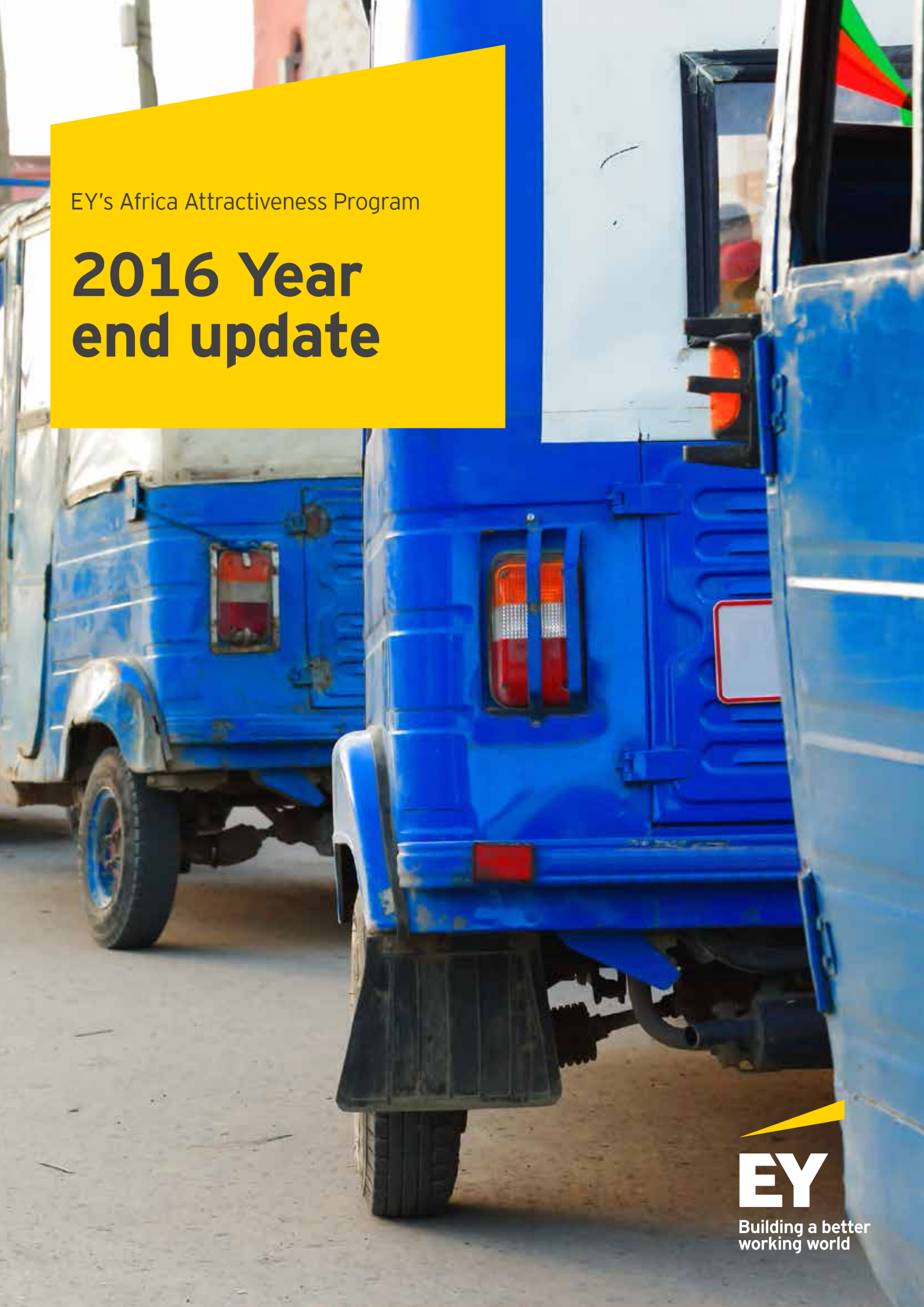
EY's Africa Attractiveness Program

2016 Year end update



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Content

Introduction

The implications of multispeed growth for FDI in Africa

2016 has been the worst year for average economic growth across Sub-Saharan Africa (SSA) in over 20 years. However, it is evident that the overall slowdown in growth masks significantly variable economic performance. The sharp downward revisions in growth forecasts this year mainly reflect challenging conditions in SSA's three largest economies, Angola, Nigeria and South Africa. Outside of these three economies, a number of bright spots remain, particularly in the East, Francophone and North African regions, where growth rates of 4% and above are still being achieved. Economic recovery in Angola, Nigeria and South Africa is likely to be a tough and gradual process. However, a diverse group of other economies – including Cote d'Ivoire, Senegal, Ethiopia, Kenya, Tanzania, Mozambique and Egypt are expected to sustain high growth rates over the next 5 years.

