attribute digital lenders advertise is speed of access. Where traditional loans could take weeks for approval, with many requirements, this is a plus from the perspective of clients. But the automation and speed raises concerns: are decisions made too quickly, and are risks adequately measured and mitigated, especially from the clients’ perspective?

Other aspects of digital credit lead to new risks compared with analog lending: start-to-finish digitization; the move from high to low touch processes; small credit amounts that grow; short-term loans; reliance on alternative data analytics; and decentralized support workforces.

WHAT COULD GO WRONG?

With analog credit, prevention of over-indebtedness centered on adequate repayment capacity, and on growth not taking place at the expense of quality.

In the digital context, the following major categories of risk have been identified (Center for Financial Inclusion, 2017/2018): Limited – if any – debt capacity analysis; Products that do not match client needs; Lack of credit reporting; Automatic renewals; Aggressive sales and marketing; Disproportionate consequences of late payments that lead to a cycle of debt.

MOBILE CREDIT SERVICES IN SUB-SAHARIAN AFRICA

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M-SHWARI KENYA

- Established: 2014
- Number of accounts: 15 million
- Value of loans disbursed: US$1.3 billion
- Non-performing loan ratio: 1.92% (Kenya: 5.3%)

M-PAWA TANZANIA

- Established: 2016
- Number of accounts: 5 million
- Value of loans disbursed: US$22 million
- Non-performing loan ratio: 8.52% (Tanzania: 8.3%)

*As at June 2016

Alternative credit scoring methods – often using elaborate algorithms that predict the probability of repayment – help to include people who have thin credit files and who would otherwise have been excluded. However, these models are a poor replacement for the repayment capacity analysis previously conducted by lenders serving vulnerable excluded populations. While the algorithm may predict whether or not an institution will be repaid, it does not consider clients’ situations and needs, and therefore, the sacrifices that clients might have to make in order to repay. Over-indebtedness is not only reflected in default, it is reflected primarily by the extent of the sacrifices that the client endures to avoid defaulting. Algorithms are institution centric, not client centric. They are meant to learn over time, becoming refined and better predictors; yet they do so at the expense of early clients who enabled the algorithm to become better fine-tuned, as they have a higher probability of defaulting and suffer dire consequences (Ngigi, 2016).

The promise of well-tuned algorithms saving costs and managing institutional risk is unfortunately skewing attention away from client risks. Over-indebtedness needs to be reframed from a client perspective: can clients afford the loan? Even if they can repay, what sacrifices are they making? Are they at risk of not being a client ever again in the future (which would hurt both the client and the provider)?

MITIGATING OVER-INDEBTEDNESS IN THE DIGITAL WORLD

Over-indebtedness is a multi-stakeholder issue, and is linked to the client protection issues summarized in the Client Protection Principles1. Prevention of over-indebtedness is a particularly tricky one, in that it requires the concerted effort of a wide range of stakeholders.

Providers have a responsibility to ensure that their practices do not lead to an oversupply of credit to clients who are unable to meet their payment obligations, and digital lenders will need to adopt a more client-centric approach to understand the risks of over-indebtedness from a client perspective. Algorithms need to evolve to take this into account.

Because only one irresponsible lender is needed in terms of over-indebtedness to negatively affect clients, it is necessary that financial consumer protection regulation evolves to guide the practices of otherwise unscrupulous digital lenders.

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1 The Client Protection Principles are a list of 7 key principles that financial providers need to abide by. Available here: https://www.smartcampaign.org/storage/documents/smart_campaign_cpps.pdf
clients, it is necessary that financial consumer protection regulation evolves to guide the practices of otherwise unscrupulous digital lenders.

Investors can, and should, use their leverage to encourage good practices by digital lenders, as they have for analog lenders. They can reward digital lenders who design and deliver appropriate products, are transparent about terms and conditions, explain to clients the risks of over-indebtedness, adopt fair and responsible practices during repayments, and help clients who cannot, but want to, repay.

Importantly, digital providers can leverage the same technology used to deliver products to educate and empower clients. Clients have rights and responsibilities. Informed consumers are better able to protect themselves and avoid becoming victims of predatory lenders.

OVER-INDEBTEDNESS IS MULTIDIMENSIONAL AND DYNAMIC

In the interest of long-term mutual benefits for both providers and clients, providers need to move away from a unidimensional definition of over-indebtedness that overly emphasizes repayment as the proxy for whether or not a client is indebted, towards client-focused definitions of over-indebtedness.

Digital credit providers need to complement credit bureau data with disbursement and repayment data on digital loans so that a fuller financial picture can emerge for digital borrowers.

Over-indebtedness is not a steady state. As the lives of vulnerable clients evolve, so do their needs and challenges. A client who may have received a loan from a responsible lender in the past may suddenly not be in a position to repay. We need to develop ways to monitor whether clients are showing signs of financial stress. Responsible institutions should be able to identify this, and work with clients until it is resolved.

The role of responsible providers goes beyond providing loans to ensuring that clients are supported if necessary. Microfinance Opportunities, in collaboration with Social Performance Solutions, has been developing a stress assessment tool that enables providers to monitor whether borrowers are incurring stress after having received a loan. Such tools are extremely important to have a full picture of over-indebtedness, and a broader suite of tools needs to be available to responsible providers.

FINTECH PROTECTS AGAINST OVER-INDEBTEDNESS

Fintech digital credit providers need to unite and agree to collective measures to tackle the problem of over-indebtedness. This will entail defining responsible digital underwriting, leveraging technology while learning from the past, expanding credit bureau reporting, and agreeing on common practices for the benefit of clients. Some fintechs are already taking the lead and through the Fintech Protects Community of Practice are working together to define and implement responsible practice. The body of evidence around risks is growing. Now is the time to define the guidelines of good practice for fintech digital lenders and identify solutions that work for clients.

"Providers need to move away from a unidimensional definition of over-indebtedness that overly emphasizes repayment as the proxy for whether or not a client is indebted, towards client-focused definitions of over-indebtedness."
What role can DFIs play in promoting the development of the African venture capital ecosystem?

Michelle Ashworth, Venture consultant, CDC Group

Over the past few years, a number of DFIs have announced the launch of venture capital investment programmes for Africa – initiatives that should help promote start-up activity across the continent, and drive the development of the African venture capital ecosystem, leading to job creation and economic growth.

In recent years a number of development finance institutions (DFIs) have announced new venture investment programmes for Africa. In 2016, European Investment Bank (EIB) and African Development Bank (AfDB) announced the Boost Africa Initiative, a joint venture that will see up to €150 million deployed in the African venture capital industry and is expected to support over 1,500 start-ups and SMEs across the continent.

More recently, in late 2017, CDC’s Intermediated Equity team secured approval to commence a programme of investing in African venture capital, which initially will entail deploying up to $75 million in 6-8 African venture funds over the next 3-4 years. Further capital is available from CDC’s Impact Fund, which will also continue to make select venture fund investments.

