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Trends and Issues in Business

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Contents

1. Developments in the Financial Services Sector

The African financial services sector experienced several recent developments. These include the challenge of mobile (or digital) money, the entry of large foreign banks to the continent, the aspirations of several local banks to develop a Pan-African footprint, and a series of local and cross-border mergers and acquisitions. These trends continue, with the Covid-19 pandemic challenging some players, while highlighting poor governance in others. This report addresses recent developments in this sector.

THE TALE OF TWO COMPANIES IN SOUTH AFRICA

South Africa's state-owned Land Bank announced liquidity problems on Monday 20 April 2020, after defaulting on a loan. The Bank declared itself unable to "meet immediate obligations to settle a repayment requirement under the terms of a revolving credit facility with one of its lenders."

According to the Bank, the latest Moody's downgrade was the trigger. Some of the Bank's lenders subsequently "withdrew their facilities with the Bank, whilst other investors reduced their rollover of maturing facilities in order to operate within their investment policies that have restrictions on the level of investments made to organisations with the Bank's current credit rating." The bank is also looking for breathing space from other creditors.

The Land Bank is a key lender to the agricultural sector. It is yet another South African state-owned enterprise whose fortunes have gone south. It blamed the Covid-19 pandemic and the Moody's downgrade of South Africa's government bonds for its woes.[1]

South African financial services giant Sanlam has put its expansion plans into Egypt and Ethiopia on ice due to the COVID-19 pandemic. According to the CEO of Sanlam's emerging markets unit Heinie Werth, they will focus on their existing portfolio to avoid overstretching their resources in the current environment.

Werth announced in September 2019 that Sanlam Emerging Markets (SEM), in advanced talks to expand into Ethiopia, was researching a potential partner in Egypt. Sanlam currently operates in 33 countries, driven by its objective to diversify away from slow-growth markets in South Africa. This objective is far more important after the downgrade of South Africa's investment rating. However, executing this strategy will now be much more difficult, given the outbreak of the Covid-19 pandemic.

Under the current circumstances, Sanlam's focus is on client retention, cost control, and claims management. Ethiopia and Egypt remain "countries of interest." Due to the challenges faced by economies on the continent, Werth believes consolidation opportunities will appear in a few months, with mergers and acquisitions certain to be on the agenda. He also expects increasing use of digital channels.

Sales took a severe knock after the breakout of the pandemic, with individual life insurance sales down by more than an estimated 50%**.** Lower claims on general insurance policies compensated for the negative impact of this phenomenon. Sanlam is doing quite well and once the situation stabilises, has sufficient resources to proceed with its strategy to acquire high-growth businesses.[2]

COVID-19 CHANGING BANKING BUSINESS MODELS

The Nigerian cities of Lagos, Abuja and Kaduna expect to see retail banking operations grind to a halt following the announcement of a lockdown and other restrictions to movement. Throughout the country, bank branches outside of areas already on lockdown will run only skeletal operations. Some banks will close by 3pm daily. Most bank staff now work on shifts and exploit online and mobile channels as their primary means to execute transactions.

Should cash become a scarce commodity, the informal sector in Nigeria will suffer. Large portions of the economy are in the informal sector, and they rely heavily on cash. Any shortage of cash will have a strong negative impact on the country's economy at large.

While in Kenya the government and the society embraced mobile money solutions, in Nigeria the government has not embraced mobile-money to the same extent, and the brick-and-mortar business model dominates. However, Covid-19 style lockdowns will force a shift in the retail banking interface.

Bankers believe the Nigerian banking system will evolve as more banks and customers move over to online and USSD banking. "Digital banking might just get its M-PESA style revolution," with mobile money brands such as Paga getting much more attention. Exponential growth in online transactions is likely, especially if the pandemic and lockdowns carry on.[3]

The South African digital Bank Zero, which postponed its plans to launch until mid-2020, still intends to launch despite the Covid-19 pandemic. As a digital bank, Bank Zero can very easily work remotely, and carry out its disaster recovery program remotely. The lockdown may benefit digital banks like Bank Zero. South African bricks and mortar banks struggle to cope with online consumer queries.

Research by BrandsEye found that banks and insurers have been slow to shift from using social media as a marketing channel toward developing it as a customer service channel. They believe that Covid-19 will force organisations in the financial services industry to place a greater emphasis on digital channels and learn to separate noise from critical messages. According to BrandsEye, social media teams need to have greater responsibility. They believe that "banks and insurers that had already begun investing in digital customer service capabilities before the pandemic will have a head start once lockdown ends."[4]

INTEREST RATES REACT TO COVID-19 PANDEMIC

Banks in Kenya have cut interest rates to the lowest level in 15 years. This followed the drop in the Central Bank of Kenya (CBK) benchmark lending rate and a reduction in demand for new loans due to Kenya's sluggish economic growth. In March 2020, the CBK cut its lending rate by 1% to 7.25%, as part of a strategy to cushion the Kenyan economy against the impact of Coronavirus. According to analysts, few high-net worth investors and companies have opted to invest in expanding their businesses or starting new ventures. This trend reflects the potential for lower sales and returns arising from Coronavirus restrictions on the movement of people and goods.

