“Alternative Sources of Finance”

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Current state of play

- Most of project finance projects have been done with loans from DFIs, ECAs and some commercial banks.
- As a result of financial crisis, many traditional lenders have left or reduced their activities, partly due to capital requirements under Basel III.
- Financing available going to extractive industries and energy sector.
- Local currency funding limited in many countries and when available, tenors are limited (5-7 years).
- Lack of depth of local capital markets, Limited access by small firms and households.
- But needs are huge; infrastructure alone requires USD$50 billion a year (and that does not include maintenance for existing assets).
- Potential sources of finance include: bond financing, institutional investors, diaspora bonds, climate finance, etc.
- But as well, need to improve domestic resource mobilization: strengthen tax administration, better control of natural resources revenues, reduce illicit financial flows.

Development assistance's changing face

Private capital flows to sub-Saharan Africa—foreign direct investment (FDI), portfolio flows and loan flows— reached $67 billion in 2012, up from $14 billion in 2002. In comparison, ODA increased to only $42.5 billion in 2012 from $18.1 billion in 2002.

Traditional Sources

- Multilateral development banks
- Bilateral institutions, Government to Government

New donors

- Brazil, Russia, India, China, South Africa, Saudi Arabia, Korea, Turkey...

New private sources

- Philanthropy: Bill and Melinda Gates Foundation, Ford Foundation
- Social Impact investors: Shell Foundation, Acumen Fund
- Vertical funds: multi-stakeholder global programmes earmarked for a specific purpose

Local sources of finance

What we have:

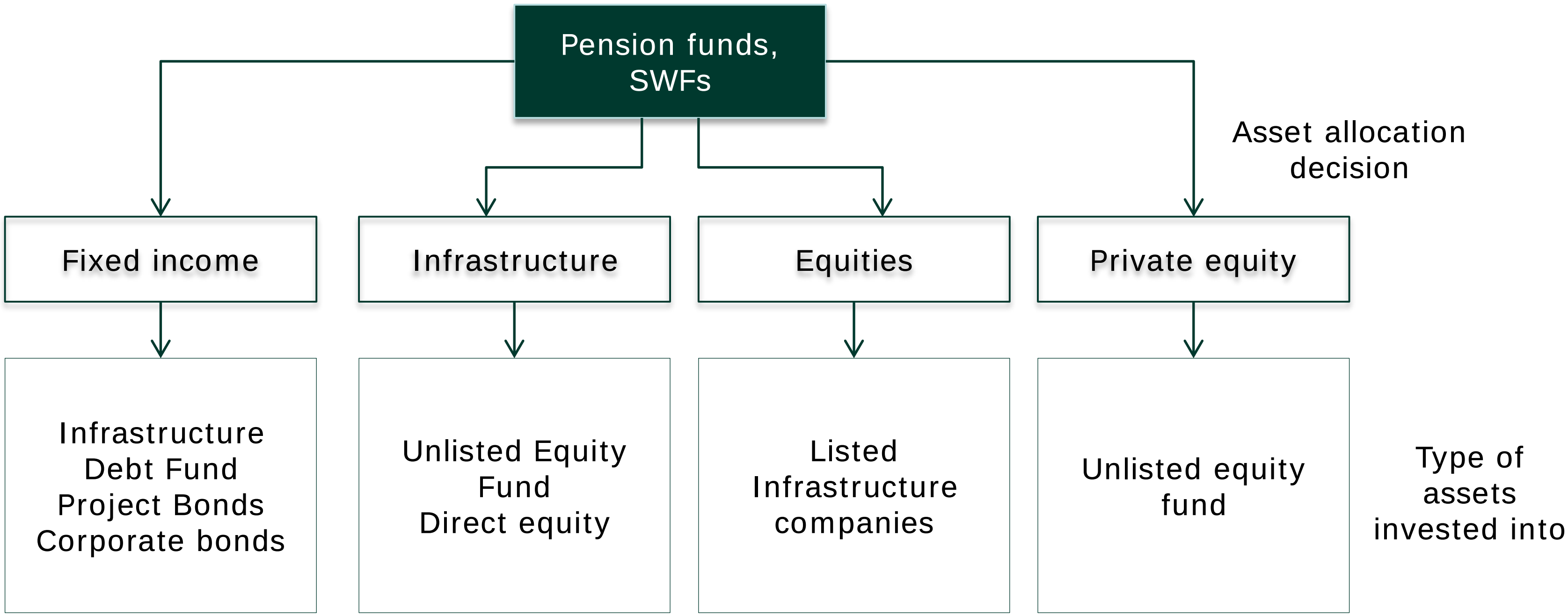
- In terms of banking depth, the financial systems are shallow.
- One in three African countries has an organized securities market.
- Insurance is highly variable across African countries, especially in the life sector, with considerable potential for development.
- Varied role of different classes of institutions, e.g. savings banks, cooperatives, microfinance institutions (often sponsored by NGOs).

What is missing:

- Non bank financing sector generally lacking, e.g. capital markets with debt and equity securities, and contractual savings institutions such as insurance companies, pension funds and mutual funds.
- Specific financial products missing due to issues relating to regulatory uncertainty, property rights, tax codes. These include leasing (a key tool for SMEs), factoring,

See ”Making Finance Work for Africa, The World Bank, 2007.

Alternative sources of capital (pension funds)



Following financial crisis, investors need:

- to invest in stable, resilient asset classes (e.g. infrastructure assets) over the long term to cover cost of capital
- an Investment strategy that generates scale
- a high degree of confidence with respect to regulatory regime
- financial structures with access to risk mitigation instruments

Source (for diagram): Pooling of institutional investors capital (April 2014), OECD

Alternative sources of capital (Private equity)

- Long term outlook for fund raising in the region looks strong.
- Renewed interest due to: growing economies, favourable demographics, increasing political stability, improved business environment.
- The landscape is changing fast as a number of global PE firms are looking to invest in Africa; no longer just South Africa but other countries like Nigeria, Ghana, Kenya, Ethiopia, Uganda, Tanzania, Zambia, Angola.
- Increase in sector related funds, e.g. Agriculture, infrastructure, real estate, natural resources, health care and consumer products.

➡ Given limited capital available from banks and public markets, private companies find it difficult to raise capital to grow.

- PE can meet some of the capital needs to support SME growth
- PE can bridge the funding gap

Microfinance

- It is estimated (in 2012) that there are 7.5 million active borrowers with a gross loan portfolio of USD 7.9 billion.
- A majority of microfinance institutions are savings and credit cooperatives, with the balance being NGOs, non bank financial institutions and banks.
- In terms of products, most provide both group and individual loan products and savings facilities are generally offered.
- Benefits cited include: access to small amounts of credit; extending education, improved health and welfare, sustainability.
- Issues for consideration:
    - ✓ Much of microfinance is led by private groups that want to fund initiatives that are important to them: education, women's health issues, water sanitation. Much needed but may not not use microfinance to its maximum potential.
    - ✓ With limited resources, should funds be channeled instead into SMEs which are generally viewed as the engine of job creation?