There are many reasons why DFIs are deploying capital in African venture capital. Investing in venture funds tends to be the most effective way of financing small tech-enabled companies and supporting entrepreneurship. Many of these start-ups are developing technology that can help formalise informal markets and/or provide solutions to local problems in areas such as agriculture, healthcare, education and financial services.

More broadly, developed venture markets are proven to drive economic growth and promote job creation. It is estimated that just under 40% of new jobs created in the US in the past 40 years have been produced by venture-backed companies (Stanford, 2015). Whilst data is less readily available for emerging markets, initial indications suggest the impact of venture capital (VC) will be similarly significant; in China, a venture market which has developed in the past 15 years, venture-backed companies are already estimated to have created 10 million new jobs.

FOCUS

CDC

CDC is the UK’s development finance institution. CDC supports the building of businesses throughout some of the world’s poorest places in Africa and South Asia, to create jobs. CDC focuses on investing in countries where the private sector is weak, jobs are scarce and the investment climate is difficult, but particularly in sectors where growth leads to jobs.
WHY DFI FUNDING IS NEEDED

Venture capital has the potential to deliver strong returns, but investing in early-stage companies (whether directly or indirectly through funds) is inherently risky. In developing markets, the risk is further exacerbated, deterring all but the most experienced private institutional investors from participating in the asset class. Many established UK funds struggle to raise capital without support from the British Business Bank or European Investment Fund (EIF); given how immature venture capital is in Africa, African venture funds would likely be almost impossible to raise without the support of DFIs.

EVOLUTION OF THE AFRICAN VENTURE CAPITAL ECOSYSTEM

In the 20 years, I’ve been investing in global VC funds I’ve had the privilege to follow the emergence of a number of new venture capital markets – first in Europe in the late 1990s, then in China in the early 2000s and India in the mid-2000s. Whilst the African venture capital market remains nascent it displays many of the same characteristics that Europe, China and India exhibited just prior to the maturation of their ecosystems:

1. REVERSE MIGRATION

Anecdotal evidence suggests an increase in returnee entrepreneurs like Iyinoluwa Aboyeji, who left Canada in 2013 to first found Andela and then, more recently, Flutterwave. We are also starting to see the emergence of companies like Movemeback, which are designed to help returnees find new jobs on the continent.

2. DEVELOPMENT OF REGIONAL HUBS

In the US a large proportion of venture-related activity takes place in Silicon Valley. In Asia, hubs have sprung up around key cities such as Beijing & Shanghai (China) and Bangalore & Mumbai (India). In Africa, regional hubs are emerging in North Africa (Cairo), East Africa (Nairobi), West Africa (Lagos) and South Africa (Cape Town).

Five precursors that predict the growth of African venture capital activity

1. Reverse migration
2. Development of regional hubs
3. Increased deal activity
4. Increased participation from US VCs
5. New market entrants
3. INCREASED DEAL ACTIVITY

In 2017 VCs deployed $560 million in 124 African venture-backed start-ups, a 53% year-over-year increase in capital invested (Partech Ventures, 2018).

4. INCREASED PARTICIPATION FROM US VCS

In China, it was the entry of US VCs that fuelled the development of the market. In the past two years, prominent US VCs have financed a number of African companies including Andela (Spark Capital), Flutterwave (Social Capital), Instabug (Accel) and Zipline (Andreessen Horowitz).

5. NEW MARKET ENTRANTS

Venture firms entering the Africa market with new funds in recent years include local VCs that are raising institutional capital for the first time, established EU VCs launching their inaugural Africa-focused venture funds such as Partech Africa and TLCom, and even experienced US venture capitalists launching new funds to target the continent, such as Raba Capital. This is in addition to an increasing number of locally based impact venture funds such as Novastar Ventures and Energy Access Ventures.

Whilst Africa’s venture capital market is showing promising signs of growth it isn’t clear how long it will take the ecosystem to develop sufficiently to support domestic entrepreneurship and significant job creation. China’s venture capital market developed relatively quickly (within 15 years), but the European ecosystem has taken much longer to develop (20+ years). Africa shares characteristics of both regions and is likely to take at least 15 years to fully develop.

CDC’s new Intermediated Equity venture programme will initially focus exclusively on investments in venture funds. We believe this is the best approach for CDC to take at this time as it enables us to build a diversified portfolio to minimise risk and will enable us to leverage our existing skillset and team most effectively.

In Phase 1 of the programme we plan to deploy up to $75 million in 6-8 seed and early-stage Africa-focused venture funds over the next 3-4 years. Given that it typically takes 6-8 years for early-stage investments to be exited, we envisage the programme will have at least two further phases, stretching out in total over a 10-year period. We chose to target seed and early-stage as this is where we felt there was the biggest gap in the market. We plan to minimise risk by diversifying the portfolio by geography, with exposure to the four key hubs in North, East, West and South Africa.

Investing in venture funds is similar, but different, to investing in private equity (PE) funds, and we have introduced new processes and procedures to execute the programme; we have tweaked our due diligence to be more qualitative (to reflect the importance of relationships and lack of data in venture); we have developed a customised approach to ESG (to reflect the lean management teams and limited bandwidth); and we have amended our standard term sheet (to reflect the need for significant follow-on capital).

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We are also pro-actively working with the broader DFI community to share learnings and expertise as well as due diligence on specific funds. As a first step to greater collaboration, in December 2017 we organised the inaugural DFI Venture Capital Forum.

HOW DFIS CAN ADD VALUE TO VENTURE INVESTMENTS

We believe there is an opportunity for the DFI community to help shape the development of the Africa venture market. DFIs can plug market gaps and anchor key venture funds, ensuring that there is sufficient capital to fund start-ups across the whole continent. We can mobilise capital from within the DFI community and from institutional investors to ensure that fund managers are able to meet their target fund sizes.

We believe there is also a significant opportunity for value additionality. Whilst there are experienced individual VCs in Africa, few managers have experience of building a venture firm, constructing a portfolio and dealing with institutional investors. This is clearly an area in which DFIs can help provide guidance. We can help install high standards of governance within funds, and their underlying portfolio companies. We think there is also potential to leverage our networks in Africa to help identify future employees, advisors and board members.

“At CDC we also plan to use our networks within the US/EU venture capital community to raise awareness of African VC within the broader VC industry, mobilise follow-on capital for later-stage companies and help transfer key learnings and expertise from the US to Africa.”

“Whilst there are experienced individual VCs in Africa, few managers have experience of building a venture firm, constructing a portfolio and dealing with institutional investors.”
A vibrant African start-up scene, though still in its infancy

Unicorns are concentrated in the United States and China

Africa only has 1 member in the highly select club of 174 unicorns identified throughout the world, i.e., Jumia.

1. Based on constantly evolving data provided by The Wall Street Journal in early 2018. The above map is not exhaustive.

Internet penetration rate by continent

Unicorns are unlisted start-ups, mainly operating in the tech sector with a valuation of at least US$1 billion.
Venture capital in Africa: a nascent sector with a bright future

In 2017, African venture capital operations only represented 1% of transactions completed throughout the world and 0.6% of total investment in the sector.


