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#### **Africa rising out of itself: The growth of intra-African FDI**

by

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Over the last decade Africa has attracted an increasing share of global foreign direct investment (FDI) inflows. China and other emerging markets are usually highlighted as important sources of this increase — and they are. However, perhaps the most significant contributor has been Africa itself.

In 2008, at the zenith of the global financial crisis, African firms dramatically expanded their Africa-wide presence. Intra-African greenfield FDI projects accounted for just 8% of all such projects into Africa in 2007, but rose to 22% in 2013, making Africa the second largest source of greenfield FDI projects into Africa in 2013, after Western Europe. Its relative contribution by capital expenditure is very similar. Relatedly, mergers and acquisitions (M&As) by deal volume shows that African acquirers have been the primary source of cross-border M&A since 2006.<sup>1</sup>

At the forefront are South African firms. The share of African countries in South Africa's outward FDI assets nearly doubled between 2004 and 2012, to 21%.<sup>2</sup> South African firms accounted for one third of all intra-African greenfield investment projects between January 2003 and January 2014, with the remainder coming from Kenya (14%) and Nigeria (12%), followed by Togo, Egypt, Mauritius, and Tunisia (20% combined).

Less risk-averse African investors look beyond the usual suspects. FDI from developed economies largely goes to South Africa, North Africa and the oil exporters. By contrast, the largest recipients of intra-African FDI projects between January 2003 and January 2014 were (in order) Ghana, Uganda, Tanzania, Nigeria, Kenya, Rwanda, and Zambia. These seven countries received over 45% of total intra-African investment projects (over 400) during this period. Moreover, intra-African FDI was the primary source of project inflows for several smaller African economies (e.g., Burundi, Rwanda, South Sudan) – even if absolute numbers are modest.

Intra-African FDI has driven investment into Africa's service and consumer industries. Local brands with strong growth are at times challenging non-African multinational enterprises (MNEs).<sup>3</sup> Perhaps most visible has been the regional expansion of African retailers, often through M&As. In response, non-African MNEs are increasing investment and expanding product ranges in Africa. This has supported

a widespread *relative* shift away from resource-seeking FDI, which declined from 35% of the number of incoming greenfield projects (and 81% of capital expenditure) in 2003, to 11% of project inflows (and 36% of capital expenditure) in 2013. A strong reversal seems unlikely soon, with the Bloomberg Commodity (price) Index at a five year low.

The rise of intra-African FDI has had two clear impacts. First, African investors are slowly becoming more competitive as they acquire complementary assets, expand scale and enhance brand value.<sup>4</sup> Second, competition in Africa is increasing. This is creating a virtuous circle as investments from companies who fear being permanently disadvantaged as late movers, or see their market positions slipping, are sucked in.

Intra-African FDI can have further benefits for lead firms and local suppliers. For the latter, product and process standards may be easier to meet. For lead firms, regional suppliers can reduce lag and lead times in production (such as for Southern African clothing production).

However, intra-African FDI is not an unmitigated blessing: pre-existing suppliers of lead firms often largely benefit (at least initially) from the resulting demand increase, while upgrading opportunities for new local suppliers will be strictly governed by the lead firm. This is because intra-African FDI is driven by large enterprises (such as Dangote and Shoprite), which confront the same forces of global competition as non-African investors by squeezing suppliers.

How then can the benefits be fostered? Governments can help local suppliers become more competitive by developing complementary infrastructure, using targeted cluster policies (including training and innovation strategies), and judiciously adopting local content requirements (when possible).

Essential for integrating smaller suppliers and upgrading producer capabilities is the facilitation of competitive market access to regional as well as *global* input and output markets. The ongoing Tripartite FTA negotiation is important in this respect,<sup>5</sup> despite concerns over the size of its potential market access gains.<sup>6</sup> Cross-border investment issues in the FTA, when negotiated, have considerable potential to create uniformity in how FDI is managed and can establish a more sustainable investment framework,<sup>7</sup> provided enforcement institutions are established.

The harmonization of labor legislation, already agreed upon by most regional economic communities, requires proper implementation and monitoring to support economic and social upgrading. This is particularly salient as investors from developing countries often have less developed corporate social responsibility codes and related standards. Finally, investment promotion agencies in African countries need to be better attuned to the prominence and particularities of African FDI.

Without these and other policies, our concern is that smaller domestic enterprises and producers risk not sharing sufficiently in the gains from intra-African FDI.

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<sup>1</sup> Mergermarket, *Deal Drivers Africa 2013*, available at [http://mergermarketgroup.com/wp-content/uploads/2013/12/Deal\\_Drivers\\_Africa\\_2013.pdf](http://mergermarketgroup.com/wp-content/uploads/2013/12/Deal_Drivers_Africa_2013.pdf).

<sup>2</sup> South African Reserve Bank, *Quarterly Bulletin* (various years), available at <http://www.resbank.co.za/PUBLICATIONS/QUARTERLYBULLETINS/Pages/Quarterly-Bulletin.aspx>

<sup>3</sup> See "The rise of Africa's B-brands," *The Africa Report*, May 16, 2014, <http://www.theafricareport.com/North-Africa/the-rise-of-africas-b-brands.html>.

<sup>4</sup> Initiative for Global Development and Dalberg Global Development Advisors, *Pioneers on the Frontier*, [http://dalberg.com/sites/dalberg.com/files/IGD-Dalberg\\_Pioneers-on-the-Frontier\\_0.pdf](http://dalberg.com/sites/dalberg.com/files/IGD-Dalberg_Pioneers-on-the-Frontier_0.pdf); BCG, *The African Challengers*, <http://www.bcg.com/documents/file44610.pdf>.

<sup>5</sup> Negotiated between SADC, EAC and COMESA.

<sup>6</sup> Tralac, "Redirecting the Tripartite Free Trade Agreement negotiations?," June 26, 2013, <http://www.tralac.org/discussions/article/5571-redirecting-the-tripartite-free-trade-agreement-negotiations.html>.

<sup>7</sup> Along the lines of the SADC Model BIT.

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