Kroll Advisory Solutions

PREPARATION CRITICAL TO COMPANIES INVESTING IN AFRICA

("AKILI NI NDONGE" - "KNOWLEDGE BRINGS REWARDS")

Melvin Glapion, Managing Director, Kroll Advisory Solutions discusses Africa's exciting growth potential.

Africa's economic performance over the past decade has outstripped any previous period, and current forecasts suggest that its economy will grow at about 5.5 per cent in 2012. Armed conflict has significantly reduced, providing the stability required for economic growth and development. State-owned enterprises have been privatised and legal and regulatory systems are being strengthened. Inflation is being brought under control, and foreign debt and budget deficits are being reduced. Foreign Direct Investment (FDI) projects are reported to be up by 27 per cent from 2010. Across the continent, African economies have opened up to international trade.

The accompanying excitement is understandable, both for the countries involved, for whom the benefits are potentially transformative, and for investors, who stand to generate handsome returns. But despite these stellar numbers, there remain lingering concerns that Africa is less stable, more corrupt, and generally riskier than other regions. Are these concerns valid, and if they are what can investors do about them?

BE SURE TO DO YOUR HOMEWORK

As the bleak outlook for domestic growth drives many Western companies to look to expand overseas into unfamiliar markets, these businesses are faced with a set of risks that they may not have encountered in previous transactions. The risk is not confined to the failure of the specific deal in question; the wider fallout may also extend to lasting damage to the investor's

Annual average GDP growth (%)

Country	2011 - 2015
India	8.2
Mozambique	7.7
Tanzania	7.2
Ghana	7.0
Zambia	6.9
Nigeria	6.8

reputation at home. Reasons for failure are many and often relate to bad reputations, exposure to fraud and corruption, undisclosed interests, personality clashes and links to organised crime. This critical information should be uncovered before committing to a transaction.

However, hidden risks are not always identified by legal and financial due diligence. Dedicated profiling should be carried out on the commercial track-record and industry reputation of potential partners and acquisition targets in order to determine whether a particular relationship presents vulnerabilities.

Know your market

Africa is a vast continent, comprising a billion people, speaking over 300 principal languages, and dispersed across 54 sovereign states. This corresponds to a bewildering array of different and often fragmented sets of rules, regulations, stakeholders and markets. This local distinctiveness needs to be fully understood and carefully navigated if investors and their partners are to succeed.

In particular, business models and growth projections need to be closely scrutinised in the light of local operating conditions. Awkward export routes, poor infrastructure (unreliable internet coverage and erratic power supply are common complaints), slow bureaucracy and uneven regional integration patterns can all combine to derail even the most carefully planned commercial objectives.

The political environment, too, requires close attention and specialist assessment. African democratisation is very real, with the one-party state increasingly the exception, rather than the rule. Most African countries have transitioned, or are transitioning, towards some form of participatory democracy. But this has not necessarily led to a more stable investment environment. As Cote d'Ivoire, Kenya and others have shown, election results are frequently contested, overturned, or accompanied by outbreaks of violence. Governments can be fragile, and brief in duration. Institutions can matter less than individuals. Fully understanding where power lies, how it is exercised, and who might bring influence to bear on your partner or acquisition target is necessary to gauge this risk and increase the chance of controlling it.

Know your partner

Inadequate reporting standards, erratic observance of regulation and information opacity make it all the more important that thorough and independent due diligence is carried out on individuals and entities which are being considered as joint venture partners or acquisition targets. Efforts should be made to understand the history of the business and the origins of capital of the founders, the accuracy of asset valuations, the existence of undisclosed beneficial owners and controversial associates, involvement in commercial disputes or litigation, and possible conflicts of interest. For example, in the DRC, investors in the natural resources sector will want to know precisely how a mineral concession was originally awarded; similarly, in the Gulf of Guinea, it will be necessary to go beyond the paper record of the 'local content' participant and identify the ultimate holder of a hydrocarbon block.

A number of prominent cases such as Haliburton/KBR in Nigeria have highlighted the risks of breaching anti-corruption regulations such as the Foreign Corrupt Practices Act and the UK Bribery Act. Many of these cases have resulted in record disciplinary fines. Joint venture partners, suppliers and third parties should be scrutinised to ensure their compliance with international best practice and regulation. Local resources will be required to penetrate beyond the press releases and fully understand a company's activities behind the scenes.

Knowledge brings rewards

All in all, the African investment arena offers an exciting and growing array of opportunities. Whilst widespread reform, improved governance, the commodities boom, increased disposable income, urbanisation and a developing services sector are all contributing to growth, an investor's chance of success is greatly enhanced when their strategy is supported by deep local knowledge, informed market insight, rigorous due diligence and accurate and independently-sourced intelligence.

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