To support banks, the CBK lowered the cash reserve ratio for commercial banks from 5.25% to 4.25%. This is expected to release an extra Sh35.2 billion (~US$328.1 million) for banks to lend to customers.

Ironically, when Kenya scrapped its cap on commercial lending rates in November 2019, it led to fears of a return to high lending rates, which had once hit a high of up to 25%.[5]

The CBK also provided additional direction to banks to keep those loans that may default as a result of coronavirus out of their bad books. This will see banks in Kenya reporting an improvement on their non-performing loans (NPL). Cooperative Bank posted an improvement in its NPL ratio from 10.5% in 2019 to 9% this year. Equity Bank will see an improvement in this ratio from 7.5% in 2019 to 6.5% in 2020.[6]

In South Africa, the Reserve Bank first cut its benchmark interest rate by 0.25% to 6.25% to prepare the economy for an envisaged slowdown. At that stage, it was expected that the economy would only have grown 0.4% in 2019. This was a cut that surprised the investment community, as they expected the Reserve Bank to wait for the decision by Moody's to either downgrade South Africa to junk bond status, or not. They then expected another 0.25% cut in March 2020.[7]

However, instead of a 0.25% cut, on 19 March, the Reserve Bank cut its repo rate by a further 1% to 5.25%, based on its expectation the economy would contract by 0.2% against a projected growth of 1.2%. Some economists feel the Reserve Bank should have done more to stimulate the economy.[8] The announcement by President Ramaphosa of the decision to lockdown the country to deal with the Covid-19 pandemic triggered the decision to cut the repo rate. The Reserve Bank then cut the repo rate in mid-April by a further 1% to 4.25%, its lowest level since 1973. The Governor of the Reserve Bank indicated this was due to the expected contraction of the South African economy by 6.1% during 2020, against the 0.2% contraction expected barely three weeks before.[9]

POINTS OF INTEREST

- South Africa's financial services sector has traditionally been one of its strengths in the annual Global Competitiveness rankings of the World Economic Forum. On "Soundness of Banks," the country ranked 19th (out of 125) in 2005, 3rd (out of 148) in 2013 and 29th out of 141 countries in 2019. Its financial system as a whole ranked 19th in 2019. It is clear that the country's overall financial system is sound.
- Despite these high ratings, there have been individual hiccups, such as the African Bank a few years ago, and then the notorious VBS Bank scandal of 2017, where management (and reportedly political leaders of one of the South African political parties) literally stole R2.7 billion. The question that needs to be asked is what happened with the Land Bank? Is this yet another case of a state-owned enterprise that is going south due to political interference and managerial incompetence (due to political appointees)? It must be said that this bank was struggling well before either the Moody's downgrade or the Covid-19 pandemic. Still, most South African banks are sound and well run.
- The Sanlam case is a good example of what South African financial services companies can achieve with competent management and little, if any, political interference. This company has expanded into financial services markets in both Africa and in South and Southeast Asia. In the latter, they are also in India and in Malaysia. Their business model is based on the premise they venture only into countries where they can add value, mostly from a back-office perspective. They are also comfortable with not being the majority shareholder and not using the Sanlam brand as the primary brand in the foreign country. They are also clear about where they do not want to be. In this regard, they chose to steer away from first world countries, where they would compete against global giants, and not to enter China as they did not understand the culture, legal system or language well enough, despite the obvious attraction of such a huge market. Strategy is also about knowing where you do not want to be.
- In only four months, Covid-19 massively impacted the economies of the world, including that of Africa. Lockdowns everywhere force behavioural changes, such as increased use of cash and social distancing. ATMs and mobile money applications now play a much more prominent role. While banks were slow to address mobile money in the early 2000s, they have picked up the pace over the past 5 years or so. The question that must be asked is, "what will the future bank look like?" When retail customers will realise they do not need or even want physical banks, we should see a strong surge in digital banks and mobile money applications development. The traditional banks will face strong challenges from non-traditional competitors, such as telecommunications companies.
- Cutting interest rates and other initiatives such as guidance to remove NPLs due to Covid-19 from financial statements are cyclical events that come and go. They do not impact the cash position of those banks, which once again highlights the old adage that profit is a perception.

2. Developments in Investments and Economics

The Covid-19 pandemic continues to impact every economy in the world. Foreign direct investments have ground to a halt, with some sectors damaged more than others. This report addresses some recent developments in the field.

CONSTRAINTS IN THE SEARCH FOR A GROWTH MODEL FOR AFRICA

The author identified a number of challenges that restrict Africa's ability to build an economic model that encourages enduring growth, addresses poverty and provides a future for its youth.

