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New Horizons in African Finance

Reducing Risk and Mobilizing Financing on a New Scale

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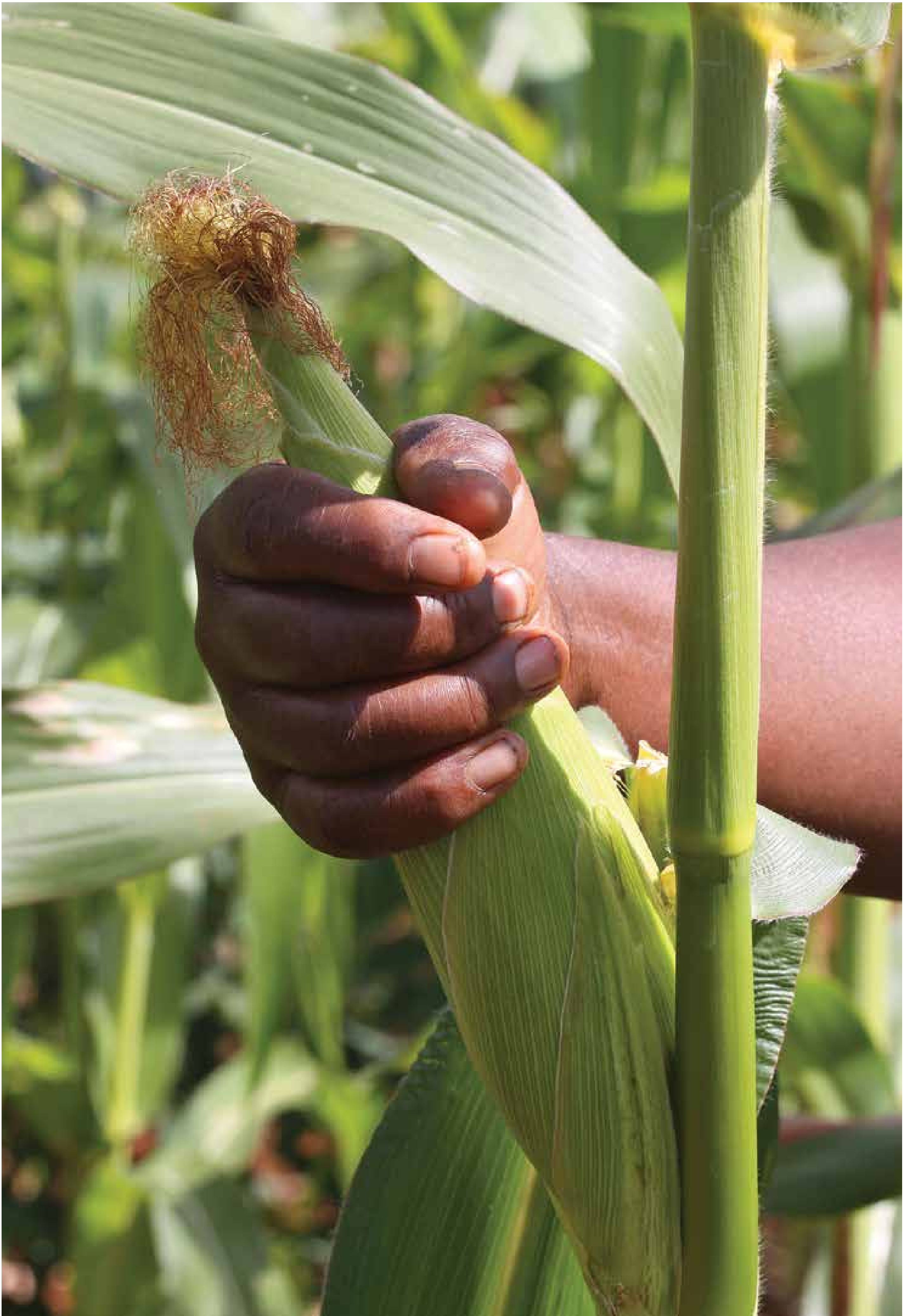

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Executive Summary

Africa is a region with enormous potential for private investors. It is a continent in transition, with rapid urbanization, increasing stability, a young and growing population, expanding internet connectivity, rising incomes, and shifting consumption patterns. Taken together, these enduring trends have created an abundance of commercial opportunities across the continent and turned the region into a place that investors cannot afford to ignore.

Yet declining commodity prices, depreciating currencies and slowing global growth have increased uncertainty on the continent and sharply reduced liquidity that companies had used to expand activities in recent years. Economies face a significant challenge to diversify and export a wider range of goods and services.

Even before recent global economic turmoil emerged, investor activity in Africa was constrained by structural obstacles and a lack of financing options that often inhibited the effective distribution and mitigation of risk associated with large-scale or long-term projects.

Fortunately, companies looking to seize still significant opportunities in Africa can benefit from additional sources of financing, as well as tools that crowd in more private sector participants and mitigate risk, spreading it among different investor classes and over longer timeframes. Tools such as blended finance, co-financing, local debt and equity instruments, private equity, and public-private partnerships are being deployed in Africa in new ways that address risks associated with low-income and fragile states. They provide innovative paths to securing financing on a scale that can match the scope of business opportunities and help manage risk in high-growth African markets.

OPPORTUNITIES IN RAPIDLY CHANGING MARKETS

Africa is not immune to the short-term economic headwinds that most economies now face, and changing conditions are causing some opportunities to fade. Trade and growth in the region are feeling the effects of a slowdown in China, while a significant drop in commodity prices and a depreciation of local currencies are creating challenges for companies and governments alike. While most African economies continue to grow, the impact of such global economic trends compounds challenges to diversifying economies and exports, and is unsettling African economies in varied ways.

Yet economies continue to grow—some rapidly—and there are still powerful incentives for businesses to seek a wider range of partners to overcome the financing challenges that come with working in the region. Notable trends include:

- *Many countries in the region are projected to exceed the regional growth rate of more than 4.0 percent over the next three years. Advanced economies, by contrast, are expected to grow 2.1 percent a year from 2016-18.*
- *Projected per-capita growth rates are impressive in numerous African countries, including Ethiopia (8.9 percent), Rwanda (6.2 percent), Tanzania (6.5 percent), and Nigeria (3.8 percent), among others (2010-2020 Compound Annual Growth Rate).*

- *Driven by a young population and rapid urbanization, household consumption is expected to continue to grow in important sectors including clothing, communications, energy, financial services, food, health, housing, and transport.*
- *Africa could absorb more than $90 billion annually in infrastructure investment but now receives about half that amount. The capital shortage going forward is projected to be particularly acute in Nigeria, Angola and Kenya, while investments in energy, transportation, and logistics offer the most potential for both impact and reward.*
- *Regional spending to adapt to climate change is expected to be between $5-10 billion per year from public and private sources. Rising temperatures and water supply issues, among other environmental issues, are creating investment opportunities for scaling up low-carbon energy sources and managing water more efficiently.*

The question for private sector entities looking to profitably address growing needs in challenging, less liquid markets is straightforward: What methods can be deployed to raise capital and mitigate risks associated with operating in African markets?

FINANCING SOLUTIONS FOR AFRICA

A more dynamic banking sector has begun to emerge and now plays a substantial role in supporting the growth of private business in Africa. Yet given the scale and long-term nature of new investment required to meet rising consumption patterns, commercial bank financing alone will not be adequate to meet the expected demand for large-scale projects with associated high risks.

Mobilization of investment from a wide range of sources is critical. To ensure that large, multi-year investments and projects can be successful, commercial finance can be further leveraged and supplemented by additional sources of capital that work together with private financiers to make more financing tools available and better spread risks across parties without misallocating it.

Approaches to financing in Africa that are both familiar and novel are being expanded upon or tried anew and offer promise for the years ahead.

- ***Public-Private Partnerships*** *are a strategy for projects with the right regulatory framework, sector planning and a high quality off-taker of services and goods to provide the comfort level private investors require to participate. Development institutions often play a critical role in bringing the private and public sectors together to provide those elements.*
- ***Co-financing*** *between private investors and development finance institutions draws on the strength of both to build confidence and spread risk beyond private sponsors and private commercial banks.*
- ***Blended finance*** *mixes concessional funds – typically from donor partners – with those of commercial development institutions and private investors in a risk-sharing arrangement, with aligned incentives that ensure that official assistance is leveraged as much as possible with private capital.*
- ***Local capital markets and tailored solutions*** *offer effective ways to access long-term, local-currency finance and protect economies from capital-flow volatility and reduce their dependency on foreign debt. Local debt and equity markets can be better leveraged by local corporations when large banks or development finance institutions provide risk guarantees or act as anchor investors, expanding access to additional funding instruments as well as new classes of investors. Other currency risks and market volatility can be addressed through tailored solutions and instruments.*
- ***Private equity****, through the assistance of anchor investors, can support the development of large and specialized funds that are able to invest in a wide variety of enterprises, including small and medium size businesses. Meanwhile, development finance institutions can help global institutional investors take equity in African companies, including through asset management.*

CASE STUDIES

Successful examples of recently financed projects come from across the African Region.

Azito 3: Nine development finance institutions teamed up to provide the $345 million in long-term finance and effect the regulatory reforms necessary to break ground on a 139 megawatt power plant expansion in Cote d'Ivoire.