We anticipate that this mixed picture – one that the International Monetary Fund recently referred to as "multispeed" growth – will be reflected in FDI patterns over the next few years. We also anticipate that investor sentiment towards Africa as an attractive investment destination is likely to remain somewhat softer over the next few years. This has far less to do with Africa's fundamentals than it does with a world characterized by heightened geo-political uncertainty and greater risk aversion. Companies already doing business in Africa will continue to invest, but will probably exercise a greater degree of caution and be more discerning. Some of them will invest at a slower pace, looking to consolidate operations and drive profitability; while others are likely to double down on their investments, using this period of economic slowdown to further strengthen positions in key markets.

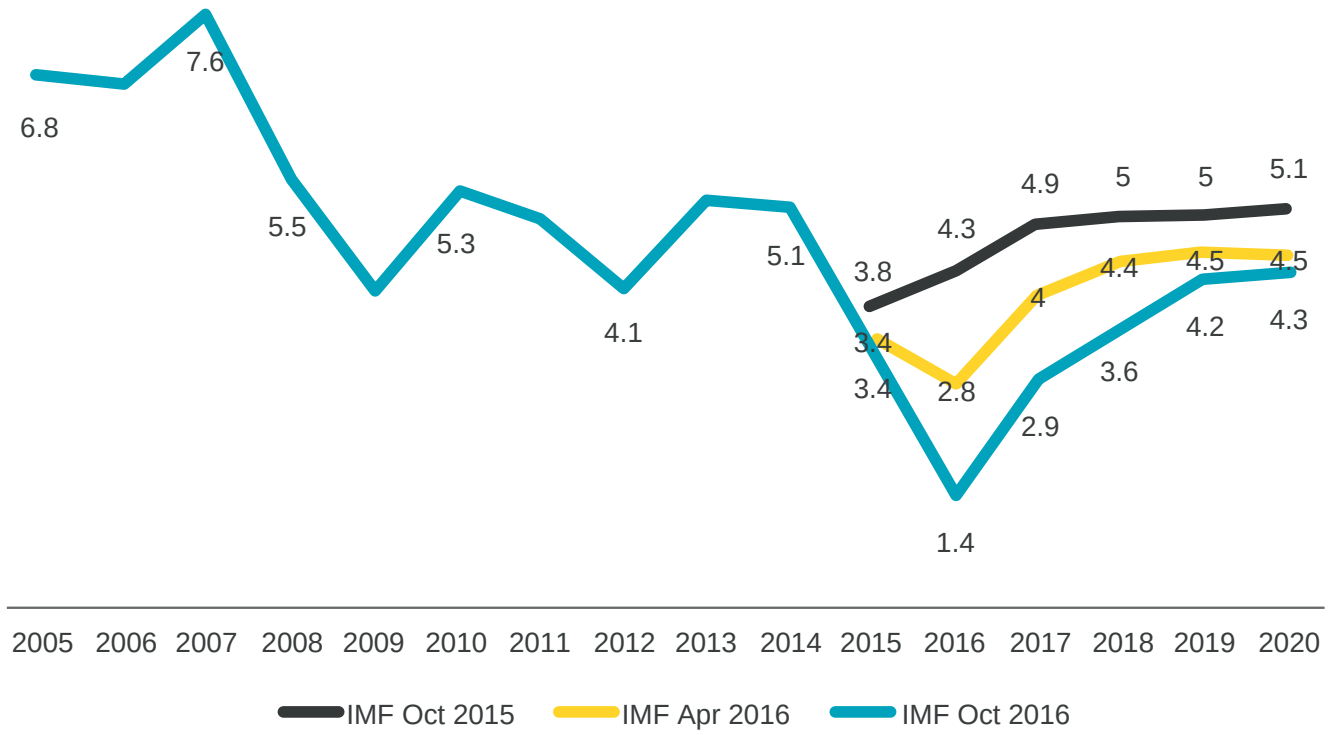
The upshot of multispeed growth and more discerning investors is likely to be a greater degree of unpredictability in terms of FDI patterns. It is also quite possible that there will be a relative slowdown in investment in SSA over the next 18 months, as investors adjust their strategies. This is evident to some extent in the relatively slower FDI activity into Africa in the first half of 2016. Whilst North Africa saw stronger FDI activity, SSA saw a slow-down in project numbers and capital inflows. However, this must also be understood in context of a generally slower FDI environment globally. Relative to the rest of the world, Africa's growth remains relatively strong, as does its FDI projects and capital inflows. The Brexit result at the end of June, and resulting uncertainty in the second half of 2016, could further impact FDI into Africa, particularly given the strong role the UK already plays as a major investor in Africa.

