

REGIONAL TRENDS IN FDI AND PRI: The Case of the African Trade Insurance Agency



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Compared with the second half of the 1990s, FDI flows into sub-Saharan Africa (SSA) during the first half of this decade have nearly doubled. The increase has been felt primarily in the extractive industries (oil, gas and mining), but also in the service sector, particularly in telecoms, finance and transportation. FDI flows in 2005 reached a record level of US\$15 billion, but then declined to about US\$12 billion in 2006.¹

With oil prices at an all-time high and commodity prices well in excess of historical levels, there are good prospects for SSA to continue attracting FDI into the extractive industries. The region's buoyant growth is also a stimulus to FDI in other sectors. The latest World Investment Prospects predicts that FDI into sub-Saharan Africa will continue on an upward path until the end of this decade. However, in relation to global FDI flows, or even to flows to emerging markets, SSA's standing is low and that is unlikely to change. Furthermore, sub-Saharan countries without significant natural resources or with small domestic markets, lack of infrastructure or skills and generally more difficult business environments are unlikely to be significant beneficiaries of the upward FDI trend.

South Africa has been critical to FDI flows in the region. Large swings in FDI flows to South Africa took place on account of a large merger and acquisition (Barclays' purchase of ABSA) in 2005, followed by net divestments in the subsequent year. In general, FDI into South Africa is more diversified than in other resource-rich countries in Africa. There have been a number of investments in a diverse range of sectors, a recent example being the acquisition of a 20 percent stake in South Africa's Standard Bank Group Ltd. by the Industrial and Commercial Bank of China.²

In addition to South Africa, China, India, and increasingly Middle Eastern Gulf states have made significant investments in SSA in sectors, such as natural resources, infrastructure, and tourism. Companies from Brazil, Malaysia, and Russia are actively investing in the region as well. Interestingly, the United Arab Emirates have invested approximately US\$380 million in Sudan. As for China, its Ministry of Commerce estimates that Chinese direct investment into Africa during 2000-2006 was US\$6.6 billion – with much of the activity coming from the private sector. It is estimated that over 800 state-owned Chinese companies are actively engaged in Africa today.³

Risks Covered by ATI

- Political risk insurance for trade & investment
- Mobile assets insurance
- Unfair calling of bonds insurance
- Inter & intra-regional and domestic whole turnover credit insurance with typical payment terms of up to 12 months
- Comprehensive nonpayment cover for single (structured) credits to:
 - Private obligors;
 - Parastatal obligors; and
 - Sovereign obligors

This article was contributed by the African Trade Insurance Agency.

Perceptions of political risk – one of the principal deterrents identified by World Investment Prospects of an otherwise rosy global FDI scenario – continue to be present in SSA. There are reasons for optimism, however. Although still present, the continent is facing far less incidents of open conflict. In addition, the region is benefiting from economic growth with average GDP growth rate for SSA of 6.1% for 2007. Growth across the region is reducing the perceived threat of transfer restrictions. Additionally, governments are doing more to allay investors' fears by actively courting foreign investor groups and starting to reform in order to create improved business environments. According to the World Bank's Doing Business project, Ghana and Kenya were amongst the top ten reformers globally in 2006/07 and were joined by Mozambique, Burkina Faso, and Mauritius as the top reformers for SSA region alone. In SSA, 52 percent of the countries introduced at least one reform last year to improve their business environment.

South-based investors are responding positively, with China and India in particular at the forefront. While their interest in extractive industries has been capturing the headlines, Chinese and Indian investment in SSA has also gone to apparel, food processing, retail ventures, fisheries and seafood farming, commercial real estate and transport construction, tourism, power plants, and telecommunications. As well Russia has been actively re-engaging in SSA, with rough estimates that the investments of four companies alone - Rusal, Nornikel, Alrosa and Renova - in the region amount to US\$5 billion. Gazprom is also seeking to strike investment deals or partnerships in the region, and already has an agreement with Sonangol (Angola).

Multilateral and private financial institutions are also helping investors mitigate political risks in their investments. In terms of number of guarantees issued, SSA was the top destination for the Multilateral Investment Guarantee Agency of the World Bank Group in FY 2007. The African Trade Insurance Agency (ATI), which in addition to export credit insurance also insures investment projects, has been

reaching out to investor groups across SSA, as well as Europe and Asia.

ATI Perspectives on FDI and PRI Trends

Since ATI's launch in 2001, ATI has received to covered project, trade and investments transactions with contract values in excess of US\$350 million. Investment insurance represents 47% of ATI's overall business and has been issued for projects in a variety of sectors as seen in the following image.

Interest in PRI coverage has come from Europe, South Africa, Mauritius, regional development banks and China with South-South projects comprising 46% of ATI's portfolio. To date, clients have had high levels of interest in Expropriation and War, Civil Disturbance and Terrorism coverage.

Central Africa is becoming an increasingly active part of ATI's portfolio with significant coverage provided for Burundi and Democratic Republic of Congo (DRC). Interest has been primarily in sectors such as telecommunications, infrastructure, and natural resources. For example, ATI is set to provide political risk coverage for a US\$100 million rehabilitation of a copper mine in DRC and has already issued such coverage for a bottling plant, a residential housing project and a cellular technology project in Burundi.