Ecobank Transnational: The pan-African bank extended lending to small businesses in eight African countries with particularly difficult economic environments in terms of fragility and low income levels. The project relied on a $110 million risk sharing facility between Ecobank and two development banks.

Cargill/SIB: An agribusiness giant and an Ivoirian bank partnered with IFC to provide financing, via a $6 million risk sharing facility, to cocoa farmers looking for funding methods to purchase better vehicles to transport product from farms to coops.

Bayport Financial Services Limited: A Zambian microfinance lender was able to issue its first medium-term note raising 172 million kwacha, or about $26.5 million, to expand lending to low and middle income borrowers and small businesses. Development finance institutions helped by providing anchor investments on the issue.

Bridge International Academies: An education company teamed with development banks and new investors to expand its low-cost private school chain out of Kenya into three additional countries, at a cost of $60 million. The partnership provided both regulatory assistance and seed investment.

Africa Improved Food Holdings: In a project that addresses chronic malnutrition, DSM, a Dutch multinational, established a nutritious food processing plant in Rwanda requiring $60 million in initial investment. This is a project of ambitious scale and risk that needed to be mitigated by reputable sponsors and responsive governments. It required strong purchase, supply and off-taker arrangements for raw materials and final products.

Helios Investment Partners: Anchor investments from IFC were made to an Africa-focused private equity firm, helping it attract otherwise hesitant investors and putting the firm on a path to raising a record $1 billion fund.

Eleme Petrochemical: A Nigerian manufacturer was transformed from a loss-making industrial giant into a world-class chemical producer with advice, $162 million in financing and deal structuring that allowed privatization of the state owned firm.

Methods exist to underwrite successful investments in Africa. In a riskier environment going forward, they are sure to become more important.

Opportunities in Rapidly Changing Markets

Africa is a region with enormous potential for private investors. In the midst of a downshift in the global economy, Africa remains a continent in transition, with rapid urbanization, increasing stability, a young and growing population, expanding internet connectivity, rising incomes, and shifting consumption patterns. Taken together, these enduring trends have created an abundance of commercial opportunities across the continent and turned it into a place businesses and investors cannot afford to ignore.

Despite those opportunities, Africa is not immune to the short-term economic headwinds that most economies face today. Global economic growth over the next two years is projected to be weaker, led by slowing growth in China and lower commodity prices after a decade-long boom. Dampened demand in both developed and developing countries is leading to a slowdown in international trade.

Yet even before recent global economic turmoil emerged, investor activity on the continent was constrained by structural obstacles and a lack of financing options that often inhibited the effective distribution of risk associated with large-scale or long-term projects.

CHANGING CONSUMPTION PATTERNS

Nevertheless, for investors the region's demographics are all-important and present significant opportunities. Urbanization is accelerating spending on transportation, from cars and motorcycles to public transport. Young people joining the work force—the median age in Sub-Saharan African is 18—will continue to create demand for housing and access to better education, health services and jobs. Connectivity via information technology is becoming a larger component of household budgets. Education, clothing, and footwear are dynamic growth sectors in most economies.

According to proprietary IFC data, food and beverages continue to account for the largest share of household expenditures. As incomes rise and basic needs are more easily met in many households, other priorities are emerging. For example, household spending on technology and transportation in Nigeria, the region's most populous nation, are each projected to grow by more than 7.5 percent per year through 2020. They are expected to rise by 11.5 percent or more per year in Ethiopia, the second most populous nation, over the same period. Growth of spending on housing will top 9.0 percent annually through 2020 in Mozambique, Tanzania and Zambia. Other examples of surging consumption abound. *See Figure 1.*

GROWTH PROSPECTS AND CHALLENGES

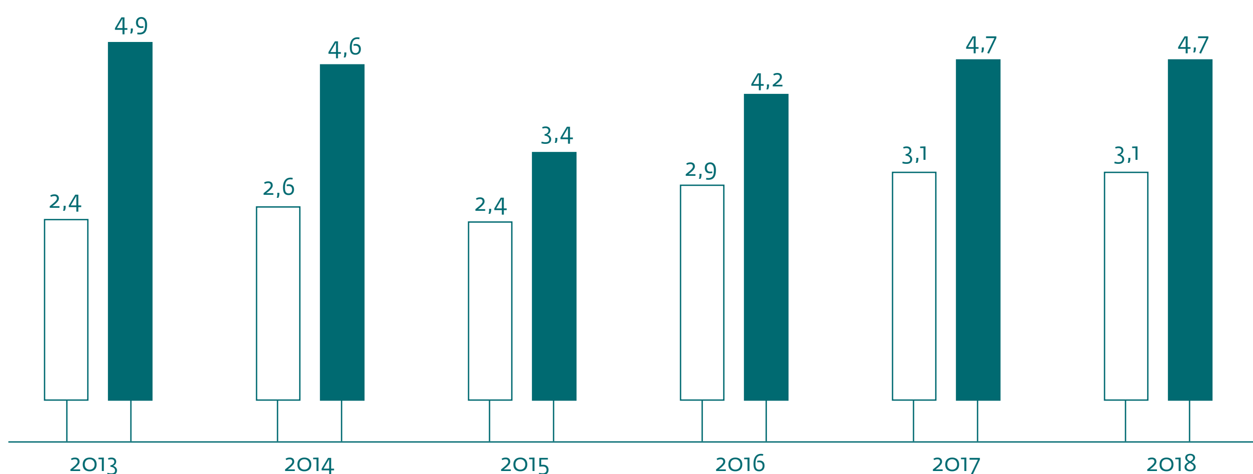
Most countries in Sub-Saharan Africa are expected to see a gradual pickup in growth over the next two years. Year-over-year growth for the region was 3.4 percent in 2015. It should rise to 4.2 percent in 2016 and 4.7 percent in 2017-2018, according to recent World Bank projections. The region's lowest-income countries are expected to continue to enjoy even higher GDP growth in the near term. With a few exceptions—South Africa is a prominent one—countries in the region are projected to sustain growth rates of more than 4.0 percent over the next three years, making the region the second fastest growing region after East Asia. (Advanced economies, by contrast, are expected to grow 2.1 percent a year through 2018.) *See Figure 2.*

FIGURE 1: **HOUSEHOLD CONSUMPTION PROJECTIONS IN AFRICA** (selected countries and sectors, 2010-2020)

SECTOR/COUNTRY	NIGERIA		ETHIOPIA		TANZANIA		MOZAMBIQUE		ZAMBIA		SENEGAL		COTE D'IVOIRE		DRC	
	Growth%	*Share%*	*Growth%*	*Share%*	*Growth%*	*Share%*	*Growth%*	*Share%*	*Growth%*	*Share%*	*Growth%*	*Share%*	*Growth%*	*Share%*	*Growth%*	*Share%*
Transport	**7.9**	5.6	**11.5**	2.1	**10.4**	4.9	**10.7**	6.1	**10.6**	7.1	**5.1**	4.1	**6.9**	8.9	**6.5**	2.8
ICT	**7.8**	1.4	**12.1**	0.9	**9.1**	0.9	**10.8**	3.0	**9.0**	3.5	**5.0**	2.0	**6.4**	9.1	**6.8**	1.1
Housing	**6.9**	12.7	**6.9**	11.0	**9.1**	2.3	**9.4**	13.4	**9.3**	18.5	**4.9**	15.8	**6.4**	12.1	**6.4**	1.9
Water	**7.3**	0.4	**7.5**	0.4	**9.7**	0.2	**9.6**	0.8	**9.5**	1.0	**4.8**	1.5	**5.3**	1.0	**6.1**	1.3
Education	**6.6**	2.0	**7.0**	0.9	**11.0**	2.1	**9.1**	0.3	**8.6**	3.3	**4.9**	0.1	**5.5**	1.6	**5.9**	2.8
Clothing and Footwear	**7.3**	3.8	**6.6**	7.6	**7.7**	6.2	**8.4**	6.3	**8.1**	3.3	**4.4**	6.2	**5.2**	6.2	**5.9**	5.6
Health	**7.6**	11.5	**6.5**	0.5	**7.4**	1.4	**9.3**	0.6	**8.6**	0.2	**4.5**	2.5	**5.2**	4.5	**6.0**	3.2
Energy	**6.7**	1.9	**5.4**	9.3	**8.2**	0.6	**7.1**	7.5	**8.0**	4.3	**4.8**	5.2	**5.2**	2.5	**5.7**	5.2
Food and Beverage	**6.2**	56.8	**5.8**	58.6	**7.3**	66.9	**6.8**	52.5	**7.7**	49.4	**3.9**	52.8	**5.0**	45.2	**5.6**	69.5
Avg Growth rate 2010-20	6.9		6.7		6.8		7.8		7.6		4.5		6.5		6.2	
Avg Population growth 2010-20	2.6		2.0		3.1		2.2		3.3		2.6		2.2		2.6	
Population 2014 (millions)	174		91		48		26		15		15		25		79	
Consumption (US$ bn; 2010)	44.5		35.2		10.7		6.4		6.1		7.1		17.7		14.3	

Sources: IFC and World Bank based on Household Surveys.

FIGURE 2: **PROJECTED GLOBAL REAL GDP GROWTH** (percent)



Note: *Figures for 2013-2014 are actual. 2015 figure is estimated. 2016-2018 are forecast.*

World | Sub-Saharan Africa

Source: World Bank, Global Economic Prospects, January 2016

While most African economies continue to grow, global economic trends and other factors are testing African economies in varied ways.

