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Africa

At the tipping point
African financial services come of age

By Noel Gordon, Francis Hintermann and Anton L. Pichler

New Accenture research suggests a promising future for the region's banking sector. But to succeed, newcomers will need to do much more than replicate traditional business models from developed countries.

In 2010, while much of the world was still recovering from the global economic meltdown, the story in Africa was remarkably different. Nigeria's economy grew 7.4 percent, Zambia's grew by 6.6 percent, Angola's by 5.9 percent and Kenya's by better than 4 percent—all on the heels of robust economic expansion through the previous five years.

After decades of sluggish growth, many African economies are expanding on the strength of rising commodity prices, increased trade and higher direct foreign investment. And although political instability, poor infrastructure and often complex governance issues continue to dog much of the continent, a number of countries are making serious efforts to address these problems.

Financial services companies are playing a key role in this transformation, helping to fuel the engines of growth and innovation. In fact, new Accenture research shows that the financial services markets in several African countries are already well established or near the tipping point of rapid growth. Those financial services companies that seize the moment in Africa will establish a lasting competitive advantage in these promising markets.

An African model

Over the past few decades, tales of the challenges of doing business profitably in many African countries have hardened into something like conventional wisdom. But Accenture believes much of this thinking is out of date.

To be sure, some economies will always be too small to attract foreign direct investment of any kind, partly because they lack the potential for building domestic and cross-border scale. Weak market infrastructure requires the development of alternative distribution and payment methods. Governance issues and red tape, coupled with limited institutional development, pose high risks for businesses. And political upheaval, as seen in much of North Africa in recent months, may either accelerate or delay modernization.

Daunting as some of these challenges are, Accenture has identified four important factors underlying growth in the region that will combine to drive a new form of financial market development in many African countries, distinct from that seen in other emerging economies.

"Leapfrogging"

The development of new financial services markets typically requires new infrastructure, tools and processes. In some cases, this is the only viable approach because of the limited legacy in terms of distribution, payments and capital markets.

Take, for instance, the development of consumer payments networks. These systems took years to become fully functional in mature economies. In Africa, by contrast, many countries are rapidly expanding their limited legacy payments infrastructure and adapting it to new international standards. For example, South Africa and Nigeria are rolling out EMV-standard chip card networks to replace fraud-prone magnetic strip cards. While cash still rules in most African economies, the new networks are helping banks to expand their electronic, debit and prepaid card businesses.

Industry convergence

A limited legacy also opens the door for companies in other industries—especially retailers and mobile telecommunications operators, such as MTN, the South Africa-based multinational telecom company—to provide financial services through their networks, boosting revenues from their customer base. Regulators in many countries have accelerated

Making the most of the African opportunity

All companies interested in expanding in Africa—not just those in financial services—face several key decisions on how to approach the market. The diversity and complexity of individual country markets mean that a single pan-African strategy will likely fall short. Instead, organizations should consider a set of four focused actions.

1. Scan the landscape. Create a dedicated Africa task force to identify and understand the relative attractiveness of different markets and sectors, and the specialist skills and competitive advantages the company can bring to those it chooses to enter.

2. Establish beachheads. Take small positions in local institutions as a base from which to seize emerging growth opportunities.

3. Develop local models. Design, build and operate models that reflect, and are focused on meeting, specific local market needs.

4. Build ecosystems. Seek out and establish partnerships, alliances and networks to help develop the local community and to support the chosen strategy going forward.

this trend by granting approval for telecom companies to offer financial services.

Technology and business model innovation

New low-cost, technology-based approaches to service provision and distribution are emerging in Africa. One innovation well suited to African markets is an automated teller machine that uses biometric authentication through fingerprint scans. Biometric ATMs enable customers who cannot read or write to access their funds.

Or take South Africa-based African Bank Investments. The company has created synergies between its African Bank unit and its retail store division. For example, African Bank partners with its Ellerines furniture stores to offer consumer-credit operations. In other organizations, innovative service offerings attuned to local cultures and needs, such as micro-agricultural loans, are also gaining ground.

