Friday@Noon

A weekly African news briefing for the Southeast Asian community

Editor: Johan Burger

NANYANG TECHNOLOGICAL UNIVERSITY SINGAPORE | NTU-SBF Centre for African Studies, Nanyang Business School

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East Africa

- **East Africa:** Since 2013 a number of European companies, e.g. H&M, Primark, and Tesco, began sourcing some of their garments from Ethiopia. There has been rising interest in East Africa, brought about by, amongst others, the renewal of AGOA, as an important center for apparel sourcing. The precondition is that buyers, governments, and manufacturers work together to improve business conditions in the region. In East Africa, Ethiopia and Kenya, and to a lesser extent Uganda and Tanzania, are of interest to apparel buyers. The governments of both Ethiopia and Kenya are taking steps to develop their domestic textile and garment industries. Challenges common to both countries include poor infrastructure, cumbersome customs processes, a dearth of technical and managerial talent, and low levels of social and environmental compliance. Apparel buyers are sourcing basic, large-volume items from Ethiopia. Although as much as 60% of exports are sent to Germany and 10% to the USA, Ethiopia accounts for a mere 0.01% of total apparel exports. The biggest advantage of Ethiopia is cost: low wages and low electricity prices. Challenges include low land-utilization rates (barely 7% of 3.2 million hectares suitable for cotton cultivation is being used), planning errors, low crop yields, quality problems, social compliance, production inefficiencies, and long lead times. Kenya's apparel industry also specializes in supplying high-volume bulk basics such as trousers, which account for 58% of its exports to the USA. The capacity of Kenya's garment factories has grown markedly in recent years, thanks to FDI from Asia and the Middle East, and support from the Export Processing Zones developed by the Kenyan government. Factories have grown larger and more efficient (production efficiencies). Challenges include longer lead times (due to a lack of a local upstream industry), comparatively high labour costs, inefficient and costly energy supply, compliance and risk, corruption, high crime rates, and poor social compliance. (Berg, A., Hedrich, S. and Russo, B. 2015. East Africa: The next hub for apparel sourcing? **McKinsey & Company** – www.mckinsey.com. August.)

- *CAS View:* It is clear that Africa still has a number of challenges that need to be dealt with in order to optimize its potential. These include labour issues, compliance, corruption, energy inefficiencies, and crime, to name but a few. However, it has so much potential. One example is the fact that only 7% of Ethiopia's land suitable for cotton production is being used. In addition, its apparel exports amount to only 0.01% of total exports. With AGOA being renewed, the USA is a very attractive export destination. Companies willing to address and mitigate the risks inherent in Africa will be rewarded for the risk they bear!

- **Kenya:** Kenyans have mostly reacted negatively to trade deals with Uganda. One of the deals agreed by President Kenyatta and Ugandan president Museveni allows Ugandan sugar back on to the Kenyan market for the first time since 2012. Kenya then banned sugar imports from Uganda when Ugandan traders repackaged cheap sugar from COMESA for resale in other markets. The new deal was criticized, saying it could bring about the collapse of local millers. Kenya's leading sugar manufacturer, Mumias Sugar, had earlier been supported by government with $9.9 million, which may have been spent in vain if the market would now be swamped by cheap Ugandan sugar. Kenyan sugar cane farmers are equally struggling as a result of lack of payments. Opposition to the sugar pact stated Kenya was able to fulfill its sugar requirements through domestic production and could even export to Uganda. Others stated that whereas the government had been asked to help some companies that were in difficulties, it now had taken the decision to import cheap sugar. Some consumers hoped the deal would open up competition in the sugar sector that would benefit consumers, while some businessmen believed the business community would benefit, as the deal would protect Kenya against the effects of a shortage of domestic sugar production. Economists felt the agreement would harm farmers in a big way. A beef and dairy products pact was also questioned, as Kenya could not produce enough for local consumption let alone for export. There have also been mixed reactions to the news of an agreement on the route for a crude oil pipeline for both countries to the

Kenyan coast from Hoima, near Uganda's border with DRC, via Lokichar in western Kenya, to the Kenyan port of Lamu, which is under construction. As Lamu is not far from the border with Somalia, security experts had expressed concerns for the safety of a pipeline there, given al-Shabab action in the region. However, studies showed the northern route was the least costly and most viable. Uganda has an estimated 6.5 billion barrels of oil in fields in the west of the country, while Kenya has around 1 billion barrels. (Houlton, S. 2015. Kenya: Many Kenyans Shocked By Sugar Deal With Uganda. **All Africa** – www.allafrica.com. 12 August.)