- Youth 'explosion: More than 60% of Africa's 1.2 billion people are aged under 25. This group are increasingly disaffected youth, hungry for political freedoms, for economic opportunities and for social fulfilment. Unemployment is a major concern as these unemployed youths are targeted as recruits by armed groups
- Poverty and inequality: Although the proportion of Africa's population living below the poverty line fell from 54.7% in 1990 to 41.4% in 2015, this figure masks enormous differences from one country to another, as indicated by Gabon (3.4% in 2017) and Madagascar (77.6% in 2012).
- Mega-cities and countryside: Megacities like Lagos and Kinshasa have grown significantly, surrounded by shantytowns where people live in extreme poverty. More than 40% of Africans now live in urban areas, compared with 14.6% in 1960. However, Africa's population is rising across Africa as a whole, although faster in towns than in rural areas. An additional problem is unemployment in towns - rural people have little interest in migrating there.
- Lost decades of growth: Due to a debt crisis and structural adjustment policies, growth in Africa slowed down significantly in the early 1980s. It took twenty years to recover. Per capita GDP also fluctuated significantly. Despite of the loss of 20 years, events pre-Covid-19 were more positive.
- New thinking needed: Africa has a low rate of industrialisation, is heavily dependent on agriculture and its service sector has only recently started to emerge. Africa is primarily still a producer and exporter of raw materials.
- Governance problems: Lack of democracy, transparency and efficient judicial systems are major brakes on African growth, and wealth is concentrated in the hands of a few. Of the 40 most corrupt countries globally, 20 are in sub-Saharan Africa.[10]

SOUTH AFRICA BUSINESS INVITED TO INVEST IN ETHIOPIA

Ethiopia's Prime Minster Abiy Ahmed invited South African businesses to invest in the planned privatization of state enterprises in his country in January 2020. Ethiopia is interested in attracting private capital in telecommunications, energy, logistics and other industries. South African investors reportedly have strong experience in in these sectors.[11]

IMPACT OF COVID-19 ON OIL PRODUCERS IN AFRICA

The Covid-19 pandemic is set to trigger substantial revenue losses for Nigeria and other African economies, especially in the oil and gas sector. The immediate effect of COVID-19 for the sector is falling demand for crude oil, leading to tumbling prices. Most analysts and operators agree that 2020 will see negative demand growth for oil globally as industries shut down and countries around the world go on lockdown, leading to oil prices falling to their lowest levels since 1991.

For oil producing countries such as Nigeria and Angola, this places immediate pressure on their budgets and macro-economic stability. All sub-Saharan Africa's producers budgeted 2020 with an oil benchmark price well above $50, with Nigeria forecasting an oil price of $57. With predictions that oil prices will not exceed $30 for the rest of 2020, most budgets will need revision, and public spending is likely to be drastically cut.

According to the Atlantic Council, the COVID-19 virus would cause Nigeria to suffer the biggest loss on the continent: US$15.4 billion, about 4% of its GDP. Congo-Brazzaville Council may be the hardest hit, with a loss representing 34% of its GDP, Angola could lose 13% of its GDP; while Equatorial Guinea, Gabon and Chad could see losses approaching 10% of GDP as the ongoing crisis unfolds.

According to the African Energy Chamber and Petroleum Industry, the airline industry in Africa will lose thousands of jobs, both for Africans and expats.[12]

AFRICA'S AIRLINES HURTING

Ethiopian Airlines, Africa's biggest and until now only profitable airline, shows a loss of US$550 million since January 2020 due to the pandemic. Despite the airline's serious financial crisis, its CEO believes the carrier can keep flying, partly by increasing its cargo business. Before the coronavirus pandemic, Ethiopian Airlines was Africa's busiest carrier, making more than 350 flights per day to more than 100 destinations.[13]

Ethiopian Airlines is softening the financial blow by finding new income streams, i.e. by focusing on cargo. Medical supplies are urgently needed all over the world. The airline is converting some of their passenger aircraft to cargo. It is also saving money by cutting back on daily flights and suspending talks with Boeing and Airbus to replace older aircraft in its fleet.

According to airline industry experts, some of Africa's air carriers are likely to go out of business during the ongoing crisis. South Africa's long struggling state-owned airline, SAA, went into business rescue in November 2019. It was recently reported in April 2020 that the country's government refused a funding request from the airline for R10 billion. According to the Department of Public Enterprises (DPE), government could not support SAA's request for further funding of R10 billion, or provide any future funding to sustain the business rescue process. Government will also not provide any further guarantees to SAA to facilitate borrowing, DPE said.

The DPE also refused to support the extension of the foreign currency borrowing limit to permit foreign financing of the business rescue plan, nor for a care and maintenance budget as proposed by the business rescuers. Due to Covid-19, SAA is hardly functioning at the moment other than flying on rescue missions. No revenue is coming in.[14]

The business rescue team subsequently offered all of SAA's 4,708 workers a severance package. This will all but shut down the business. However, labour representatives at the airline believe it can still be saved if drastic measures are taken. They provided several alternative suggestions, such as insourcing all services at SAA, downgrading of overnight accommodation for pilots and cabin crew, and even moving SAA staff who work on SAA domestic routes to SAA's subsidiary Mango in a bid to save jobs. Mango is set to take over SAA's domestic routes.