The development agenda

Multilateral and regional development organizations—including The World Bank, CGAP: Consultative Group to Assist the Poor (an independent policy and research center based in Washington, D.C.) and the African Development Bank—have in recent years launched individual pan-African initiatives to set common regulatory frameworks, processes and standards for financial markets. In addition, the African Development Bank, along with other institutions, has set up the African Guarantee Fund for small and medium-sized enterprises and launched the African Financial Markets Initiative, which is intended to develop stability and transparency in local capital markets.

Private-sector players are participating in the development agenda as well. Netherlands-based Rabobank has used its expertise to help create joint venture partnerships in microfinance and with cooperative lenders in the agricultural sector in several countries throughout sub-Saharan Africa.

Changing landscape

While Africa's growth potential is promising, latecomers may well need to move quickly to take advantage of

the new opportunities in financial services. Rising income levels are putting financial services within reach of many Africans for the first time. But once consumers have access to a particular bank or insurer, the cost to switch is relatively high, so companies that hang back now may find that the early movers have already gained an unassailable lead at a defining moment.

Many African and foreign financial services companies are already staking out positions to take advantage of underserved provided markets.

A wave of mergers and acquisitions in recent years means that soon there will be fewer regional or pan-African companies available to buy.

A wave of mergers and acquisitions in recent years—Barclays' stake in Absa in South Africa, for example, and its purchase of Banque du Caire in Egypt and Nile Bank in Uganda—means that soon there will be fewer regional or pan-African companies available to buy. In addition, many banks are pursuing relationships with telecom providers—such as Equity Bank and Safaricom in Kenya, or Standard Bank and MTN in South Africa—to develop their mobile banking capabilities. Telecom providers typically establish close partnerships with only a few selected banks, so their dance cards could soon be filled.

To provide a standard for benchmarking the maturity and attractiveness of financial markets in Africa, Accenture has developed a Tipping Point Index to rank the financial market readiness of 17 of the continent's largest economies. We compared a range of key factors such as financial infrastructure, consumer financial services and economic development, and used the results to divide the African nations into four distinct groups. The first two groups have exceeded the tipping point of rapid growth; the third group is nearing that tipping point, while the fourth has a long way to go (see chart, page 5).

Established markets are relatively deep and mature, with a diverse and thriving financial sector. They have reasonably large stock and bond markets, a high percentage of bank assets and retail deposits relative to GDP, and a high percentage of people with bank accounts. Only two African markets currently fit this description: South Africa and Mauritius.

Forging ahead economies tend to be fairly large, mid-level-income countries. These economies often have a relatively well-developed institutional framework yet still await critical financial reforms. They have emerging stock and bond markets and fast growth in bank assets relative to GDP, but a lower percentage of people with bank accounts. Their business environment (as measured by such World Bank indicators as the ease of establishing a company and the ability of foreign companies to operate freely) tends to be more difficult than those in established markets. But these countries are undertaking relevant reforms. These economies include Nigeria and Botswana.

Next movers—Namibia, Senegal and Ghana among them—have high potential and are in the process of overcoming entrenched barriers of low income, limited financial access, and institutional or governance deficiencies. They may lack fully developed payment systems and stock and bond markets, or they may have significant barriers in other areas.

Transitional economies are currently constrained by poverty, little or no access to financial services, a low level of banking assets, difficult business and civil environments, a lack of financial infrastructure or all of the above. These economies include Angola, Gabon and Tanzania.