Financial markets are suddenly volatile, with a resurgence of risk aversion toward developing countries that is expected to continue through the near term. Investor appetite is diminishing across asset classes, as evidenced by portfolio outflows and reduced foreign direct investment. Emerging market currencies, including those across Sub-Saharan Africa, will remain under pressure as the US dollar strengthens. Consequently, the abundance of liquidity and low borrowing costs experienced by Sub-Saharan Africa and other developing regions over the last few years has been reversing.

Furthermore, domestic conditions in some African countries remain difficult compared to the period before 2008, with higher fiscal and external deficits and higher levels of debt. There are signs of deterioration in bank balance sheets in many African economies, particularly those that rely on commodity exports, with non-performing loans rising and tight domestic conditions pushing down lending margins. In addition, inflation has begun to inch higher, though at the moment it remains at historically low levels. African countries also face a significant challenge to diversify their economies and build competitiveness to export a wider range goods and services.

Still, per capita gross domestic product in the region has been rising rapidly since 2000 and is projected to exceed $4,700 in 2020, up by 50 percent over the 2010 level. The projected 10-year annual growth rate of per-capita GDP (2010 to 2019) is 5.5 percent, second only to emerging Asia, according to IFC projections. And projected rates of per-capita growth are more impressive still in numerous African countries including Ethiopia (8.9 percent), Nigeria (3.8 percent), Rwanda (6.2 percent), and Tanzania (6.5 percent). *See Figure 3.*

From 2010 to 2015, private consumption accounted for almost 60 percent of total economic growth in Africa, a contribution of 2.8 percentage points per year on average. As a result, the retail sector grew more than 10 percent a year over the 2008-2013 period, *more than any other emerging market region.*

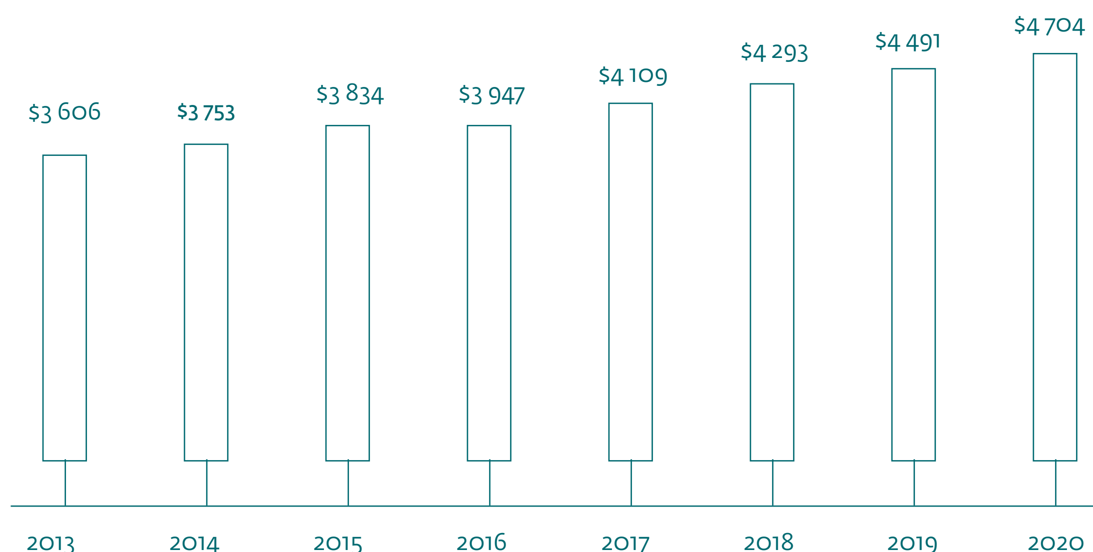
The bottom line is that Africa's economies continue to grow, its citizens are becoming wealthier, they have access to more disposable income, they are connected to the rest of the world more than ever, and they are hungry for the broad variety goods and services that businesses can offer.

BUSINESS PROSPECTS IN A SHIFTING ENVIRONMENT

Companies in Africa and from around the world have seized on these opportunities over the past decade, expanding both at home and regionally. And the region's potential has inspired a new breed of global private investor looking to tap substantial opportunities in Africa. Gross capital flows to Africa increased from just $9 billion in 2005 to $49 billion in 2014, according to IFC data.

But recent economic headwinds are having an impact. Gross capital flows to Africa declined in 2015 to $40 billion. South Africa, with a slight increase in flows last year, was the exception, apparently a flight to perceived quality relative to other regional markets on the part of international investors. *See Figure 4.*

FIGURE 3: **SUB-SAHARAN AFRICA, GROSS DOMESTIC PRODUCT** (based on purchasing-power parity (PPP) per capita GDP)



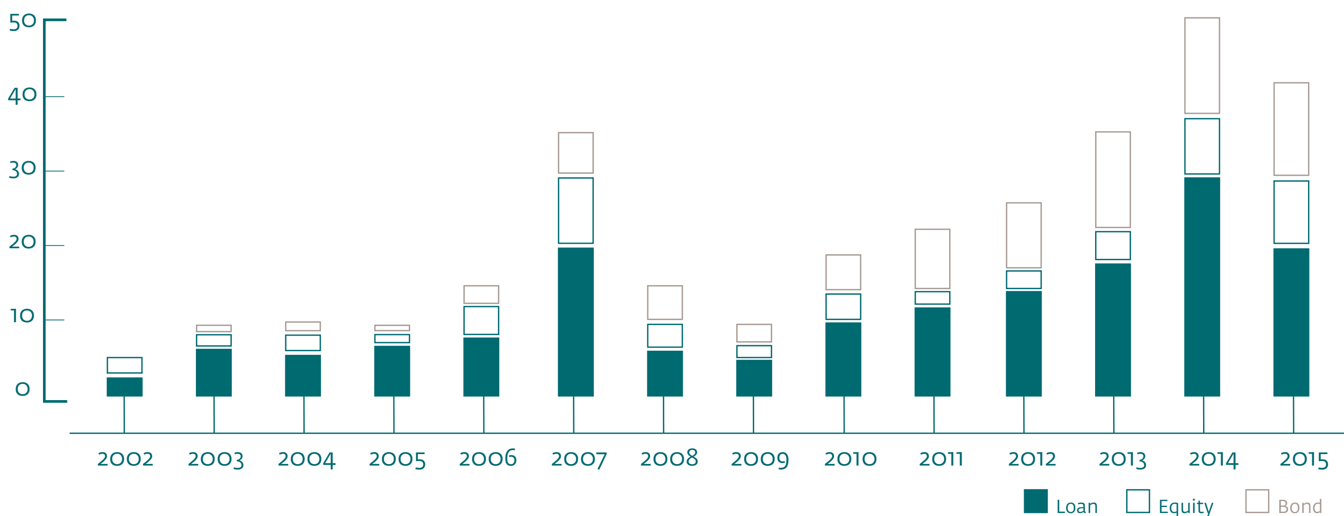
Source: IMF

And Africa's thirst for capital remains significant. The continent lags all other global regions in terms of reliable access to electricity, sanitation facilities, water sources, and paved roads. Infrastructure projects across Africa could absorb a combined $93 billion annually, yet spending on such projects was half that as of 2009, according to a 2014 World Bank Group report. The related capital shortage going forward is projected to be particularly acute in Nigeria, Angola and Kenya, and investments in energy, transportation, and logistics offer the most potential for both impact and reward, World Bank figures show.

There are many examples of sectors where opportunities for investment are not sufficiently funded.

- *Financial services: Only about 15 percent of adults in Sub-Saharan Africa had deposit accounts as of 2012, according to World Bank figures. Yet with incomes rising rapidly across the continent – and surpassing the critical $1,000 level – retail banking in the region is expected to grow at a 15 percent annual rate through the end of this decade.*
- *Manufacturing and services: Consumers are demanding a wider range of affordable goods and services. Construction materials, energy efficient machinery, real estate, retail and tourism are among the many areas where competitive businesses are likely to thrive in coming years.*
- *Housing: Housing is struggling to keep pace with African cities, which are absorbing some 40,000 new people every day. Already in Nigera, for example, there is an estimated 17 million unit housing shortage and in Kenya the shortage is estimated at two million units.*
- *Education: Public education systems in many countries face challenges in providing quality education to the poorest children, with more than 50 million children out of school in Sub-Saharan Africa, according to World Bank estimates. Governments have committed to achieve 'education for all' by 2030; to do so additional capacity will need to be created for 127 million students.*
- *Healthcare: Sub-Saharan Africa bears 24 percent of the global burden of disease but only accounts for about one percent of global health expenditures. The supplies of both health care workers and hospital beds are short of demand. Investment opportunities are expanding for health service providers, pharmaceuticals, and medical technology that promote greater access to affordable, quality healthcare. The sector also lacks consolidation, with too many small actors working independently, creating opportunities for companies that manage change on a large scale.*

FIGURE 4: **GROSS CAPITAL FLOWS TO AFRICA FELL BY 28% IN 2015** (US $bn)



Sources: IFC Research – Global Markets: Gross Capital Flows and FDI Flows to Africa

- ***Climate Change-Related Business:*** *The World Bank estimates that annual regional spending to adapt to climate change will be between $5-10 billion from public and private sources. Rising temperatures and water supply issues, for example, are creating investment opportunities for scaling up low-carbon energy sources and managing water more efficiently.*

The question for private sector entities looking to profitably address growing needs in challenging, less liquid markets is straightforward: What methods can be deployed to raise capital and mitigate risks associated with operating in African markets?

