

Presentation by Mr. Patrick Helson*

Thank you Mr. Chairman,

Good morning everybody. I am delighted to be here to represent CDC Capital Partners. I will try to be brief.

I will tell you a bit about who we are. I am going to say something about what I think are the winning attributes of the investments that we like to make in Africa, and then I am going to give you three examples from CDC's experience, from which I think that we can draw some helpful lessons.

I wanted to share with you our mission statement, because I think that it has much in common with those of the IPAs that are represented here today. I think we share the same goal, which is to mobilize investments to benefit poorer countries by growing sustainable local businesses. That is what CDC is all about. CDC started life 50 years ago as a government institution, and has been migrating over the last six years to the private sector. I believe that the introduction of private sector disciplines and skills to our mission can only help this task of mobilizing capital because the whole game at the end of the day is about aligning the interests of everybody, all the stakeholders involved in bringing capital into Africa and the only way you can do that, I believe, is by giving everybody a financial incentive to mobilize this capital.

Table 1 presents some of our highlights in 2003: We have invested US\$ 180 million of government money in Africa directly. We have also raised US\$ 77 million of third party money.

Table 1. 2003 highlights

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| <ul style="list-style-type: none">• US\$ 180 million of UK Government money invested directly;• US\$ 77 million of third party funds raised;• US\$ 43 million of equity co-investments made by third parties;• US\$ 58 million of new capital introduced when CDC made an exit;• US\$ 217 million of new third party loan facilities for CDC portfolio companies; and• Successful exits made from a Tanzanian gold mine with an internal rate of return (IRR) of 33%, a Zimbabwe manufacturing company with a 21% IRR, and a Ghanaian bank with a 17% IRR. |
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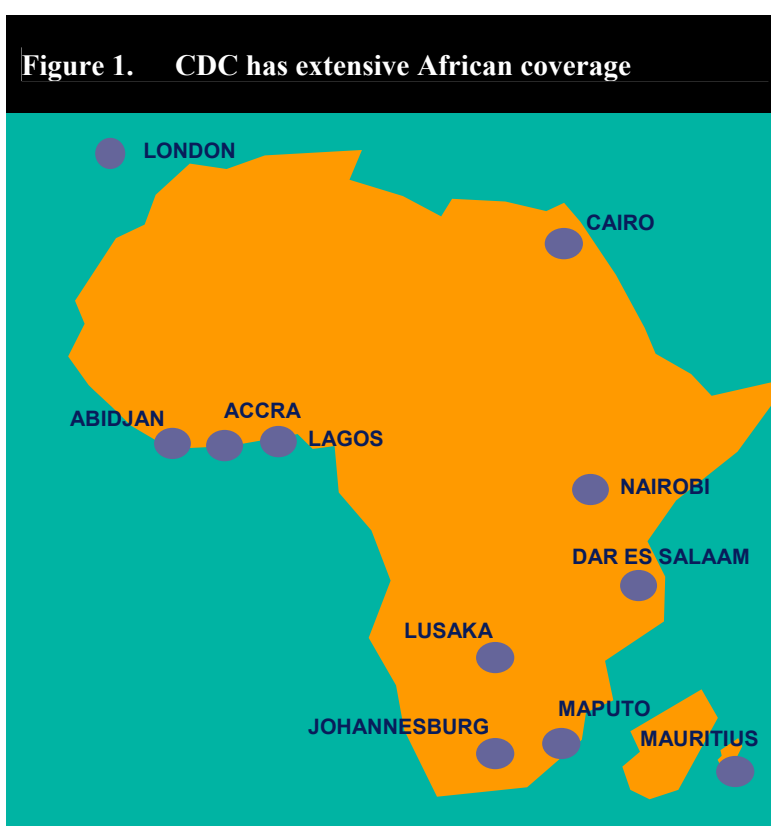
I want to point out that Africa is not short of capital. There is capital queuing up at the borders of the continent, waiting to invest, and our job and the job of many of you as well, is how do we persuade that capital to come into Africa? Let us flag that Africa can also be a very successful place to invest. CDC has made three successful exits this year, from a Tanzanian gold mine, where we made a 33 per cent return for our investors; a manufacturing company in Zimbabwe, where we made a 21 per cent return; and finally, a Ghanaian bank, where we made a 17 per cent return. Who would have thought that you can make a 21 per cent return in Zimbabwe in its current state, but we did. Moreover, these are US-dollar returns, not local currency returns.

