

# OEG *Findings*

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## Successful Investments in Sub-Saharan Africa

Over the past three decades, IFC has invested over \$2 billion in more than 300 enterprises in sub-Saharan Africa. Although its experience with mineral projects and credit lines has been good, many of its investments in Africa have yielded disappointing results. Other multilateral and bilateral agencies and private institutional investors have had a similar experience. Nevertheless, IFC and others have had some successes. In a recent review that focused on 10 enterprises that yielded financial and economic returns of at least 10 percent in real terms, IFC's independent Operations Evaluation Group (OEG) sought to identify the factors distinguishing this sample from the less successful ventures. The study examined where the investments were made, who the sponsors and managers were, the characteristics of the businesses, the strategies adopted, and IFC's own role.

### Countries

Although some of the successful investments were in extremely difficult countries, most were in countries with relatively benign enabling environments. Countries with unrealistic exchange rates, overdue needs for structural adjustments, major infrastructural inadequacies, and important governmental impediments to success provided few opportunities (other than mineral-based enclave projects) for investments capable of yielding satisfactory financial and economic returns.

The successful ventures, however, were not entirely free from country problems, and some suffered from extremely unfavorable conditions. These ventures were, nonetheless, able to prosper—essentially because of the inherent robustness of the underlying business and because of committed sponsors and managers who identified problems at an early stage and sought aggressively to cope with them. (See Box 1.)

**Box 1.** One successful company was extraordinarily resourceful in dealing with severe foreign exchange shortages. Before the foreign exchange constraints became too severe, the venture built up its raw materials inventories to cover two years' requirements. It integrated backward to produce its principal raw material. It helped others develop production of local raw materials as substitutes—albeit imperfect—for imports. And it made arrangements to recycle materials contained in its products.

Other companies dealt with infrastructural inadequacies by installing standby generating capacity, drilling their own bore holes for water, setting up their own telecommunications facilities, developing their own transport systems by road, river, or air, and even assuming responsibility for road maintenance. In one case, because of recognizing that a crucial bridge was in danger of collapsing, a company stationed equipment at the bridge to transfer freight to lighter vehicles.

These ventures also recognized the importance of good government relations and attempted to foster them by showing they could operate efficiently; providing attractive working conditions, good training, and opportunities for local staff to advance; sharing in local concerns, including protecting the environment; and earning a reputation for being straightforward and operating within the host country's laws. Building the necessary understanding and confidence took time but ultimately paid off. (See Box 2.)

**Box 2.** When government interference with prices became unbearable, two ventures threatened to curtail their operations. These threats were effective for three reasons. First, the threats were credible. The sponsors were truly willing to walk away from their investments. Second, the host governments were capable of meeting the companies' demands and would have been subject to intense pressure if the companies actually closed down. Third, the companies had earned some degree of trust and understanding from the local authorities before making the threats.

In contrast, soon after it went into operation, another company started threatening to close if illicit imports were not curbed. The foreign partner was new to the country, did not adequately understand the political context, and had not developed a relationship of trust and confidence with the government. The government would have found it difficult to curb illicit imports, may not have considered the threats to be credible, and may have considered that the pressure resulting from a shutdown would be manageable. The government did not accede to the threats, the foreign partner was forced to sell its shares and give up management, and the venture has never performed satisfactorily.

### Sponsors and Management

The study identified three characteristics of the sponsors and managers of the successful enterprises. First, these sponsors and managers, whether local or foreign, were committed to the long-term success of their African ventures. Rather than merely complaining about the host government and local staff and assuming that efforts on their own part would be futile, the sponsors and managers of the successful ventures have had confidence in the prospects of dealing effectively with local problems and in the possibility of achieving high productivity, high quality, and competitive costs. They have demonstrated perseverance in striving to overcome problems and achieve these goals, for example, through developing new raw materials sources, introducing new products, and making technological improvements and innovations. Finally, they have had a positive attitude toward the potential of their local staff, have been willing to devote substantial resources to training them, and have assigned them important responsibilities.

Second, the sponsors and managers of the successful ventures showed great agility in adapting to emerging problems and opportunities. These ventures typically had one predominant shareholder who had clear responsibility for management. When changes of direction were needed, decisions could be taken without lengthy debate and executed without delay. They also had an effective forum for reflecting on emerging problems and opportunities and deciding how to deal with them, delegated responsibilities well, and developed a trained, experienced work force.

Third, the managers of most of the successful ventures were very much aware of current management thinking and practices in developed countries and had adopted many of these practices in their African operations. These managers were not in a backwater but rather kept up to date on what was happening worldwide and applied new ideas in running their companies. (See Box 3.)

**Box 3.** The differences between successful and unsuccessful companies are highlighted by the comments of the chief executives of one of the study's successful ventures and one of the unsuccessful ventures visited for the study. The chief executive of the unsuccessful company lauded his local workers for being well-disciplined, and he justified the high number of expatriate managers by saying that Africans were unwilling to take orders from other Africans. The successful company's chief executive considered rather that success depended on collaboration, encouraging workers to solve problems, and mobilizing staff energies based on the provision of information and encouragement. He considered that expatriates were generally not well adapted to dealing with local people and problems.