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Tipping Point Index research methodology

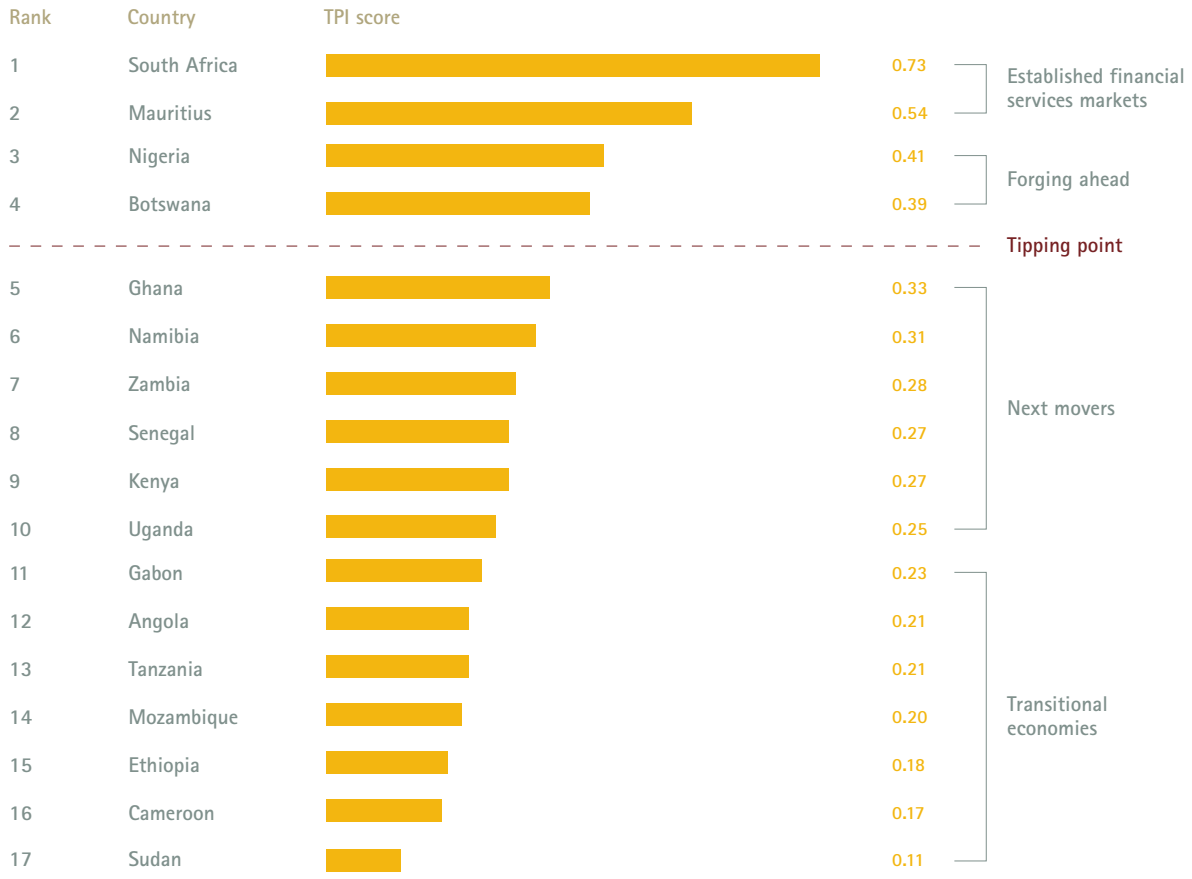
To assess the financial market readiness of 17 leading economies across Africa, Accenture developed the Tipping Point Index to rank those countries in terms of the likely onset of rapid economic growth (something to date achieved by only four countries).

We used a set of 29 variables across three categories: financial infrastructure, consumer financial services and economic development factors. The data came from leading public institutions—including the International Monetary Fund, The World Bank, CGAP: Consultative Group to Assist the Poor, the Bank for International Settlements and the World Economic Forum—as well as from leading research and commercial institutions, including Credit Suisse, Swiss RE, the International Telecommunication Union and Pyramid Research.

Most of the data is year-end 2009. In some cases, the latest available data or cross-references to additional sources have been used, or excluded where no reliable data was available. Once compiled, the data for each variable was compared across the country peer set, with a score of 1.0 assigned to the highest-performing country and 0.0 for the lowest performer; countries between those two were scored according to their relative performance.

The total score for each country was then determined by a simple average across all of the variables. We also examined the performance of countries across the two dimensions of business environment and market attractiveness for financial services entrants. We identified each variable as being primarily associated with either business environment, such as ease of doing business or availability of technology, or market attractiveness, such as percentage of people with access to bank accounts or income per capita.