However, from our perspective, any shorter term shifts in FDI levels will be cyclical rather than structural. We anticipate that the evolution of the composition of FDI – increasing diversification in terms of sources, destinations and sectors – will continue. Over the longer term, as economic recovery slowly gathers pace and as many African economies continue to mature, we also anticipate that levels of FDI will remain robust and will continue to grow.

Economic update

Africa's immediate growth prospects have slowed, but with differing regional dynamics

SSA GDP growth forecast (at constant prices)



Source: ***IMF World Economic Outlook***, October 2016

SSA's growth forecasts for 2016 have fallen to a two decade low. The World Bank expects growth of 1.6% this year, down from a previous estimate of 2.5%. This continues a pattern of downward forecast revisions this year.

However, beneath the averages and headlines, the growth dynamics across different individual countries and sub-regions are very mixed. The 'heatmap' below provides a snapshot of macroeconomic resilience across some of the key SSA economies, and illustrates just how variable economic performance is across different parts of the continent. The color of each block represents the longer-term position for that metric – green being positive and red negative. The color of the circle in the block represents the current trend.

	Government debt	Current account	Exchange rate	Inflation	GDP growth
Angola					
Côte d'Ivoire					
Ethiopia					
Ghana					
Kenya					
Nigeria					
South Africa					
Tanzania					
Zambia					
DRC					

Source: Exchange rates from Oanda.com; GDP growth; IMF Inflation; Current Account, Government debt - all from TradingEconomics.com

It is clear from this illustration that the three largest economies in SSA – Angola, Nigeria and South Africa – remain under pressure. In the six months since March 2016, the position of Angola and Nigeria in particular has deteriorated, with the Nigerian economy entering a recession and Angola forecast to register zero growth this year. Sustained low oil prices, and the subsequent deteriorating terms of trade that both economies have experienced since 2014, has led to a growing current account deficit and rising government debt levels.

Although growth in SA remains low, there have been some improvements in key macro-economic indicators in the past six months – including the current account deficit and a somewhat stronger currency. This indicates at the very least that the economy has stabilized, and may in fact be a signal of a gradual recovery.

In fact, there are signs that the worst of the economic downturn across the continent may be over, and that growth will recover, albeit gradually. For one, there has been some recovery in commodity prices, and the forecast is for a continued gradual rise in prices. Currencies have been less volatile in many instances (with the exception of Nigeria - for very specific reasons). That in turn has helped contain inflation, which is either slowing or at the very least, holding steady at current levels. This allows for monetary easing, which is supportive of rising consumer spending, and that is critical to the continent's longer term growth prospects.

At the same time, and in contrast to challenging economic conditions in the 'big 3', many of the East African and Francophone economies have remained resilient. Kenya , Ethiopia, Tanzania, Cote d'Ivoire and Senegal are among the African economies still expected to grow in the high single digits this year and next (and through 2021). This partly has to do with the major exports of many of these economies being less impacted by declining terms of trade. In addition, investment in infrastructure, domestic consumer spending and the continued evolution of services and manufacturing, continues to spur growth in these economies.

The key to overcoming weak global demand lies in enhancing diversification policies. Economies that span a broad range of sectors tend to fare stronger in such periods. Nigeria and Angola provide strong evidence of reliance on a single commodity, as both economies either face or are already in recession.