We have seven offices of our own, as well as a link with a joint venture that focuses on the SME sector called ORIOS, of which CDC owns 50 per cent. The combined offices of CDC and ORIOS are shown in Figure 1. We are all over Africa. We have been there for 50 years. We believe that it is part of our skill, part of our unique value added, that we have close, on-the-ground relationships in many African countries.

* Chief Operating Officer of CDC Capital Partners Africa Region. This text is based on an edited transcript of the spoken presentation.

Our current portfolio amounts to US\$ 400 million, which includes investments of US\$ 120 million in the power sector in Africa this year.

In terms of the funds that we manage, we have US\$ 350 million to invest in the next three years. The capital is there if you can bring us investment proposals with the right kind of attributes. We receive an awful lot of investment proposals from Africa – thousands a year. Mostly they do not have the attributes that we are looking for. The things that we are interested in are expansion or change-of-control finance, rather than start-up finance. Obviously many of you will be thinking that so many of the opportunities in Africa will be in start-ups, but start-ups are extremely risky, even in the most developed markets. In England, if you put money into a start-up, you have got a 70 per cent chance that you will lose all your money. In Africa, where you have the compounded risks of political risk and government risk, you are not going to get foreign investors putting money into start-ups because it is simply too risky.



The second thing that we look for is experienced management. Again, Africa gets accused of lacking an experienced management depth. I disagree with that. We have many investments with many absolutely world class African managers who are very skilful at earning much higher returns than foreigners working in those markets. Of course, it is certainly true that you often have opportunities in Africa where the management is inexperienced. This is not necessarily a bad thing because it gives you an opportunity for a joint venture, which people have referred to already, where you can have a foreign company come in and bring you the international management skills and links to markets that can make the African company thrive.

We look for a track record of success. We usually get presented with companies that have a history of making losses. Again, if you invest in a loss-making company, you actually have a 90 per cent

chance of losing your money. But there are plenty of businesses out there with profitability that we could be backing and growing.

Out of a thousand prospects that get brought to our door, I would say that less than ten have attached simple projections of what this company could do if we put our money into it. We need a profit and loss calculation; a cash flow is crucial, and a balance sheet for, say, three years or five years rolling forward. We do not need a 50-page business plan very impressively produced at great expense that does not actually tell you if this investment will generate cash. That is what people are interested in.

And finally, limited currency risk is required because in the African environment many economies suffer from currency volatility. In the last two years, our investments have gone through a helter-skelter of evaluation because of what has happened to the round of devaluing and then appreciating and then devaluing again. I am hoping that those of you that work for IPAs will explain how we judge these things when you get business plans put across your desk: Which proposals we would take forward and which ones we would not.

Let me tell you some specifics about three CDC investments.

MSI is an investment we have made for currently US\$ 46 million outstanding across Africa. It is a Pan-African mobile telephone company. It is a fantastic business. It operates in twelve different countries and it is full of lessons for investors into Africa. The main lesson for me from MSI – which was very frustrating for MSI, but of great relevance to the kind of IPA and investor audience at this Round Table – was that they found it difficult to connect the thinking between different government departments, particularly regarding taxes. We often see short-term pressure from the tax authorities to collect tax revenues that can be at the expense of a more beneficial longer term strategy. Let me give you an example of what I mean. In MSI's case, one of the things that MSI has to do is to take phone calls from the government-owned telephone system and the government has to pay a fee for that. So when people ring from a government line onto a mobile line, there is what is called an inter-connect fee that has to be paid across to MSI. The governments in certain countries owe MSI a lot of money for these fees and do not have the cash to pay those fees. So, with a bit of lateral thinking in some countries, the government departments have agreed to apply the money owed from the government against the tax owed by MSI for the profits it has made. This is extremely helpful for MSI's investor and it means that the government has also settled that liability. That would be my main point.

