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BRICS AND AFRICA, Partnership for Development, Integration and Industrialisation

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Summary of intervention

Presidents and Chairmen, chairman of the day, comrades and colleagues

- Refocuses the continental investment debate appropriately
- I will not bother you with statistics or magnitudes, which we all already know about
- I will focus on principles that should change our behaviour and approach towards each other, as partners
- This is far more important than the rands and cents, we can throw at the challenges that face us

1. Investing in infrastructure vs investing in development
    1.1. Infrastructural gaps pose one of the biggest constraints for our economies
    1.2. Could be single biggest challenge for continental growth and development
    1.3. The lack of rail infrastructure and the inadequate capacity to generate electricity add 30%-40% to the cost of goods traded among African countries... Compromises our production possibility frontiers
    1.4. Recently, a study revealed that at least 20% of food produced, wasted between the farm gate and the table ... Increases our economic dependency and human vulnerability
    1.5. Given resource endowments, these are avoidable constraints
    1.6. Focus on investing towards eradicating these, is key
    1.7. "Investing for optimal investing..." ensuring that investments work for society. Investing to unlock the capacities of our economies
    1.8. "Investing right" ... For growth, unemployment and poverty reduction
    1.9. Infrastructure enhances the efficiency of the economy, thus making this possible to achieve these objectives
    1.10. Integrating investment decisions to the underlying weaknesses of the macro economy

1.11. "Developmental investment strategy" is in response and recognition of this link
1.12. Four pillar system - economic, social, green & SMME development
1.13. This is not only a South African strategy... It is continental

2. Reliance on own resources vs FDI - sustainability?

2.1. Significant capital resources on the continent
2.2. These need to be mobilised appropriately and optimally
2.3. Collaboration can improve the effectiveness of investing, at the level of continent
2.4. Need for continental collaboration, amongst long term funders, not only DFIs but also pension funds (Gaps are vast and resource requirements are huge... Inga, airports)
2.5. If not well managed, FDI stifles long term sustainable growth, due to medium term capital reversals
2.6. Deprives domestic economy of higher and predictable reinvestments
2.7. South African experience is a case in point
2.8. The Brics partnership is key to minimising these negative implications

3. Sustainability is key

3.1. Can only be underpinned by policy certainty and predictability
3.2. Comparable policy and regulatory framework across continent
3.3. Ensuring crowding in of private sector
3.4. So, investments cannot take place in isolation of investor perception

4. Integration

4.1. Can only be aided by higher level of commonality of future outlook
4.2. Collaboration
4.3. Single economic entity at the continent
4.4. Risk equalisation
4.5. Long term view on investing... NDP
4.6. This will allow for persistent investing which is prerequisite for successful industrialisation
4.7. SMME and entrepreneurial development focus

5. What are the challenges?

5.1. Investment vs institutional
5.2. Energy
5.3. Transport, rail, road, air...
5.4. Technology, ICT
5.5. Water & sanitation
5.6. Agriculture, 15% cultivated
5.7. Housing
5.8. Education & health
5.9. The "S" on Brics should be seen as representing the sentiments and aspirations of the entire continent
5.10. This extends the dynamics that this institution should deal with
5.11. Deepening of institutional cooperation, deal with underlying potential, perception and expectations
5.12. So, it cannot only be about bricks and mortar! It cannot only be about financial intervention. It should go much deeper than that.
5.13. Dealing with the underlying macroeconomic imbalances is paramount
5.14. That is how intricate the challenges are and that is how astute we should respond in this partnership.

I thank you

DETAILED VIEWS ON SUBJECT

CONTEXT

1. Africa's history has been that of a continent with poor infrastructure, widespread corruption, political instability, wars, poverty and high unemployment. However, over the past decade this story has been changing; and with Africa's population set to overtake China's by 2035, the potential rewards of investing in Africa cannot be ignored.

2. Sub-Sahara Africa's historical GDP growth rate over the last five years was 7.8% vs. 3.9% world average. Projected growth over the next five years, 2013E to 2017E, is expected to be approximately 6.9% vs. 5.7% for the world, 2.7% Euro area, 5.1% U.S. and 10.2% Asia including China.

