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CEO Briefing Report

Africa investor provides a family of products and services that support our clients' investment processes in major asset classes across Africa. Our goal is to leverage our deep understanding of Africa's financial markets to turn data-driven insights into tools that our clients can use to meet their investment process needs.

PRIVATELY motivated

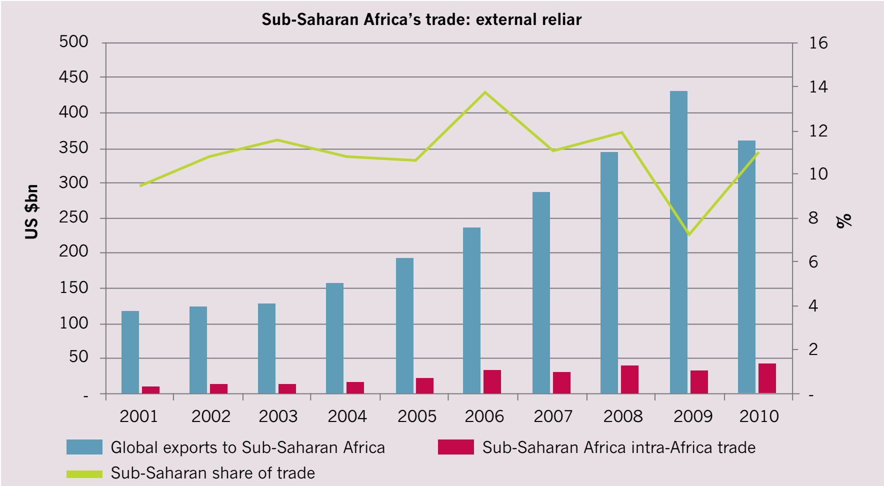
The lack of an integrated economic space in Africa is a major inhibiting factor to the growth of trade. Africa investor takes a look at some of the private investments that are giving regional economic integration a boost

The lack of integration amongst Africa's economies is often cited as a key reason for the lack of progress in building sustainable African economies. Historically, Africans have traded externally more comfortably than internally and investment patterns have followed this, but the last decade has seen much of this change.

There is a plethora of evidence and studies showing how the lack of integration in Africa is costing the continent billions of dollars in lost opportunity every year. A UNECA study, which showed that a car exported to Abidjan from Japan would cost US $1,500 as compared to $5,000 for the same car to be exported via land from Addis Ababa on the other side of the continent, is the starkest evidence that Africa's ability to trade with itself is hamstrung.

The reasons for this are too many regulations, too many border posts, corruption linked to these, too little infrastructure and hence too little trade, making the economies of scale too small. It thus becomes a self-perpetuating circle that suggests new infrastructure cannot be justified because of the low levels of trade.

As the chart illustrates, the levels of intra-African trade have averaged less than 11% a year for the last decade, much of this as a result of the primary-produce nature of most economies in the region and the lack of well developed manufacturing bases, as well as the logistical difficulties illustrated below.



Source: Whitehouse & Associates, based on UN Comtrade data

Clearly, the lack of an integrated economic space on the continent is a major inhibiting factor to the growth of trade. That is beginning to change, however, and the private sector is driving a good deal of this change. In previous eras, much of the continental integration driven by political agendas was incremental and tedious. The rationale for extensions of roads, rail, telecommunications and power – and even the maintenance of existing infrastructure – gradually subsided in the eighties and nineties as commodity prices fell, mineral and agricultural output dropped and utilities struggled to pay the bills.

A more conducive space

Today, we see a very different set of circumstances. The last decade has seen several key drivers of development dovetailing to create a space that is far more conducive to the rapid upscaling and expansion of infrastructure along key routes and hence creating a more integrated continent as a whole. The key to these developments, as in the past, is the desire to extract and export the mineral and energy assets of the continent. Key anchor projects in the coal, copper, oil and gas, iron ore and platinum sectors are providing a renewed impetus for projects aimed at linking the continent.

These major projects are not only adding the gravitas needed to underpin the integration of the continent, but they are also providing the bedrock for the development of associated industries as well as the expansion of other industries – notably agriculture, but also construction materials, building and social infrastructure.