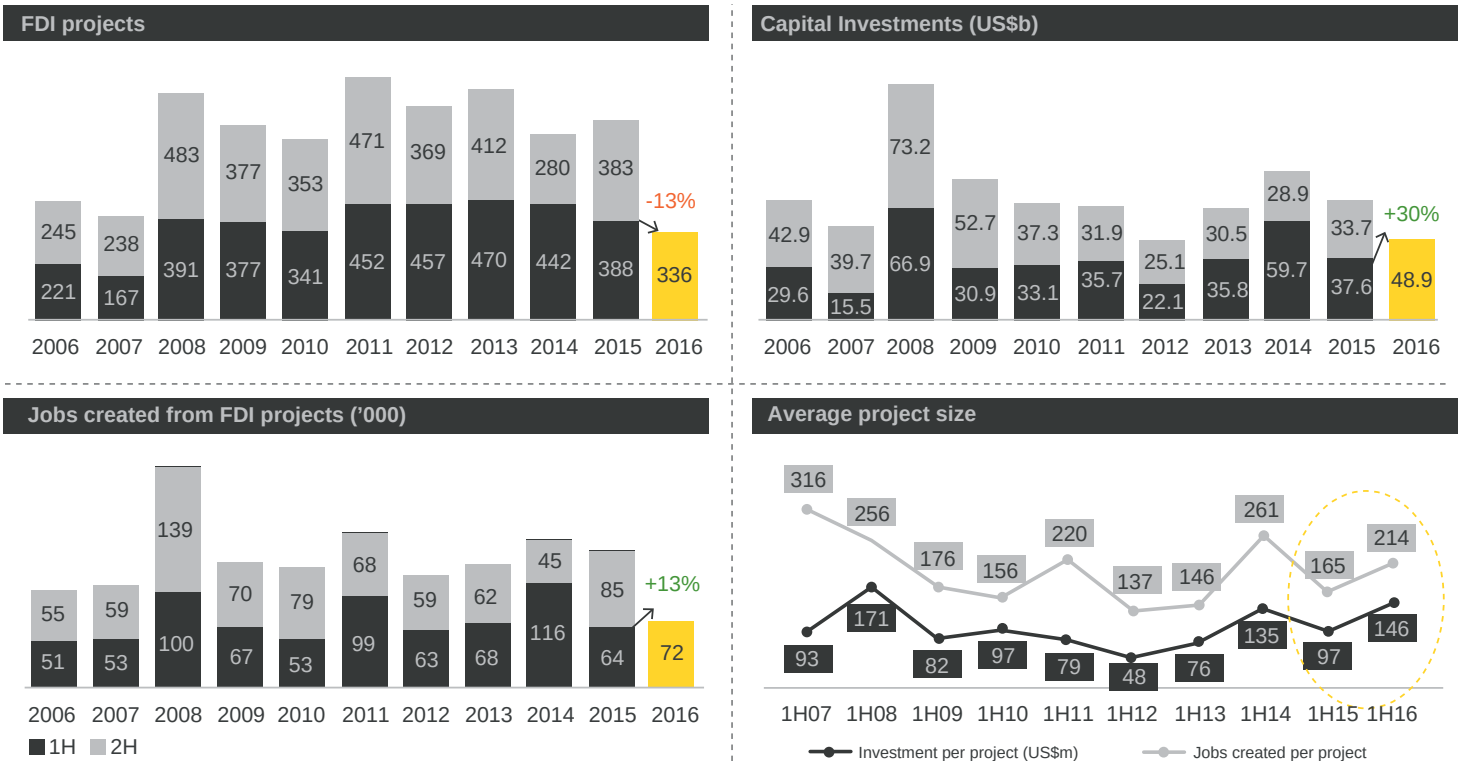
The resilience in certain African economies reinforces the need to accelerate the process of diversification in others. Diversification clearly requires structural economic reforms, and each country is at a different point along this path. This provides enormous opportunity for growth across the region, as investors respond to pragmatic policy reforms and seek opportunities across growing consumer, services and industrial sectors.

FDI update

FDI in 1H16: fewer projects, but growth in capital and jobs

In the first six months of 2016 (1H16), greenfield FDI projects in Africa were down 13.4% on 1H15 levels. However, the capital value of total investments across the continent rose 30.0%, with the average capital investment per project increasing from US97m to US$145m in 1H15. Similarly, job creation in Africa resulting from FDI projects was also up, rising 12.6% from 1H15 levels. This means that an FDI project in Africa on average created 214 jobs in 1H16 compared to 165 jobs during the same period in 2015. These capital- and job-intensive projects were largely directed toward two sectors: transport & logistics and real estate, hospitality and construction (RHC).