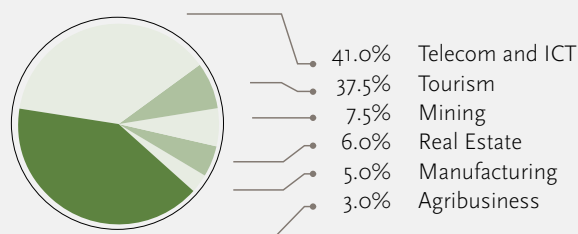
ATI – Widening its capacity and reaching out beyond SSA

ATI works in cooperation with a global network of public and private institutions including the world's second largest ECA, Atradius, several Lloyd's of London syndicates, and the Multilateral Investment Guarantee Agency (MIGA), a member of the World Bank Group. Through these cooperation agreements, ATI has been able to expand its capacity to cover projects by sharing project risks with partner organizations. In fact, ATI has been involved in US\$206.7 million in deals as of November 2006 although the organization allocated only US\$29.9 million to these projects.

In support of growing trade and investment links with Asia, ATI has signed a Memorandum of Understanding with Sinasure, China's Export Credit Agency, with the objective of supporting Chinese FDI into Africa with increased insurance capacity provided by Sinasure.

South-based investors are increasingly active in SSA. ATI has done much to reach out to these groups where PRI is being considered for projects. In particular, India and China but also across the SSA region itself.

Sector Exposure Since Inception



The Benefits of ATI's capital and legal structure

Capital restructuring increases ATI's capacity.

ATI was founded with US\$100 million in seed capital that was granted by the World Bank's International Development Agency (IDA) in form of individual loans to each member country. ATI's underwriting capacity for each country was linked to these country contributions.

ATI is in the process of completing capital restructuring that converts these individual IDA credit contributions into common equity, thus creating one common pool of funds that can be used for projects across member countries. This process will be completed by 31st December 2007. ATI is better able to diversify its portfolio of projects, increase country exposure ceilings, and seek additional capital contributions. At the end of the process, total paid up capital will be over US\$134 million.

Benefits of being a pan-African organization

- Economies of scale that benefit member countries
- Increased portfolio diversification
- Access to reinsurance on international markets
- Status as supra-national organization means not subject to domestic political risk
- Individual country obligations on guarantees without operational oversight

Membership

ATI has been working to expand its membership from its initial 7 founding members and has added 5 African countries to its ranks. Currently, Liberia is in the process of joining and a series of West African countries have expressed growing interest in joining. However, ATI is also looking beyond the boundaries of sub-Saharan Africa to Northern Africa, India, and China as well as potential corporate and multi-lateral entities.

ATI has seen growing interest in African markets and by broadening its

Members

Burundi, DRC, Djibouti, Eritrea, Kenya, Madagascar, Malawi, Rwanda, Sudan, Tanzania, Uganda and Zambia

membership seeks to continue to facilitate investment in Africa by formally expanding its ability to provide coverage for projects in the region, thus broadening its potential investor pool.

Case Studies

Shelter Afrique Transaction

ATI provided coverage for a US\$2 million loan issued by Shelter Afrique, a pan-African habitat and housing organization, for a residential housing project in DRC. This loan was issued to Société Immobilière Khasam (SIMKHA), a private investor who also provided an additional US\$3 million in capital for the project. The funds would be used to construct two residential blocks in the Gombe site in Kinshasa in an attempt to address the demand for residential housing.

One of the effects of the war on DRC has been a significant need for infrastructure and housing development. Kinshasa, in particular, is facing a substantial shortage of housing and considerable growth in the city's population. The Shelter Afrique - SIMKHA project fits in with the overall priorities and plan that Government of DRC has prepared with assistance of UNDP and UN-HABITAT.

Brarudi Transaction

ATI issued a Political Risk Insurance policy to Eastern and Southern African Trade & Development (PTA) Bank to cover a US\$10 million loan which was being extended to Brasseries et Limonaderies du Burundi S.A.R.L (BRARUDI), Burundi's only beer and soft drinks bottling plant. The PTA Bank loan covered the cost of replacement of the first bottling line and related plant, machinery, equipment and services to be supplied by Heineken, a shareholder in the Brarudi. The US\$10

million funding constitutes a Line of Credit to the PTA Bank from KBC Bank NV of Belgium.

This support demonstrates how ATI, can directly support the Burundian economy, by providing the missing link needed to unlock the financing from a financial institution overseas, ATI is creating growth in the Burundian private sector in a sustainable manner. ATI also demonstrated that banks can indeed increase their financial exposure to viable transactions, by mitigating country risks which otherwise prevent the provision of capital by lending institutions for private commercial transactions.

This policy contributed towards an important objective in creating an enabling environment for private sector activities and diversification of the economies of ATI member countries towards manufacturing activities. Brarudi is one of the largest manufacturing firms in Burundi, with its share of taxes representing well in excess of one third of all collected tax revenues in Burundi. It is also among the largest employers in Burundi. With on average 50% of employment in Africa being in the agricultural sector, this diversification is essential throughout the continent.

Footnotes

1. *Economist Intelligence Unit, World Investment Prospects to 2011: Foreign Direct Investment and the Challenge of Political Risk, 2007.*
2. "Foreign investors eye Africa with new enthusiasm," *Reuters, December 14, 2007.*
3. "800 Chinese state-owned enterprises active in Africa, covering every country," *Mining Weekly, September 28, 2007.*