# Project 5 - Cracking the Next Growth Market: Africa

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## Problem Definition

In recent years Africa's economy has shown massive growth. The overall demand for commodities has grown beyond even that of India's and China's. Along with this, telecommunications, retail, financial and construction industries are expanding at an impressive rate. When all of this is added to the preexisting agricultural economy of the continent, it provides a platform for both international corporations and individual angel investors to enter the market and profit off its growth. We will now discuss a risk analysis of entering the African economy, a market entry strategy for companies wishing to do so, which sectors of the market are attractive and which ones are risky, and finally a forward suggestion on how multinational corporations can minimize their risks when entering the economy.

## Risk Analysis

This section will analyze the risks of multinational corporations that are entering the African market. One of the most significant issues that international companies face is the political turmoil within the African continent. Many African countries have unstable governments that are in constant states of revolution. This leads to the economies of those companies being in a very volatile state. This means that at any time they could have immense growth (such as what is currently happening) or they could have a period of rapid economic recession. Due to this, these economies become very high-risk markets for corporations which means they are more reluctant to enter them. Another big risk that faces the multinational corporations that want to enter the African economy is the current infrastructure. While the economy in Africa is growing rapidly, it remains a developing third-world country. This means that the infrastructure is weak. The continent remains poor and there is famine, disease, and poverty throughout the countries. This means that the consumer markets in Africa are in a state of constant flux. Until they settle down, there is no guarantee that the number of consumers will remain high enough to accommodate for the corporations to remain in the market long enough to get a return on their investments. While all of these are risks that should be considered, there are also many advantages that should be considered. One of the main advantages is that right now Africa is still in an early entry stage, which means it comes with all the advantages of an early mover into the economy. Being first allows a company to establish strong brand recognition and customer loyalty as there is no other current competition in the market. Another big advantage is setting the baseline for the market price for any new items that they bring into the economy. In this next section, we will discuss a market entry strategy that will allow multinational corporations to minimize these risks and maximize these advantages.

## **Market Entry Strategy**

To develop an effective market entry strategy for Africa, the background of the continent's economies must first be understood. Africa is made up of over 50 countries and is decidedly not homogenous, thus providing opportunities for focused investments. In Africa, there are four types of markets, the largest of which are the diversified economies. These comprise Egypt, Morocco, Tunisia, and South Africa and make up the most advanced economies in Africa. The citizens of these countries have higher GDP per capita and more discretionary income than elsewhere on the continent. In addition, the political stability in diversified economies makes it ideal for businesses to provide services. The downsides are low education, infrastructure development, and higher cost of labor than Southeast Asia. The second tier of the African economies is the oil exporting countries. These countries are rich in natural resources but are generally politically unstable and wholly dependent on the value of their commodities. Transition economies, such as Ghana, Kenya, and Senegal, have lower GDP per capita and less discretionary income, although there is relatively developed infrastructure in banking and telecommunications. However, there is virtually no competition regarding retail. This provides an opportunity with retail for growth and success. Finally, pretransition markets are the final level in African economies. They have many risks and will need their economies to develop further before investments should be considered.

With this overview of Africa's economies, the most effective market entry would be one of two strategies: a focus on retail in either the diversified market or the transition market. In the diversified market, an investor should strive to acquire regional players via acquisitions to take advantage of the limited infrastructure already in place before expanding. In addition, foreign mid-level managers should be brought in to bridge the education gap and provide training services to local talent. These retail stores in countries like Egypt or Morocco should focus on selling high end non consumable goods. This would allow the business to cater to those customers with higher levels of discretionary spending. Likewise, transition economies also provide a unique and profitable business opportunity for retail. Due to the lack of competition, business development and establishment is much easier. To accommodate customers with lower incomes, solutions such as selling smaller quantities of goods, providing credit lines, and offering payment plans are necessary for success. These differing investment styles will allow for further profitable growth and development of Africa.

## Identifying Attractive Sectors

Opportunities are opening in sectors such as retailing, telecommunications, and banking as Africa's economy progresses. According to UN data, Africa offers a higher return on investment than any other emerging market (Chironga). Competition is less intense and few foreign companies have a presence in Africa. Companies that enter Africa now can shape industry structures, segment markets, and establish brands.

Formal retailing is split in large market shares in most African countries, which grants global players an attractive incentive to move in. Economic and GDP growth, coupled with an emerging shopping culture and a boom in retail space, is energizing the retail sector in Africa (Moriarty). Shoprite had just one store outside its home country of South Africa in 1995, but has since become the continent's largest food retailer, opening 71 stores in other African nations (Chironga). Countries such as Egypt, Morocco, South Africa, and Tunisia have well developed manufacturing and service industries, which make them ideal places for consumer facing businesses to anchor their operations. Transition economies, such as Ghana, Kenya, Uganda, and Senegal, can also offer a strong consumer base for retailing as there are fewer diversified economies in this region, which translates into less competition and rapid growth.

Telecommunications has been an important driver of Africa's economic growth in the last five years (Gaibi). Telecom companies in Africa have added 316 million subscribers--more than the entire U.S. population--since 2000 (Chironga). Data services is a large source of growth within the continent. Experience in other countries suggests that a 10 percent increase in broadband penetration translates into additional GDP growth of 0.5 to 1.5 percent (Gaibi).

Applications such as mobile health care will provide significant benefits and help governments to stretch thin resources further. In fact, it is estimated that 80 percent of health care issues can be resolved by mobile phone, at a cost per capita that is 90 percent lower than that of traditional healthcare models (Gaibi). By tapping into the telecommunications sector, investors are likely to achieve available revenues and profits.

Africa's banking sector has grown rapidly in the last decade. Almost 50 percent of the growth at Africa's largest banks came from portfolio momentum--the market's natural increase--compared with only about 17 percent from inorganic (or M&A-driven) sources (Gaibi). Strong overall market expansion underpins this portfolio momentum. The financial sector is growing faster than GDP in most of the continent's main markets. For example, between 2000 and 2008 Kenya's GDP grew 4.4 percent per annum whereas its financial sector grew by 8.5 percent per annum (Gaibi). Financial reforms have largely enabled this growth. For example, Nigerian banking reforms in the mid-2000s prompted a swift consolidation (from 89 to 25 banks between 2004 and 2006) that unlocked the sector's potential--bigger banks with better capabilities could drive down their costs, allowing them to penetrate a larger portion of the unbanked population and to ride on the back of rapid economic growth (Gaibi). Attractive opportunities can be found in banking by expanding current product offerings, increasing product penetration, bringing the unbanked into the financial system, and capitalizing on the rise of a new consumer class by developing innovative service and channel offerings (Gaibi).

## How Multinationals Can Minimize Risk

According to a report by the McKinsey Global Institute, *Lions On The Move*, there are a multitude of ways for multinational companies and foreign investors to adapt to the unique qualities and risks associated with markets in Africa. For consumer-facing companies, they must overcome the low penetration of formal retailing. Due to issues such as poor infrastructure, brick and mortar storefronts often aren't the best way for products to reach consumers. As such, a strategy of combining retail stores with street vendors would be for the best. Additionally, by targeting both upper and lower-income markets, multinational companies and foreign investors are sure to catch the largest swath of economies in transition. Should these entities limit themselves solely to upper-income markets, they would also be geographically limited to those countries with diversified economies that had pre-existing retail markets. This leads into the final point, that multinational companies should grow roots across a range of African markets with differing levels of profitability, growth, and risk attributes. By changing how multinational companies and foreign investors operate in these ways, they stand to minimize some of the risks present in African markets and take full advantage of the lucrative and rapidly growing opportunities present there.