Venture capital in Africa: a large degree of asymmetry

Based on available data, there is a large degree of asymmetry in terms of both geography and investments sectors. 80% of funds raised in 2017 mainly went to three countries – South Africa, Nigeria and Kenya.

Focus on 12 African countries

In 2017, African start-ups raised a record $556 million. Nigeria, South Africa and Kenya have a more advanced support ecosystem (funds, incubators, accelerators, regulatory environment, etc.) than other countries on the continent.


The amounts shown on the map are in US$ billions

The main sectors financed by venture capital in Africa

In 2017, the three main sectors financed by venture capital in Africa are fintechs, off-grid solar power and e-commerce. Strongly represented in the United States, Asia or Europe, the artificial intelligence (AI) or biotechnology sectors are still lacking on the continent.


The financing life cycle of a start-up

Source: Proparco; Vernimmen; Wikipedia Commons, 2018.
Supporting digital innovation ecosystems: what role for DFIs?

Christine Ha, Digital & ICT Project manager, AFD

When it is properly supported, digital innovation can act as a powerful catalyst for achieving sustainable development goals (SDGs). Innovation dynamics are very important in Africa and play a key role in devising sustainable inclusive solutions tailored to the context of these countries that provide people with access to basic goods and services that are currently of a poor standard, such as energy, education and healthcare. But digital innovation needs to be nurtured in a continent where support structures and seed financing are very rare commodities. In this context, development institutions are in a position to stimulate investment, bolster support structures and support human capital development in specialised areas.

FOCUS

AFD

AFD is an inclusive public financial institution and the main actor in France’s development policy. It makes commitments to projects that genuinely improve the everyday lives of people, in developing and emerging countries and in the French overseas territories. AFD works in many sectors – energy, health, biodiversity, water, digital technologies, training – and supports the transition to a safer, more equitable and more sustainable world: a world in common. Its action is fully in line with the Sustainable Development Goals (SDGs).

Through its network of 85 agencies, AFD operates in 109 countries and is currently supporting over 3,500 development projects. In 2017, it earmarked EUR 10.4bn to finance these projects.

The digital transition is a gilt-edged opportunity to achieve sustainable and inclusive development. Innovative digital apps can provide vulnerable populations with access to essential goods and services. For example, “mobile money” enhances access to financial services, “pay as you go” can facilitate the purchase of such things as solar energy, “mobile health” can help deploy remote diagnosis solutions *inter alia*.

In many domains, these digital solutions are enabling sectors to develop by leapfrogging some of the stages they had to go through in developed countries. These innovations are frequently deployed by start-ups who have been able to transform the constraints specific to their operating environment into value-creating opportunities.

SHORTAGE OF SUPPORT AND ACCESS TO FUNDING

Nevertheless, these successes mask the challenges facing the vast majority of entrepreneurs, particularly in Africa. According to a study carried out by the firm of Roland Berger for Agence française de développement (AFD/Roland Berger, 2017), start-up momentum in Africa is weak when compared with elsewhere. There are only 0.3 start-ups per million people in Sub-Saharan Africa, 9.6 in South Africa, and 1.3 in Morocco – versus 43 in France. This discrepancy is due to the dearth of support structures and seed funding for start-ups. It is during this key phase (diagram opposite) – considered highly risky by investors – that support and seed financing are crucial for transforming an innovative idea into a marketable product.

In order to develop and grow, start-ups generally need structures that can partner them in each phase of their development. The support structures in question, just like coworking spaces, are gradually emerging across Africa, however the incubators and accelerators that offer more comprehensive support are not nearly up to speed yet. They are struggling to get off the ground due to a lack of both public and private sector support.
However, aside from the dearth of support structures, the number one problem facing African entrepreneurs is scarce funding: 87% of project backers consider this to be very difficult to obtain. The collateral required, coupled with the high interest rates charged by African banks are often insurmountable barriers. Alternative sources of finance such as crowdfunding, business angels, venture capital or seed funding remain very limited in their scope and concern very few projects. Private equity in Africa is often focused on growth capital, mostly for well-established SMEs, and specialised seed or venture capital funds are virtually non-existent outside of South Africa.

Development institutions can be catalysts here and encourage governments to set up digital investment programmes for example, or spearhead initiatives to finance start-ups and help structure the various stakeholders and initiatives while continuing to strengthen the sector, especially in terms of human resources.

“South Africa, Nigeria and Kenya absorbed 80.3% of investment, followed by Egypt, Ghana, Morocco and Rwanda.”
ENCOURAGING PRO-DIGITAL INVESTMENT

Broadband access and 3G or 4G mobile coverage – which make it possible to distribute digital services – will be one of Africa’s key challenges over the next 10 years. According to the International Telecommunication Union (ITU, 2017), only 22% of Africans currently use the net. As well as boosting network coverage, Africa also needs its own resources – particularly servers – to cut network access costs and develop local content and services that are adapted to the needs of local populations. Investing in digital infrastructure is the first step in placing Africa on the road to more inclusive and sustainable social and economic growth. These capital-intensive projects could be co-financed by development institutions.

In addition to developing digital infrastructure, innovation funding needs to be diversified and made more accessible. To be sure, the number of African start-ups that have managed to raise seed funding (for the start-up phase) and venture capital (for the development phase) grew by 17% between 2015 and 2016. They managed to raise US$ 129 million in 2016, of which more than 24% went into fintech start-ups (i.e., financial technology start-ups). South Africa, Nigeria and Kenya absorbed 80.3% of investment, followed by Egypt, Ghana, Morocco and Rwanda. Nevertheless, the portion of start-ups that are being funded remains small: only 3.6% of African tech start-ups that looked for seed or venture capital funding in 2015 actually managed to raise any, even though the funding potential should reach US$ 1 billion by 2020 (Partech forecast). Furthermore, the business angels who are present in very small numbers or in an unstructured form only concern very small numbers of projects and crowdfunding is struggling to take off due to an ill-adapted regulatory framework.

Better access to funding for African start-ups is therefore a key imperative. As a development institution, ADF needs to support conditions that open up and enhance market attractiveness and financial backers can do this in a number of different ways. They can for example participate in seed or venture capital funds or encourage investment through risk pooling mechanisms that benefit funds and finance institutions. They can also deploy enterprise support initiatives like interest-free loans, similar to those provided by the Afric’Innov fund supported by AFD.

BRINGING STAKEHOLDERS TOGETHER AND SUPPORTING HUMAN CAPITAL DEVELOPMENT

As proof of the dynamism of the sector, numerous innovation initiatives are taking off across the Continent with the backing of a whole host of institutional and private stakeholders and associations. However, these stakeholders, often working alone, are struggling to get start-ups off the ground and it is absolutely essential to bring innovation ecosystems together in order to structure them and consolidate their action. And here again development institutions can be of help by facilitating exchanges and sharing best practices between different players and by structuring networks of mentors and business angels. They can also help create an environment and regulatory framework that is more conducive to enterprise and research. This support, which can take the form of funding or technical assistance, is absolutely indispensable for unlocking the full potential of digital innovation.

