AFRICA RISING

IN SPITE OF CHALLENGES AND RISKS, SUB-SAHARAN AFRICA REPRESENTS CONSIDERABLE OPPORTUNITY FOR MULTINATIONAL COMPANIES. SEMIH OZKAN LOOKS AT THE CASH MANAGEMENT ISSUES

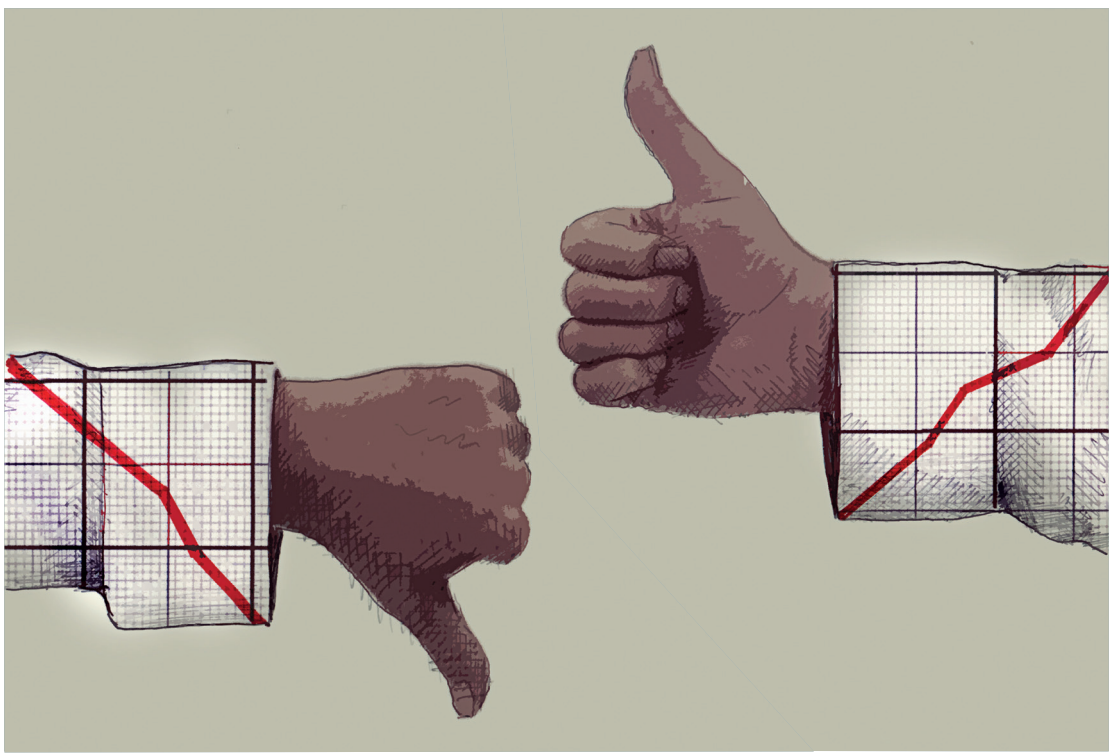
Since 2000, Sub-Saharan African economies have grown with considerable force. According to the International Monetary Fund (IMF), nominal GDP increased from $395bn in 2000 to approximately $1.5 trillion in 2016, with an average growth rate of 5.1%. After successively strong years, the pace of growth slowed considerably, registering just 1.5% in 2016, the slowest performance since 1994. The decrease has been attributed mainly to declining commodity prices and a rebalancing in global demand, particularly in terms of the Chinese economy. Internal structural reforms also slowed.

The fall-off in the rate of growth immediately prompted questions around the whole Africa Rising narrative. However, Africa still leads SWIFT's worldwide commercial payment growth list for 2016, and the IMF expects a recovery in its GDP rate to 2.7% for 2017. There is widespread agreement that the region's growth story is bona fide and that long-term fundamentals remain very strong.

Africa's success is rooted in its growing and rapidly urbanising young populations and its potential to leverage its natural resources in world markets, while also swiftly developing domestic markets. According to consultants McKinsey & Co, the combined opportunities could equate to around $5.6 trillion in household and business-to-business spending by 2025. What is more, thanks to tax incentives, better governance and the improving business environment, some commentators anticipate manufacturing capacity will increase radically.

This outlook means Africa will continue to attract interest and commitment from regional and international companies. However, corporates face wide-ranging challenges, in terms of managing complex and diverse business environments, as well as addressing the pressures of running day-to-day operations within inadequate and fragmented, albeit progressively improving, financial and regulatory frameworks.