The proposal by the business rescuers requires SAA to sell its assets, which include property, aircraft spares and trade debts. This process would take between six to 12 months to execute.[15]

Another South African state-owned airline, SA Express, is also under business rescue. Their flight routes typically serve smaller cities in SA. As the business rescue practitioners believe the airline has no reasonable rescue prospects because it has run out of cash, they launched an application at the end of March 2020 to liquidate the airline. According to the business rescue team, the struggling airline has no reasonable prospect of survival.[16]

Another South African airline company, Comair, which owns airlines kulula.com and British Airways in South Africa, cannot afford to pay employees their full salaries. Comair asked staff to either take leave or unpaid leave for the extended lockdown period. Staff that exhausted their annual leave were required to take unpaid leave. The carrier expected 10% of its workforce, or 200 employees to be affected. Comair undertook to cover 40% of basic salary (or unpaid leave) for the initial lockdown period. In addition, Comair informed employees on 24 March 2020 that it would pay April salaries on the last working day of the month, and not on the 25th of the month as usual. Prior to the lockdown implemented by the South African government, Comair announced in March a restructuring process after reporting a loss of R564 million for the six-months ending December 2019. Its reported 3% growth in revenue was insufficient to cover a 14% increase in additional costs.[17]

POINTS OF INTEREST

- In terms of the constraints of developing an African growth model, all of those factors remain important (and have been for quite a while). It seems Africa is unable to deal with them. The lack of a, "new thinking required" factor, is probably the root cause of the precarious position in which Africa finds itself. One cannot solve a problem with the same mindset that caused it. If ever there was a time for a new mindset, it is now. Covid-19 is asking questions from Africa, questions we do not yet fully understand, and definitely do not know the answers to.
- Oil futures plunged into negative territory on Monday 20 April 2020 for the first time in history. The commodity's latest round of sharp selling comes as uncertainty mounts around storage for excess oil. Demand for crude has plummeted since the coronavirus outbreak has frozen activity worldwide. Apart from South Africa, Africa's biggest economies rely heavily on oil revenue to fuel state budgets and public spending and ensure macro-economic stability. These countries now have to return to the drawing board and redo their budgets. Some, like Nigeria, have budgeted on an oil price of close to US$60 per barrel. The oil price currently (25 April 2020) is at US$21.44 (Brent crude). This requires oil-producing countries on the continent to diversify their economies to reduce their dependence on oil revenues. This reality is not news, but is also yet to be done.
- Africa's airlines, as in the rest of the world, are hurting. South Africa now enters a situation where the government has few options: to close down the national airline, or to severely restructure it into smaller entities that address different parts of the value chain. Covid-19 is the final nail in the coffin of a once-proud airline, brought to its knees through political interference, corruption and mismanagement on a grand scale. The only profitable airline in Africa, i.e. Ethiopian Airlines, also faces some serious challenges, after taking a US$550 million knock. Ethiopian Airlines is well run and set a benchmark for other airlines in Africa. Its precarious current situation results from Covid-19. The airline should be back on its feet once the global situation normalises, which will not be soon.
- The economies of countries around the globe are severely impacted by Covid-19. Many commentators point out that there will be a "new normal." This means we will not be able to return to our old ways of doing business and running our economies and societies. What will this new normal look like? If capitalism is to die, what will replace it? How will the poor countries of the world develop into the likes of a Sweden, Finland or Denmark, where there are no poor people? These are questions that must be debated intensively and answered through action. And the above questions are perhaps too important to leave to politicians.

3. Developments in the Pharmaceutical Industry

The NTU-SBF Centre for African Studies previously noted the potential for development of a local/continental pharmaceutical industry in Africa in earlier Digests. The continent has a huge burden of disease and imports most of its medication. There is ample opportunity for investment in this sector. This report addresses recent developments in this sector.

A CONTINENTAL / REGIONAL APPROACH TO DEVELOPING A PHARMACEUTIAL SECTOR

With 11% of the world's population, Africa carries 25% of the world's disease burden. Policymakers, regulators and industry experts see urgent needs for affordable pharmaceuticals. They are exploring the potential of the upcoming African Continental Free Trade Area (AfCFTA) to achieve this goal. They identified pooling the procurement of essential drugs and products and expansion of local pharmaceutical production in Africa as critical pathways to universal healthcare on the continent.

The Economic Community of West African States (ECOWAS) published its plan to support the development of the pharmaceutical industry in the region. The new set of documents includes a regional reference framework and country-specific roadmap documents. The UNs Industrial Development Organization (UNIDO) produced the roadmap, with financial support from the West African Health Organization (WAHO).

The roadmap points out needs for "coordination and strengthening of continental initiatives to harmonise medical products regulation, provide guidance and technical support to improve access to quality, safe and efficacious medical products and health technologies" on the continent.[18]

The ECOWAS plan encourages African countries to embark on an ambitious approach to harness the comparative advantage and competitiveness of their pharmaceutical companies. This strategy will require financing instruments to facilitate pooled procurement. The roadmap includes recommendations for a strategic fund, levies, and social bonds that link to financial markets.

UNIDO and WAHO expect these tools to strengthen the West African pharmaceutical manufacturing industry. They hope to improve the sector's long-term viability. The roadmap covers "pertinent aspects including access to investment and technology, human resource development, strengthening quality infrastructure and policy incentives that would enable the sector to improve access to high-quality and affordable essential medicines and contribute to the economic growth of the ECOWAS region."[19]

FAKE MEDICATION

Fake medication in Africa is a serious problem, and puts many lives at risk. One example is the WHO alert issued in 2019 on fake Augmentin sold in Kenya and Uganda. This is the second of its kind.

To deal with fake medication, Kenya, Uganda and Rwanda collaborated to inspect imported medicine at the port of Mombasa, the common port of entry for the three countries. They also carried out batch-by-batch inspections of pharmaceutical products and identified high-risk traders, subjected to stricter checks.