Fewer but larger project (both by capital and jobs created) in Africa in 1H16



Source: fDi Markets

North Africa's recovery continues

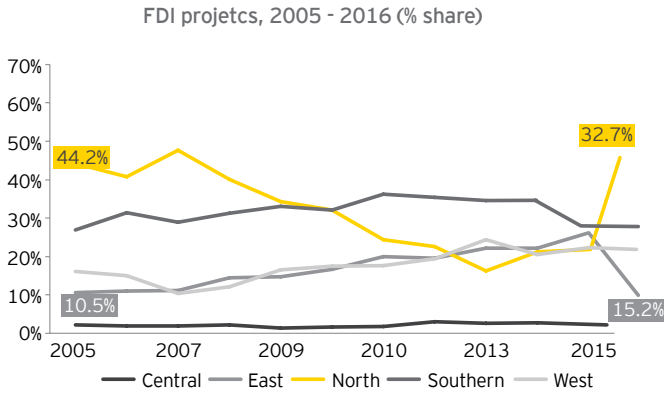
In 1H16, North Africa continued its recovery, attracting 23.6% more FDI projects than in 1H15, and triple the capital investment than 1H15.

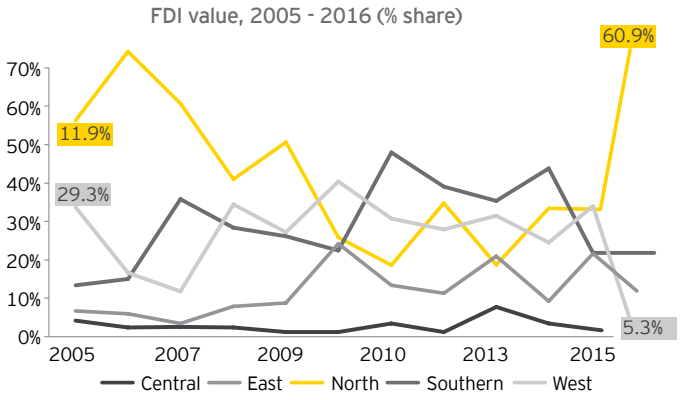
North Africa rebound strongly after a weak 1H15

	FDI projects			Capital investment (US$b)		
Destination region	1H16	1H15	%change	1H16	1H15	%change
North Africa	110	89	23.6%	29.8	9.9	199.2%
Southern Africa	92	106	-13.2%	9.8	7.4	32.6%
West Africa	75	81	-7.4%	2.6	11.3	-77.3%
East African	51	103	-50.5%	6.2	8.7	-29.2
Central Africa	8	9	-11.1%	0.6	0.2	180.3%

Source: fDi Markets

North Africa regains a clear lead, last seen in 2009





Source: fDi Markets

Within North Africa, **Egypt** remains the largest investment destination, posting a 32.4% increase in FDI projects over 1H15. This accounts for a 43% share of the sub-region's capital investment. During this period, there was notable growth in investment into two sectors, namely business services and RHC. Chinese investors were the most active, contributing more than one-fifth of the FDI projects in Egypt. This strong performance seems to lend credence to economic reforms currently underway in the country, including a reduction in income tax rates and new mechanisms to resolve commercial disputes. Even so, the Egyptian economy is estimated to require an additional US$300b over the coming years to reach its potential.[1]

Other North African economies – including **Morocco, Algeria** and **Tunisia** – also reported higher inward investment project numbers in 1H16. In contrast, investment slowed in most hub economies across SSA, including **South Africa, Ghana, Nigeria, Kenya** and **Mozambique.** Interestingly, **Cote d'Ivoire** continued its rise, with FDI projects increasing 28.6%. Technology, media and telecommunications (TMT) drew the most interest, particularly from French investors.[2] Investors in Côte d'Ivoire are encouraged by its robust economic growth (averaging 8.9% since 2012) and strong focus on developing infrastructure.[3] The country has also made strong progress in improving its business climate, evident from its move up the World Bank's Doing Business rankings from 177th in 2013 to 142nd in 2016.[4]

