Converting Africa’s potential into profit

The opportunity for consumer products companies
Foreword

African markets represent an exciting but challenging growth opportunity for consumer products (CP) companies. Sustained growth rates, improving business conditions and a rising consumer class are driving increased levels of investment in Africa. However, the complexity of the region’s fragmented markets and diverse consumers means that it remains a real challenge to convert potential into profits.

In this report we explore both the opportunities and the challenges that Africa presents to CP companies. We examine Africa’s longer-term growth trajectory and, more specifically, foreign direct investment (FDI) trends in the broader retail and consumer products (RCP) sector over the past seven years. What our analysis shows is that, together with strong economic growth and rising levels of consumer spending, investment in the sector has been robust in recent years.

At the same time, and notwithstanding a compelling growth story, Africa is not for the fainthearted. All emerging markets come with their risks, and African markets are not fundamentally different from most other emerging markets in this regard. However, the defining challenges of doing business in Africa are arguably the sheer scale of the continent and the diverse and fragmented nature of its markets. It is challenging enough to simply travel around the continent, let alone do business across its vast patchwork quilt of 54 different countries.

Due to its size and complexity, Africa can be intimidating for those who do not have much experience of its business conditions or who are contemplating ambitious expansion plans after having operated in only one or two African markets for many years. EY’s own African growth journey, together with work we have done to support client expansion, as well as focused analysis of growth leaders on the continent, has enabled us to distill insights and critical success factors that we believe will be useful to you as you seek to unlock the potential of Africa’s rising consumer class.

First, we provide a set of 21 higher-level questions, linked to 7 interrelated capabilities that should be used to “stress-test” your strategic thinking on Africa. These same questions should be revisited periodically to ensure clarity and alignment on the why, what and how of what you are doing in Africa. These questions are then followed by an outline of what we believe are five critical success factors specific to CP companies entering into and expanding across African markets.

Our basic message is that the African opportunity is real and there remains a window to act. However, that window is now narrowing, and the cost of entering African markets is beginning to rise. Companies with an already established presence continue to expand and entrench their advantages. Doing business in Africa is challenging, but not overwhelmingly so. In our opinion, the risk of missing this window is likely to be far greater than any of the risks you will encounter in actually doing business in Africa.

Elaine Parr
EMEIA Advisory Centre
Consumer products

Derek Engelbrecht
Africa Sector Leader
Consumer products
Africa's rise is real

Africa’s rise over the past decade has been very real. While skeptics still abound, and there are people who still seek to debate the point, the evidence of Africa’s clear progress is irrefutable. Over this period, a critical mass of African economies has grown at high and sustained rates – so much so that, despite the impact of the ongoing global economic situation, the size of the sub-Saharan African (SSA) economy has more than quadrupled since 2000.

Looking forward, forecasts indicate that many parts of the region will continue to experience relatively high growth rates, with a number of African economies predicted to remain among the fastest growing in the world for the foreseeable future.

Source: IMF World Economic Outlook Database, April 2004

*Estimates
For companies seeking to grow and investors seeking higher returns, the African growth story is a compelling one. While most developed economies continue to struggle, Africa clearly offers an exciting opportunity for investment and an alternative to the ultra-competitive Asian and other emerging markets. It is not surprising, therefore, that investor interest in Africa has been on the increase. Our 2014 Africa Attractiveness report shows that perceptions of Africa’s relative attractiveness as an investment destination have improved dramatically over the past four years, while FDI projects into SSA grew at a compound rate of 19.5% between 2007 and 2013.
Consumer-facing industries rise in prominence

The ongoing diversification of economic activity in Africa and a growing African consumer class is encouraging increased FDI in consumer-focused services and manufacturing sectors. The shift of investment from extractive to service-oriented sectors is apparent when examining the last decade’s FDI data. In 2004, investment in natural resources accounted for over 25% of all FDI projects in Africa. In 2013, this proportion was only 5%. In 2013, the retail and consumer products sector was the second largest for FDI projects, accounting for 17.5% of all projects in Africa. It was also the lead sector in terms of job creation during the year.