Human capital development is also essential for digital innovation. By 2025, it is estimated that Africa will need 30,000 IT engineers and 120,000 developers so there is a big need to boost under-graduate expertise in computer technology. Development institutions can help out in a number of ways: supporting higher education institutes that wish to develop enterprise programmes, creating technical learning

REFERENCES
programmes (i.e., web and mobile development, UX and UI design, data, architecture and cloud computing), or setting up coding schools (similar to French schools such as Simplon, École 42 or WebForce3).

A number of institutional funds have launched digital innovation support programmes in Africa: “Boost Africa” (African Development Bank and European Investment Bank), “Startup Catalyst” (World Bank), and “Challenge Funds” (Swedish international development agency). In a similar vein, AFD Group has launched the annual “Digital Africa” awards (box below) which single out African start-ups that have come up with innovative pro-development solutions, and “Fonds Afric’Innov” which gives support to entrepreneurs in the start-up phase. AFD is also throwing its weight behind several operators and stakeholders in development infrastructure and digital solutions and investing in a number of venture capital-type projects through its subsidiary Proparco.

The digital economy is one of the few sectors in which Africa has succeeded in bridging the gap with developed countries and African development is now intrinsically bound up with this sector. The digital innovations being deployed by start-ups have transformed business models and value chains while also fostering greater inclusiveness through innovative tailored solutions. Based on its strong market growth potential – e-commerce contributed US$ 18 billion to African GDP in 2013 and this is set to top US$ 300 billion by 2025 – the digital economy is synonymous with hope, particularly for African youth. Partnering digital innovation across the Continent means providing Africa with the resources it needs to tackle economic challenges for years to come.

**The Digital Africa Challenge**

Since 2016, “Digital Africa” has been awarding an annual prize to African or French start-ups that make a significant contribution to African development by coming up with innovative solutions. It is organised jointly by AFD, Bpifrance and FrenchTech and it showcases the best digital innovation talent in Africa – or working for Africa. The competition is open to African and French entrepreneurs with projects in the start-up or creation phase that are targeting the African Continent. Every year, it rewards a short-list of 10 start-ups (five African and five French) by showcasing their projects and giving them access to the support of the French and international digital ecosystem to help them get their solutions to market. With nearly 550 applicants in 2016, and more than 750 in 2017, the awards are an unqualified success. Here is the list of the winners for 2017:

- **Etudesk (Côte d’Ivoire):** Etudesk is an e-learning platform that provides students, job-seekers and workers with business-type courses that enhance their professional skills.
- **Ville Propre (Morocco):** Ville Propre (or Clean City) is a mobile social app that aims to help clean up polluted urban areas and maintain them to the standards expected by local inhabitants.
- **Tuteria (Nigeria):** Tuteria is an online platform that puts people wishing to learn into contact with local experts who have been “peer-verified” by their communities.
- **LishaBora (Kenya):** LishaBora provides inputs and practices and co-manages products for Kenyan smallholder dairy farmers. This start-up also provides fodder management and general farming services and helps unlock access to bank loans and credit.
- **Volkeno (Senegal):** Volkeno is developing a distance learning device for studying new technologies, even when there is no internet connection, for the ultimate purpose of facilitating the professional integration of young people.
**Case Study**

**Why and how does Orange finance innovation in Africa?**

**Grégoire De Padirac, Investment manager, Orange Digital Ventures (ODV)**

Africa is on the move”, stated Barack Obama during his visit to Kenya in 2015, pointing out the spectacular digital revolution in the country of his ancestors. This revolution in Africa is mainly mobile. These major changes are based on mobile phones and their most simple technologies (SMS, USSD, etc.). It is commonplace to mention this “leapfrog”, which makes it possible to bypass shortcomings in infrastructure with mobile services for financial inclusion, energy supply, education, healthcare, etc. This has already resulted in success stories, such as Jumia, Interswitch, M-Kopa Solar, Andela, etc. This is precisely the gamble taken by Orange in making Africa a real growth driver. The Group today operates in 21 countries, has over 121 million clients, a turnover of EUR 5.2bn and a headcount of 20,000. More than one African in ten benefits from Orange’s services.

While this revolution is based on the investments made by operators, it is especially the new generation of entrepreneurs which is giving the continent all the momentum it is currently gaining. An operator is a special player in this ecosystem. It is central to the process. Beyond its network, it is the gateway to the market, whether via its communication and billing interfaces (its API, or application programming interface) or, more simply, its network of retail outlets. Few players in Africa have a distribution network as extensive as an operator like Orange. Indeed, we have over 700,000 retail outlets on the continent.

Africa, which has already experienced some entrepreneurial success stories, is powering up and seeing the emergence of a new generation of entrepreneurs in innovation. However, digital Africa still focuses on a few epicenters, which receive the bulk of venture capital finance. The challenge will lie in repeating the Nigerian, Kenyan and South African successes in other regions on the continent.
BUILDING CLOSER TIES BETWEEN THE TELECOM OPERATOR AND THE STARTUPPER: A STRUCTURAL CHALLENGE

To reinforce its position as the African leader in the digital transformation, it was essential for Orange to include partnerships with innovative start-ups in its DNA. Innovations have gathered such a pace that the myth of the almighty power of large groups has been largely debunked, including on the continent.

But being a natural partner of entrepreneurs is not a matter of course and requires two major changes, which the Group has made. Firstly, remedy a certain mistrust on the part of entrepreneurs for which the operator appears to be an inaccessible contact, yet is sometimes key to their scaling up. Secondly, the corollary is to overturn the culture of partnerships with start-ups in-house, via initiatives which facilitate the establishment of relations and decision-making. More generally, it involves taking a less defensive approach that is more open to co-creation. All this has been done in the context of the Group’s various Open Innovation programs. It is a challenge faced by all large companies and especially in French-speaking Africa, where there is still the widely predominant feeling that strength is measured by the rigor of procedures.

Consequently, to address these issues, Orange has managed to build up a series of Open Innovation initiatives over the years. To name but a few flagship initiatives: training (Sonatel Academy with Simplon in Dakar, a Master’s to train data scientists in Abidjan in partnership with the polytechnic school and INP-HB), acceleration with the four Orange Fabs in the MEA zone, the social entrepreneur award, the partner incubators (CTIC, CIPMEN, etc.), the Orange Partner and Bizao programs to open access to the Group’s APIs and, recently, investment in start-ups. Indeed, investment is a particularly effective tool for improving the Group’s capacity to “connect” with innovative actors. This is both because it meets a simple and practical need of companies, and because they are decisions which can be made rapidly, as long as there is appropriate governance. Finally, it is often a sound basis from which to build sustainable partnerships.