3. The key misconception is that African growth is driven primarily by commodity exports. While, commodities exports are still providing steady income for African governments to finance development, recent studies have shown that growth in consumer consumption is three times more than growth in commodities exports. Thus, in addition to resources, the following are also driving Africa's growth:

   a. **Macro-economic changes:** in the 1990's the economic growth in Africa was stifled by heavy debt burdens. These have since been reduced from 80% in the 1990's to 60% in 2000s due to better fiscal management and monetary policies. Inflation has also tapered off from 22% in the 1990s to 8% currently.

   b. **Investment in infrastructure**: About 50% of Africa's improved growth performance over the last decade has been attributed to the mobile telecommunications sector revolution. The main driver of the mobile sector was widespread market liberalization which led to about US$28 billion private investment in new ICT networks. As a result, more than 300 million new mobile subscribers were added between 2000 and 2009.

   c. **Consumer demographics**: Africa's population will surpass 1.6 billion by 2030, up from approximately 1.0 billion currently. This growth is driven by declining infant mortality, increased life expectancy and higher birth rates. The population is young (41% under 15 years), with a growing middle class that has disposable income to actively participate in the economy. Sub-Saharan Africa's middle class is about 34% of total population up from 27% in 2000. The rate of urbanisation in Africa is still high, so it is likely that the "emerging consumer" phenomenon will continue. Urbanisation however brings with it its own set of challenges as greater pressure is placed on city infrastructure, particularly roads, water, electricity and suitable housing.

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d. **Increasing Foreign Direct Investment**: Given the saturation of markets for investors in historically lucrative economies such as China, global investors have started to turn their attention to Africa. This trend is likely to continue.

e. **Political stability**: After 1990, most of the 48 countries in sub-Saharan Africa legalized opposition parties and held multiparty elections. Many of the remaining African authoritarian regimes have weaker domestic support bases and face organized opposition and civil society.

4. Despite these positive trends, infrastructure (particularly power) is still the major constraint to doing business in Africa. The poor state of roads, lack of rail infrastructure outside of South Africa and the inadequate capacity to generate electricity add 30%-40% to the cost of goods traded among African countries.

5. Addressing Africa's infrastructure challenges will require sustained spending of US$93 billion per year representing around 15% of Sub-Sahara Africa's annual GDP. This is a cumulative total need of US$850 billion until 2020. However, current annual spend is US$45 billion resulting in an annual funding gap of US$48 billion. Clearly, there is room for a significant amount of further investment.

6. Overall, significant risks such as execution, political and structuring risk exist. But given the size of the opportunity, all stakeholders including the PIC will have a significant role to play in building and investing in Africa's infrastructure.

GENERAL CONSTRAINTS / ISSUES TO CONSIDER

7. There are however some hurdles to overcome when investing in the Continent (either as individual entity or in collaboration with others). These include:

   i. A decision as to what **risk appetite** will be adopted and what the minimum required rate of return will be. Participants should take a long term view of sustainable returns, rather than a strict short term profit motive (this is especially necessary in the infrastructure space);

   ii. The **institutional capacity** sometimes in the host country is not sufficient to facilitate investment by international / outside entities. Working with governments to facilitate investment (and in an ethical way) will be important.

   iii. Some countries on the rest of the Continent are sensitive to the "**dollarization**" of their economy.

   iv. The **creditworthiness** of entities requiring capital is often a challenge.

   v. **Exchange rate risk**: the volatility of the domestic currency against the dollar (or any other currency used as the core currency of the contract).

SECTOR SPECIFIC COMMENTARY

Drilling down to a more detailed level on some specific sectors, it is useful to note the following:

8. Infrastructure includes Energy (electricity), Transport & Logistics, Information & Communications Technology, Water & Sanitation; as well as social infrastructure and other related sectors such as resource mining. Below is an overview of the specific challenges and opportunities in the key sectors:

- **Energy**

1. *Challenges:*

    1.1. On the supply side, the electricity sector represents Africa's greatest infrastructure challenge with 30 countries facing regular power shortages. Electricity access in Sub-Saharan Africa is only 25%, compared with 50% in South Asia, and 80% in Latin America. Outside of the North African countries and South Africa, Sub-Saharan Africa's power consumption, at 120 kilowatt-hours (kWh) per person per year, is barely adequate to power one light bulb per person for two hours each day.

    1.2. On the demand-side, a key question for most investors is whether African households can afford to pay for modern infrastructure services including power. World Bank research shows that a typical subsistence power bill ranges from US$2 – US$8 per month; and this cost is well within the affordable range for most households in middle-income countries.

7. *Opportunities:* The total investment required for the African power sector is about US$40 billion per year, almost three times current expenditure. There are a number of regional efforts to address Africa's electricity shortage; for example the $330 million Kariba-North hydropower expansion project and the $860 million Zambia-Tanzania-Kenya power interconnection project.