- In 2013, Procter & Gamble announced plans to spend US$450m to upgrade existing plants and build new ones in Africa. US$175m will be used to construct a plant in South Africa to make products such as detergents, and US$200m will be spent on a baby-care products plant in Nigeria, which is already under construction.
- In early 2014, SABMiller announced that it will invest US$110m into its Nigerian brewery, continuing its expansion into the African beer market. The US$110m investment will go into tripling the brewery’s annual capacity from 700,000 to 2.1m hectoliters, and it will be operational from early 2015.
- Nestlé is investing US$70m to grow its Nigerian business. Nestlé’s investment will focus on further developing its distribution channels. Nestlé launched 10 mobile vans in 2014 in an effort to reach consumers in heavily populated districts. This number could expand to 2,000 over the next few years as the company builds scale and seeks to enter more remote areas where there is little retail presence.
- Unilever has also indicated recently that it would invest US$150m in a new plant in Nigeria, after investing a similar amount over the past two years.
- Mondelēz announced plans in 2013 to invest US$400m, largely aimed at capacity upgrades that will be spread over two phases, with the first phase of investment expected to be worth a quarter of the total outlay.
- Danone has grown its African business in the past 2 years via acquisitions. It recently purchased a 49% stake in West Africa’s largest maker of frozen dairy products, Fan Milk International (which had been purchased by Abraaj for US$300m). This year it acquired a 40% stake in Kenyan dairy company, Brookside. The deal will allow Danone to enter one of Africa’s biggest milk markets.
- South Africa headquartered Tiger Brands, Africa’s largest indigenous food producer, has driven an ambitious expansion strategy via a combination of exports, joint ventures and acquisitions – the most high profile of which has been the approximately US$180m for a majority stake in Dangote Flour in Nigeria.
- ShopRite, the leading retailer on the continent, now has over 160 stores across 16 different countries outside of South Africa. At the beginning of 2014, it announced its intention to open an additional 44 stores outside of South Africa by June 2015.
- Following Walmart’s US$2.4b acquisition of 51% of African retailer Massmart in 2011, plans have been announced for the launch of 10 pilot food retailing stores in Nigeria’s commercial capital of Lagos over the next two years.
- Access to real estate remains a real challenge for retailers in many African countries. Africa, a fund which develops and owns various shopping centers across Africa, is addressing this as an opportunity. So far, it has already made several investments in China, in both the Accra and West Hills Malls, Zambia and Mozambique.

Sources: Business Monitor International; various company sources

FDI projects in Africa

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<tr>
<th>Years</th>
<th>2007</th>
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</tbody>
</table>

Share of extractive sectors in FDI projects in Africa dropped to an all-time low in 2013.

Sources: FDI Intelligence, EY analysis

In 2013, ShopRite announced plans to spend US$450m to upgrade existing plants and build new ones in Africa. US$175m will be used to construct a plant in South Africa to make products such as detergents, and US$200m will be spent on a baby-care products plant in Nigeria, which is already under construction. In early 2014, SABMiller announced that it will invest US$110m into its Nigerian brewery, continuing its expansion into the African beer market. The US$110m investment will go into tripling the brewery’s annual capacity from 700,000 to 2.1m hectoliters, and it will be operational from early 2015. Nestlé is investing US$70m to grow its Nigerian business. Nestlé’s investment will focus on further developing its distribution channels. Nestlé launched 10 mobile vans in 2014 in an effort to reach consumers in heavily populated districts. This number could expand to 2,000 over the next few years as the company builds scale and seeks to enter more remote areas where there is little retail presence. Unilever has also indicated recently that it would invest US$150m in a new plant in Nigeria, after investing a similar amount over the past two years. Mondelēz announced plans in 2013 to invest US$400m, largely aimed at capacity upgrades that will be spread over two phases, with the first phase of investment expected to be worth a quarter of the total outlay. Danone has grown its African business in the past 2 years via acquisitions. It recently purchased a 49% stake in West Africa’s largest maker of frozen dairy products, Fan Milk International (which had been purchased by Abraaj for US$300m). This year it acquired a 40% stake in Kenyan dairy company, Brookside. The deal will allow Danone to enter one of Africa’s biggest milk markets. South Africa headquartered Tiger Brands, Africa’s largest indigenous food producer, has driven an ambitious expansion strategy via a combination of exports, joint ventures and acquisitions – the most high profile of which has been the approximately US$180m for a majority stake in Dangote Flour in Nigeria. ShopRite, the leading retailer on the continent, now has over 160 stores across 16 different countries outside of South Africa. At the beginning of 2014, it announced its intention to open an additional 44 stores outside of South Africa by June 2015. Following Walmart’s US$2.4b acquisition of 51% of African retailer Massmart in 2011, plans have been announced for the launch of 10 pilot food retailing stores in Nigeria’s commercial capital of Lagos over the next two years. Access to real estate remains a real challenge for retailers in many African countries. Africa, a fund which develops and owns various shopping centers across Africa, is addressing this as an opportunity. So far, it has already made several investments in China, in both the Accra and West Hills Malls, Zambia and Mozambique.

Sources: Business Monitor International; various company sources
Breakdown of FDI in the RCP sector in Africa

Number of FDI projects

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<thead>
<tr>
<th>Year</th>
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FDI value (US$ billion)

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<td>2.5</td>
<td>7.1</td>
<td>3.4</td>
<td>4.6</td>
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</table>

FDI projects by functions (% share, 2007–13)

- Sales, marketing and support: 7.9%
- Retail: 40.8%
- Manufacturing: 43.3%
- Others: 8.0%

FDI value by functions (% share, 2007–13)

- Sales, marketing and support: 23.2%
- Retail: 24.0%
- Manufacturing: 34.4%
- Others: 10.4%

FDI projects and value by source countries (% share, 2007–13)