“ Innovations have gathered such a pace that the myth of the almighty power of large groups has been largely debunked, including on the continent. ”

“The positive dynamics for investors on the continent are continuing, in particular with the announcement of the creation of new funds, like Partech Africa […] or Tlcom Africa Fund.”
CREATE A FUND FOR INNOVATIVE AFRICAN START-UPS

This is what the initiative of Orange Digital Investment (ODI), the Group’s strong arm in digital investment, is all about. Indeed, Orange Digital Investment covers three types of activities: Orange Digital Ventures (ODV), which directly invests like a venture capital fund in minority tickets in early-stage start-ups in the context of appropriate governance, with a presence in Paris, London and, since recently, Dakar; investments in funds of funds: Iris Capital, Partech Africa, Paris Saclay Seed Fund, etc.; and more late-stage corporate venture investments (strategic digital monitoring and equity investments, such as Jumia, Deezer and Dailymotion).

In June 2017, during the Afrobytes conference, Pierre Louette, Deputy Chief Executive Officer of the Group and Chairman of Orange Digital Investment, announced the launch of Orange Digital Ventures Africa (ODVA), a EUR 50m fund based in Dakar dedicated to African start-ups. Through this new initiative, Orange has completed its system with a specifically African program. Investments in start-ups with activities related to the continent (or adapted to this market) had already been made by ODV, such as Afrimarket, Afrostream and PayJoy. However, given the opportunity offered by Africa and our ever-increasing commitment to support its digital emergence, it was necessary to scale up in order to fully grasp the opportunity related to this African digital revolution.

Consequently, ODVA is investing up to EUR 3m for a first round, following the start-up rounds, with the capacity of following in the subsequent rounds. The investment themes are in line with the Group’s strategic priorities in the zone: fintech, eHealth, energy, agritech, govtech, edutech, etc. Our investment strategy is to leverage our assets in Africa (client base, distribution network, API, Orange Money…) in order to support start-ups which have already experienced strong growth in their domestic market and aim to rapidly go international.

It all involves becoming, through investment, a fully-fledged player in the digital revolution by being a partner of the future pan-African champions of tomorrow, whether they are based in Africa or elsewhere. The presence of the fund in a French-speaking country makes it possible to reach territories where there are a wealth of opportunities and which are often neglected by international investors. Orange Digital Ventures aims to combine the best venture capital with the best assets of a large group like Orange. Consequently, as an investor, ODV has the objective of maximizing the financial return, but also aims to create strategic value for the Group, to accelerate sustainable partnerships with innovative actors or, more simply, the learning process for new economic models, new products or technologies. For ODV, it is a way of providing strategic value to the entrepreneurs it supports. ODV also ensures that it maintains a barrier between the investment team and the rest of the Group in order to avoid conflicts of interest, the circulation of sensitive information, etc. Finally, ODV is an evergreen fund which styles itself as a long-term financial partner, unlike other more traditional investors.

“Our investment strategy is to leverage our assets in Africa [...] in order to support start-ups which have already experienced strong growth in their domestic market and aim to rapidly go international.”
AFRICA AS A NEW FIELD FOR INVESTMENT IN INNOVATION

The positive dynamics for investors on the continent are continuing, in particular with the announcement of the creation of new funds, like Partech Africa (of which Orange is one of the partners) or Tlcom Africa Fund (TIDE). An instructive comparison with India clearly illustrates Africa’s potential: a relatively similar population (for Africa and India, 1.2 and 1.3 billion inhabitants, respectively) and a GDP equivalent to USD 2,300bn. Yet Africa’s mobile penetration rate is double that of India (46% against 22%), but in comparison Africa’s start-ups only raised EUR 366m in 2016, according to Partech, against EUR 4bn for Indian start-ups over the same period. This clearly illustrates the growth prospects we could expect for the continent’s digital ecosystem. Pending the confirmation of these dynamics by emblematic “exits”, it is today that we need to support the “gazelles” of tomorrow.

However, this optimistic description should not hide the fact that digital Africa remains very scattered between just a few hubs mainly based in English-speaking Africa. One of the main questions that remains is how to reproduce the Kenyan, Nigerian and South African digital dynamics in other regions, in particular in French-speaking Africa which is sorely lagging behind. The example of the Kenyan model underscores the role that the traditional operator played in the emergence of its digital ecosystem. Indeed, the successful launch of a mobile money range of services and the opening of its APIs played a key role by giving entrepreneurs the means to invent new services. Orange has taken this route with optimism. There are still just a few ingredients missing for the digital French-speaking Africa to actually emerge (seed funds and business angels, accelerators, proficiency in languages, etc.), but there are sound bases: a huge market of 120 million people in 24 countries, connected and well-trained young people who increasingly aspire to be entrepreneurs in innovation, monetary stability, previous entrepreneurial success stories (Intouch, Wari, Afrimarket, etc.), and a generation of “repats” (a population from the diaspora, educated in Europe or the USA, which settles on the continent) with a wealth of expertise, international networks and enthusiasm for achieving its “African Dream”. ■

**Comparisons between India and Africa**

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<tr>
<th>Parameter</th>
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<td>GDP</td>
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<td>Mobile phone penetration rate</td>
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<td>&gt; 22%</td>
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<td>Funds raised by start-ups in 2017</td>
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CASE STUDY

Supporting start-ups in Africa: Schneider Electric’s approach

Christophe Poline, Sustainable Investment Director, Schneider Electric

In Africa, Schneider Electric implements a strategy based on supporting innovation, by taking a commercial approach tailored to people’s needs, managing two specialized impact funds which focus on social innovation, and supporting local capacity building.

Africa will have two billion inhabitants by 2050, i.e. a quarter of the world’s population. Half of them will be aged between 15 and 30. The continent will need to address a number of challenges, including climate and energy challenges. In 2016, out of the 1.06 billion people who did not have access to electricity, over half (588 million) lived in Sub-Saharan Africa (IEA, 2017). This figure could reach 645 million by 2030.

Consequently, if we expect to resolve global energy problems, specific action is required in Africa. There is a need to increase the energy supply, a prerequisite for its development, without exacerbating climate change, which already seriously affects the continent. Achieving this requires both developing renewable energies and deploying energy efficiency solutions.

Working for the development of a sustainable economy in Africa by promoting innovation also allows Schneider Electric to position itself in an expanding market. By supporting local entrepreneurs and taking part in the development of innovative projects, the Group is seeking to be at the forefront of social and technological innovation, while contributing to building new economic models. Schneider Electric’s objectives in Africa are implemented in the context of its energy access program, which comprises three complementary areas.

FOCUS SCHNEIDER ELECTRIC
Schneider Electric, a leader in the energy transition, aims to give companies the capacity to address the energy and climate challenge, while taking action to make energy accessible to all. For example, the Group has undertaken to promote the implementation of lighting solutions and means of communication for 50 million poor people over the next ten years, while supporting – via the Schneider Electric Foundation1 – access to high-quality education for all.