FUNDING SOURCES AND IMPEDIMENTS

There are numerous sources of funding, including domestic and international bank loans and local and international equity and bond markets. The problem is that several of those sources are chronically underdeveloped in Sub-Saharan Africa, while others are currently constrained by recent economic headwinds or the continued fallout from the global financial crisis of 2007-2008.

There was a steep drop in bank loans for African infrastructure projects after 2007, most likely a consequence of new capital requirements imposed on commercial banks since the financial crisis. Overall, loans to emerging market infrastructure fell after 2007, slowly recovering through 2014 before turning down again. Bonds and equity have followed a similar pattern. *See Figure 5.*

Africa's banking sector remains underdeveloped even compared with other emerging market regions. The sector lags all other regions in terms of access, depth, efficiency and stability, according to a 2012 World Bank study. While the financial sector has grown and matured in recent years, it is highly concentrated—the three largest banks held 78 percent of bank sector assets as of 2011—and the focus remains on lending to high-margin corporate clients, as opposed to retail banking to individuals and small enterprises.

And regional capital markets—with a few notable exceptions—lack the size and liquidity necessary to make a significant contribution to Sub-Saharan Africa's capital needs. The Johannesburg Stock Exchange is more than three quarters of total Sub-Saharan Africa's market capitalization and the Nigeria Stock Exchange less than 10 percent. Outside of South Africa and Nigeria, stock market capitalization in the region remains low at only 10 percent of GDP, a fraction of that in other emerging markets. Market liquidity remains a problem region-wide.

Domestic debt markets, while growing, remain shallow and are dominated by government securities, which account for three-fourths of total bond market capitalization. Only South Africa has a deep domestic bond market. Corporate bond markets outside that country remain nonexistent or in an embryonic stage.

FIGURE 5: **AFRICA GROSS CAPITAL FLOWS TO INFRASTRUCTURE BY ASSET CLASS** (US $bn)

Sources: Dealogic; Global Markets – IFC Research (CGEIR). Data as of December 31, 2015.

Finance Solutions for Africa

The abundance of opportunities across Sub-Saharan Africa, and the appetite of institutional investors to take advantage of them, stand in stark contrast to the limited approaches available to finance projects. Businesses and investors in Africa are searching for new methods to underwrite potentially profitable ventures on the continent.

Increased availability of commercial bank financing and funds, along with the slow but steady growth in domestic capital markets and other sources of commercial financing, are all encouraging signs. These already play a major role in supporting the growth of private business in Africa and they will become increasingly critical in coming years. But given the rapidly changing demographics of the region and the need for investment on a far greater scale than in recent years, commercial finance alone cannot underwrite long-term, large-scale projects in Africa with high risks.

In addition to being the world's lowest-income region, Africa has many fragile and conflict affected states. In fact the region accounts for half of the globe's countries defined as such by the World Bank Group. While governance is improving, it remains weak in most markets. Africa remains the most difficult region in the world in which to do business. Poor perceptions of Africa may be exaggerated, but all of the above factors contribute to actual risks that must be managed and mitigated. *See Figure 6.*

At the same time, part of the attraction of Africa is the improving climate for business. In the 2015 and 2016 World Bank Group *Doing Business* reports, African countries made up five of the top 10 most improved global economies for ease of doing business. Included in the top 10 were: Benin (2015 and 2016), Cote d'Ivoire, Democratic Republic of Congo, Kenya, Mauritania, Senegal (2015 and 2016) Togo, and Uganda.

Addressing Climate Change

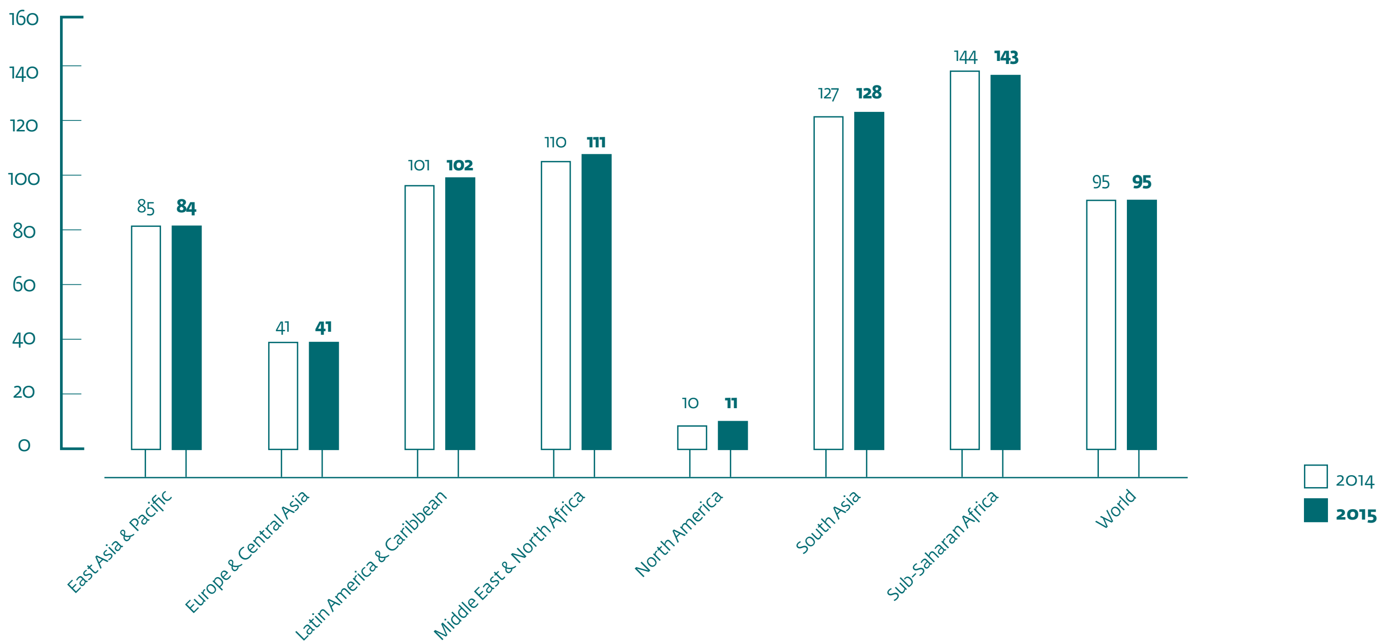
Urgent energy access needs and the impact of climate change require new models that encourage renewable sources of energy.

Scaling Solar brings together multiple World Bank Group services under a single engagement aimed at creating viable markets for solar power in each client country. The program enables governments to competitively and transparently procure privately owned and funded solar power stations in the shortest time and at the lowest tariffs possible.

Scaling Solar includes an all-in-one package of advice, project documents templates, risk management products, finance, and insurance designed to attract leading private sector developers to new geographies. The project is being implemented across multiple countries in Africa, creating a regional marketplace and giving even small countries the purchasing power of larger markets.

In 2015 Zambia's Industrial Development Corporation announced that 48 companies sought to prequalify for their two initial 50 megawatt solar projects under Scaling Solar. From these, 11 companies, including many of the top global solar developers, qualified for the tender that was released in February 2016. Senegal is now also preparing a Scaling Solar tender and several other countries are expected to follow.

FIGURE 6: **EASE OF DOING BUSINESS INDEX** (1=most business-friendly regulations)



Sources: World Bank, WDI Datbase, *Doing Business*

Certain other countries have made large strides in recent years. Rwanda, for example, has made consistent improvements in its investment climate to become the second easiest place to do business in Africa. Within the region, Rwanda falls behind only Mauritius, another country that has consistently undertaken reforms to make the country more hospitable to investors.

To ensure that large, multi-year investments and projects can be undertaken, existing sources of finance can be leveraged and supplemented by other types of financing and support, including private sector development financing, donor funding, a mix of public and private financing, and more debt and equity instruments that work together to better spread risks across parties without misallocating it.

Fortunately, there is a combination of strategies and innovations in financing and risk mitigation now being employed in Africa that can provide those methods.

PUBLIC-PRIVATE PARTNERSHIPS

PPPs are a tested strategy, especially for large infrastructure projects and other projects involving public services. They can be applied to numerous sectors, from core infrastructure to health, education, and other areas.

Power generation, for example, which is lacking across the region, requires large-scale funding, the appropriate regulatory framework, sector planning and a high quality off-taker to provide the comfort level that private investors require to participate. Development institutions often play a critical role in bringing the private and public sectors together to provide all of those elements.

In 2012 nine development banks teamed up to provide the long-term finance, regulatory reform and power purchase agreements necessary enable a 139 MW natural gas power project to go forward in Cote d'Ivoire. It will increase electricity production at an existing plant by 50 percent with no incremental gas consumption.

CASE STUDY

Azito Energy

Meeting Africa's Power Needs

Public funding has proven insufficient to meet Africa's enormous power needs. For large infrastructure projects, especially power generation, establishing the right financing, regulatory framework, sector planning, and a quality off-taker can provide the comfort level that private investors require to participate. Development institutions can play a critical role in bringing the private and public sectors together.

Despite being blessed with a huge endowment of natural gas reserves, hydro capacity, and other natural resources, Sub-Saharan Africa is massively underpowered. Generation capacity is lower than that of any other world region and is marked by unreliable supplies, high prices, and low rates of access. Some 600 million Africans lack access to electricity, according to a 2015 report by McKinsey & Co.