We then calculated the performance for each country for these two indicators. For market attractiveness, however, we weighted the ranking on the basis of measures that identified the absolute size of the financial services market, because larger economies offer more potential scale return for financial services companies.



Source: Accenture analysis

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There is a considerable gap in terms of the maturity and attractiveness of financial services between the two established markets and the forging ahead economies. The ranking of next movers and transitional economies is, in some cases, affected by a dearth of available data or a lack of market infrastructure like equity capital markets. Note that some of the transitional economies—such as Angola or Mozambique—may have hidden potential that could be released through institutional development.

We further analyzed the TPI findings to produce a Dual Factor Index, which examines the business environment and market attractiveness indicators separately (see chart, page 7). The most attractive country for financial services investment—aside from clear market leader South Africa—was Nigeria.

The growth potential of the African financial services market is both reflected in and increased by the expanding number of active players.

Entry strategies

The growth potential of the African financial services market is both reflected in and increased by the expanding number of active players. A number of European banks have long-established presences in Africa, and the past five years have seen them strengthening their involvement by leading a new wave of investment in sub-Saharan Africa.

In addition to Barclays' majority stake in Absa, Portuguese bank BPI retains a 50.1 percent interest in BFA in Angola (having sold a 49.9 percent interest to Unitel, Angola's leading mobile phone operator) and Credit Suisse took a 40 percent stake in Finance Bank in Zambia.

The European banks' entry strategies were historically based on their home countries' traditional areas of economic and political influence. These institutions have tended to offer corporate banking and retail banking services for foreign companies, major local companies and relatively wealthy local retail consumers.

In recent years, competitors based in emerging markets have disrupted the former dominance of European banks. Some Chinese banks, for instance, have been providing corporate loans and infrastructure financing throughout sub-Saharan Africa, frequently under arrangements with host governments—which often control the natural resources sector—that give Chinese companies access to land and minerals. China also provides both de facto sovereign lending, in the form of the cancellation of government debts, and loans directly from Chinese banks.

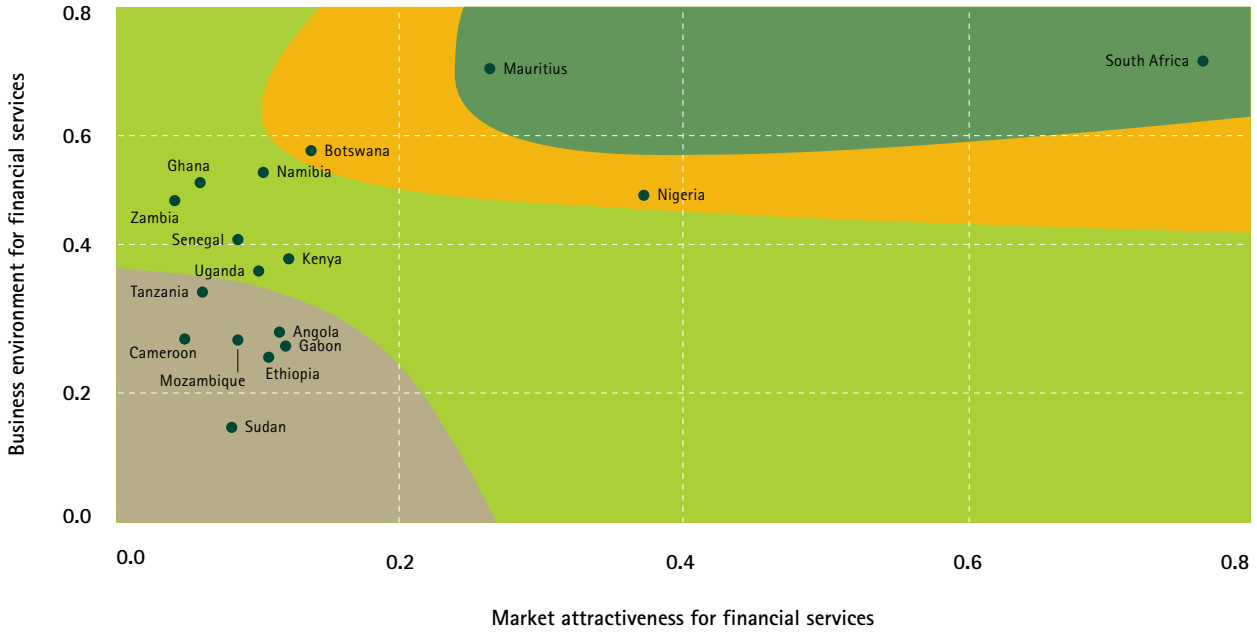
Joint ventures are also becoming common. For example, the Industrial and Commercial Bank of China bought 20 percent of South Africa's Standard Bank and formed a commercial partnership with it for corporate banking services. And Bank of China created a partnership with Togo-based Ecobank, which operates widely across Africa, to facilitate trade and investments between Africa and Asia.