- US: 11.8% (10.5% projects, 19.7% value)
- UK: 9.9% (11.8% projects, 9.9% value)
- Spain: 8.0% (4.6% projects, 9.9% value)
- South Africa: 7.1% (4.9% projects, 9.9% value)
- Switzerland: 6.1% (6.4% projects, 6.4% value)
- France: 5.8% (4.0% projects, 5.8% value)
- UAE: 5.5% (4.4% projects, 5.5% value)
- South Korea: 3.0% (3.0% projects, 3.0% value)
- Italy: 2.7% (4.8% projects, 4.8% value)
- India: 3.8% (9.9% projects, 3.8% value)

Key destinations by FDI projects (% share, 2007–13)

- South Africa: 61.9% (19.0% projects, 61.9% value)
- Nigeria: 10.7% (10.7% projects, 10.7% value)
- Egypt: 8.3% (8.3% projects, 8.3% value)

The opportunity for consumer products companies...
Scale and diversity make Africa an inherently complex environment in which to do business

Despite Africa’s ever-improving prospects, the continent remains a complex and challenging environment in which to do business. For any organization with growth ambitions, there is still a need to proceed with care and due diligence. While we would argue that many African markets are not fundamentally different from markets in other rapid-growth regions, there are some key differences. Foremost among these are the sheer scale of the continent and the diversity of its many countries.

Although many of us still sometimes lump “Africa” together in our commentary and comparisons as if it were a single market, it does, of course, comprise 54 sovereign states – representing more than a quarter of all independent countries in the world. However, for most companies, very few of these individual markets are likely to provide the kind of scale, in the shorter term at least, that makes them commercially attractive in and of themselves.

As a result, any kind of growth strategy in Africa almost invariably has to take account of multiple markets. And, as one looks to sort through opportunities and risks across these markets, it quickly becomes clear that opportunities and risks differ widely from country to country and region to region.

To further complicate analysis, language, taste and cultural dynamics are as diverse as anywhere else in the world, with French, Arabic, English, Portuguese, German, Spanish, Dutch and Italian influences mixed with numerous indigenous languages and cultures. At the same time, operating across borders in Africa means having to come to terms with very different (and often fragmented) sets of rules, regulations and stakeholders.
Capabilities for successful strategy execution in Africa

Despite this complexity, or perhaps because of it, a number of companies are thriving. Based on our analysis of companies leading growth in Africa, as well as our own experiences of expanding and integrating our practice across 33 countries on the continent and supporting dozens of clients at different phases of their African growth journeys, we have identified a set of capabilities that we believe are critical to the effective execution of growth strategies in Africa.

These capabilities take the shape of a systemic model that can be used to stress-test strategic thinking and execution wherever on its African growth journey an organization may be. The model is characterized by seven interconnected capabilities (Ps) and is similar in structure to the 7-S model popularized by Tom Peters and Robert Waterman in their book *In Search of Excellence*. The seven Ps are separated by a “yellow line,” distinguishing between the harder elements of strategy formulation and execution (those that require intellectual acuity – IQ), which are above the yellow line, and the softer elements (those that require emotional intelligence – EQ), which are below the yellow line.
As this model illustrates, thinking about strategy execution is not just a matter of formulating a clear strategy, re-engineering processes or implementing new systems or structures — which is often where organizations focus most of their efforts. In Africa, people and human relationships really do matter, and it is particularly important to emphasize the softer, human elements. Ultimately, though, there needs to be a high degree of alignment among all the Ps.

1. Why Africa, why now?
2. What are our core capabilities, and how can we leverage these into new markets?
3. What is our unique value proposition and what will be the basis of our competitive positioning?

Planning

Given the scale, complexity and fragmented nature of the African continent, making well informed choices about which markets to enter when and via which mode are critical. However, planning for growth in Africa is a complex exercise, and too much time and energy can be spent looking for definitive answers in a spreadsheet. Ultimately, there is no substitute for spending time on the ground, in-market. It is also important to strike the right balance between sticking to the plan — and, more fundamentally, the core business purpose — and adapting to different needs and circumstances across diverse markets.

1. Are our priorities for growth across Africa clear and well-articulated?
2. Have we done a thorough analysis of needs, opportunities and risks (without getting stuck in analysis paralysis), and have we spent meaningful time on the ground in markets we are considering entering?
3. What are our nonnegotiable business principles, policies and processes (and conversely, where can we be flexible)?

Portfolio

While we are positive about the growth potential in Africa, we are also realistic about the relative immaturity and risk, as well as the current lack of scale, in many individual markets. There will be challenges, and perhaps even failures, so balancing risk across a number of different markets is important. A sizable African portfolio provides three critical advantages:

- It will mitigate the risk of political or economic instability in any one country materially impacting overall earnings
- Early mover advantage in many markets that are still at an early stage of development
- Sufficient critical mass to make the overall African portfolio material enough to matter

1. Are we actively managing a portfolio that spreads risk and balances revenue/profit generation with growth opportunity?
2. Can we be No. 1 or 2 in the markets we choose to enter and operate in?
3. Can our portfolio of regional markets provide enough critical mass to generate financial results that matter?
People

Strategies are not self-executing. Organizations that are serious about seeing through their African investment in the longer term have found – and will continue to find – that genuinely investing in people can bring significant rewards. Human talent and energy is abundant in Africa, but there is often a shortage of technical and management skills. Sustainable success in Africa will increasingly turn on the ability to effectively bridge this gap and to put human resource development at the heart of strategy execution. For most sectors, it will be particularly critical to strike the right balance between a dynamic mobility program and recruiting, developing and retaining talented and committed local staff.