And the gap between supply and demand is growing. Because new household connections in many countries are not keeping pace with population growth, the electrification rate, already low, is actually declining. At the same time, the high penetration of diesel generators across the continent – with prices three to six times what grid consumers generally pay – strongly indicates that African businesses and consumers are willing to pay for electricity. McKinsey predicts a period of rapid electrification for Africa in coming decades.

Yet in the immediate aftermath of a long civil war and a contested and violent election in Cote d'Ivoire, it seemed all but impossible for a private entity to embark alone on a major power infrastructure project in 2012. The risks, from political volatility to regulatory and currency risk to a lack of local expertise, among many others, were just too daunting.

To enable just such a project to go forward, in 2012 nine development finance institutions teamed to provide the long-term finance and design regulatory reforms necessary to break ground on a 139 megawatt power plant expansion in Cote d'Ivoire.

The power plant is located near Azito village in Cote d'Ivoire's Yopougon district, about 6 kilometers west of the port of Abidjan. It was initially built in 1998 and now majority owned by Globeleq Generation Holdings, a power generation developer focused on emerging markets.

An expansion and modernization of the existing Azito plant was estimated to cost $430 million and would require financing and technical expertise, currency hedges, interest rate swaps, insurance against political risk, a reliable fuel supply and end-user purchase agreements. It was a large and complex package to pull together, beyond the scope of any private investor.

Enter IFC. The development bank provided a $125 million anchor investment and arranged another $220 million in long-term loans from eight other development banks. World class turbine technology was procured from General Electric and experienced contractors, including Hyundai Engineering and Construction, were brought in to build, operate and maintain the facility.

A reliable supply of natural gas was organized among several regional producers while the national government and the private utility CIE were contracted to off-take and distribute the power produced. And the World Bank engaged the Cote d'Ivoire government on energy sector reform and financial management.

As part of the expansion, the existing plant was fitted with two heat recovery steam generators, a 140MW steam turbine generator, one steam condenser, and an air-cooled cooling water system. Essentially, the technology makes use of waste heat generated by the existing gas turbines to produce steam which drives another generator, thereby reducing the need for additional fuels to increase the plant's capacity.

Those add up to an expanded facility that will generate 50 percent more power with no incremental gas consumption. It is expected to reach 2.3 million additional customers and is a successful example of a major investment in Cote d'Ivoire following the recent crisis.

Opportunities to replicate the Azito plant's successful expansion are proliferating across Africa, yet are all but untapped. New private sector power capacity created in 2012-2014 was just 6.0 percent of annual demand for new capacity across Africa. And the continent could absorb $490 billion of capital for new power generating capacity over the next 25 years and an additional $345 billion for transmission and distribution, McKinsey reports.

KEY RISK MITIGANTS

Financing risks:

- Development bank long term finance, providing comfort to other investors
- Strong financial standing of project sponsors
- IFC swap, fixing interest rate on the debt for 15 years

Operational Risks:

- Project sponsors very experienced in power sector
- Experienced international contractors

Market/Off-Taker Risks:

- MIGA equity guarantee on the concession contract and political and transfer risk
- World Bank engagement in sector structural reforms and financial management

CASE STUDY

Ecobank

Bringing Credit to Small Businesses

Committed to inclusive lending and looking for more customers, a pan-African bank wanted to extend lending to small businesses in eight countries with particularly difficult economic environments in terms of fragility and income levels. The project involved a $110 million public-private risk sharing facility and additional risk mitigation measures.

Small and medium sized enterprises have been poorly served by the banking industry in Sub-Saharan Africa. Fewer than one-in-three medium sized firms in the region have a bank loan or line of credit, according to a World Bank survey; for small firms it is fewer than one-in-five.

In fragile and conflict affected states those firms represent the backbone of the economy and provide the bulk of employment, yet they receive just one-quarter of all loans and credits. Part of the explanation is that there is a general lack of knowledge about the creditworthiness of such firms. In addition, FCS countries lack institutional lending capacity and have poor financial infrastructure and generally suffer some level of macroeconomic instability. The unfortunate result is that banks in those countries have little appetite to lend to SMEs.

Ecobank Transnational Inc., the largest pan-African bank, with a presence in 36 countries, had been strong in corporate banking since its incorporation in 1985, but was also committed to serving small and medium business enterprises and retail customers.

A project to expand SME lending to more economically challenged countries in West and Central Africa, however, required the kind of assistance that development banks can provide.

The lending package Ecobank put together with IFC and the UK's Department for International Development in 2015 was designed to overcome the challenges of lending to smaller businesses with high risk profiles in very poor countries, including Burundi, Chad, Cote d'Ivoire, Democratic Republic of the Congo, Republic of the Congo, Guinea, Mali and Togo. DFID participated through the Global SME Finance Facility.

The centerpiece of the Ecobank package is a $110 million risk sharing facility between IFC and Ecobank, with further risk mitigation provided by DFID, which is available to the eight Ecobank affiliates in the target countries.

The facility also provides Ecobank affiliates tools to build scale in SME lending, including advisory services and SME finance training. There is also a pricing incentive for Ecobank affiliates that achieve 50 percent facility utilization within 12 months.

The new facility means improved access to finance for smaller enterprises in the eight countries, stronger financial sectors, and better employment opportunities. For Ecobank it means a broader customer base and – eventually – stronger economies to lend into.

KEY RISK MITIGANTS

Credit risk of SMEs in fragile situations

- The IFC Risk Share Facility
- DFID additional risk mitigation
- Ecobank risk management framework and IFC's bank training support

Supervision challenges

- IFC's well-structured supervision model

CO-FINANCING WITH DEVELOPMENT BANKS

Another approach to mobilizing funds and spreading risk is co-financing. Through it investors can gain a greater level of comfort via a lead development bank's connection with governments, its financial strength, its willingness to remain through difficult economic conditions, and its financial imprimatur, all of which help attract other financiers.

Nigeria's Eleme Petrochemicals was transformed from a poorly performing industrial giant into a world-class chemical manufacturer when IFC provided advice, financing and deal structuring to allow privatization of the state owned firm. It was acquired in 2006 by Indonesia's Indorama International Finance, after which production increased from 8,502 metric tons per annum in 2006, to 282,286 mtpa four years later.

Similarly, NewGlobe Schools, which runs Africa's largest network of low-cost private schools, teamed with development banks and new investors to launch an expansion of its Bridge Academies chain out of Kenya into three additional countries. The partnership provided seed investments and regulatory assistance, and Bridge is now on its way to educating one million students from low-income communities at 2,100 schools by 2020.

BLENDED FINANCE

Blended finance is an approach that can be used to enable the private sector to invest where it would not otherwise be possible. The idea is to mix concessional funds – typically from donor partners – with those of commercial development institutions and private investors in a risk-sharing arrangement, with aligned incentives to make sure official assistance can be leveraged as much as possible with private capital.

In 2015, IFC agreed to provide a $21.5 million loan and $4.5 million equity investment in Dutch Africa Improved Foods Holding in Rwanda. This loan comes with support from the donor-funded Global Agriculture Food Security Program, and is intended for the construction and operation of a 45,000 tons-per-year processing plant in Rwanda for fortified cereals to treat child malnutrition. The project will source raw materials through existing farmer cooperatives in Rwanda and through the government. It was designed with the help of the World Food Program, the food aid branch of the United Nations, which has agreed to buy a significant portion of the final product and distribute it in Southern Sudan, Uganda, Burundi, and other countries.

Another example is agribusiness giant Cargill and Cote d'Ivoire's Société Ivoirienne de Banque, which in 2015 were able to partner with IFC to create a truck leasing program in Cote d'Ivoire that provides more reliable vehicles to collect cocoa beans from the field.

CASE STUDY

Cargill/SIB

Securing a Supply of Cocoa through Loans to Farmers

A four-party risk-sharing facility involving private and public sector actors brought cocoa farmers in Cote d'Ivoire access to medium-term finance allowing them to pare back their biggest cost component—old and unreliable vehicles used to collect cocoa beans from the field.

Cote d'Ivoire is among the world's largest producers of cocoa beans and their export is a mainstay of the West African nation's economy. Nearly all cocoa production in the country comes from small farmers, many of whom belong to farming cooperatives. Yet logistics has historically proved a major challenge for those farmers, as bad roads lead to problems with damaged vehicles, and proper maintenance and repair has often proved to be prohibitively expensive.

Coops have access to short-term financing through exporters, but the duration of those loans has generally prevented them from access to new trucks. Thus they have resorted to second or third-hand vehicles which involve huge maintenance costs. Cocoa collection via existing or older trucks is the largest component in the coops' cost structure.

In 2013 agribusiness giant Cargill, a major global purchaser and processor of cocoa, established Cargill Coop Academy, a program to help Cote d'Ivoire cocoa cooperatives better manage their businesses by teaching management, governance, finance, auditing, and marketing skills. The program is part of a broader Cargill effort, called Cargill Cocoa Promise, to secure a reliable supply of cocoa, much of which is grown by smallholder farmers around the world, in order to meet a rising global demand for cocoa and chocolate products.

