

A TRIP TO ETHIOPIA



Recently, the PAPE Fund Managers team visited Addis Ababa to undertake a due diligence appraisal on a South African company into which it is considering a capital investment, and which is viewing Ethiopia as a territory of substantive growth. Our arrival in Addis Ababa was relatively stress free (compared to a similar experience the same week in Lagos, Nigeria) and we were checked into the Ramada Hotel in the city centre. As the capital of Africa's second most populous country Addis Ababa provides a useful contrast to the general chaos of central Lagos: in Addis, traffic in the main streets is orderly and respectful of pedestrian crossings and traffic lights. Members of the team all felt very secure driving and walking around the city, and visiting the less-formal parts of the economy provided some colourful adventure.

The combination of strong Arabic and African influences across culture and demographics has resulted in a very interesting society, as reflected in their quiet demeanour, food and drink and even the Aramaic calendar to which the country still adheres. The PAPE Fund Managers team found the visit to Addis Ababa to be very interesting, stimulating and thought provoking, particularly in the context of a private equity investor's perspective and we learned much about the country's growth prospects as an investment destination. To this end the following extracts are sourced from Ethiopia Business News,[an online publication] Ethiopia is considered to be Africa's star performer, with its industry continuing to improve in line with the country's economic expansion. For more than a decade the country has boasted the world's fastest growing economy, driven by a reform-minded government. With a population of over 107 million, it is definitely a market to target.

Ethiopia's economy is projected to grow by at-least 7-9% in 2020. Ethiopia is also Africa's oldest independent country and its fastest growing economy today. With a large population and an average annual economic growth rate of 10% over the past 15 years, it represents unique opportunities Ethiopia's location gives it strategic dominance as a jumping off point in the Horn of Africa, close to the Middle East and Europe markets. This rapid economic growth, a conducive investment climate, large consumer market size and high-level government commitment towards FDI attraction have contributed to making the country the second largest recipient of FDI in Africa. East Africa, the fastest-growing region in Africa, received \$7.6 billion in FDI, of which Ethiopia absorbed nearly half and is now the second largest recipient of FDI in Africa after Egypt. Key attributes include:

Strategic location between Europe and Asia

In addition to its strategic positioning as a long-haul transfer hub, Ethiopia is increasingly becoming an important destination for manufacturing, especially in the ready-made garment sector. With the success of multiple business models, suppliers are pressurised to reduce the turnaround time between design and final delivery. One of the easiest ways to achieve this is to stay closer to the brands. However, most big brands don't currently have interesting alternatives closer to their regions, heavily relying on Asian countries for cost reasons. Bangladesh's manufacturing sector is increasingly gravitating towards Ethiopia to maintain its low-cost advantage and, additionally, stay closer to key brands in Europe. With a strategic location and low-cost labour, Ethiopia is uniquely positioned to succeed in the manufacturing space.



Images taken by PAPE Team during their trip

Privatization of State-owned enterprises

Ethiopia is one of the world's largest untapped markets, and there is an increasing belief that privatization of state-owned enterprises could be one of the ways to attract potential investments and spur the economy. There are plans to offer minority stakes in airlines, power and telecoms to global investors. The possibility of railway projects, hotels and key manufacturing industries have already created enough interest to boost investor confidence and in turn, the possibility of attracting investments. The government has also created five industrial parks that have spurred the creation of 45,000 jobs, with the aim to set up a total of 30 and increase their manufacturing from 5% to 20% of GDP.

Greater social stability

Ethiopia is historically recognized as a volatile country in sub-Saharan Africa. However it has been increasingly turning toward openness and democratic processes. Ethiopia has received new political and financial support from a number of parties, including the European Union, the World Bank and the IMF. The new policies were also well received by the Ethiopian diaspora, a big contributor to the economy through remittances. The steps taken towards national security and political reconciliation - such as lifting of the state of emergency, releasing political prisoners, and reforming tough laws on anti-terrorism, media and civil society - are considered positive by international observers. The country's large infrastructure investments are beginning to bear fruit and the provision of public services such as education and health has increased dramatically.