In addition, Brazilian banks have plans to enter Portuguese-speaking countries, such as Angola, Mozambique and Cape Verde, and Indian banks are looking to enter countries in East Africa, such as Kenya, with which they already have significant trade.

To date, intra-African competition has been based largely on traditional regional and business areas of influence. Nigerian banks' expansion from West to East Africa, for example, was effectively halted by the recent domestic and global financial turmoil and the decision to restructure the local market. But the current transformation of the Nigerian financial markets may herald a change in the competitive

The TPI Dual Factor Index: Rating the markets

Accenture used a set of 29 variables to calculate the potential for launching financial services businesses in various African countries. The variables were divided into two categories: "business environment" (which includes factors such as availability of technology) and "market attractiveness" (which includes qualities such as per capita income).



Note: For the variables in the market attractiveness category, we weighted the measures related to the absolute size of the market more heavily since the larger economies offer more potential scale return for financial services companies.
Source: Accenture analysis

dynamics among indigenous African banks across the region (see sidebar, page 8).

Meanwhile, South African banks, such as Standard Bank, are expanding northward across sub-Saharan Africa, establishing a multi-country retail presence and sophisticated corporate and investment banking services. And Moroccan banks are expanding into several countries in West Africa; Attijariwafa Bank, for example, has moved into Mali, Gabon and Congo.

Reaching the unbanked

Whether foreign or indigenous, many banks in Africa traditionally focused their retail banking services on middle- and upper-income customers. In recent years, rising incomes in many African countries, including Botswana, South Africa and Nigeria, have prompted banks to seek to expand their customer base and penetrate large unbanked populations.

The challenge lies in how to serve emerging customer segments efficiently and profitably. In urban areas, large numbers of new customers are relying on branch networks, but in rural areas, the cost of a traditional brick-and-mortar presence is prohibitive. Mobile financial services have become more popular, although many of these offerings remain limited to payments and money storage, with no mobile mechanisms yet available for savings and credit or insurance. To extend coverage in new ways, retail banks are looking to lower the costs of distribution, banking products and operations.

Equity Bank in Kenya, for instance, has built a business model where all three approaches work in concert.

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Nigeria and Uganda: Different growth drivers

A small group of African economies has broken from the pack, notably South Africa and Mauritius (see story). They have relied on a few common growth drivers (strong economic growth, positive demographics and deepening financial markets) while simultaneously addressing the fundamental barriers that have historically hobbled financial services (political instability, poor infrastructure, underdeveloped human capital and a weak business environment).

For other markets—those with the potential to move ahead—new triggers of financial services growth are now emerging, pointing to the rapid development of those markets or business segments. The specific path to growth varies from country to country. Consider the recent experiences of Nigeria and Uganda.

Nigeria: Building on strength

Nigeria is a story of big numbers about to get even bigger. It's one of the largest economies in Africa, with a GDP of $169 billion in 2009, according to the IMF World Economic Outlook, and a GDP per capita (in purchasing power parity) of $2,274. What's more, forecasts call for strong growth across the board.