- **Transport & Logistics Sector**

8. *Challenges:* Investment in roads, rail, ports, and air transport is needed if Africa is to realize its economic potential. Africa's existing railways are aging and as a result rail traffic has declined. African port traffic volumes remain modest by global standards because existing ports are increasingly capacity constrained and not large enough to receive calls from major shipping lines. Regional hubs exist in Durban for Southern Africa, while Mombasa (Kenya) and Dar es Salaam (Tanzania) compete for a hub role in Eastern Africa. These regional port hubs help concentrate traffic but capacity remains an issue.

9. *Opportunities:* Opportunities in the Transport & Logistics sector relate to efforts to enhance and integrate the national logistics systems including roads, rail, ports, aviation, pipeline and storage infrastructure as well as logistics companies. Regional transport links are

being planned and developed by regional economic communities and member countries. Examples are the US$6-8 billion Lekki road and deep sea port project in Nigeria and the

US$440 million Mombasa Nairobi Addis Ababa Corridor Development Project which is a section of Trans-African Highway from Cairo to Cape Town.

- **ICT Sector**

10. *Challenges:* Despite the significant achievements in the ICT sector, there is still substantial room for improvement. For example, the cost of mobile services remains high: $10 in Sub-Saharan Africa vs. $2 in Asia. The differential persist because many African countries still lack access to submarine cables and broadband service.
11. *Opportunities:* A number of continental and regional organisations are promoting regional integration in the ICT sector. The most recent being, the US$1.5 billion ACE (African Coast to Europe) submarine communications cable along the west coast of Africa between France and South Africa. The ACE Cable will connect 23 African countries, either directly for coastal countries or through land links for landlocked countries.

1. Water & Sanitation Sector

12. *Challenges:*

    1.3. Africa's water resources are abundant, but owing to an absence of water storage and irrigation infrastructure, the resources are grossly underutilized. Access to piped water is confined to the most affluent segments of the population. An annual investment of about US$22 billion is required to improve water and sanitation access.

    1.4. In addition to water storage, there is further need to distribute water for agricultural use. At present, only 7 million hectares are equipped for irrigation; this is about 5% of Africa's cultivated land but produces 20% of agricultural production value.

    1.5. Lastly, global food production needs are projected to increase by about 50% over the next 40-50 years due to growing world population. Sub-Saharan Africa has over 60% of the world's uncultivated arable land but only 15% of its available arable land is currently used. Thus Africa is well positioned to meet this agricultural demand growth. However, significant challenges to land cultivation and improving yields remain; and a key constraint is distribution of water for agricultural use.

13. *Opportunities:*

    1.1. Potential opportunities include water storage and agricultural irrigation including pipelines, dams as well as waste water management. Various projects are being planned at this stage one being the US$1.5 billion Lesotho Highlands Water Project which is an ongoing water supply project with a hydropower component, developed in a partnership between the Lesotho and South Africa Government. It comprises of a system of several large dams and tunnels throughout Lesotho and South Africa.

1.2. In terms of food production, opportunities also exist given the availability of arable land. Focus in a number of countries can also go beyond only agriculture itself, but also agro-processing.

Role of the PIC

9. PIC involved in a number of infrastructure projects either through debt, equity and / or fund of funds. For example, in the renewable energy space, looking to diversify and expand the countries power base, mostly in the wind and solar arena. Apart from fully subscribing the IDC Green bond to the value of R5billion, the PIC has thus far approximately R900 million committed to the renewable space directly.

10. In terms of housing, the PIC has amounts approved and / or committed approximately R2.5billion; education R1.13billion; hospitals about R220million. There is continually a pipelines of deals developed in not only the infrastructure space, but what could more broadly be termed the developmental space (approved investments in Isibaya space thus far total approximately R32billion).

11. PIC does not only look to enter into projects on its own. Preference is to have investment partners. Opportunities for cross-country collaboration exist. Greater dialogue should occur on the Continent between DFI's and between BRICS institutions who are allocators of capital and investors. This process has begun in pockets but can be broadened. It's important to realise that solving the funding problem is not a government problem alone: it is a collective one, and one that cannot be solved without the private sector and / or without the help of attracting foreign governments and investors seeking decent returns.

12. Some have called for funding models other than PPPs and other partnerships: to include bond sales and other capital market innovations. The problem currently is that for many countries on the Continent, capital markets are still embryonic. However, with government backing for bond sales and capital market development, capital market growth could act as a further enabler for foreign investors to provide some of the capital required for necessary infrastructure. South Africa has done this to a certain degree with infrastructure bonds and other bonds issues by state owned entities. The success of these ultimately depends on government and entity balance sheets, which in turn relies on sound fiscal and monetary policy management. Credit ratings naturally as a result also matter for capital raising.