Youthful potential

More than 70% of citizens in Ethiopia are under 30, and nearly 50% are under 15. In 2017, a World Bank report found that enrolment in higher education had multiplied fivefold since 2005, with the number of public institutions increasing from

eight to 36 over that period. In a world where service industries account for 65% of global GDP, these are the type of education policies that seem adapted to the new global context. Technology and knowledge-based industries have the potential to thrive, due mainly to the cost advantages and the availability of human capital in Ethiopia. Human capital is fast becoming a key economy-boosting asset.

Promising start-up ecosystem

Local challenges around mobility, agriculture, infrastructure and healthcare for a country of Ethiopia's size are being turned into a series of opportunities by the start-up movement. Sustaining a strong Ethiopian economy requires the existence of a local start-up ecosystem. The government is focusing on an environment where entities such as universities, large companies, service providers, research and funding organizations come together to allow local entrepreneurs to get off the ground and to scale up. Investors are optimistic as the government plans to unlock two of the most heavily regulated sectors - banking and telecoms.

Key economic factors in Ethiopia's growth story

Ethiopia's growth is expected to stay high in the future, supported by continued economic recovery and export-import expansion as new manufacturing facilities and infrastructure come online. Ethiopia is ranked 57th (which is higher than its regional peers i.e. Kenya, Rwanda and South Africa) for its conducive macroeconomic environment (World Economic Forum, Global Competitiveness Report). Growth forecasts of more than 7% from the International Monetary Fund and the African Development Bank place Ethiopia among the world's growth leaders over the medium term.

Ethiopia is a member of the Multilateral Investment Guarantee Agency (MIGA), a World Bank affiliate which issues guarantee against non-commercial risks in signatory countries and of the World Intellectual Property Organization (WIPO).

Ethiopia has concluded over 30 bilateral investment promotion and protection agreements, of which 11 are with individual European Union Member States. Significant other partners include China, India, South Africa, and Russia, and a number of regional economic partners (Israel, Egypt, and Sudan, among others).

Addis Ababa has emerged as a regional hub and is home to key international organizations such as the African Union (AU) and the United Nations Economic Commission for Africa. Addis Ababa is also the main air hub for Africa and the home of Ethiopian Airlines, which has won repeated recognition as the best airline in Africa. Ethiopian Airlines offers flights to 101 international passenger destinations (57 in Africa, 20 in Europe and America and 23 in the Middle East and Asia), 22 domestic passenger destinations, and 35 cargo destinations (21 in Africa, 11 in the Gulf, Middle East and Asia, and 3 in Europe). It carries two thirds of Africa's air freight. Expanding road networks are connecting national and regional markets and the country offers the cheapest electricity rate in Africa and the whole world. Government is rapidly expanding and improving the country's telecommunication service. Power production has increased steadily over the last ten years, with 99% of energy being sourced from clean energy in the form of hydropower.

Ethiopia offers a comprehensive set of incentives, particularly for priority sectors such as customs duty payment exemption on capital goods and construction materials, and on spare parts whose value is not greater than 15% of the imported capital goods' total value. The fiscus offers tax exemption of up to 6 years for manufacturing and agro-processing, and of up to 9 years for agricultural investment. Additional it offers 2-4 years income tax exemption for exporting investors located within designated industrial parks and 10-15 years exemption for industrial park developers.

The PAPE Fund Managers team departed the country via the very impressive new Addis Ababa Bole International Airport and flew Ethiopian Airlines to Johannesburg. The impression we had gained from this visit was a country in a hurry to grow its economy and serve the needs of its 107 million citizens. It certainly is an African economy that cannot be ignored by fund managers and investors, and we intend keeping a close watch on developments there. The government has declared August 16th 2020 as the date of national elections and it is widely believed that these should be free and fair.