1. Are we clear on what key skills and competencies are required in setting and scaling up in new markets (and the investment required in human resources)?
2. Are we prepared to make sufficient investment in putting people on the ground in new markets?
3. Do we have the right balance between mobility/use of expats and a robust program for recruitment and development of locals in the markets we operate in?

Patience

Whatever one’s answer is to the “why Africa” question, there is no doubt that one of the key drivers has to be financial returns. Given Africa’s economic growth story over the past decade, and the fact that a number of organizations are already generating healthy returns from African operations, this is understandable. However, there is a very real danger that “HQ” will expect too much too soon from investments in Africa. It generally takes time and investment to generate any kind of meaningful returns from African operations – most of the companies that are successful today have been operating in Africa for many years. Over time they have gained skills, experience and understanding, developed relationships and markets, established competitive positions, evolved operating processes and systems and built up a meaningful African portfolio. There are no shortcuts, even for seasoned operators, but the eventual returns from the portfolio will be worth it.

1. Are we prepared to invest upfront without expectation of quick returns?
2. Are we prepared to invest ahead of the curve in developing and even creating markets over the longer term?
3. Do we have the appetite and will to invest in developing long term relationships across different levels of government, business and civil society in the markets we operate in?

Partnerships

Relationships matter in Africa. Strong local business partnerships are often critical to success – an effective local partner can help a new market entrant to hit the ground running, providing support with, for example, navigating bureaucracy, coming to terms with local operating issues and helping understand consumer or client dynamics. At the same time, there will be ever increasing pressure for multinationals to demonstrate their long-term relevance and commitment to local economies. Fostering good, proper relations across government and civil society will be increasingly vital to realizing strategic aims.

1. Are we clear on our preferred mode of entry into new markets (e.g., acquisition, JV, license agreement, etc.)?
2. How are we going to ensure we are locally relevant over the long term?
3. Do we have the culture, mindset and capabilities to support open and active engagement with external stakeholders?

Perspective

A common belief held by companies successfully doing business in Africa is that to succeed in the long term one must deliberately adopt a glass half full rather than empty perspective; that it takes a positive mindset to succeed in Africa. There is no doubt that if you set out expecting difficulty and risk, you will find it easily enough, and this will probably put a brake on any growth plans. High performing companies in Africa have tended to look for the opportunities first and only then factored in risks. At the same time, those who are succeeding will also tend to have a “learning” perspective; entering new markets with a genuine respect for local dynamics, and with a belief that the organization has both something of value to contribute but also much to learn to be able to operate effectively in the local environment.

1. Do we consciously adopt a glass half-full perspective, looking for opportunities first before considering how to manage risks?
2. Are we actively working with governments and communities in different African countries to contribute to a broader growth and development agenda?
3. Are we actively learning from and adapting to local environments (with humility and respect)?
Five critical success factors for consumer products companies

The 7Ps model cited earlier is broadly relevant to almost any company with a cross-border growth agenda in Africa. At any level of detail beneath this, the issues will clearly be more specific for different sectors and circumstances. For consumer products companies that are driving expansion in Africa, and moving one level down, we would highlight five factors that we believe are particularly critical for success.

1. Choosing which markets in which to compete

Given the diverse and fragmented nature of Africa’s many markets, making well-informed granular choices about which markets to enter, when and how, is crucial. At the same time, though, market selection is also framed by the challenge of effectively “connecting the dots” across multiple operations and territories: not only ensuring that the African “portfolio” (whatever shape or form that may take) is big enough to matter, but also that multiple in-country and cross-border risks are effectively managed, operating efficiencies are gained and, ultimately, the whole is greater than the sum of the parts.

Whether entering into or expanding across Africa, a good starting point is to develop a structured analytical framework for prioritizing markets in which to expand and for assessing different strategic options. Too often, we have found that thinking on Africa generally, and on specific markets, is based on ill-informed opinion — either unduly pessimistic or overly optimistic — and completely divorced from current realities. We therefore stress the importance of having fact-based conversations about Africa, informed on the basis of rational analysis rather than anecdotes and conjecture.

To begin with, we have found it useful to develop a market assessment matrix drawing on a balanced set of risk and opportunity indicators to provide a simple but effective framework to rationally assess the pros and cons of different African markets.

Any number of indicators can be used, but, to illustrate the point, we have created composite country risk and opportunity indices and then plotted the position of selected countries on a graph. On the horizontal (x) axis, we plot where each country ranks on the composite risk index, while, the vertical (y) axis, the ranking of an opportunity index is plotted.