People without access to electricity

1. Under the aegis of Fondation de France.

1.06 BILLION PEOPLE throughout the world

including

588 MILLION PEOPLE in Sub-Saharan Africa

PRIVATE SECTOR & DEVELOPMENT
DEVELOPING A SELF-FINANCED COMMERCIAL APPROACH

In Africa, Schneider Electric markets products and solutions which primarily target rural communities. This range of services comprises individual solar systems (portable lamps to recharge mobile phones), individual electrification solutions (solar home systems – SHS) or collective systems (decentralized micro solar power plants, water pumping and solar lamps) to meet the needs of households, public services and companies.

The development of this commercial part of Schneider’s activities in Africa is based on its self-financing capacity. Trade margins are calculated to allow all the costs to be covered, while providing consumers with an affordable price. This “inclusive business” component also contributes to the deployment of innovations thanks to the payment terms it grants, which allow pilot projects to be prefinanced or distribution grids to be created.

SUPPORTING INNOVATIVE START-UPS VIA IMPACT FUNDS

To support innovation in Africa, Schneider Electric initially created impact financing tools. In 2009, the Group set up one of the first impact funds led by an industrial group, Schneider Electric Energy Access (SEEA). In 2015, it continued this policy with the creation of Energy Access Ventures (EAV), the first impact fund including an industrial group and development banks (EIB, CDC Group, PROPARCO/FFEM, OFID, and recently joined by FMO).

The SEEA fund supports companies that fight against the energy divide in Europe, Africa, and now in Asia. This EUR 7m vehicle is today supporting eleven innovative companies, generally in the start-up phase, and provides them with financial support and technical assistance to allow them to successfully scale up. The EAV fund, for its part, is specialized in access to electricity in Sub-Saharan Africa with much more substantial resources for operations (EUR 75m), allowing it to contribute to the development of the six companies supported since it was set up.

While social innovation determines the choice of the projects supported by the fund, their economic dimension is, of course, taken into account. For example, SEEA was one of the first investors in Fenix International (box below). The fund also supports technological innovation. The funded companies have spearheaded the deployment of Pay-As-You-Go models, for instance. A number of start-ups are seeking to exploit these innovations. For example, cooperation between telecommunications companies and energy start-ups today allows mobile payments, microinsurance and access to weather forecasts for farmers.

Fenix International

This company is today one of the main players on the domestic solar systems market in Uganda. It is currently expanding its business to Zambia and Côte d’Ivoire. Fenix has a significant social impact. For example, over 100,000 solar systems have been sold and benefit one million people, which has allowed them to “avoid” USD 8.8m of spending. With the takeover by Engie, Fenix is going to be able to continue its development. The SEEA fund has played the role of an “accelerator” for this company by investing right at the start of the project.
BUILDING SKILLS BY SUPPORTING TRAINING

A training program completes the strategy to support innovation in Africa. While only three million young Africans a year find a job (out of 10 to 12 million who enter the job market every year), activities in the energy sector offer them stable opportunities.

Consequently, to address the current lack of resources and technical skills at local level, the Schneider Electric Foundation supports actors in vocational training for energy activities and entrepreneurship: marketing, sizing, installation, maintenance, operation of electrical installations. Over 140,000 people have been trained in electricity activities and 950 entrepreneurs have been supported since the program was set up – the objective for 2025 is to reach one million people trained and 10,000 entrepreneurs supported.

INNOVATION IN AFRICA: WHAT PROSPECTS?

Finally, the local reinvestment of financial flows needs to be promoted. Today, the financial flows from developing countries which are directed towards industrialized countries far exceed the amounts earmarked for development assistance.

To strengthen innovation in Africa, beyond the support for training and the action of the impact funds, Schneider Electric promotes new strategies and new ways of working. For example, if energy players located their production in Africa rather than in China, the continent would have new sources of income, which would strengthen its autonomy. Indeed, the sustainable development of Africa necessarily requires its empowerment.

Furthermore, priority needs to be given to social entrepreneurship (where economic efficiency is at the service of a social mission), impact investment (where both financial and social returns are sought) and training, so that local expertise can take ownership of technological innovations.

Finally, the local reinvestment of financial flows needs to be promoted. Today, the financial flows from developing countries which are directed towards industrialized countries far exceed the amounts earmarked for development assistance. Since 1980, the equivalent of GDP in the USA – i.e. USD 16.3bn (The Guardian, 2017) – has circulated from the South to the North and the financial interest related to the debts of South countries stands at USD 200bn a year. The fact that the investments made by countries in the North are profitable is not called into question, but certain reforms could, nevertheless, reestablish a more equitable balance for Africa, by promoting the local reinvestment of financial flows. Indeed, financing for innovation in Africa – a need given the challenges mentioned above – should also be financing for innovation for Africa.
From the dream of a cashless Africa to a constantly expanding start-up: the Zoona story

Mike Quinn, CEO, Zoona

Founded in 2009, the Zambian start-up Zoona is now in full expansion. Like all venture capital-backed start-ups, Zoona has been through its fair share of ups and downs. Its founder Mike Quinn gives us his personal account of these decisive steps.

In February 2012, I wrote a lengthy essay called “My Mobile Transactions Story” which detailed my start-up journey from stumbling upon founding entrepreneurs Brad and Brett Magrath to closing a $4 million Series A venture capital investment. I shared many of the challenges we overcame to achieve that milestone. It’s now six years later and that story is due for an update.

THE DREAM OF A CASHLESS AFRICA

One night in Lusaka, Brad was out with an American colleague from USAID talking about his vision when the spark occurred. He sent Brett the ‘now-famous’ text message that he had an idea for their next venture and that it was going to be big. A few months later, the brothers had a $200k grant from USAID to launch a pilot to digitize cash payments in the cotton sector. At this time, it was common to see trucks full of cash with armed guards carrying AK-47s driving down horrible rural roads.

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In the beginning, there was Brad and Brett, two entrepreneurial brothers from Kitwe, Zambia, who dreamt of a cashless Africa where companies, small businesses and consumers conducted all of their business via mobile transactions. Brett was in his early thirties, married in Cape Town after quitting his cushy job at JP Morgan in London, while Brad, several years older, was married in Zambia and looking to get off the corporate ladder. They tried a few ventures that all started out promising but left them both broke and nearly broken.

In Lusaka, Brad was out with an American colleague from USAID talking about his vision when the spark occurred. He sent Brett the ‘now-famous’ text message that he had an idea for their next venture and that it was going to be big. A few months later, the brothers had a $200k grant from USAID to launch a pilot to digitize cash payments in the cotton sector. At this time, it was common to see trucks full of cash with armed guards carrying AK-47s driving down horrible rural roads. An international cotton company invested in the brothers, they applied for and received a Bank of Zambia payments’ license, and they set up a company called Mobile Transactions.

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While this was happening, I was completing my MBA at Oxford where I was a Skoll Scholar for Social Entrepreneurship. I had previously spent 2.5 years as a volunteer in Ghana and Zambia with Engineers Without Borders Canada and completed a MSc in international development at the London School of Economics. I was hungry to get back to Africa where I wanted to be an entrepreneur and have an impact but I too was broke and saddled with student debt. I first convinced my fiancé to take the plunge and move to Zambia with me on a whim, and then an early stage investment fund to buy me a plane ticket to search for entrepreneurs to invest in. I sent one email to an American colleague from USAID I knew from my volunteer days (thankfully the same one who knew Brad!) and the day after I arrived in Zambia, I was face to face with Brad and Brett and hearing their inspiring vision.