These views did not stop him from using some expatriate managers. Indeed, virtually all the successful companies did so. Given the limited availability of experienced managers and engineers, few large ventures can do without some expatriates, at least at the outset. Moreover, drawing on expatriates can contribute to technology transfer and more rapid development in most countries, even in the developed world. Although the successful ventures generally used some expatriates, they also took a longer term view to the development of enterprises that would prosper and grow on a sustainable basis and, to that end, were willing to devote the resources needed to train and promote local staff.

### **Characteristics of Businesses**

The successful ventures all benefited from structural competitive advantages-exceptionally strong business intrinsics that allowed them to succeed despite country problems.

The export-oriented enterprises had access to local raw materials that were relatively inexpensive, had special characteristics (for example, taste or texture) permitting sales in niche markets, or both. Some of these enterprises had taken the initiative to develop the supply of local materials, for example, by providing technical assistance or by helping establish cooperatives. Some created a competitive edge because of their ability to add greater value to the raw materials, based on their location, their production facilities, or their efficient collection, processing, or marketing operations.

The ventures selling mainly in their domestic markets did not rely on high import duties or quantitative restrictions, which are notoriously difficult to enforce. Rather, they were able to compete with imports due to natural protection arising from high transport costs, the high costs associated with smuggling, the importance of speed and service, perishability, or brand names. Moreover, these enterprises were sheltered from excessive domestic competition because the markets were too small for more than one supplier or because of patents, proprietary technology, or brand names.

Aside from these ventures, one city hotel was successful because local conditions discouraged construction of additional capacity, and a leasing company was successful because of the inherent advantages of leasing in many developing countries. Other types of successful businesses could presumably have been identified by a more extensive study.

### **Successful Strategies**

Although structural competitive advantages may create opportunities, they must be complemented by appropriate strategies if they are to lead to success. Indeed, in advanced economies today, competitive advantages are created more often by selecting and carrying out the right strategies than by natural conditions. These created competitive advantages may be less common in Africa and other countries in the developing world, but they are not absent. Competitive advantages based, at least in part, on appropriate strategies have played a significant role in the success of the ventures reviewed for this study.

Businesses can seek competitive advantages by supplying the market at lower cost or by differentiating their products, services, or both from those offered by competitors. Manufacturing costs in Africa are generally high. Indeed, this review found that IFC's investments in ventures that have had to compete principally on the basis of price failed to generate returns of 10 percent or higher in real terms.

Rather than competing on the basis of low costs, the successful ventures pursued differentiation strategies. All the successful ventures put great emphasis on high quality. The export-oriented ventures took advantage of the natural qualities inherent in their raw materials but also devoted special care to processing to derive



maximum benefits from these natural qualities. Two food processors sought to meet European hygiene standards on a consistent basis and to supply products that could be marketed in countries willing to pay extra for high quality. One made major changes in its production process to maximize the yield of premium products. Another food processor packaged its produce by hand to give an attractive appearance and, thus, permit premium prices.

The successful enterprises selling in domestic markets also emphasized quality. One produced a higher quality product by using a more modern process than its competitor. Some others stressed fashion. Some based their strategy on identifying quality with brand names.

In contrast, many of the unsuccessful ventures believed that they could get by with low-quality goods because local consumers would have to buy whatever they supplied. When recessions led to domestic market contraction, these firms sought to export but could not realize satisfactory prices due to their poor quality. In one case, failure to take adequate measures to avoid bacterial contamination ruined a company's reputation in its home market and put in doubt its ability to survive.

Several of the successful enterprises, particularly export-oriented enterprises, emphasized speedy and reliable deliveries. They were aware that African producers had a poor reputation in these respects and went to great lengths to show customers that they were reliable. For example, one exporter invested in work-in-process inventories that could be quickly processed to customer specifications and then shipped to Europe by air. It was thus often able to deliver finished products more quickly than its European competitors. This venture and others devoted special attention to securing timely export clearances to avoid delays.

Other successful enterprises gave importance to different forms of service. One packaging materials venture, for example, gave substantial assistance to potential clients. One exporter developed the capacity to tailor product size or packaging to the requirements of individual clients.

### **IFC's Role**

IFC's role in the successful investments has very much depended on the needs of the ventures. In some, it has done little more than provide necessary financing and financial advice. In others, it has made crucial contributions going well beyond its financial roles. Indeed, without IFC, many of the projects would not have gone ahead, and several might not have succeeded.

IFC cannot ensure success by playing an active role. But success will, in many instances, depend on IFC's providing extensive help, advice, and guidance throughout the period when it is associated with a venture. If IFC is to contribute to development in Africa, it will have to devote substantial staff time to structuring and supervising relatively small investments, even if it does not recover the full costs of these efforts.