A third dimension (indicated by the size of the bubble) can be included to add some richness to the conversation. To illustrate, we have provided an example of what a matrix may look like for a company looking for consumer-related opportunities, overweighting those indicators that we feel are more indicative of attractive consumer growth trends.

It is important not to view this as a definitive assessment of any of these markets. As much as we believe it is critically important to begin from a rational basis of fact, we also recommend not simply reducing market analysis to a closed model in which various indicators are simply combined in terms of their weighted importance. Such models can provide a useful starting point but can also give the misleading impression that there are absolute answers in searching for market potential. In reality, there will be different answers for different organizations with different priorities, and as priorities change over time, so will the answers.

A matrix such as this is therefore inherently flexible. Positions will change depending on the indicators included (which will be determined by key drivers of risk and opportunity in a particular organization), as will the relative weightings given to those indicators. The categorization of markets will also depend on where you set your “thresholds” on the risk and opportunity axes.
Success

Risk opportunity matrix oriented toward consumer-facing sectors


Opportunity indicators
1. GDP (current US$)
2. Population (m)
3. Urban population (% of total)
7. Country wealth (1=income, 2=lower income, 3=upper middle, 4=high income (non-OECD), 5=high income (OECD)
8. Mobile penetration (% of population with mobile access)
9. Population growth (annual %)
10. Literacy rate (total population %)

Risk indicators
1. Ease of doing business overall rank (out of 184 countries)
2. Transparency International Corruption Perceptions Index (0=highly corrupt, 100=very clean)
3. Strength of investor protection index (0=unfavourable, 10=favourable)
4. Quality of overall infrastructure (1=extremely underdeveloped, 7=extensive and efficient by international standards)
5. Corporate maximum tax rate (%) (non-OECD)
6. Logistics Performance Index: overall score (1=worst, 5=best)
7. Perceptions of governance: regulatory quality percentile rank (0=lowest, 100=best)
8. Perceptions of governance: rule of law percentile rank (0=lowest, 100=best)
9. Democracy score (1=autocratic, 10=democratic)
10. Mo Ibrahim Index of African Governance: overall score (0=worst, 100=best)
Conducting rational, fact-based and cross-comparative analysis provides an essential starting point for developing strategies for growth in Africa. However, we suggest not investing too much in a process of this nature. Assessing markets and developing strategies for growth in Africa is a complex exercise, and too much time and energy is sometimes spent looking for definitive answers in a spreadsheet. The numbers should instead be an aid to help define growth priorities, risk appetite and investment criteria more clearly and to enable informed strategic dialogue and decision-making. By converting a set of numbers into a framework for informed conversation, the market assessment matrix provides this enabling tool.

Building on this kind of quantitative exercise, we also recommend conducting qualitative analysis by applying relevant “thematic lenses” to whatever kind of ranking system or matrix you may have developed. Applying different lenses to various markets will help build up a greater richness of perspective and lead to far more robust decision-making.

What is relevant to any organization will clearly depend on various sector-specific, organizational and circumstantial factors. For illustrative purposes, a largely English-speaking company expanding from a South African base and looking for consumer-related growth opportunities might apply the following lenses framed by simple hypotheses to help narrow and stress-test choices:

<table>
<thead>
<tr>
<th>Lens 1</th>
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<th>Lens 3</th>
<th>Lens 4</th>
<th>Lens 5</th>
<th>Lens 6</th>
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<tr>
<td>Language and geographic proximity</td>
<td>Regional groupings</td>
<td>Urbanization trends</td>
<td>FDI trends</td>
<td>Infrastructure investment trends</td>
<td>Company footprints</td>
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**Hypothesis**

- Countries geographically proximate to South Africa and that have English as their language of business are more attractive.
- Countries that form part of more coherent regional groupings are more attractive.
- Markets with more highly concentrated and urbanizing populations are more attractive.
- Countries with higher levels of FDI investment are more attractive.
- Countries with higher-quality infrastructure and higher levels of active infrastructure projects are more attractive.
- Countries with a strong presence of consumer-facing companies are more attractive.

By systematically working through an assessment process of this nature – one that combines both fact-based analysis and strategic dialogue among key decision-makers – the logical sequencing for growth across the continent generally becomes clearly evident. However, it is important not to expect definitive answers to your strategic questions from this or any other kind of analytical exercise; doing business in Africa means learning to deal with uncertainty and complexity on an ongoing basis. The key is to use both quantitative and qualitative methods to critically evaluate risks, opportunities and strategic options based on your unique business drivers and critical success factors. The sooner the shift is made from analysis to getting feet on the ground in key markets, the better.
2. Shaping propositions for Africa’s diverse consumers

There is significant latent potential across a range of consumer product categories in Africa. With the expansion and success of the likes of SABMiller, Heineken and Diageo, beer is a relatively well-developed category. Despite this, and as the graphic below from SABMiller illustrates, there remains enormous latent potential for growth in formal alcoholic beverages.

However, a picture like this needs to be broken down to better understand this potential. Given its scale and diversity, it is probably more helpful to develop several strategies for Africa rather than conceiving of a single “one size fits all” strategy. This extends beyond regions or countries or cities to consumers themselves. There is an increasingly useful body of work emerging to assist in understanding and segmenting Africa’s many different consumers.