[1] "Egypt's Sisi Closes Economic Conference With Call for Further Investment," The Wall Street Journal website, http://www.wsj.com/articles/egypts-sisi-closes-economic-conference-with-call-for-further-investment-1426439594, accessed 28 September 2016.
[2] "Buzzing Abidjan puts Ivory Coast on road to revival," Financial Times website, http://www.ft.com/intl/cms/s/0/8dff1068-1f08-11e5-ab0f-6bb9974f25d0.html?siteedition=intl#axzz3ep5OwtsX, accessed 18 March 2016; "Burger King to Open First West Africa Restaurant in Abidjan," Bloomberg website, http://www.bloomberg.com/news/articles/2015-12-01/burger-king-to-open-first-west-africa-restaurant-in-ivory-coast, accessed 21 March 2016.
[3] World Economic Outlook Database, IMF, April 2016; "Ivory Coast aims to entice investors with 'new vibe' of stability and growth," The Guardian website, http://www.theguardian.com/global-development/2016/mar/07/ivory-coast-entice-investors-stability-growth-infrastructure, accessed 29 March 2016.
[4] Doing Business 2016, World Bank, October 2015

Asia-Pacific investors to the fore, led by China and Japan

In line with previous years, Western Europe remained the largest regional investor in Africa, contributing 35.1% of FDI projects and 17.8% of capital investment in 1H16. At a country level, the US retained its lead with 13.1% of total FDI projects, focused mostly in TMT and transport & logistics.

France emerges a strong challenger

France announced 43 FDI projects in Africa in 1H16, up 19.4% on 1H15, entailing investment of US$1.1b, and creating 3,259 jobs. The more notable development was in terms of rankings, with France almost closing the gap with the US. Compared to 1H15, French companies were particularly active in TMT (34.9% of FDI projects) and business services (18.6%). Morocco remains the favored destination, with Cote d'Ivoire moving up to the second most preferred destination for French companies.

Asia-Pacific investors gain traction

There has been a surge in investment from Asia-Pacific, with the region becoming the second largest when measured by FDI projects. In 1H16, these investors, particularly from China and Japan were also the largest contributors both by capital value and FDI jobs.

China

Chinese-sourced FDI into Africa saw a dramatic increase in 1H16 compared to 1H15. FDI projects were up a remarkable 209%, making China the third biggest investor in the continent. In fact, both capital investment and jobs created in 1H16 surpassed those recorded in any year since 2005. Chinese investors were particularly prominent in the automotive and transport & logistics sectors.

Almost one-third of FDI projects were directed toward Egypt. In January 2016, Chinese President Xi Jinping visited Egypt, and committed to a US$700m loan for the National Bank of Egypt. China and Egypt are planning US$15b investments across 15 electricity, infrastructure and transport projects.[5]

China's evolving economic ties with Africa[6]

There has been much interest in the nature of China-Africa economic ties. Since the late 1990s, Sino-African trade has grown rapidly, with China now Africa's largest trade partner. In 2015, China's exports to Africa stood at US$94.4b while imports from the continent were valued at US$51.3m. China exports a wide variety of consumer and capital goods to Africa but imports mainly commodities such as oil, minerals and other natural resources.

Now, looking at the greenfield foreign investment picture, our data shows that since 2005, China has invested in 227 FDI projects in Africa, totaling an investment outlay of US$30.3b and creating 92,333 jobs. Interestingly, this investment is well-diversified across sectors, covering resource-oriented ones such as mining and metals, services as well as manufacturing. Our data also reveals diversification of Chinese investment across more countries, covering both resource-rich nations such as South Africa, Nigeria and Angola, and agriculture exporters such as Kenya.

[5] "China's Xi visits Egypt, offers financial, political support," *Reuters website*, http://www.reuters.com/article/us-egypt-china-idUSKCN0UZ05I, accessed 28 September 2016.
[6] The evolving role of China in Africa and Latin America, Economist Intelligence Unit, 2016; "China's Investments in Africa: What's the Real Story?," *Knowledge@Wharton website*, http://knowledge.wharton.upenn.edu/article/chinas-investments-in-africa-whats-the-real-story/, accessed 3 October 2016; "A Fork in the Road," IMF website, http://www.imf.org/external/pubs/ft/fandd/2016/06/chen.htm, accessed 3 October 2016.