However, Kenyan President Uhuru Kenyatta recently lifted these enhanced mechanisms, put in place only two months earlier. The state agencies inspecting imported cargo at the port were reduced from 30 to 3 to accelerate cargo clearance. Most cargo representing imported goods — including pharmaceutical products — is now pre-inspected at the port of origin. These recent steps increase the risk created by fake medicine in East Africa.

Some have suggested that the Importers and Small Traders Association in Kenya was behind Kenyatta's decision as they felt that the many agencies at the port delayed clearance of their cargo, especially when imported in consolidated containers.[20]

A recent report observes that "infighting between regulatory agencies under the Kenyan Ministry of Health for control of the lucrative business of making and importing pharmaceuticals is being blamed for the proliferation of substandard and counterfeit medicines on the market, exposing Kenyans to health risks and even death."

According to Kenyan sources, cartels reportedly attempted, amidst the bureaucratic infighting and chaos, to force consignments of medicines that had failed quality tests onto the market. Accusations include charges that importing companies bribe rogue officers in the Health ministry to circumvent WHO standards for human medicines, medical devices and veterinary medicines.

The parliamentary Committee on Health, well aware of the interagency squabbles, gave them time to negotiate. More than a year later, there is no solution.[21]

DEVELOPING PHARMACEUTICAL MANUFACTURING CAPACITY IN AFRICA

A pharmaceutical manufacturing company specialising in the manufacturing of high value products will be set up in Malawi, according to a January 2020 report. Investors will provide approximately £50 million to set up the capability to produce specialised drugs such as antiretroviral medicines for HIV, malaria and cancer medicines, as well as other high value medicines. The goal is to make Malawi a manufacturing hub for the region.

Cipla Quality Chemical Industries Limited, a pharmaceutical company that manufactures medicines used in antiretroviral, malaria, hepatitis and cancer treatments, is involved in the investment.[22]

A Maltese company, Evolve, is investing in a pharmaceutical laboratory in Ghana to produce medicines in line with European standards. According to the CEO of Evolve, Chris Busuttil, Ghana was a natural choice, as the country is going through an industrialisation process. Doing business in Ghana would be easy for Evolve as the local population all speak English and are very punctual and trustworthy.[23]

MERGERS IN PHARMACEUTICAL INDUSTRY

In Ghana, three local pharmaceutical companies, i.e. Ayrton Drug Manufacturing Limited, Starwin Products Limited and Dannex Limited merged into one entity, Dannex Ayrton Starwin (DAS) Plc. DAS Plc subsequently listed on the Ghana Stock Exchange (GSE) to provide local and foreign investors the opportunity to invest in the company. The merged entity now trades on the Accra bourse under the name DAS Pharma.

According to the Managing Director of the GSE, Ekow Afedzie, the listing of DAS Plc was historic as it was the first time that two listed local companies had merged with a non-listed local company to list on the GSE.

The three indigenous pharmaceutical companies have operated in Ghana since the 1960s. The merged entity, now the largest pharmaceutical manufacturer in Ghana, will benefit from a strong distribution network, strong product portfolio, economies of scale, and strong human resource base. DAS will be a significant player in the pharmaceutical industry, by tapping into the synergies derived from the merger. These will enable the newly merged firm to improve operating efficiency, optimise cost, grow volumes and profitability, and achieve the company's growth ambitions. These factors will maximise shareholder value.[24]

POINTS OF INTEREST

- Africa has the potential to develop a sound and healthy pharmaceutical industry by pooling its resources, both physical and intellectual. It has a huge market of more than 1.2 billion people, which is set to grow to 2.4 billion by 2050, and over 4 billion by 2100. It is also experiencing a huge burden of disease, while its strongly growing consumer class is developing lifestyle diseases associated with the Western middle class, such as diabetes. As stated in the introduction and in previous reports, Africa mostly imports its medication, and mostly the generic versions. This emphasises the investment opportunities in this sector in Africa. Some foreign global pharmaceutical companies have already established a presence on the continent, but they are currently only a drop in the bucket.

- Although the case studies above highlight Kenya's problems with fake medication, it is a continental challenge that must be fought tooth and nail. In addition to the bureaucratic infighting, a lack of coordination over borders also contributes to the absence of a coordinated response to fake medication. Corruption and bribery also play a role, sadly. Africa cannot afford this situation. The USA has legislation in place where should a US company be found guilty of actions abroad that are illegal at home, it will be deemed to have been committed in the USA. More countries should adopt this approach; we should then find less instances of corrupt actions in source countries where pharmaceutical products are involved.
- The growth of manufacturing capacity and M&A activity create entities that can tap into the economies of scale for production, with all the concomitant benefits. Africa needs more manufacturing capacity and it needs more large companies that can benefit from scale and scope. The opportunity is there! Now all Africa needs are willing investors. One answer to the question of what the new normal looks like, in my view, is that there will be more equitable access to medication for all. The developed world should remember this. In this case, as a sweetener, companies will do well by doing good.

4. Developments in Retail

Retail companies face mixed fortunes in Africa. Some are struggling, whilst others have been growing in leaps and bounds. For some, Covid-19 sounded the death knell after a brief period of struggle. This report addresses recent developments in this sector.