In 2015 Cargill wanted to expand the Coop Academy program in Cote d'Ivoire to improve the coops' profitability by reducing the burden of maintaining old trucks. To do so it collaborated in a risk sharing facility – along with IFC, an Ivoirian bank and the Global Agriculture and Food Security Program – to add a financing arm to the Coop Academy. With access to finance, coops could lease trucks to more easily and efficiently collect beans from the fields.

IFC and Societe Ivoirienne de Banque, Cote d'Ivoire's fourth largest bank, agreed to equally share the credit risk in a $6 million portfolio of medium-term (three-year) truck leases provided by SIB to the coops. Cargill was the off-taker for the cocoa produced by the coops and made the deal bankable by arranging to service the coops' debt on the leases from the proceeds of the coops' cocoa sales, thereby mitigating the credit risk involved.

Last September 43 cocoa cooperatives in Cote d'Ivoire took delivery of new trucks at a ceremony in Abidjan. Medium-term financing is now available to 70,000 underserved smallholder farmers through 100 cooperatives. For Cargill that means a stronger cocoa value chain and a more reliable supply of cocoa beans.

The hope is that the multiparty credit arrangement involving both private and public sector entities can be replicated for other crops in Cote d'Ivoire and beyond, giving farmer cooperatives across Africa access to medium-term finance to cut costs and improve profitability.

KEY RISK MITIGANTS

Financing Risk:

- The 4-partite Risk Sharing Facility between Cargill, SIB, IFC and GAFSP
- Cooperatives' long track record of serving Cargill's working capital advances

Sector-Specific Risk: Cocoa sector

- Successful implementation of the sustainable trading margin regime for coops following the 2012 reforms

Environmental/Social Risk:

- Requirements for coops to certify mitigation of child labor and traceability risks through the sustainability and supply chain management programs by Cargill
- SIB environment and social due diligence and monitoring of eligible coops

CASE STUDY

Bayport

Tapping Bond Markets to Expand Lending

Bond markets, though underdeveloped in Africa, are beginning to emerge as a realistic financing option for private companies looking to invest in the continent. Multilateral development banks can issue bonds in local currencies to help develop nascent bond markets as well as assist corporations with private issuance by providing risk guarantees or acting as anchor investor.

Less than one quarter of adults in Sub-Saharan Africa had an account at a formal financial institution in 2012, compared with about half of adults worldwide, according to IFC research. Lacking a financial infrastructure that includes a place to save money securely, safe and efficient means of transferring money, and access to credit and insurance, the majority of people on the continent are often barred from making productive investments in their families and businesses.

Access to financial services and credit is slightly greater in Zambia, where the banking sector is better developed than many African nations. Still, a large portion of the Zambian populace, especially in rural areas, remains unbanked and vulnerable to unscrupulous or unregulated loan activities due to poor access to financial services, according to KPMG. And even in countries with fairly developed financial sectors, services are often directed exclusively toward established businesses and higher income households. Only 16.4 percent of small firms in Sub-Saharan Africa have a bank loan or line of credit, compared to 29.5 percent in developing countries across the globe. In Zambia it is only 5.2 percent.

Bayport Financial Services Ltd., Zambia's largest microfinance lender and its market leader in payroll based lending, wanted to expand lending to low and middle income borrowers and small businesses, unlocking the credit market to ordinary Zambian citizens while tapping a large new customer base.

Capital markets are a traditional source of funds for an expansion of bank lending, yet debt and equity markets are underdeveloped and illiquid in many African countries—if they exist at all. And domestic debt markets are dominated by government securities in Africa. Zambia is no exception: As of 2014 there hadn't been a Zambian kwacha (ZMW) corporate bond issuance in five years.

Cooperation with multilateral development banks enabled Bayport to end that dry spell and tap capital markets for the funds it needed to expand lending. IFC first developed a constructive dialogue with Zambian capital market regulators through a *Zambezi* bond issuance in 2013. The development bank then used its extensive experience with capital markets transactions—both in Zambia and more broadly—to help Bayport plan its own issuance that could be appropriately structured and launched in a timely manner.

IFC and African Local Currency Bond Fund, a unit of the German-government owned development finance institution KfW, also made funding commitments: IFC committed to purchase 35 percent of the issue as an anchor investment in the Bayport bond and ALCB Fund promised to buy 13 percent. Those investments were catalytic, as IFC's imprimatur enhanced the issuer's profile and created a comfort level for other investors, eventually attracting pension funds and insurance companies to the transaction.

Investor interest in the issue was robust enough that Bayport increased the offering by ZMW 21 million, from the initial 150 million planned. In the end, the company was able to issue its first medium-term note, raising ZMW 172 million, or about $26.5 million. Not only did the issue break a long dry spell for the market, it was the largest corporate bond issuance in Zambian history.

In addition to expanding Bayport's lending base and profit potential and encouraging Bayport's efforts to strengthen responsible finance practices, the Bayport bond project helped deepen Zambia's domestic capital market, a critical ingredient to financing the country's domestic economy. It also had a positive impact on the private sector by establishing strong financial practices and demonstrating the possibilities for tapping capital markets to fund new business ventures in Africa. Bayport's example is expected to encourage other enterprises in the region to pursue bond issuance as a means of broadening their investor base and lowering their funding costs.

Perhaps most important, the credit now available to low and middle-income workers and small businesses in Zambia will encourage investments in business ventures, small scale agriculture, education and home improvement, and those in turn will generate economic growth and new sources of profits for other private enterprises.

KEY RISK MITIGANTS

Financing Risk:

- IFC's presence in the bond program, providing comfort to investors
- IFC's sound technical expertise to support structuring of the bond program

Operational Risks:

- Competent mid-level management
- IFC's knowledge of Zambian bond market through the issuance of Kwacha denominated "Zambezi" bond in 2013
- IFC's strong relationship with the Company's senior management, its creditors and the arranger (Barclays/ABSA)

Meeting the Housing Challenge

Housing is especially important due to the impact it has on the overall economy and capital markets. The housing sector produces jobs, from day laborers to masons, engineers, and architects. Investments in housing create a domestic, self-reinforcing cycle of employment and growth.

Yet today Africa's mortgage market is tiny, and housing markets with millions of homes have only a few thousand outstanding mortgages. Increasing mortgage availability would spur the creation of less expensive housing constructed through more efficient means. That in turn would reduce interest rates that now carry premiums to offset risks and costs of construction. Standardized mortgage contracts and terms would reduce transaction costs. For the lowest income households, microfinance for housing improvements could be applied to improve living conditions in existing informal settlements.

IFC is making long-term financing available through equity investments in wholesale mortgage liquidity facilities in Nigeria, countries of the West African Economic and Monetary Union, and Tanzania. These facilities issue long-term bonds and then on-lend the proceeds to their commercial bank members, thereby making mortgage financing available at longer maturities.

To further increase mortgages, IFC has made $100 million in lines of credit available directly to commercial banks in Kenya, Rwanda, and Uganda. Over time, IFC will work to link primary lenders directly with local pools of investment capital through a variety of means, including securitization, real estate investment trusts, and covered bonds.

The development bank guaranteed 50 percent of an up-to-$6 million leasing portfolio through a risk sharing facility with some of that risk assumed by donors through the Global Agricultural Food Support Program.

A similar approach was used with Ecobank, a pan-African full-service banking group. IFC supported a project to extend Ecobank lending to small businesses in eight African countries with particularly difficult economic environments in terms of fragility and income levels. The project uses a $110 million risk sharing facility between Ecobank and IFC and the UK's Department for International Development.

Where development needs exist, there are opportunities to use blended finance to expand business. In most African markets, for example, financial institutions have yet to develop a sustainable strategy to address the significant market gap in serving women, creating a missed opportunity that also constrains private sector development.

Rawbank in the Democratic Republic of Congo introduced "Lady's First" banking, offering specialized services to women. IFC provided advice to help establish services and invested in Rawbank with support from the Global SME Finance Facility, a donor facility IFC launched in 2012 to expand lending by development institutions to small businesses in emerging markets. The project supports lending to women and micro, small and medium sized enterprises.

CAPITAL MARKETS AND TAILORED SOLUTIONS

Deep, efficient local capital markets are a particularly effective way to access long-term, local-currency finance, the foundation of a thriving private sector and a key driver of jobs and growth. Sound local capital markets protect economies from capital-flow volatility and reduce dependency on foreign debt. Beyond local markets, other currency risks and market volatility can be addressed through tailored solutions and instruments.

The development of such markets is a priority for development banks. IFC promotes them by issuing non-government local-currency bonds, paving the way for other issuers. In addition to providing local currency finance to meet the needs of the private sector, development banks can work with governments and regulators to promote reforms and policies supporting local capital markets and local currency finance.

IFC has issued bonds in 18 local emerging-market currencies, from Armenian dram and Chinese renminbi to Indian rupee, Peruvian soles, and Zambian kwacha. Loans, swaps, guarantees, risk-sharing facilities and other structured products are other methods used to hedge foreign exchange, interest rate, and commodity price exposure.

With assistance from development institution anchor investments, Zambia's Bayport Financial Services Limited, a microfinance lender, was able to issue its first medium-term note raising 172 million kwacha, or about $26.5 million, in 2014, the first corporate bond issuance in Zambia in five years. Proceeds from the offering will expand Bayport lending to low and middle income borrowers and small businesses. IFC first developed a constructive dialogue with Zambian capital market regulators through a prior Zambezi bond issuance in 2013.