However, after suffering a banking crisis in 2009, ongoing financial reform is essential to Nigeria's future. The crisis was caused largely by poor risk management, governance problems and speculative lending. Now the Nigerian government and the country's central bank are undertaking fundamental reforms, including repairing bank balance sheets and opening up the market to foreign ownership. Such reforms have made good progress to date, and have refocused banks on supporting the real economy.

Financial services are thinly provided at present, and just 15 percent of adults have access to a bank account. That makes the country an attractive proposition for banks looking to grow their retail franchises. According to Accenture analysis, if the share of adults with a bank account reaches the forecast 20.3 percent by 2015, that would translate to 8 million new customers.

With a median age of 19.2 years (compared with a global average of 28.4 years), Nigeria's population is relatively young, which bodes well for the labor supply. The nation has a long history of urbanization, which helps the economics of branch networks. Another promising indicator: predicted strong growth in income as measured by GDP per capita—a 5.6 percent compound annual growth rate through 2014. And rising incomes mean that more households are moving into the middle class, a key prerequisite for a strong retail banking system (see chart, page 7).

Besides basic retail banking services, business opportunities could also include mobile payments and providing Islamic banking services (half the country's population is Muslim). For financial services companies in Nigeria, the main challenges are achieving operating efficiencies, lowering the cost of service and navigating the country's somewhat difficult business environment.

Uganda: Innovation at scale

Uganda's story is different. It's a relatively small economy, with a 2009 GDP of $15.8 billion (less than a tenth the size of Nigeria's) and a per capita GDP of $1,210. Here, innovative, low-cost solutions will be imperative for success in financial services.

The banking market is small, at $5.3 billion in assets in 2009, although that represented a twofold increase since 2006. Growth has been spurred by rising incomes; a strong economy driven by oil, trade and inward investment; and a regulatory and business environment that has been more stable than those in many neighboring countries (see chart, page 7).

A key challenge for banks on the retail side in Uganda is to find ways of serving large, low-income populations profitably, as many residents live far from existing branches. One solution may be to reach certain customer segments through partners. Banks could, for instance, develop correspondent banking relationships with organizations that already have broad national coverage, such as retailers or the postal service.

Another solution may be to partner with mobile phone providers. Roughly one-third of Uganda's population had access to mobile phones in 2009, while just one-fifth had access to a bank account at a branch. Mobile payment services have a solid footing here, and are provided by a number of operators, including MTN and India-based Bharti Airtel (which acquired Zain Africa in 2010); France Telecom-Orange has announced its intent to enter this market as well. MTN Uganda, the largest player in the market, had roughly 1.5 million MobileMoney users by the end of 2010 and expects to have 3.5 million by 2012. MTN has teamed with its banking partners, Stanbic and United Bank of Africa, to offer MobileMoney, which lets customers send money, buy airtime and make basic utility payments from an MTN mobile phone, and, in turn, gives the company an additional revenue stream for its airtime business.

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Launched in 2004 with a focus on communities and microfinance, this model today underpins one of the most profitable and efficient banks operating in that country.

The bank has three different types of branches to meet different customer needs: a prestige branch that serves more affluent cutomers; a regular branch for the majority of individuals and small businesses; and mobile branches through vans driven to rural communities, typically for one day a week, where a permanent branch is not yet viable. Bank representatives also set up booths in markets and similar locations, where they provide basic financial education. Equity Bank has also partnered in Kenya with Safaricom to provide M-KESHO, a simple savings account service, to existing customers and to those who use the popular M-PESA mobile payment service.

Africa's growth potential is about to be unleashed, and many of the long-term barriers to growth are receding. Financial access and financial services infrastructure are quickly improving for the benefit of foreign entrants that want to be part of the African growth story. With several countries now reaching the tipping point for an acceleration in domestic and international financial services, it's time to take a serious look at Africa for both traditional and innovative business models.

But the window of opportunity is closing rapidly. Decisions that companies make now with regard to Africa will shape their future ability to participate in the continent's rapid expansion over the coming years.

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