- *CAS View:* There is always a fine line between protecting one's industries against foreign competition, and protecting one's consumers against high local prices. Whole industries have been destroyed in the process of opening up borders. South Africa's textile industry comes to mind. However, this places pressure on local industries to ensure they remain productive and competitive. It remains an important question to what extent governments have to protect their local industries. This issue becomes more complicated in an economic cooperation pact, such as EAC. Both countries have negative current account balances as well, which would place their currencies under pressure. The quantum of the exchanges will be the determining factor for any benefits either of the parties is to gain from the agreements. It does seem the export of the beef and dairy products to Uganda, and the export of oil through Kenya, is supposed to make up for the sugar deal, which seems to be sweet for Uganda. Kenya's unemployment rate of 40% is another worrying factor in this deal. What happens when the sugar industry implodes? And what happens to the political stability when the disgruntled unemployed turn to extremist organisations such as al-Shabab? Running a country is definitely not for the faint of heart!

West Africa

- **Nigeria:** Pres Muhammadu Buhari intends to break up the NNPC, which manages the oil assets of Nigeria, to ensure taxpayers get their fair share. His challenge is to depoliticize the NNPC and to disentangle its vested interests and its rogue commercial operations. Buhari made cleaning up the NNPC a key issue in his election campaign. He plans to split the NNPC in two, creating a regulator and a vehicle for investments. So far he has fired the board and management of the company and replaced its chief with Emmanuel Ibe Kachikwu, who was executive vice-chairman of Exxon Mobil Africa. He has also ordered a review of oil-swap contracts and barred 113 vessels from loading oil and gas. According to Buhari, about 250,000 barrels of Nigerian oil (10% of daily output) are stolen daily. This has damaged Nigeria's integrity and compromised individuals and institutions. The amount involved is mind-boggling. Apparently the NNPC has diverted more than $30 billion in oil revenue from the state since 2009. That exceeds the annual economic output of more than half the nations in Africa and roughly equals the federal budget. The situation is increasingly desperate as government coffers are "virtually empty" due to the halving of Brent crude prices the past year. Oil exports account for about two-thirds of government revenue. For all its importance to Nigeria, the NNPC is largely inscrutable. In 1978 it was reported that the NNPC failed to remit the equivalent of about $3.5 billion it owed the Treasury. In the 1990s, an investigation found $12 billion in oil revenue was unaccounted. The Nigeria Extractive Industries Transparency Initiative stated at least $23.2 billion due was not deposited into the national accounts from 2009 to 2011. More recently, it was alleged that the NNPC retained as much as $50 billion in oil revenue that was due the government. A PwC audit for the period from January 2012 to July 2013 found the NNPC should refund as much as $4.29 billion to the government. This excludes money owed to other companies. Corruption would vanish if Buhari refocused the NNPC as just a regulator "so people like us can get on with the job," said Kola Karim, head of a Nigerian oil explorer. Producing about 60,000 barrels a day, Karim's Shoreline Group could be pumping more than double that amount if the NNPC was not a partner in his business and with civil servants slowing investment decisions. (Mbachu, D., Bala-Gbogbo, E. and Wallace, P. 2015. In Hunt for Missing Billions, Buhari Targets Nigeria Company. **Bloomberg Business** – www.bloomberg.com. 10 August.)

- *CAS View:* The general view of the NNPC is not a favourable one. It is frequently stated that should Buhari route out corruption, he would have done Nigeria a massive favour. Fixing the oil industry would help to get Nigeria back on track to become the "lone superpower of Africa". And it seems that would require that the NNPC is dealt with appropriately. Buhari has made his intentions clear, and the amounts involved are indeed staggering. It now remains to be seen whether he would be able to disentangle the NNPC to cleanse it of any corruption. It would seem to be a herculean task! These kinds of issues unfortunately divert attention from other very lucrative investment opportunities in Nigeria, which is a pity. CAS reported last week of opportunities identified by the Governor of Imo State in the fields of tourism, education, health and poultry, to name but a few. Singaporean companies such as Indorama, Tolaram , Olam , PIL and Wilmar , to name but a few , have already shown upon the benefits of investing in Africa in general, and in Nigeria specifically.

- **Ghana:** According to the Ghanaian ministry, Ghana National Petroleum Corporation (GNPC) has appointed the Japanese trading company Mitsui & Co Limited to help develop infrastructure for its natural gas production. Mitsui will assess how best to construct a second plant to process raw natural gas from the Tano basin. Ghana, which exports cocoa, gold and oil, is expected to produce about 250 million cubic feet of gas daily by 2018 from its main west Tano basins. State-owned GNPC has stakes in Ghana's major oil and gas blocks, including the flagship Jubilee field, and it has plans to become a national supplier of gas. Ghana produces an average of 100,000 barrels of oil daily and 140 million cubic feet of gas from the Jubilee field, operated by a consortium led by Tullow Oil. Two other fields, Tweneboa-Enyenra-Ntomme, operated by the consortium, and Sankofa, operated by Italy's ENI, are expected to come on stream in 2016 and 2017 respectively. (Anon. 2015. Ghana appoints Japan's Mitsui & Co as key gas production partner. **The Africa Report** – www.theafricareport.com. 13 August.)