Companies from Western Europe, Asia-Pacific, North America and the Middle East are among Africa's direct investors. However, if these corporates are to thrive there, treasurers need to take steps to manage the underlying challenges and risks to implement sufficient controls, transparency and efficiency across their business in the region. That task is not helped by the region's financial and regulatory landscape.



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CASH AND LIQUIDITY MANAGEMENT

Treasurers everywhere aspire to a single point of access for all transaction and information needs across their operations. In Africa, local realities are simply not on their side, mainly because of the region's still-evolving financial and regulatory landscape. Treasurers confront broad challenges in terms of implementing their treasury agenda on a daily basis, challenges that

differ from market to market. An established Africa-aligned cash and liquidity management structure, one that presents sufficient visibility and control over cash flow, is the foundation to doing business in the region.

In terms of local capabilities, transaction accounts are fortunately available in many key regional economies for resident and non-resident companies. These per-country capabilities are the basis for all banking services, including payments, collections and liquidity management. Yet the region is still predominately made up of cash-based economies. Cash payments and collections remain a reality given the population's limited access to formal financial systems. This, of course, poses considerable operational and control risks for treasurers, from collection to security and reconciliation. Happily, electronic banking capabilities are progressively taking hold and are available for treasurers in many key regional economies. That being said, treasurers still need to employ, depending on their underlying business, a variety of cash-based solutions, such as doorstep banking and cash-in-transit arrangements, to facilitate cash-based transactions and to manage associated risks and embedded costs.

Unless a cash-based transaction is necessary, payments can also be made electronically via a range of secure data-transfer channels, including telegraphic, domestic electronic fund transfers and real-time gross settlements. However, international payments, at least in many key regional economies, are still subject to exchange controls and central bank reporting requirements. Likely driven by this fact, the region has the highest domestic versus cross-border commercial payments ratio in the world, according to SWIFT.

Collections can also be made electronically, albeit in a limited way, through electronic receipts or direct debits in many countries. Payment and collection capabilities have been steadily growing in sophistication in recent years. More advanced channel solutions, such as Host-to-Host and even SWIFT for Corporates arrangements, have been implemented by a number of companies in the region to connect to banks through single, secure and standard channels. In this context, the region, particularly Kenya and Nigeria, is leading the world in terms of mobile money developments. While the majority of transactions are still retail in nature today, corporate-related solutions are already on the way.

Liquidity management is another far-from-straightforward issue, in view of various exchange controls and regulations. According to PwC's recent survey, *The Africa Business Agenda 2017*, transfer pricing and withholding tax are ranked very high on regional executives' agenda, followed by consumption taxes, corporate tax, and customs and excise. There are tailor-made solutions available locally for treasurers to optimise liquidity by netting balances, pooling or sweeping them physically or notionally. That being said, the region's notoriously fragmented regulations can rule out the prospect of sufficient visibility and cash-flow control gains. Consequently, discussion around regional treasury centres, along with shared service centres, are moving up the treasury strategy agenda.

Until recently, companies have largely operated decentralised treasury models. However, their increasing scope of activities has been prompting treasurers to move towards centralised models, focusing activities into locations such as South Africa, Mauritius and even Dubai, all of which serve as suitable locations for the region. To determine the location for a centre, treasurers need to take into account regulatory issues, the efficiency of legal frameworks, tax and double-tax treaties, financial markets and products, human resources and infrastructure. A high level of comparison among these locations based on the key evaluation factors cited above would give treasurers an idea about each location's particular pros and cons. However, the final decision depends on each company's unique needs, driven by their scope, experience and strategy in the region.

Africa will continue to attract interest and commitment from regional and international companies

RISKS

Without a doubt, doing business in the region is challenging and risky, since there are notoriously tangled commercial, financial and regulatory constraints. While the region as a whole has made noticeable progress regarding the financial and regulatory landscape, including regionalisation efforts, to facilitate swift inbound and outbound flows, many key regional economies still demand extensive documentary requirements. In this regard, over-regulation is a serious concern for treasurers, since it potentially causes trapped-cash situations, which can increase underlying FX exposures.

OPERATING IN AFRICA – RISKS AND OPPORTUNITIES

- FX risk is a major concern. Africa has 50-plus currencies and a myriad of related exchange controls.
- Many key economies are experiencing liquidity shortages, particularly the US dollar for spot conversion.
- Conversely, local FX markets may represent an opportunity for bringing offshore non-deliverable forwards into play.
- Funding remains a key challenge, with longer cash-conversion cycles bringing additional costs. Local currency borrowing is an option in some markets. Meanwhile, the drive to centralise operations is accelerating.
- Treasurers continue to tap local banks for overdrafts, import and export finance, and asset-based finance. Supply chain finance is also gaining ground.

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