The continent is badly integrated, however, with large swathes of the continent having no direct access to logical trading points. This is changing quickly though as the desire to open up the potential of much of Africa's interior gathers pace. In addition to this, there is a growing momentum away from current development and project nodes that is adding a natural urgency to the development of more integrated infrastructure, and thus trade and regulatory environments, in the region.

It is worth noting that despite the oft-painted picture of a resource grab being driven by large state-owned Chinese companies and their Indian, EU and US competitors, much of the new development is being driven by mid-tier and junior operators, both African and foreign. They're nimble, less risk averse than the majors and are bringing a new generation of financiers to the table.

National and private African oil companies are developing smaller or marginal fields with roughly 30 local oil companies operating in Nigeria alone.

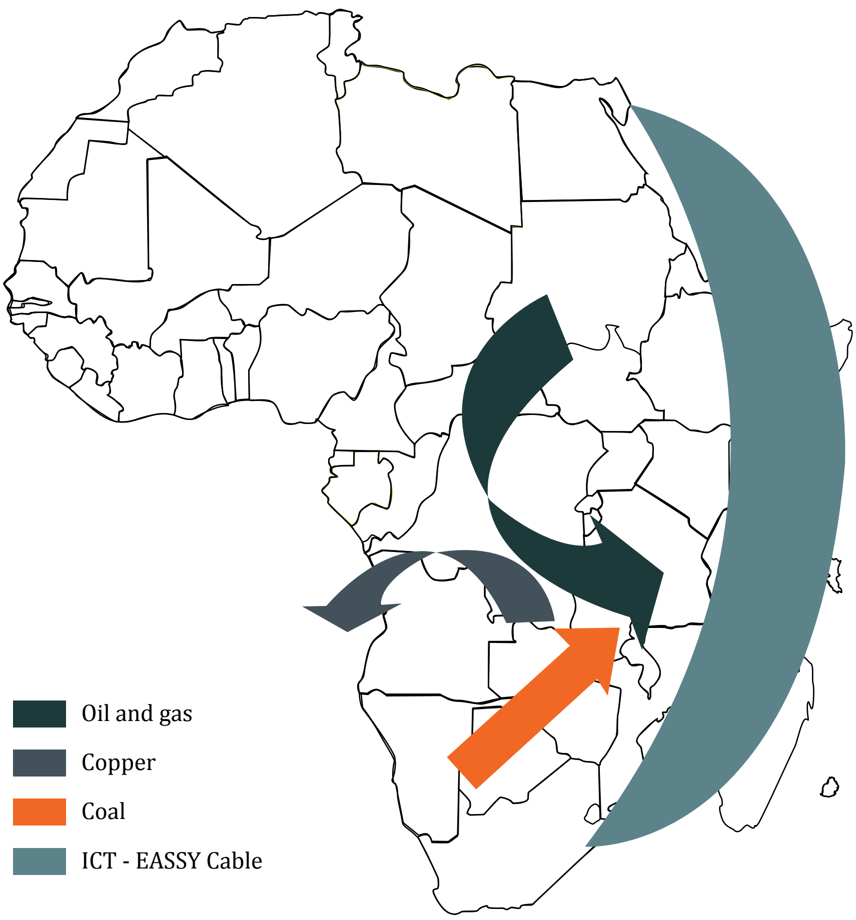
First Quantum Minerals (Australian-Canadian listed) has emerged in the last decade as a key mining operator in Zambia, and until recently in the DRC, whilst Tullow Oil (Irish, London listed) is the leading oil developer in Ghana and Uganda.

Central Africa

There are exciting mining developments in Central Africa around a regional cluster of large scale iron ore projects that have the potential to position the region as the next global iron ore province. The deposits straddle an area in the northern Congo, northern Gabon and southern Cameroon and they have already attracted investments from a number of companies including Sundance Resources, Legend Mining, Core Mining, Equatorial Resources and Xstrata. These deposits are in remote regions and the development depends on the development of a route to sea. The key players have reached agreement on the development of a rail corridor through to a custom-built iron ore export terminal at the Port of Lolabe in Cameroon.

Aside from the large infrastructure,

Major regional corridors in Africa



developments such as these create a myriad of downstream opportunities for suppliers of various goods and services including housing, food and beverages, power, telecommunications, mining equipment and consulting services.