Beyond local debt, deploying capital market instruments such as cross-currency swaps can be critical to helping companies manage the risk of market volatility and finance successful projects. In Senegal, for example, IFC and the Overseas Private Investment Corporation provided financing for the 53 megawatt Cap des Biches power plant with project developer ContourGlobal, the Government of Senegal, and Senegal's national electricity utility. The project's innovative financing model was customized to the needs of the private sector operator to allow ContourGlobal to finance the project with an 18-year IFC swap to Euros of OPIC's $91 million US dollar financing. The approach reduced the risk of currency movements to provide stability by ensuring that revenues match debt service obligations. The project will provide electric power to 100,000 Senegalese.

A Role for the Private Sector in Basic Human Development

Good health, education and nutrition are the foundations of human development. It is difficult to care for domestic or rural household responsibilities, hold a job, or care for a family if you are malnourished, sick, or lack relevant skills and knowledge. Expanding access to health and education services and improved nutrition is a central element in any strategy to eliminate poverty and reduce inequality. In developing countries, the poor often turn to private sector health and education providers for access to services, as well as food and other basic needs.

- The World Bank estimates that over 50 million children are out of school in Sub-Saharan Africa. Governments have committed to achieve 'education for all' by 2030; to do so additional capacity will need to be created for 127 million students.
- Sub-Saharan Africa bears 24 percent of the global burden of disease but only accounts for 1 percent of global health expenditures. The supplies of both health care workers and hospital beds are short of demand.
- Over 165 million children under the age of five are stunted, and over 80 percent of malnourished children live in South Asia and sub-Saharan Africa. Extreme poverty is exacerbated by chronic malnutrition, or stunting, in children under the age of three.

CASE STUDY

Africa Improved Foods

Nutrition on a Larger Scale in East Africa

In a project that addresses chronic malnutrition, DSM, a Dutch multinational, established a nutritious food processing plant in Rwanda. This project of ambitious scale needed risk mitigation by reputable sponsors and responsive governments. It required strong purchase, supply and off-taker arrangements for raw materials and final products.

In 2015, IFC agreed to provide a $26 million financing package. It comprised $21.5 million in loans from IFC and mobilized from other sources, and $4.5 million in equity to Africa Improved Foods Holding. The donor-funded Global Agriculture and Food Security Program private sector window provided key support to this project with $8 million of the $26 million financing package intended for the construction and operation of a 45,000 tons-per-year processing plant to produce fortified cereals to treat malnutrition in nearly one million children.

This project created a partnership involving several parties: DSM; the UK's and the Netherlands' development finance companies CDC and FMO; the World Food Program; the government of Rwanda; and the Clinton Health Access Initiative. It will source raw materials through farmer cooperatives in Rwanda and through the government, thereby providing a stable market for farmers' produce.

The off-taker agreement with WFP, the food aid branch of the United Nations, is a key anchor for the project. The WFP plans to distribute the product in Southern Sudan, Uganda, Burundi, among other countries. Rwanda has also agreed to purchase a portion of the output to distribute to the most vulnerable, while the remaining output will be sold in the retail market.

The project aims to develop a suite of nutritious products produced locally for young children and women, based primarily on local agricultural products and that suit local eating habits. After Rwanda, a similar plant is planned for Ethiopia.

The first phase of the project in Rwanda is expected to cost nearly $60 million in capital expenditure and working capital. IFC has played a leading role in the financing and helped to bring in FMO and CDC as equity partners.

The Clinton Health Access Initiative played a key role in developing this project, especially by bringing the public parties and DSM to the project. CHAI has no financial interest in the project but sees this initiative as important in addressing health issues in Sub-Saharan Africa.

KEY RISK MITIGANTS

Financing risks:

- Provision of patient equity capital by GAFSP, IFC, FMO and CDC
- Provision of long-term debt by IFC and other financiers
- Off-take agreement denominated in US dollars to match currency of debt

Operational Risks:

- Highly experienced sponsor, contractor and management team

Market/Off-Taker Risks:

- Guaranteed off-take by UN's World Food Program and the Government of Rwanda

CASE STUDY

Bridge International Academies

Expanding Education That Gets Results

Africa's largest network of low-cost private schools teamed with development banks and new investors to support the Kenyan-based school and launch expansion into three additional countries. Its strong partnerships provided seed investments and assistance navigating new regulatory environments.

Many African nations struggle to provide affordable quality education to the poor in their societies. Limited classroom space, high absentee rates among teachers, hidden fees, and non-standardized curriculums all contribute to create obstacles that low income families often cannot overcome.

Three years ago NewGlobe Schools Inc. wanted to expand Bridge International Academies, which at the time operated 250 low-cost schools in Kenya. The goal was to increase the number of schools, which serve families living on $2 or less a day, to over 400 in Kenya and to replicate the Bridge model in Uganda, Nigeria and India. The ultimate objective is to provide access to education for 3.5 million low-income students by 2020 and 10 million by 2025.

Bridge Academies' innovative strategy delivers quality education to children of poor families at low cost. It leverages data, technology and scale to standardize everything from content development and teacher training to academy construction and billing. Computer tablets provided to Bridge Academy teachers allow them to deliver scripted lessons and track lesson completion and assessment scores.

Bridge schools are generally built on greenfield sites located in high density, low-income communities where children have to walk no more than 500 meters to the school. Its academies reach operational sustainability after just one year, on average.

The highly standardized and replicable model allows Bridge to charge students an average of just over $6 per month in fees, making them affordable to 90 percent of the people in the communities where they operate and encouraging poor families to send both boys and girls to school to improve their lives and prospects.

With an estimated price tag of $60 million and the new regulatory hurdles inherent in a cross-border expansion, NewGlobe's expansion project turned to development banks, including IFC, the World Bank, and CDC, the UK's development finance institution, for help. IFC made a $10 million preferred equity investment and CDC invested $6 million. The Gates Foundation invested $10 million, existing NewGlobe investors put in $15 million and new investors another $15 million. A $10 million loan was arranged from the Overseas Private Investment Corporation, the US government's development finance institution.

The funds were used primarily for new country expansion (71 percent) and new schools in Kenya (14 percent), and development of Bridge's software and general operations. IFC and the World Bank helped Bridge understand and navigate government policies and regulations in the three new markets.

Today Bridge educates more than 100,000 students in 400 nursery and primary schools across multiple countries. Bridge Academy students consistently outperform their peers in public and other low-cost private schools in reading and math, according to independent testing. Additionally, the World Bank has launched a rigorous, independent impact evaluation of the Bridge International Academies program in Kenya, which will be the first large-scale, randomized, controlled trial of fee-paying schools in sub-Saharan Africa.

In November 2015, Bridge's first class of students sat for the national exams in Kenya, and early results are positive. Bridge's very first academy in Mukuru Kwa Njenga, which opened in 2009, was one of 19 of its academies with a 100 percent pass rate and average scores that exceeded the national average. Bridge founders Jay Kimmelman and Shannon May were named Social Entrepreneurs of the Year, World Economic Forum for Africa, in 2014.

KEY RISK MITIGANTS

Financing Risk:

- IFC's provision of highly needed long-term financing to support Bridge's early stage expansion

Operational Risk:

- High replicability of Bridge's business model and success in Kenya

Market and Regulatory Risks:

- Action plan initiated by IFC, World Bank and other development partners to support Bridge's cross-border expansion
- World Bank assistance in understanding and navigating government regulations in the new markets
- NGS certification as an examination center for 134 of its schools

CASE STUDY

Eleme Petrochemical

A Turnaround Plan for an Underperforming Manufacturer

Nigeria's Eleme Petrochemicals was transformed from a poorly performing and loss-making industrial giant into a world-class chemical manufacturer by an Indonesian investor after IFC provided advice, financing, and deal structuring to allow privatization of the state owned firm.

Nigeria, Africa's most populous country, also has Sub-Saharan Africa's largest hydrocarbon reserves, making it an ideal place for petrochemical manufacturing. The nation is also a major consumer of polyethylene and polypropylene, chemicals used to make plastic products, from toys to soda bottles.

Yet in the early 2000s Nigeria's downstream chemical sector – processing, manufacturing and distribution – remained significantly underdeveloped, rendering the nation a net importer of the chemicals.

Eleme Petrochemicals, one of two state owned ethylene manufacturers in Nigeria, had suffered operational problems since it opened in 1995, including inadequate maintenance, a lack of spare parts, equipment breakdowns, and other inefficiencies. The result was an unacceptably low capacity utilization rate at the plant with frequent and prolonged shutdowns.

The company badly needed a turnaround capital investment program to return it to profitability. With Nigeria's government looking to privatize Eleme, Indonesia's Indorama Group approached IFC for assistance in acquiring the company, its first investment in Africa.

In 2006 IFC structured a turnaround capital investment plan for Eleme and Indorama that included a $50 million loan by IFC, an $80 million syndicated loan with 12 other partners, and a $32 million loan from German development bank DEG and Netherlands' development bank FMO.

IFC worked with Indorama to put a two-tier structure in place with two special purpose vehicles to finance the purchase plus a turnaround maintenance program to return the Eleme plant to full capacity utilization. The total cost of the project was $400 million, including $225 million for the acquisition, $130 million for the maintenance program, $30 million for working capital and $15 million for transaction expenses and other general expenses.

Other measures were taken to smooth the acquisition and turnaround, including improvement of the plant's environmental standards and significant involvement of the surrounding community, including a 7.5 percent equity stake owned by the local government.