A year later I found myself asking my retired parents in Canada to mortgage their house and wire $100 thousand dollars into a Zambian bank account to save the company from bankruptcy and become a partner in the business. With an ultimate leap of faith, they said yes, after which Brad and Brett made me CEO to lead the company into its next phase. My first move was to convince my MBA colleague Keith Davies to quit his investment banking job and cash in his pension to join us as our CFO. The future was bright.

Only it wasn’t – not yet, at least. A few months later we had burnt through all of our cash (again) and lost a major contract that was the source of most of our revenue. We were left scrambling again but managed to raise some convertible debt to survive a little longer and also buy out our corporate shareholder. We finally had some runway and took advantage of it to raise a Series A investment. We signed a $4m term sheet with Omidyar Network and Accion at the end of 2011 and closed the deal in February 2012 with feelings of great relief and accomplishment.

“As Nelson Mandela once said, “After climbing a great hill, one only finds that there are many more hills to climb.” He couldn’t have been more correct. If the beginning was about not running out of cash, the middle was about how to build a business. Our agriculture payments’ product had failed as the demand for cash was too high from small scale farmers and we had not yet cracked the supply side. Meanwhile, we were inspired by the exponential rise of M-Pesa in Kenya and pivoted into building a franchise agent network to allow Zambians to send and receive money within the country. But unlike M-Pesa, we didn’t have a customer base, a distribution network or a brand to launch from, and had to start from scratch.

What we did have, though, was purpose and perseverance. We selected young entrepreneurs as agents, treated them as our core customers, and invested in the most promising ones to expand to more outlets. We also rebranded from the functional “Mobile Transactions” to the meaningful “Zoona”, which translates to “It’s real” in Zambia. Our model spilled into Malawi while we built a customer service and technology centre in Cape Town to support both markets.

“FOCUS ZOONA
Zoona is an African FinTech business that helps communities thrive. Since launching in 2009, Zoona has grown to an active customer base of 2 million consumers with 3,000 agents in Zambia, Malawi, and Mozambique and has processed over $2 billion in transactions. In 2015, the Nike Foundation and Unreasonable Institute selected Zoona as one of the world’s top start-ups for helping girls out of poverty based on a microfranchise model that empowers girls and young women to become entrepreneurs.

A year later I found myself asking my retired parents in Canada to mortgage their house and wire $100 thousand dollars into a Zambian bank account to save the company from bankruptcy and become a partner in the business.”
The results started to show. We started achieving exponential growth with new customers turning into repeat users and agents expanding to more and more outlets. Some of our top agents grew to employ dozens of people and transact with over a million dollars per month. We also achieved the milestone of a million active customers and turned profitable as a group. Once again, the future was bright.

But then came the great Zambian currency crash of 2015. The copper price slid downwards following a sharp reduction in demand from China, which hit the Zambian economy hard. The currency depreciated by half in a three-month period, and so did our revenue while our expense base in Cape Town was fixed. This led to a difficult period of consolidation, but we managed to pull through it and raise a $15 million dollar Series B investment led by the IFC in 2016 to start growing again.

Since then, we have scaled up our team, invested in preserving our entrepreneurial and purpose-driven culture, and expanded our agent network. We have also developed new products, including payouts of international remittances from South Africa with Mukuru as a partner, airtime and utility payments, and our own mobile wallet and digital storage product for customers to keep their money safe. Our customer base has reached 2 million active users who transact over $60 million per month at our 3,000 agents, and we are poised for our next phase of growth.

“I'M MORE PASSIONATE THAN EVER TO FULFILL ZOONA'S MISSION”

Where will my Zoona story end? Once the problem is solved. There are currently three billion people in the world who lack access to or who are underserved by the formal financial service sector. I’m more passionate than ever to fulfill Zoona’s mission of helping communities thrive and achieve our wildly important goals: build products and services that improve people’s financial health and well-being of one billion people; unleash emerging entrepreneurs to create profitable businesses that create one million jobs; prove that a purpose-driven business can be a global model for growth and impact.

Zambia and Malawi are our starting points where we want to go deep and fully prove our model. Once we do, we plan to expand to achieve Brad and Brett’s original dream of a cashless Africa. As we say at Zoona: Let’s make it real.
“I’m hopeful about emerging companies entering the world of venture capital-backed start-ups”

Grant Brooke, Co-founder and CEO of Twiga Foods

Twiga Foods is a B2B marketplace platform that sources produce – initially only bananas – from farmers at above-market prices and delivers them to retailers at below-market prices, accomplished through technology and economy. Core values have provided guidance in building this business differently and in its context. Today, Twiga is Kenya’s largest logistics-serviced seller of fresh produce.

Three years ago, on the stage of an international pitch competition, I stood in front of judges and a thousand entrants with a single PowerPoint slide of a banana, which simply stated “This is a Banana”. Its simplicity got a big laugh.

A few months prior to this event, Peter Njonjo and I had launched Twiga Foods: a B2B marketplace platform that sources produce from farmers at above-market prices and delivers them to retailers at below-market prices. Vendors no longer have to walk to large-scale open-air markets at 4 am; instead, we deliver better-quality products, at lower prices, to their doorsteps. Farmers can stock their products on Twiga, and have a persistent and predictable market partner. We accomplished this through technology and some economics rules. The reason prices were high is that the retail sector is very fragmented – 96% of African commerce occurs in SME shops. The way to solve this was to get a number of retailers onto a single platform for just one product to start: bananas. For farmers, this meant a reliable market in an agricultural sector that is rife with market uncertainty.

The service proved extremely popular, and has now scaled beyond bananas. Today, Twiga is Kenya’s largest seller of fresh produce, as we have become the digital commodities market we set out to build, with logistics as a service beneath. In a country where 42% of consumer spending is on food, it’s a massive problem to tackle.
I’ve always wondered what a venture capital LP meeting would be like for a VC when they explain that they are investing in a Nairobi-based company that, on the outside, looks like a tech-based banana distributor. Africa’s challenges and opportunities are remote from the realities of most VCs and LPs: thus, these could look strange to the world’s venture capitalists. Bridging this gap is the core job of an early-stage CEO.

TACKLING PROBLEMS

Not only do Africa’s venture-backable challenges look different from what many VCs are used too, its most successful venture companies also look strange to many VCs. Entrepreneurs cannot easily satisfy preconceived notions of venture-backed businesses, while solving problems in a scalable and sustainable (and profitable) way. This is why so many international companies and well-funded cookie-cutter models have failed on this continent: these businesses have been removed from their contexts.

So, I would like to explain how our core values – Own Your Problems, We Sell Bananas, and Be Good – are guiding us in building a business differently and fully in its context.

