The role of private equity investment in Africa's transformation

By Angela Simpson and Lydia Shadrach-Razzino

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The impact of global geopolitical and economic turbulence and the challenges of the pandemic have led private equity (PE) investors to carefully assess which sectors are expected to do well in Africa and where they can find high quality assets at the right price. Healthcare, technology, media and telecommunications (TMT), energy, infrastructure and financials have emerged as the most active sectors by value in Africa in the last few years, with PE investment in general rising substantially despite economic challenges. Rapid innovative developments in these sectors have attracted the attention of PE investors, and it is clear that the continent is open for business.

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The rise in PE investments in Africa was recently confirmed in a report by S&P Global Market Intelligence. The report notes that private equity and venture capital investments in Africa soared 66% year on year in 2022 to $7.7bn, the highest aggregate value for the region in the last five years. S&P pointed out that this big jump was due mainly to the acquisition of hospital operator Mediclinic International PLC by a consortium comprising its shareholder Remgro and Switzerland's Mediterranean Shipping Company (MSC), which is valued at more than $5bn. In terms of transaction volume, PE transactions have shown a steady climb in the region since 2018, reaching 404 deals in 2022. Both value and volume being on a steady climb is reflective of an optimistic environment.

Increased access and transformation

Expanding access to quality healthcare services and increasing domestic pharmaceutical manufacturing capacity dominate Africa's healthcare sector development agenda, and investment has been following in support of these objectives. Technology-focused healthcare delivery models, which allow for easier access to medical advice and care, especially in Africa's rural areas, had already begun easing the constraints of the traditional delivery model and driving further investment in digital healthcare across Africa before the pandemic hit, and have taken off since then. PE investors in this sector usually show long-term commitment, understanding of individual markets and strong partnerships with local stakeholders and governments, with the overall aim of improving access to public healthcare.

The TMT sector has been playing a positive role in transforming businesses in Africa, opening the sector up to competition, introducing new services and disrupting incumbent business models. The impact of the pandemic boosted existing trends, for example, digitalisation and the remote delivery of services. Well before Covid-19, businesses in Africa had been turning to technology to reduce costs, improve processes, grow customers, provide access to those without it and enhance innovation.

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Finance

Aligned to this, the financial sector is leading the way in developing new technologies, such as artificial intelligence systems, advanced analytics and digital trade finance platforms. Financial institutions in sub-Saharan Africa (SSA) have an important role to play in facilitating trade between the multitude of diversified economies with different financial systems following the implementation of the African Continental Free Trade Area (AfCFTA) agreement. This increased demand for new financial products and services has led to a corresponding increase in investment in the SSA financial sector.

Further, the African fintech space has shown incredible resilience to global market turmoil and there is still a lot more room for growth in segments such as such as alternative lending, digital investment and neo-banking. African economies are buoyed by young populations that are increasingly entrepreneurial and driven by technology-led innovation. Digital infrastructure is also attracting investor interest; there is an imbalance in the supply of data centres, for example, compared to the growth expected from consumers that need more data and are spending more time online.

Free trade agreement

AfCFTA is also providing numerous new opportunities for PE investors. The free trade agreement has seen the consolidation of a $1.3bn market with a combined GDP of $3.4tn. The start of trading in 2021 resulted in an increase in investor sentiment as investors took note of the agreement's first movers. AfCFTA is unlocking significant growth opportunities for the continent, providing the chance for countries to diversify their economies, scale production capacity, and widen the range of products made in Africa, in particular boosting the production of manufactured goods.

AfCFTA is also acting as an impetus for African governments to address their infrastructure needs and overhaul regulations relating to tariffs, bilateral trade, cross-border initiatives, and capital flows. The World Bank has noted that AfCFTA is expected to increase Africa's income by $450bn by 2035, as well as boosting intra-African trade by more than 81%. So far, beneficiaries of trade under AfCFTA have included a Kenyan car battery company and a women-owned Rwandan coffee company - both have taken advantage of the lower tariffs to export their products to Ghana. This is all good news for PE investors seeking new opportunities.

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More power

The energy sector in Africa has also been attracting PE investor interest. Access to power on the continent is hampered by the lack of access to competitive funding, the dire state of Africa's utility infrastructure, and the need for energy policy and legislation to be adapted to boost investment. However, new systems and networks are being designed around future environmental stressors and energy demands without having to consider the limitations of old infrastructure. With the use of mobile technology and the lack of existing electricity transmission networks, these developments are providing an opportunity for African communities to gain access to power by leapfrogging the traditional model of centralised generation and transmission of power.

New and cost-effective solutions that utilise renewable energy, green hydrogen, battery storage and smart power technologies, as well as the global drive towards a decentralised, decarbonised, and secure energy supply that addresses climate change and stimulates economic growth, are all leading to innovative PE investment opportunities.

ESG focus

There is also a growing focus on green, low-carbon, and sustainable initiatives in Africa. Environmental, social, and governance (ESG) have been incorporated into PE funds' general investment considerations for several years now, but it's fair to say that these are no longer nice-to-haves. Community healthcare, energy efficiency, staff training and qualifications, the reduction of greenhouse gas emissions, the highest standards of governance and best business practices, inclusion and diversity, social impact, and litigation risks are some factors they have been considering. Alongside the increased focus of equity investors on ESG, most lenders and investors are also prescribing particular ESG principles that a company must meet in order to receive funding.

Developments across the continent and the rapid innovation across sectors, in addition to the growing demand for services in key sectors, have resulted in PE investors having an important role to play in financing the continent's exciting transformation.

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