Standard Bank, for example, recently released a report analyzing the rising middle class in Africa. This analysis covers 11 key SSA economies, accounting for 75% of the region’s GDP (excluding South Africa) and, among other things, reveals significant differences in terms of the size and proportion of different income bands between countries. As the following graph illustrates, Nigeria dominates in terms of the sheer number of middle class households (defined as having consumption of US$8,500 – US$42,000 annually in constant 2005 terms), while Angola and then, perhaps somewhat surprisingly, Sudan, have the highest proportion of middle class households. Conversely, a much larger majority of people in East African countries have not yet reached middle class status and would still be categorized as low income (household consumption of under US$5,500 annually), including 99% of Ethiopians, 97% of Tanzanians, 96% of Ugandans and 92% of Kenyans.

Source: SABMiller
Risk opportunity matrix orientated toward consumer-facing sectors

One of the key points here is that the potential for different categories and brands is going to be different in each of these markets and will require a variety of approaches and propositions. To take this one step further, it would also be useful to overlay spending power against actual spending on a given category in specific markets to understand where there may be underdeveloped categories with the potential for meaningful growth.

To illustrate this, we have done some high-level analysis of city-level data, mapping average household income levels to spend on personal care products. It is clear that this particular category is relatively immature and underdeveloped in most African cities. Johannesburg provides a benchmark, with relatively high levels of spend on personal care products in both absolute and relative terms. Lagos, with its large population, clearly provides an attractive opportunity for consumer-facing companies. However, these consumers already spend a relatively high proportion of income on personal care products. This may be considered a positive to the extent that the category is already relatively developed, but also indicates that competition is likely to be quite intense. In contrast, the Angolan city of Luanda, with comparatively high disposable income levels and proportionally low spend on personal care products, stands out as a city-market with potential for category development.

3. Controlling the route to market

The fragmented nature of Africa’s many markets, combined with often underdeveloped infrastructure, means that supply chain and logistics will be a challenge. However, probably the greatest operational challenge for most consumer products companies in most African markets is to gain control of the route to market and point of sale. It is, after all, at the outlet where the consumer ultimately buys the product and where the battle for share of discretionary spend is won or lost.

What makes it so difficult to manage the route to market in the majority of African markets is that traditional trade (i.e., small dispersed outlets, open-air markets, informal vendors, etc.) represents an average of more than 80% of the retail market across the continent. Although formal retailers such as ShopRite, Massmart, Spar and Nakumatt are expanding, traditional trade will continue to dominate most markets for the foreseeable future.

Because of the various challenges involved in getting products onto shelves in these fragmented markets, many companies adopt a more passive wholesale-type model, effectively outsourcing distribution to a third party. The logic is understandable: do not overinvest upfront; rely on someone who understands local market dynamics; and give yourself time to learn about how things work. However, we believe that this approach is a mistake for anyone who is serious about realizing the long-term African consumer opportunity.

High performers in African markets have a well-designed distribution network that combines efficiency with flexibility. For companies covering multiple markets, the distribution network may feature a combination of direct coverage and partnerships with third-party distributors, wholesalers and even micro-entrepreneurs. A key factor, though, is a degree of control, which is often achieved by teaming a directly employed sales force with distribution partners.
There is a growing body of research that underscores the fact that brand recognition and loyalty are important to many African consumers, so success in many categories will often depend on visibility at the point of sale. As a result, the directly employed sales people would generally focus on the relationship with the traditional retailer at the outlet, visual merchandising, making products more visible than those of competitors and brand image, as well as perhaps helping to manage inventory and assisting both distributors and informal retailers to develop their capabilities.

1 See for example, “The Diverse People of Africa,” Nielsen, March 2012

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**Coca-Cola’s micro-distribution model enables an effective route to the consumer in informal market settings**

Coca-Cola Sabco (CCS) is one of the Coca-Cola Company’s largest bottlers in Africa, operating 121 bottling plants and employing about 9,500 people in seven African countries. CCS has local shareholding in every African country it operates in. Local shareholders are either prominent business people or, in the case of Namibia and Mozambique, the government, but all generally play an active role and often on the local board.

One model that has worked well for bottling company Coca-Cola Sabco in parts of East Africa is the Official Coca-Cola Distributor (OCCD) approach, a model whereby the local bottling factory partners with a number of “micro-distributors” – local entrepreneurs, each of which is given responsibility for a defined geographical area (generally a 1km radius in an urban environment, servicing at least 500 outlets). These OCCDs have become a central element in Coca-Cola Sabco’s core distribution strategy in several countries and are responsible for 70% or more of sales volumes in Ethiopia, Kenya, Uganda and Tanzania. In this manner, Coca-Cola Sabco has not only addressed their core route to consumer challenge, but it is also creating numerous economic opportunities for local entrepreneurs and their employees.