OWN YOUR PROBLEMS

“Own your Problems” is fundamental to the Twiga business design: we do not outsource core business functions. That would simply be too risky at this point. We do not easily trust outsiders, consultants, brokers, contractors: in our experience they will let you down more often than not. While it is great to have ecosystems where you can outsource 50% of your work to preexisting providers, I have a giant list of examples showing that is not the case here. Hence, if you can control it, control it.

Buy assets: When we started, finding a lorry to lease in Nairobi meant walking down the highway, picking them out of a queue and negotiating. Over time, we learned that it was easier and more capital efficient for us simply to buy vehicles. We have found as we have scaled that more options have emerged to take them off our balance sheet. Fadi Ghandour, founder of Aramex and one of our board members, gave me some good advice on this: ‘Whatever the finances say, you’re going to be the one managing the vehicles.’
The “buy high, sell low philosophy”: We made a commitment early on to pay farmers more and sell to vendors for less. This meant customer acquisition was not a challenge, but our ability to execute on our promise was. Choose your battles carefully, and be sure of winning them. Know your unique selling point (USP), and use it.

Make oneself redundant: For Twiga there is not a preexisting talent pipeline. Nobody had built Twiga before. We are one of the few organizations where making oneself redundant is a key performance indicator. We try to grow people into new layers of management that are always ready. Making oneself redundant is how to grow the organization.

BE GOOD

Where the easy thing to do is the wrong thing to do, do the right thing. While we have faced challenges in the near term, I am thankful we have stuck to this. The first few years of a start-up can be an experience of dodging ethical bullets concerning who invests, who you hire and how you work with government. The company you decide to be when you are small is the company you will be when you are big.

Get arrested: This does not have to be literal, but for us it has been. Several of our senior managers, myself included, have been arrested for defending our staff when they do what is right, generally in refusing a shakedown or a bribe. Take the opportunities to stand for what is ethically right, and that way of working will stick as one of the core cultural stories in your business. As your business grows, your reputation will grow for being a good actor, you will get friends in high places who support your vision, and ethical challenges will become less of a problem.

Create trust: I was once asked whether Twiga was not just the biggest “broker.” Reflecting on it, I realized our biggest USP is being a trusted, good, formal, actor in a market full of informality and uncertainty. What separates us from brokers is we are only interested in the farmers and buyers who want to build long, lasting relations with us, and we design our products around them. In a market full of traders, we are the only ones waking up every day asking how we can make food cheaper.

Kenyan-only hiring: While at times controversial with investors, this principle has been essential in building Twiga. It is hard to call yourself good when you are allowing global inequalities into your business. Foreign developers earning more than locals is not only unfair, but it also creates resentment in your company, and resentment is the single biggest corroder of culture. As we prepare to go international, we will necessarily become international, but the principle of not reflecting inequalities that breed resentment will not.

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WE SELL BANANAS

When in the African eCommerce space players were aiming for tens of thousands of stock-keeping units (SKUs), our banana revenue alone made us one of the largest tech commerce players in Kenya. While we are doing more than bananas now, it is worth keeping in mind that the average Kenyan household buys only about 50 different consumer products a month. To build a unicorn in Africa – a relatively small consumer economy – you had better be in a segment with a lot of spending.

Say no: We are good at saying no as an organization. Lots of people want to partner with us, use us to distribute their products, to build things on our platform, to photo op with us, and so on. We are not easily distracted from our core objective of selling bananas. I was once given the academic advice, “Early in your career, say something specific about something specific, and once you do that, you can say it all.” The same holds for business, do something specific about something specific, and a few years down the line you can do it all.

No advertising: We do not make markets, we make them more efficient. Eyeballs in Kenya are extremely expensive relative to user spend. We have focused on keeping our acquisition cost low (a direct visit and a crate of free produce), our acquisition rate high (92%), and our payment rate short (one delivery). Your USP should be evident without massive spend to convince people.

Stand and deliver: Every Monday, Twiga managers send a pre-read on what they accomplished the previous week, what they will accomplish in the current week, what help they need to get it done, and any topics they would like to discuss.

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I do this once a month in a board meeting, and spend my weeks helping our managers accomplish their ‘stand and delivers’. It is painful, time consuming, often disappointing, but will make you a much better company. The job of a CEO is to create pressure, while at the same time creating safety, two seemingly opposed goals. I do this by being rigorous on structure, but soft in person. Your board needs to do likewise. The repeated check-ins will help to ensure that nobody gets off the core mission; for us, selling bananas.

Our pathway is not the only pathway to success, and we have miles to go. Hence, I am extremely hopeful about the hundreds of emerging companies in this market who will be entering the world of VC-backed start-ups to both create value for investors and, more importantly, build meaningful things for our communities.
There is no doubt about it, Africa is enjoying healthy venture capital-driven start-up momentum. And this impression will be confirmed if you read the articles in this issue. Just one statistic is enough to bear this out: in 2017, African start-ups raised a record US$ 560 million compared with US$ 366 in the previous year.

However, the positive dynamic masks a contrasting situation across the Continent where the three major hubs – South Africa, Nigeria and Kenya – hoover up over 75% of Africa’s total venture capital investment. And, despite the strong growth, these figures are still very low compared with amounts invested in other parts of the world. The parallels that Grégoire de Padirac traces between Africa and India in his article (pages 34-37) speak volumes: despite comparable GDP and populations and African mobile phone penetration rates that are nearly twice as high, African start-ups attracted 13 times less investment than their Indian counterparts in 2017.

Nevertheless, looking to the long term, African entrepreneurs (and the investors who back them) will be able to draw upon the Continent’s considerable strengths. Driven by a young and rapidly-growing population, its market potential is vast and largely untapped. The bulk of the demand focuses on low-cost solutions adapted to poorer populations. Thanks to the latest technology and high mobile phone penetration rates, these solutions can now be distributed at an affordable cost.

So we are not all that far away from witnessing a real take-off in African start-ups. As Michelle Ashworth, venture capital specialist with UK-based development finance institution CDC points out in this issue (pages 22-25), many of the indicators that were apparent in Europe, China and India just before their ecosystems reached maturity are currently present in Africa: African entrepreneurs returning to the Continent after time spent abroad; development of regional hubs; significant increase in transaction volumes; growth in foreign investment, notably from the US; and new funds on the market.

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But despite these encouraging signs, African entrepreneurs are still faced with many problems and it is absolutely essential that all stakeholders are geared up to helping them overcome these. Governments need to put more money into physical and digital infrastructure and create a more conducive legislative environment. As Maurizio Caio of TLcom stresses, the Continent also needs more venture capital funds like TLcom Capital or Partech Africa that will apply
Since 2009, Proparco has coordinated the Private Sector & Development (PS&D) initiative, examining the role of the private sector in southern countries. Issued as a quarterly themed magazine and specialist blog, the PS&D initiative presents the ideas and experiences of researchers and actors in the private sector who are bringing true added value to the development of the countries.

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