As a result of the turnaround program, production at the Eleme facility increased from 8,502 metric tons the year of the acquisition to 282,286 metric tons per year in 2010. Eleme now supplies polymer products to over 200 plastic processing companies in Nigeria, supporting the country's value-added downstream chemical sector and boosting small and medium size businesses that use polymers as an input. Eleme employs 1,200 Nigerians in the Rivers State region and now exports products to Europe, Asia and other African nations.

The Eleme turnaround helped turn Nigeria into a net-exporter of polymers, which now account for 10 percent of the country's non-oil exports.

KEY RISK MITIGANTS

Financing Risks:

- IFC anchor financing, demonstrating support in a risky market
- IFC led due-diligence process on behalf of lenders
- Investment structure fair to all parties

Operational Risks:

- Indorama strong track record of delivering projects on budget and on time in diverse areas
- Experienced technical advice from SK Corporation
- IFC's base case under low capacity utilization assumptions reflecting potential inconsistent feedstock supply

Social & Country Risks:

- Employees and local community co-shareholders via local government
- Indorama proactive role in managing relationships with local communities
- Insurance against terrorism and sabotage

CASE STUDY

Helios

Raising Private Equity Funds Focused on African Opportunities

While only about 1.0 percent of global private equity goes to Africa, PE financing is gaining a foothold and PE funds raised a record $4.0 billion in 2014 to invest on the continent.

Helios Investment Partners used an equity injection from a development bank to attract investors who likely would have otherwise hesitated to expose capital to the many risks and obstacles that Africa presents. Africa lacks an institutional investor base with a long-term market view, so development banks can serve as a pillar of market investment that brings others along during good times, and can also play a countercyclical role by remaining involved when other investors flee.

Too often ignored by global investors, Africa has long suffered from an inadequate supply of long-term equity capital, with almost no PE funds investing in the continent until recently. The paucity of capital has been especially acute for investments in start-ups and small and medium size enterprises due to the risks inherent in Africa's generally small and often fragile markets.

Helios already had a record of spotting and investing in start-ups and high growth firms primarily in West Africa, including a well-known telecom tower leasing firm in Nigeria that demonstrated resilience despite challenges in growing its business. IFC provided an anchor investment of $20 million to Helios's first Africa fund in 2007. That helped draw additional investors to the fund and it eventually secured total capital commitments of $304 million.

With a growing reputation for solid returns and an extensive knowledge of the African marketplace, Helios raised a second fund, Helios II. It initially struggled to close amid the fallout from the global financial crisis. IFC came forward with a commitment of $60 million to the fund in 2010. That helped provide the comfort other investors required and resulted in a second successful closing at $908 million. IFC and Helios co-invested in projects, sharing both risks and incentives, to provide additional financing.

Helios II is now fully invested in ten companies across various sectors on the continent including oil and gas, financial services, e-commerce and electronic payments, advertising and telecom infrastructure. It is focused on growth opportunities located in Nigeria, Ghana, Angola, Cote d'Ivoire, Kenya, Tanzania and Uganda.

IFC also made an equity investment of $25 million to Helios's third fund (Helios III). That fund had a goal of closing over $1 billion in commitments and surpassed it in early 2015, with $1.1 billion, the largest Africa fund in history. Investors in the fund included sovereign wealth funds, corporate and private pension funds, endowments and foundations, as well as development institutions. The fund made its first investment in late 2014, buying a stake in a Nigerian firm that invests in oil and gas, on-line retail and micro lending.

Emerging markets, including Africa, enjoyed a steady flow of investment until recently. Yet in 2015 that reversed and became a large net outflow (including a two-thirds drop in PE investments) with investors suddenly becoming much more selective.

For long-term investors like development institutions focused on the private sector, market downturns offer new opportunities. In fact, returns on private equity investments in Africa have done relatively well in recent years, with a quarterly average internal rate of return of 10.29 percent from 2012 to 2015.

IFC's early, continuing commitment to Helios made it possible to mobilize significant further private capital by the PE firm and paved the way for other firms looking for returns in a low-yield world.

KEY RISK MITIGANTS

Financing Risks:

- IFC's presence with a long-term horizon, providing stability and comfort to other investors
- Debt facility for the fund prudently set at 17% of fund size

Operational Risk:

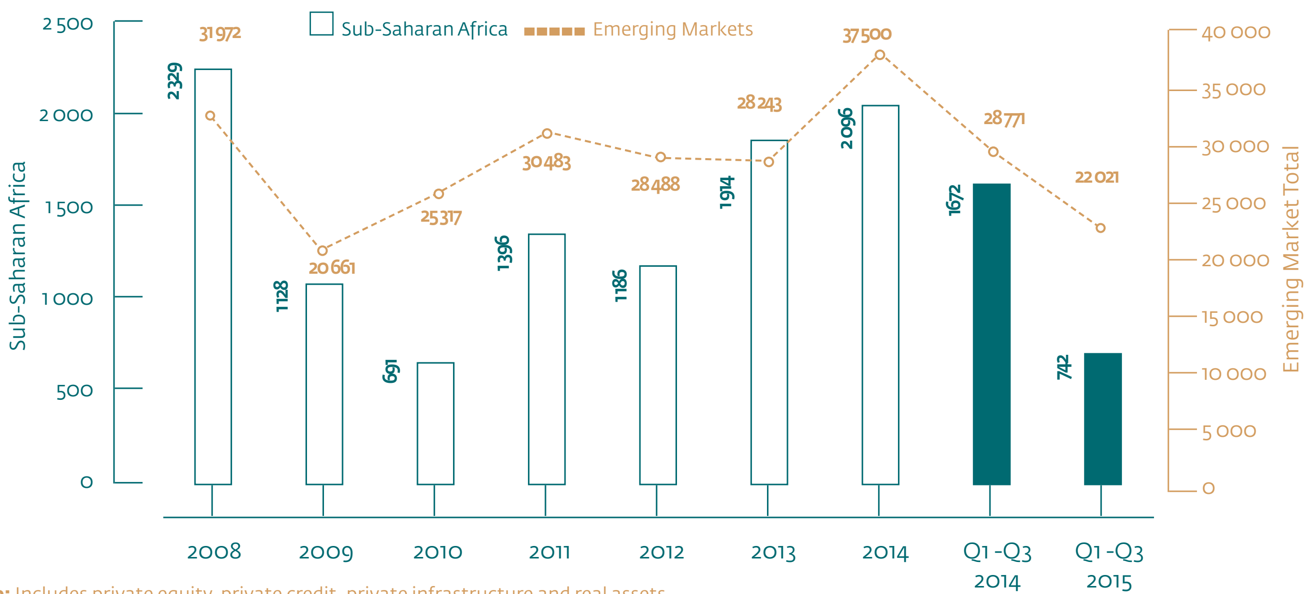
- Allocation of the profit to incentivize the team and facilitate team cohesion
- Helios team experience with start-up ventures and knowledge of target countries
- Locally-based staff recruited to provide guidance to portfolio companies and maintain local contacts
- The 1% total capital commitments of the fund managers, indicating strong alignment of incentives

PRIVATE EQUITY

Private Equity funds are another financing option gaining prevalence in Africa. An initial $20 million equity injection from IFC in 2007, followed by another $60 million in 2010, were made to Helios Investment Partners, an Africa-focused private investment firm. The development bank's anchor investment attracted otherwise hesitant investors, putting Helios on its way to a capital commitment goal of over $1 billion. Meanwhile, development finance institutions can also help global institutional investors take equity in African companies.

The IFC Asset Management Company, for example, offers a new way to expand financing for development and help investors benefit from IFC's extensive investment experience in developing countries. Since it was established in 2009, AMC has set up nine investment funds, with assets approaching $9 billion by 2015, including a number of funds specifically focused on Africa. *See Figure 7 and 8.*

FIGURE 7: **CAPITAL INVESTED THROUGH PRIVATE EQUITY** (US $mn)



Note: Includes private equity, private credit, private infrastructure and real assets.

Source: EMPEA Industry Statistics, data as of 30 September 2015.

FIGURE 8: **PRIVATE EQUITY INVESTMENT IN AFRICA BY SECTOR, 2014** (US $mn)

Source: EMPEA Industry Statistics

MEETING THE MARKET CHALLENGE

Certainly challenges remain to investing in emerging markets in general, and in Sub-Saharan Africa in particular. Investors looking at opportunities in the region must consider political and sovereign risk, currency risk, regulatory uncertainty, governance and corruption issues, and a lack of local expertise and suitable investment vehicles, among other factors. Even in developing economies with mature capital markets and stable political systems, achieving the investment grade rating that many institutional investors require often remains a challenge.

Therein lies the role for development finance institutions, which can help mitigate risk and "crowd in" private investment by:

- *Contributing anchor funding to provide the confidence and creditor status investors require.*
- *Providing institutional investors with new ways to tap African markets, such as through IFC Asset Management Company, which provides equity investment alongside IFC.*
- *Providing insurance against political risks such as expropriation and terrorism.*
- *Providing currency swaps to eliminate foreign exchange volatility.*
- *Providing structuring and technical expertise to ensure bankability.*
- *Improving local policy and regulatory environments.*
- *Supporting regional governments with project selection and preparation.*
- *Strengthening domestic capital markets and promoting cross-border investment.*

Even in difficult economic and risk environments, methods exist to underwrite successful investments in Africa.

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