Source(s): Coca-Cola Sabco

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**Nestlé is experimenting with direct-to-consumer models to build brands in informal markets**

Over 80% of Nestlé’s business in the region is in traditional trade (small stores and the informal sector). Consumer activation, branding and controlling the route to market is critical in this context. Nestlé achieves this partly through a combination of its own sales force and outsourcing to trusted third party distributors.

An increasingly important element of Nestlé’s distribution model in African markets is direct to consumer. Nestlé has been among those at the forefront of creating entrepreneurial opportunities for ice cream and coffee vendors.

The latest of these micro-partnerships is the My Own Business initiative. The company provides the vendor with a Nescafé coffee dispenser they can strap onto their backs and individual cups of coffee can be sold in markets, at events, roadside, etc. This initiative was launched in Nigeria in 2012, and it is now also operational in Burkina Faso, Côte d’Ivoire, Cameroon, Ghana, Senegal and Kenya. It is also being extended to the DRC, Ethiopia, Angola and Mozambique.

Source(s): Nestlé
4. Innovating for local context

It may be stating the obvious, but markets in Africa do not come “ready to do” business. There are generally significant gaps in terms of institutions, infrastructure, value chains and on-the-ground capabilities. Successful companies proactively invest in addressing these gaps, creating competitive advantage and thriving not only in spite of, but also because of their ability to do business in sometimes difficult conditions.

There is an important point about mindset here: the African business environment is inherently complex and requires a willingness to think differently and innovate for local conditions. One of the more obvious areas to focus on is product and packaging innovation. Because a large number of African consumers have limited disposable income, leading companies like Unilever and Nestlé have developed a “small unit pack, low unit price” approach.

Unilever, for example, produces small packs of detergent, soap, margarine, toothpaste, cooking oil and bouillon cubes at prices that low income African consumers can afford. Independent and informal traders have been doing this for decades—buying in bulk and then breaking up and selling in small portions to customers. What Unilever has done is both formalized the approach, but also, by introducing branded packaging, entrenched its key brands in the minds of many African consumers. As Nielsen research indicates, although Africa’s consumers are very diverse, a key similarity is that brand loyalty is a key purchase driver.¹

Food producers also need to take cognizance of Africa’s diversity and local tastes. Nestlé sells more than 100 million Maggi stock cubes a day in West and Central Africa alone. However, they also adapt the flavors of their cubes across different markets according to diverse local preferences. They are now even going a step further, with their African R&D center, which was established in Ivory Coast in 2009, looking at ways to prepare Nestlé products using locally sourced ingredients, such as cassava, sorghum and millet.

However, product and packaging innovation is only one dimension of what is required to succeed across Africa's diverse and fragmented markets. Due to the institutional, infrastructure, capability and value chain gaps that one will often encounter when doing business in Africa, business models that work well in other parts of the world can rarely be simply transplanted to the African environment. You have to think differently about how to adapt to this kind of environment in a way that optimizes investment, manages costs and mitigates risk. This may require stretching beyond the boundaries of what corporate headquarters may consider “core competencies”—with more proactive involvement, for example, in developing local agriculture or establishing distribution networks.

Unilever has been at the forefront of innovating pack sizes, packaging and pricing to meet local needs

Unilever has been consciously embedding corporate responsibility - part of its broader Sustainable Living Plan that it is rolling out to the continent - in the way it does business in Africa. One key focus has been to make its products available for poorer consumers in Africa through innovations such as its “small unit pack/low unit price” concept, whereby it sells small packages of cooking oil, salt, laundry detergent, toothpaste, shampoo, etc.

The company’s distribution network has also been adapted in some markets for informal traders who have working capital constraints.

For example, goods are effectively given to street traders on one week credit, and the payment is collected a week later when the trader has accumulated some cash from his or her market - Unilever has introduced its direct-to-consumer distribution scheme to Africa – Shakti – that has been so successful in India (approximately 45,000 Indian women sell Unilever products directly to 3m households). Beginning in Nigeria and Kenya, Unilever aims to employ tens of thousands of vendors that would be selling directly to consumers. To set up their business Unilever provides microfinance for its vendors and in the process provides a livelihood for people who might otherwise struggle to find work.

Source(s): Unilever.

Diageo’s Senator Keg illustrates the win/win growth opportunity when innovation focuses on local challenges and conditions

Diageo has a long history in Africa dating back to when Guinness was first shipped to Sierra Leone in 1827. Among its interests is a majority shareholding in East African Breweries Limited (EABL). With local presence and knowledge, Diageo identified the opportunity offered by an emerging consumer class in the early 2000s. However, they faced the common challenge of producing a product that was affordable to a still poor mass market but that could still generate a profit. The poor in Kenya often consumed homemade brews sold illegally. These illicit products were often contaminated with methanol, fertilizers or battery acid and caused blindness and even death. This presented a big opportunity for Diageo. Providing a safe, ultra low-cost beer to compete with illegal suppliers could play a crucial role in both resolving alcohol-related health problems and in achieving the targeted growth for Diageo.