MSI found it very valuable if the IPA is a one-stop shop. Otherwise, whose door do we knock on to take this issue to the government? To whom do we say that we would like to set off taxes owed against the inter-connect fees owed? In some countries, it is very difficult because the IPA is not a one-stop shop and you do not know who to talk to and there are many doors to knock on. My lesson learned from this is that you should make the investment promotion authority a true one-stop shop, which means that it has to be empowered and have the full authority of the President, and in return there should be a direct reporting line. I think that this can make your work much more effective.

Investors love transparency and clarity. MSI needs to set up lots of stations to put telecoms masts all over Africa, but if there is confusion over land registration and land ownership and tenure, it slows down the roll-out of these telephone systems.

These masts are in remote areas and can be vandalized. We all know it. So we need to provide physical security over assets like that. You will hear different views on incentives and whether it is good for you to offer incentives. In MSI's case, or in any major infrastructural investment, my argument would be that it can be very helpful to have some tax incentives to help the cash flow when you are setting up in a new country. If you have to go in and put in enormous capital investment and you are taxed fully straight away, then your cash flow is very tight indeed.

Publicize your successes. MSI featured in an article in the *Financial Times* last week. This is fantastic publicity for Africa, and we need to get across the fact that there is plenty of money to be made in Africa, and that it can be a very successful investment destination. This sort of *Financial Times* article, which was written by a journalist about the company, is very effective. What is not effective is a kind of centre spread in *The Economist* paid for by the government investment promotion authority saying why should you bring your money to this country. You want to let your success stories speak for themselves because the more you can remove the sense of government from around the investment process, the happier investors will be to bring their money.

The privatization of a road in South Africa has been very successful for us. I will only pick out one of these points, the most controversial one. When you are deciding which assets to put up for privatization first, many countries make the mistake of putting up their second tier, the lower quality assets, because the government wishes to hang on to the top quality assets. You have got to start marketing your respective countries because you are competing for all this capital. You have got to start acting like you are marketing a product that you are selling in a shop, and if you want to be a successful shopkeeper, you do not sell second-rate assets, you sell your best assets. Even if it means that you might make a bit of a loss first, you should not be worried by that because if you can have one great privatization, it will attract the attention of the world's investment community and they will say, that is a fantastic country to do business with, what else can we do there? Sell some of your top assets first; treat it as a loss leader. You will get in more business later. It will do you good.

If the tone of what I say sounds like this is what Africa should do all the time, I must apologize for that. I am also conscious that if I apply many of these rules to how Britain sells itself, we fall short as well, so these are meant to be lessons actually for everyone to learn. I am just applying them to the African context because that is what we are talking about today.

East Africa Gold Mines in Tanzania is my final example. They were a hugely successful investment for us with a return of 33 per cent in hard currency. It is a wonderful example of where you should be plugging the gap in terms of market failure and where you should be letting the private sector do its own thing. What happened around East Africa Gold Mines was that the Tanzanian Government used commercial industrial specialists to design or revise their Mining Act in 1990 and they made it extremely commercial and extremely world competitive. It guaranteed security of tenure for the mines that were operating different sites. It guaranteed that if any minerals were found the companies could exploit those minerals. This is a very strong legal environment that attracted lots of interest. Tax incentives were given, there were no duties paid on new equipment needed for these mines, foreign exchange was liberalized, foreign currency bank accounts were allowed, and people could service their foreign currency debt. The Government did not seek ownership or control. They only took a royalty, which was very important. They were happy to step to one side but they aligned their interest to the success of this business by accepting a royalty payment.

The public sector's role in this, and the role of IPA, the World Bank and the UNDP, was that they gave the market and the specialists lots of market data about the quality of Tanzania's mineral wealth, all sorts of surveys. And that was a fantastic plugging of market failure because that really interested the investors and made them come into Tanzania. If you want to know something about the results: In 1996, there was US\$ 80 million of expenditure in the mining sector in Tanzania, in 2002 it was US\$ 400 million. Tanzania now has five modern gold mines, world class, worth over US\$ 600 million. I think that it speaks for itself.

Thank you very much.