COVID-19 AGGRAVATES WOES FOR RETAILERS

The Covid-19 pandemic in South Africa led to a significant reduction in the number of shoppers. The South Africa's second-largest clothing retailer, Edcon Holdings, reported at the end of March 2020 that it may not be able to re-open at the end of a three-week national shutdown to combat the Covid-19 virus outbreak. Edcon is the owner of the Edgars and Jet chains. According to the CEO, Grant Pattison, March revenue would be R400 million (US$23 million) below the retailer's forecasts. The bulk of Edcon's 1,100 clothing stores were closed during the lockdown, costing about R800 million.

Due to the failure to meet March sales targets, and the expected drop in collections of the debtor's book, Edcon only had liquidity sufficient to pay salaries and would be unable to honour any accounts payable during the initial lockdown period of three weeks. Edcon employs 18,000 people and its suppliers employ many more.

Edcon last year secured R2.7 billion from lenders, landlords and the Public Investment Corporation in a restructuring plan that freed the retailer of all interest-bearing debt after years struggling with high borrowings.[25]

Curfews and movement restrictions have greatly reduced shoppers since the viral infection began to spread in Kenya. This caused Shoprite Holdings to close its Waterfront branch, one of its bigger stores in Kenya, and lay off all staff. This closure will affect 104 workers. Shoprite was an anchor tenant at the Waterfront mall.

Shoprite opened its first store in Kenya in 2018, followed by another two stores. It earlier intended to open seven stores in Kenya, with six of those in Nairobi. Due to the pandemic, those plans are on hold.[26]

In South Africa, a number of clothing retailers collectively offered R220 million to landlords to cover their rent during the Covid-19 lockdown period. These retailers include The Foschini Group, Truworths, Mr Price Group, Woolworths and Pepkor. The offer amount reflects 20% of their normal rentals plus utilities consumed.

These clothing and other retailers who do not provide essential services are not allowed to trade during South Africa's five-week long lockdown. Landlords offered an industry-wide relief package for retail tenants that are hardest hit by the suspension of trade.

Other retailers, including Yum! Brands, which owns KFC, moved to withhold rentals due for some of their outlets.[27]

COMPETITION LEADS TO CONTRACTION OF OPERATIONS

Botswana retailer Choppies four years ago embarked on an aggressive expansion drive across Africa. It recently announced the discontinuation of operations in several African countries, among them Kenya, Tanzania and Mozambique, and placed its South African business up for auction. It also restructured its outstanding loan estimated at US$56 million to provide it some breathing space from losses attributable to serious competition in the retail industry. Choppies now intends to concentrate on growing its market share in Botswana.

The firm also recapitalised to the tune of US$12.76 million and completed a restructuring exercise to reposition itself in the sector. The fresh capital comprises US$8.51 million loan from two founding shareholders and US$4.25 million from trading operations.

Negative cash flow over the past two years for Choppies' South African subsidiaries depleted reserves that were earmarked to pay off suppliers. Manufacturers and channels consequently refused to supply goods, leading to stockouts in its South Africa stores, followed by loss of market share.

Choppies at one time operated 217 stores in Botswana, South Africa, Zimbabwe, Zambia, Kenya, Tanzania and Mozambique.[28]

PRE-PANDEMIC RETAIL GROWTH

The pandemic brought a period of expansion in the retail sector to an abrupt end. In Kenya, Carrefour generated sales revenue of Sh18.7 billion (~US$1745 million) from its Kenyan outlets in 2019. This was a 28% increase from its 2018 sales revenue of Sh14.6 billion (~US$136.2 million). According to the franchise holder in Kenya, Majid Al Futtaim from the UAE, the increase could be ascribed to its aggressive expansion bid across major towns in Kenya since its launched in Kenya in 20916. Their strong growth over the past four years had been based on attracting a strong clientele base among the country's expanding middle class. Carrefour intends to continue the expansion of its business across key markets in Africa.

Carrefour expanded its footprint in Kenya after taking over retail space previously occupied by struggling supermarket chains, including Nakumatt and Uchumi, as well as opening new outlets to cash in on the underserved market. Further planned openings in Kenya are delayed due to the current Covid-19 pandemic.[29]

Majid Al Futtaim has also opened the first Carrefour Store in Uganda. The store stocks more than 20,000 high-quality products from international and local brands. Majid Al Futtaim Hypermarket in Uganda has so far recruited 130 Ugandan employees and has contracted 60 more from external local companies. The company has also engaged 230 Ugandan suppliers to stock the Carrefour store in Uganda.[30]

South Africa's Shoprite Group gained market share in its core business in South Africa in the first half of its financial year ending December 2019. The company's store expansion drove its 9.8% sales growth to R61.1 billion in its core South African business. It is eyeing a larger share of SA's premium food retail segment, which accounts for about 75% of its business.

The group uses three main brands, Shoprite, Usave, Checkers and Checkers Hyper, to trade through 1,632 stores. The group's Checkers supermarket chain, focused on the premium sector, grew merchandise sales by 11.2% in the 26 weeks ending December 2019.

Shoprite opened 82 stores during 2019. It also gained 1.1% market share to 31.6% in its core South African business. In its non-SA operating segment, which includes 14 countries, sales grew 4.8% in constant currency terms, but fell 3.1% in rand terms.[31]

FINAL CURTAIN FOR NAKUMATT

Struggling Kenyan retailer Nakumatt finally saw the writing on the wall when its creditors in early January 2020 unanimously voted to dissolve the firm after its revival strategy failed. Nakumatt owed banks, suppliers and landlords Sh38 billion (~US$354.5 million).