Besides trade and FDI, Chinese companies and state-related entities have financed and built many infrastructure projects across the continent, including ports, roads, railways, dams, telecom networks, power stations and airports. One notable example is the October 2016 launch of a Chinese-built railway linking Addis Ababa in Ethiopia to the port of Djibouti, involving an investment of US$4b.[7]

At the 2015 Forum on China-Africa Cooperation held in December 2015, the Chinese President committed US$60b in funding support to Africa to boost agriculture, encourage industrialization and build roads, ports and railways over the next three years.[8] Similarly, in July 2016, Chinese companies and banks reached US$17b worth of preliminary cooperation pacts with African counterparts in sectors such as infrastructure, energy, pharmaceuticals and technology.[9]

Japan

In 1H16, Japan became Africa's fifth largest investor, tying with South Africa. Japanese investors were responsible for 15 FDI projects on the continent, up from 8 in 1H15. Both capital investment and jobs created increased in 1H16, up 766% and 61%, respectively. By sector, there was an uptick in FDI activity in TMT, DIP, agri-products and coal, oil and natural gas. More than half of Japanese FDI projects were directed to South Africa, followed by Mozambique, Tanzania and Botswana. In recent years, Japan has deepened ties with Africa in a bid to secure resource supplies and in return, fulfil the continent's demand for infrastructure. In August 2016, Japanese Prime Minister Shinzo Abe announced US$30b investment in Africa, including US$10b for electricity generation projects and for the upgrade of urban transport systems and ports.[10]

[7] "Major Chinese-built railways in Africa," *Xinhua website*, http://news.xinhuanet.com/english/2016-10/06/c_135733943.htm, accessed 6 October 2016.
[8] "China's Xi cheers African leaders with pledge of $60 billion for development," *Reuters website*, http://www.reuters.com/article/us-china-africa-idUSKBN0TN0MD20151204, accessed 30 September 2016.
[9] "China, Africa ink $17 billion preliminary cooperation pacts: Xinhua," *Reuters website*, http://www.reuters.com/article/us-china-africa-idUSKCN1081PF, accessed 1 October 2016.
[10] "Japan's Abe Dangles $30 Billion at Africa Leaders in Nairobi," *Bloomberg website*, http://www.bloomberg.com/news/articles/2016-08-27/japan-s-abe-dangles-30-billion-at-african-leaders-in-nairobi, accessed 11 September 2016.

Automotive and transport and logistics gain traction

Our half-year report indicates that the potential of Africa's growing consumer class holds steady. Collectively the consumer facing sectors, namely TMT, Consumer Products and Retail (CPR) and financial services remain the primary beneficiaries of FDI projects into Africa in 1H16.

TMT remains the leading sector

During 1H16, TMT attracted 23% of FDI projects in Africa, up 6.9% on 1H15. French companies were the largest investors, with projects growing to 15 in 1H16 from 5 in 1H15. Digital transformation is gaining momentum in Africa, paving the way for continued, strong TMT investments. Internet usage has grown from 16.7% in 2013 to 22.5% in 2015. Mobile subscriptions have also gone up sharply, with Africa recording the strongest growth of any region in 2015.[11]

Transport and logistics gains importance

With a 19.2% increase in FDI projects, transport & logistics became the fifth largest sector in 1H16. Thanks to substantial investments from Chinese companies, the sector also ranked second in terms of FDI capital value, and was the third largest contributor of FDI jobs. Global transport and logistics providers see an opportunity to 'connect' Africans to markets, given the relatively underdeveloped state of infrastructure.[12]

Automotive creates more than a fifth of total jobs

FDI projects in the automotive sector continued to grow in 1H16, originating mostly from Chinese, German and French manufacturers and suppliers. Morocco, South Africa and Algeria were the largest destinations given their dominance in this space. Interestingly, the automotive sector emerged as the top FDI jobs creator in Africa in 1H16. One example is France's Renault, which already has two plants in Morocco, committing to invest US$1b in the country, creating 50,000 jobs.[13]

Automotive revs up in Africa

Opportunities for Africa's automotive industry are looking increasingly attractive, on the back of rapid urbanization, improving infrastructure and road connectivity, as well as favourable government policies. Though historically an importer of automobiles, the continent is expanding its manufacturing base. The promising automotive markets include:

- **South Africa:** The automotive sector is the country's largest contributor to manufacturing GDP. The South African Government's auto-incentive program has prompted many automakers including Toyota Motor Corp., Ford Motor Co. and BMW AG to set up operations in the country. The sector has potential to expand production to more than 900,000 vehicles annually by 2020. In August 2016, Chinese state-owned Beijing Automotive International Corp. reached agreement with the operator of an industrial development zone in Port Elizabeth, to invest US$819m in a new plant.[14]
- **Morocco:** The country has positioned itself as an export base for Europe, the Middle East and Africa. In 2015, Ford Motor Co. and PSA Peugeot Citroen announced plans to expand operations in Morocco.[15] Peugeot is planning a US$632m assembly plant near Kenitra, with capacity to build 90,000 vehicles a year, scheduled to start production in 2019.[16] Following Peugeot's investment announcement, Morocco expects its annual automotive exports to reach US$10.2b by 2020.[17]
- **Algeria:** In a bid to reduce dependence on expensive imported vehicles, the Algerian government is promoting investments and creating a pro-business climate for the automotive sector. French manufacturer Peugeot-Citroën and Italy's Iveco have already outlined plans to build new assembly factories in the country over the next few years.[18]
- **Nigeria:** In a move designed to cut imports and reduce the economy's dependence on oil, government is offering incentives including lower import tariffs, tax holidays for producers and clamping down on vehicle smuggling. Automakers including Honda Motor Co., Nissan, Ford and Hyundai are already building capacity in Nigeria. Over the next five years, the country plans to assemble 500,000 vehicles annually.[19]

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[11] *Statistics*, International Telecommunications Union, 2016.
[12] "6 reasons to invest in Africa," *World Economic Forum website*, https://www.weforum.org/agenda/2016/05/6-reasons-to-invest-in-africa/, accessed 16 September 2016.
[13] "A NEW MAJOR RENAULT PROJECT IN MOROCCO; 10 BILLION DIRHAMS, 50,000 JOBS," *Royaume du Maroc Ministere de l'Industrie, du commerce, de l'Investissement et de l'Economie Numerique website*, http://www.mcinet.gov.ma/~mcinetgov/en/content/new-major-renault-project-morocco-10-billion-dirhams-50000-jobs, accessed 23 September 2016.
[14] "Chinese to Invest $819 Million in South African Car Industry," Bloomberg website, http://www.bloomberg.com/news/articles/2016-08-19/chinese-to-invest-819-million-in-south-african-car-industry, accessed 6 October 2016.
[15] "Paying Less in Slump Lifts Morocco Above Oil-Pumping Neighbors," *Bloomberg website*, http://www.bloomberg.com/news/articles/2015-09-14/paying-less-in-slump-lifts-morocco-above-oil-pumping-neighbors, accessed 17 March 2016.
[16] "Peugeot Plans $632 Million Morocco Car Plant in Africa Push," *Bloomberg website*, http://www.bloomberg.com/news/articles/2015-06-19/peugeot-plans-90-000-car-plant-in-morocco-in-africa-growth-push, accessed 18 February 2016.
[17] "Morocco sees $10 billion from auto industry exports by 2020,"*Reuters website*, http://www.reuters.com/article/us-morocco-economy-autos-idUSKCN0SS14Q20151103, accessed 24 May 2016.
[18] "Algeria's auto industry moves up a gear," *HSBC Global Connections website*, https://globalconnections.hsbc.com/uae/en/articles/algerias-auto-industry-moves-gear, accessed 5 October 2016.
[19] "Nigeria Targets 80% Local Manufacturing in Auto Industry," *Bloomberg website*, http://www.bloomberg.com/news/articles/2015-12-03/nigeria-targets-80-local-manufacturing-in-auto-industry-by-2023, accessed 17 September 2016.

Conclusion

FDI patterns in Africa for the first six months of 2016 reflect, to a large extent, broader macroeconomic trends. Many of the economies that are under pressure have experienced a slowdown in FDI flows – perhaps most notably Nigeria and SA. Conversely, economies with a positive growth outlook - such as Egypt and Cote d'Ivoire – have experienced strong growth in FDI flows. This multispeed picture – in terms of both economic and FDI performance is likely to persist for the next few years.

We do not, however, anticipate a sharp decline in overall FDI levels in Africa. A key factor here is the structural evolution in FDI in Africa over the past decade – from a high concentration of source countries and destination markets and sectors, to a far more diverse FDI landscape. As a result, risks and opportunities are being spread much wider, and there is no longer an over-dependence on a limited group of investors or sectors to drive FDI performance.

Looking forward, the uneven nature of opportunities across Africa will make it a more challenging investment environment over the next few years. Nevertheless, as economic recovery gathers momentum in key economies, so the current uncertainty will begin to ease. For those already doing business in Africa, now actually may be the ideal time not only to consolidate, but to consider doubling-down on investments to further entrench relationships and market positions. As Winston Churchill famously said, "Never let a good crisis go to waste."

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