- *CAS View:* While the focus is generally on Chinese FDI in Africa, Japan has a stated intention to rapidly increase its exposure to the African continent. Here is an example where a Japanese company is getting involved in Africa. In the beginning of September, Ethiopia is hosting an Africa Japan Business Investment Summit in Addis Ababa. Japan is clearly doing its utmost to play catch-up. It realises that countries such as China and India have a head start and that the early bird in Africa will catch the worm. Sometimes it is stated that the investment opportunity is too expensive. The counter argument is what is the cost of non-investment? Countries that have not asked themselves this question might rue the omission at a later stage.

Southern Africa

- **South Africa:** In '*How South Africa Works and Must Do Better*', Mills & Herbst argue that an unemployment rate of 33% is an overwhelming challenge that South Africa has not yet dealt with. If left unaddressed, it will be impossible to lift millions out of poverty and nation-building will inevitably prove fraught. In spite of significant achievements since 1994, South Africa's growth record has been poor by comparison not only to expectations, but of the record of other countries 21 years into their 'independence' - South Africa's per capita GDP rose by 30%, while Singapore grew nearly 400% and Botswana's 600%. Three challenges are raised: the sustainability of providing emergency assistance to poor and vulnerable people of South Africa; Government's expansion of the civil service, which created a fiscal drain and has served to price people out of jobs in the private sector; labour volatility makes it clear that the Tripartite Alliance is not working effectively to manage this relationship. The authors recommend critical steps government must take: 1) Develop a sharp focus on growth and employment; every government action must be evaluated against whether growth and employment are enhanced. 2) Incentivise employment by limiting minimum wage increases and making it easier for employers to fire and redeploy workers. 3) Fix the SOE's and firms that the state invests in. 4) Address many of the unexpected (and sometimes unintended) consequences of legislation that emerge at the local level after legislation is adopted. 5) Fix the education system in the country so that employers can hire skilled workers. Steps business must take: 1) Develop a longer-term perspective on relations with workers. 2) Promote skill acquisition. 3) Improve communications with government, as they frequently talk right past each other on critical issues. Finally, labour has to realise that, while protecting the interests of union members, its actions have collateral effects on the economy. South Africa faces considerable economic and social challenges, but they are not as great as the difficulties the country has already overcome in its transition from apartheid to democracy and economic isolation to global integration. However, the longer it takes to fix problems, the more difficult the recovery.

- *CAS View:* Mills and Herbst make it clear that government, business and labour are together responsible to solve the challenges South Africa faces. Playing the blame game will help no-one. The advice is sound, and the essence lies in a cooperative and focused effort on growth, as well as educating South Africans. They also make it clear that there is hope for a prosperous South Africa, provided they deal with the challenges facing South Africa, and do it sooner rather than later.

- **South Africa:** According to ISS, South Africa does not face a crisis despite high crime, unemployment and inequality, though weak growth and poor governance have made it more likely things could go badly wrong. Despite a thin margin for error, there is still reason for optimism. Although SA requires a comprehensive resetting of key social, economic and political systems, a deeper analysis does not indicate a crisis, and South Africa's growth prospects are quite healthy. While the next 5 to 10 years might be quite uncomfortable, SA was in a "sweet spot" for economic growth due to its growing population and government's investments in water, sanitation, health and education. South Africa's transition to greater political and economic inclusiveness was making steady progress. The proportion of the black segment in the top Living Standards Measure has increased from 4% in 1994 to 29% by 2014. Due to government's investing in long-term growth, SA would grow because the fundamentals were positive, despite wastage, corruption and patronage. Uninspiring leadership and a recent loss of vision by the ruling party should not hide the remarkable progress achieved, including rolling out of essential services, alleviating poverty and the provision of broad-based education, despite flaws in implementation. The impact of investments in education takes almost a generation to realise, but South Africa will reap the benefits of investments made since 1994. In spite of high unemployment, the increase in employment levels from 15.1 million people in 2015 to a forecast of more than 25 million by 2035 will have a positive effect on tax revenues, the size of the economy and social stability. On the negative side, without a near revolution in policy coherence and government efficiency, there is little chance of average GDP growth levels reaching 5% over the medium to long term. Weak leadership, poor governance and lack of delivery might even cause the ANC to lose its majority as early as 2024. A demand for effective implementation and policies that delivered jobs, education and services was likely to increase. Unemployment had grown every year since 2008, and although the prognosis for improvements in South Africa's employment rate was not good, Cilliers emphasised the positive impact of expected growth on overall employment. (Cilliers. J. 2015. SA at risk but not in crisis. **Institute for Security Studies** – www.issafrica.org. 12 August.)

- *CAS View:* In spite of poor symptoms, it does seem that South Africa has a lot going for it on the medium to longer term. What is essential is that it should get its leadership sorted out. Without it, there will be no positive direction, and South Africa will find itself in that crisis. The above 2 articles recognize the challenges, but also shown upon positives. What South Africa needs is the political will to bring about the changes the two articles are referring to, as well as the business and social cohesion to make this work. The longer South Africa takes to deal with the issues, the more social cohesion comes under pressure and the more disconnected the unemployed become from society at large.