Private companies are becoming more and more important in the funding, building and operation of existing and new infrastructure in the region

East-central and East Africa

In broad-brush terms, there are three major spines of resource development that are driving integration in southern, east-central and east Africa.

The first of these is the 'new oil frontier' that roughly traces the Great Rift from South Sudan through Uganda, eastern DR-Congo, Rwanda, Tanzania, Mozambique and ultimately the northern reaches of Madagascar. It includes early exploration and development of resources in all of these countries as well as potentially in Somalia, Eritrea, Ethiopia, Kenya and Zambia. As a result of this activity, there is already planning or early development of:

- An oil pipeline from Uganda's fields through to Kenya's port at Mombasa, plus a refinery in Uganda. Potentially, Uganda's refinery will also process Sudanese oil;
- The LAPSETT development from Lamu to Ethiopia and Sudan will reduce reliance on the Mombasa-Nairobi link and will place Kenya in a position to service South Sudan. There is intense competition to open up South Sudan, roughly 650,000km^2, but there is less than 100km of paved roads. This development will improve the livelihood of over 15 million people in North Eastern, Eastern, Rift Valley and Coast Provinces, through access to markets for agricultural produce.

Further south

The Mtwara Corridor in Tanzania is being spurred on by two key developments at either end of it:

- The discovery of potentially huge reserves of gas and possibly oil in southern Tanzania.
- The development of the Mchuchuma-Liganga coal, iron and power complex close to the border with Malawi.
- Whilst not regional yet, it has the potential to link into Malawi and beyond through off-take agreements that would fund the development of roads and ports on either side of Lake Malawi. In return for Tanzania extending the networks, Malawi would fund their use through purchases of power, fertiliser and other industrial products from the downstream oil and gas sector.
- Zambia is eyeing this development, with plans to redevelop the port of Mpulungu to gain access to growing markets in the Great Lakes, as mining and other developments in these countries pick up.

The second major area of development is the growing coal belt across southern Africa, stretching from Botswana through Zimbabwe and South Africa to Mozambique's massive Tete coal fields that are transforming central and northern Mozambique.

- Deposits are also being developed in Zambia, Tanzania and potentially Malawi (on the periphery of the main coal belts). This is spurring rail, road and port infrastructure to export anywhere between 50Mtpa and 100Mtpa of coal from Mozambique;
- Possible line extensions through Malawi, South Africa, Zimbabwe and Botswana to ensure landlocked areas have access to ports;
- Vale has begun rehabilitating the Nacala Corridor and will build a new dedicated coal port and terminal; Rio Tinto, Ncondezi Coal and Revuboe are studying the potential to do likewise.

There is potential to develop vast tracts of agricultural land along these routes and the government of Mozambique anticipates up to five new rail lines in the country to cope with this demand. These will need finance from government, donor finance institutions and private companies in order to come to fruition.

The third major area of development is the great Copperbelt region of Zambia and the Congolese province of Katanga. It is a well-established mining area, but many of the newer developments are moving west, through the Northwest Province of Zambia towards the border with Angola. The mines that are being developed are large mines and this is spurring the private development of:

- Fully serviced new towns being established in remote locations;
- At least one proposed rail line linking into the Angolan system, with a second possibly linking through to the south into Namibia;
- Redevelopment of the airport at Solwezi, allied to the development of an industrial park to service the broader regional mining community;
- Expansion of existing private power suppliers into the area in order to meet the growing demands of the mines and their staff;
- Establishment of new private power and utility companies, which are generally looking to take a broader regional approach, expanding into the DR-Congo, Malawi and Zimbabwe.

In many of the instances outlined above, it is private capital that is paying for the infrastructure, although obviously this cannot be outside of the approval of national governments and their regional partners.

The integration of the region is being further spurred by companies that are taking a regional approach to manufacturing. This is especially true of cement and other industrial inputs, with companies from Mozambique to Angola, Zambia and Tanzania all vying for a piece of Katanga Province's market. The importance of this market has also seen Zambia and the DRC sign a bilateral trade agreement to foster deeper economic ties between the two countries. Nigeria's Dangote has also seized the opportunity and is in the process of establishing new plants from South Africa to West Africa, which will eliminate the need for imported cement across much of Southern East and West Africa.