In response to this challenge, the company created a new product – a beer called Senator Keg – to tap the approximately 60% of consumers who drank only illegal alcohol. Senator Keg offered potential consumers not only a safe drink but also a stepping-stone to a new, aspirational drinking experience. However, it was not as simple as simply creating a new product; Diageo had to rethink it entire value chain – virtually every part of the network was redesigned and innovated to reduce cost and increase relevance to this particular market segment. Senator Keg was a tremendous success by any measure, gaining over 40% of the Kenyan beer market.

Source(s): Diageo
5. Being locally relevant

There is ever-increasing pressure for multinationals to demonstrate their long-term relevance and commitment to local African economies. Rather than simply viewing Africa as a set of new growth markets in which to import and distribute goods to a growing consumer class, there is an expectation that companies will contribute meaningfully to local economies through capital investment, job creation, supplier and enterprise development, and skills and technology transfer. The long-term winners in Africa will embrace the imperative to be locally relevant rather than view it as a cost of doing business.

The concept of shared value — the idea that you can pursue profit with purpose; that you can do business while having a direct positive economic impact on the communities in which you operate — is particularly relevant in the African context. The organizations that have been the most successful in Africa are taking a long-term view. They realize that there are no shortcut and, more importantly, they realize that for their business to grow sustainably over the longer term, the economies and communities in which they operate need to grow sustainably. The bigger the skills pool, the more jobs and economic opportunities are created; the larger the spending power of consumers and government, on one hand, the greater the number of opportunities for business growth there will be on the other.

Coca-Cola’s model of distributing in key African markets via independent micro-distributors is a good example of shared value in action. Not only is the company creating economic and employment opportunities for thousands of Africans, it is also enabling systematized access to numerous small and informal outlets that would otherwise be very difficult and far more costly to reach.

Although there is a trend in the consumer products sector to move to global, above-market sourcing and production, many leading companies doing business in Africa are focused on being as close as possible to the markets they serve. SABMiller, for example, operates over 50 breweries and bottling plants across the continent, employing thousands of locals in its various production facilities.

At the same time, sourcing malting barley (a key brewing input) locally has become an important part of SABMiller’s business model in many African countries. In Zambia, for example, SABMiller has developed a malting barley sector from scratch. SABMiller initially had to import all the barley it used in Zambia but, through its work with local farmers, Zambia is now a net exporter of barley, creating employment opportunities for more than 4,000 local people.
A key factor in Nestlé’s success in Africa has been having production facilities in or close to the markets they serve and expanding its existing factory in Nairobi and building new factories in Angola and the DRC.

In total, Nestlé currently operates 29 factories on the African continent, providing direct employment to approximately 15,000 people and indirect employment to more than 50,000. Nestlé products are sold in all the 54 countries across the African continent.

Source(s): Nestlé

Leading companies are thinking differently about how to add value to local African markets

Diageo has recently installed containerized spirits blending and packaging mini plants known as “Cubes” in Ghana and Nigeria. The plant – initially for Gilbey’s gin – is housed inside five connected shipping containers, and provides Diageo a way to test demand for new drinks while minimising capital deployment.

Small, prefabricated factories are also being used by Danish dairy Arla Foods in the Côte d’Ivoire. They produce 25g sachets of milk powder in a housed inside three containers shipped from Copenhagen. The facility was up and running in weeks and cost a more traditional factory would cost them.

Nestlé is also developing a more sophisticated “modular” type factory, but one that will cost about a one third of a traditional factory. Depending on complexity, a traditional Nestlé factory can take 15 to 24 months to build and cost approximately. By contrast, Nestlé says it can build a modular factory in less than a year.

The first Nestlé products arrived in South Africa as early as the 1870s, but the company’s presence in the country was formally entrenched in 1916 when it was registered as a company. Local production started in 1927, the same year Nestlé started distributing its products in a second African country, Morocco. From 1957 onward, the company began a process of establishing a presence in virtually every single African country. Starting with the newly independent Ghana. in what is now its Central and West Africa Region (a total of 22 countries), Nestlé then moved into Nigeria and Côte d’Ivoire in 1959, followed by Senegal in 1961 before over time spreading to neighbouring countries.

At the same time, the company was expanding from East Africa across what is today its Equatorial African Region (a total of 21 countries from Kenyan in the east to Angola in the west).

Nestlé has invested approximately US$165m over the past three years in the EAR alone, including upgrading...
Conclusion

African markets present consumer products companies with a significant growth opportunity. Many consumer markets and categories remain substantially underdeveloped, and although competitive intensity is increasing, markets in other rapid growth regions like Asia and Latin America are still generally far more competitive.

However, Africa’s size, diversity and complexity mean that the opportunity is counterbalanced with significant challenges. In this report we have highlighted a set of seven capabilities that our research indicates are essential for effective strategy execution and sustained high performance in Africa. In additions we have highlighted five factors specific to consumer products companies that are critical to longer-term success.

We have no doubt that the risk-reward equation is a very attractive one for those companies that are serious about doing business in Africa over the long term, that are committed to making the right kind of investment to become locally relevant and that are able to get the balance right between the imperatives for growth, profitability and risk management.
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