Nakumatt had no assets to collateralise any additional funding, while the administrator was of the opinion it would be difficult to "attract an investor to inject the substantial amount of equity required to restructure NHL's balance sheet due to the current high degree of financial leverage."

Nakumatt grew from a mattress shop in Nakuru to eventually have branches across Kenya and East Africa. The 60 branches it had ion February 2017 dropped to 6 in September 2018. These were sold to Naivas for Sh422 million (~US$4 million) in November 2019.[32]

POINTS OF INTEREST

- In the retail sector, non-food retail groups, such as Edcon in South Africa, are severely impacted by the pandemic. In Edcon's case, the entity was struggling long before Covid-19. The closure of the stores due to lockdown increases the potential for closure of the group. It remains to be seen whether its creditors and investors will try to flog a dead horse.
- Food retailers on the continent were generally doing well, except in countries where they do not yet have a critical mass of customers. The food sections of Shoprite, Woolworths and Carrefour are all doing well. However, Covid-19 sharply curtailed the number of consumers visiting Shoprite's flagship store in Nairobi, which led to its closure. Shoprite has never been comfortable in the East African countries of Kenya and Tanzania. It withdrew from Tanzania in 2014, and only recently ventured into Kenya in 2018. This was probably due to the implosion of the local chains of Nakumatt and Uchumi and the expansion actions of Carrefour and Choppies into Kenya. One never got the feeling that Shoprite was excited about Kenya.
- Kenya has been a difficult market for retailers, although it does seem Carrefour is doing well. Choppies, on the other hand, exited the country. Kenya has become a graveyard for many retail groups, local and foreign. The message this sends is, "buyer beware"!

5. Developments in Trading

Covid-19 already severely impacts global trading. Global supply chains have all taken a knock. Many logistics experts question the use of long global supply chains and suggest adopting shorter regional supply chains, or in some cases national supply chains, to reduce vulnerability to global shocks such as Covid-19. This report addresses recent developments in this sector.

INDIA GROWING ITS TRADE PRESENCE IN AFRICA

India has long been an active trading partner in Africa. India's High Commissioner to Nigeria Mr Abhay Thakur reports that Nigeria alone accounted for 20% of India's trade in Africa for 2018. In that year, India's total trade in Africa grew by approximately 18% to US$14 billion. This made India Nigeria's largest trading partner.

In addition to growing its trade with Nigeria, India cooperates with Nigeria in the areas of maritime security as well as in other areas. The thriving Indian community in Nigeria, approaching 50,000 people, conduct their own businesses and employ a large number of Nigerians.[33]

REGIONAL ACTIONS TO PROMOTE TRADE & EXPORTS

Some countries in Africa have changed their mindsets about where and with whom to trade. Tanzania's Prime Minister Kassim Majaliwa at the 4th SADC Industrialization Week and Exhibition in August 2019 had urged his manufacturing sector to tap into the benefits of the country's membership of the Southern African Development Community (SADC) and target the huge market in the 16 member states of the SADC. He expressed his opinion that the Tanzanian industry manufactured goods that could be competitive in the SADC market and elsewhere. He referred to the high quality of goods manufactured by large, medium and small industries in Tanzania, including leather goods, food and beverages. He also recommended that these Tanzanian companies partner with the companies in the other 15 SADC members states to produce goods for exports.

While attending the exhibition, Tanzania's President John Magufuli opined that SADC member countries should do business among themselves to increase capital and promote industrial development within their regional bloc and the African continent at large.[34]

COVID-19 IMPACTING TRADE

In late February 2020, a number of African states urgently sought alternative sources of consumer goods and raw materials formerly imported from China. The Covid-19 pandemic disrupted supply chains and stockpiles were depleted. Rwanda was one of quite a few in this position of having to look for new sources. The country's imports from China include electronics and electrical equipment, machinery, building materials, ceramic products, footwear and textiles, furniture, and vehicle parts.

To aggravate the supply chain situation, RwandAir suspended flights to China on 31 January, which also affected business travel and trade between the two countries.

From its side, China had been resuming production in other provinces, with the exception of Hubei province, with the work resumption rate in some provinces rising above 70% by the end of February. However, prices of goods imported from China are expected to rise in the coming months, unless spread of the coronavirus is contained.

The Permanent Secretary in Rwanda's Ministry of Trade and Commerce, Michel Sebera, indicated that Rwanda had been experiencing scarcity in the market, and they expected the situation to worsen.

Countries such as Turkey, India, Dubai and Egypt were identified as alternative sources of goods previously imported from China. Rwanda expects increased costs associated with these alternative sources. Imports from China account for 20% per cent of Rwanda's total annual imports.

Not only imports are a problem. Rwandan sellers of coffee, chilli and other products on Alibaba's T-mall e-commerce platform struggle to ship their goods to China, following the suspension of flights by RwandAir.[35]

Tanzanian trade with China is disrupted by the Covid-19 pandemic. According to Tanzania's Minister of Industries and Trade, Innocent Bashungwa, "the crisis in China" triggered a significant drop in passenger and cargo volumes to and from the two countries."