Put into broader terms, these broad developments are slowly beginning to integrate much of the region. However, governments and their finance partners, with the best will in the world, do not have the liquidity or technical capacity to drive much of this development. As a result, private companies are becoming more and more important in the funding, building and operation of existing and new infrastructure in the region, as it moves towards higher levels of output and greater integration.

Lack of integration in Africa is costing the continent billions of dollars in lost opportunity every year

African banks, especially from South Africa, Nigeria and Kenya, but also other countries, have been deeply involved in much of this development and are playing an increasing role, along with traditional financiers from the EU. Other emerging sources of private capital are now emerging from Japan, Korea, the Middle East and Asia, aside from the well-established Chinese funders.

Conclusion

There is a long way to go in most of these developments, but it is clear that as the continent develops, so will the sophistication of the provision of critical infrastructure. Private capital, private planners, private project developers and private operators that have begun to emerge in critical areas such as power are going to have a far bigger role to play in the development of rail, roads, ports, airports, industrial parks, telecoms and pipelines that are vital at both a national and regional levels.

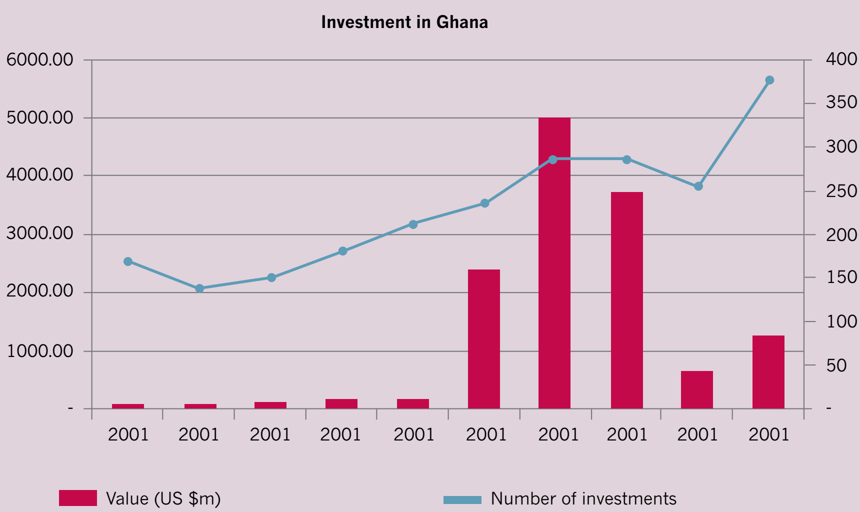
The example of Ghana (see box) is being replicated in Mozambique, Angola, Uganda, Tanzania, Zambia, parts of the DRC and elsewhere. Moreover, Nigerian banks, industrial conglomerates and service providers are swiftly moving into key markets, largely, but not exclusively, in West Africa, whilst Kenyan and South African companies have done the same in their spheres of influence.

Governments in the region acknowledge this, albeit reluctantly in some instances, and as such, it seems certain that the resources boom underway in many countries will be accompanied by far more privately-led integration of the region's infrastructure, trade and regulatory environments. Ai

Investment in Ghana

A snapshot of Ghana's development is instructive as it has many indicators of what can be expected across sectors and countries. The new millennium saw a resurgence of Ghana's mining sector, leading to a surge in investment in other key sectors:

- Eight top-tier mining operators have opened up much of the south-western third of Ghana and created Africa's second largest gold producer in a matter of years. Four pre-production and five exploration companies are sustaining this development;
- Nine new banks entered the market from 1999 to 2008, with eight of these foreign. All of the foreign banks, bar one, were African (from Nigeria and South Africa);
- Possible re-launch of Ghana's bauxite production and downstream aluminium industry;
- Tullow could have up to two billion barrels of oil, with at least seven other companies exploring for oil;
- Launch of the oil and gas sector in Ghana has led to the West Africa Gas Pipeline finally coming to fruition, which will be critical for stable power in Ghana;
- A complete revamp of the Sekondi-Takoradi area is planned, including development of airports, port, housing and hotels as a result; as well as a possible new oil refinery (US $6 billion);
- Government revenues will increase by $0.5bn a year, with savings in fuel imports of $0.5bn to $1bn a year; GDP growth is expected to reach 13% a year for 2011 and 2012, before stabilising at 5% to 7% through to 2016.



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