China was the largest foreign investor in Tanzania with a total investment of more than US$7 billion in 2019. Bilateral trade volumes between the two countries in 2019 amounted to US$3.976 billion, making China Tanzania's largest trade partner for three consecutive years.

Small-scale traders in the popular Kariakoo Dar es Salaam trading centre, where a wide variety of imported products from China and other Far East countries are traded, have also complained about the cessation of commodity shipments from China.[36]

In the editorial of 14 March, the editor of the East African addressed the Covid-19 pandemic. He stated that governments had the dual responsibility of protecting people from contracting the disease, and businesses from the economic fallout. Due to the impact on air transport and the closure of ports, cross-border business activity is sharply down, resulting in shortages of many imported goods.

Businesses that rely on imports, mainly from China, have started to report shutdowns. Regional trade will also suffer, as commodity dependent economies such as South Sudan and Tanzania become the transmission path for the impact of falling commodity prices in international markets.

The Covid-19 crisis has a dual impact on the regional economy. It affects both the domestic and external sectors of the economy. A slowdown in trade will impact export earnings, while tax revenues will suffer from a dip in imports. Given their high dependence on trade taxes, government revenues in the region will be reduced and governments will consequently experience a lot of pressure to balance their budgets.

Due to the low levels of external reserves in the region, governments will need to reduce their consumption and implement measures to stimulate their economies. They should also emulate the USA and China, which announced stimulus packages to keep their economies going. Kenya has already announced a US$5 million stimulus package for its tourism industry.[37]

The Covid-19 pandemic reduced trade across the entire continent, including among members of the East African Community. The region has seen border closures and a slowdown in cross-border trade. While Kenya and Tanzania have not closed their borders, they did restrict movement of people and vehicles, causing business at their common Namanga border point to grind nearly to a halt.

All trucks from Tanzania importing goods into Kenya are to be escorted by Kenyan police from the border point to their destination and then back.

Few passenger vehicles from Kenya are allowed entry into Tanzania, while medical officers first clear truck drivers ferrying goods to the country. Bus companies have switched to transporting goods to mitigate losses.

The stringent measures are intended to reassure stakeholders that both countries are open for business and all efforts are being made to remove health risks associated with the Covid-19 in the two countries.[38]

PROTECTIONISM KICKS IN

Kenya's government announced towards the end of March that it would suspend importation of second-hand clothes to restrict the expansion of new coronavirus infection and to improve the sales of locally made clothes. Suspension of imports will increase the losses the sector is already experiencing due to poor sales attributed to the slow business environment brought about by the coronavirus.

There was also a call for incentives to local garment makers to boost their production. A private sector proposal stated that Kenyan goods could be priced competitively if factories could receive access to cheap power and tax breaks, which in turn would create more employment opportunities.

Kenya's export of new clothes account for more than 90% of its AGOA exports to the USA, which netted the country Sh68 billion (~US$633 million) during 2019.

The lucrative second-hand clothing market saw traders from China opening shops in Gikomba, Kenya's largest informal market for second-hand clothes. In response, Kenya formulated a new investment policy that identifies sectors that are reserved for domestic investors only. However, the success of this policy remains to be seen. A previous attempt to curb imports of second-hand clothes failed following threats of retaliation by the governments of the source markets.[39]

POINTS OF INTEREST

- China is Africa's largest trading partner, and has been for a number of years. This creates a dependence on China for both imports and exports amongst African countries. Most African countries have a negative trade balance with China. India's outreach to Africa will provide the continent's business leaders with an alternative source and destination. It is true that the per capita GDP of China is US$7755 (US$16186 on purchasing power parity basis) against that of India at US$2104 (US$6899 on purchasing power parity basis), which makes China a more lucrative target market. Yet, to reduce their vulnerability, African governments must move to diversify their markets and sources. India recently launched, together with Japan, the Asia-Africa growth Corridor as a counter to China's BRI. Granted, Covid-19 has everything on hold for the foreseeable future. Africa must reduce its unbalanced dependence on China.

- This factor gains greater urgency when taking into consideration the slowing down of goods from China for African businesses. Many African SMEs have been forced to cut back or even close their businesses, partly due to the lack of customers, yet also to the lack of stock.

- A few years ago, Kenya, Rwanda, Tanzania and Uganda announced increased tariffs on the import of second-hand clothing. Much of this was coming from the USA. The USA subsequently informed them that the African Growth Opportunity Act (AGOA), which supports tariff-free trade between a large number of African countries and the USA, does not provide for such actions by African governments. The USA made it clear it would retaliate should these countries go ahead with the tariff increases. Rwanda was the only country that did proceed, while others scrapped the idea. It is now interesting to see Kenya raising the issue once again. Note that in addition to the USA, China also has a significant footprint in this market. Kenyan indebtedness to China is high, with the latter providing many loans for infrastructure development in Kenya. The nature of the retaliation by China and the USA against Kenya might play an important role in the future actions of Tanzania and Uganda towards protection of the local textile industries.

- One sympathizes with the desire of African governments to protect their local manufacturers. Once again, what will the new normal look like in terms of a global trading regime? When will fair trade replace free trade, bearing in mind that free does not necessarily equal fair from the perspective of frontier and emerging market economies?

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