ECONOMIC REPORT ON AFRICA 2020

INNOVATIVE FINANCE FOR PRIVATE SECTOR DEVELOPMENT IN AFRICA

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CHAPTER 1: RECENT ECONOMIC AND SOCIAL DEVELOPMENTS IN AFRICA

RECENT NUMBERS:

- Africa is the second fastest growing region in the world, estimated to have grown 3.4% in 2019
- COVID-19 pandemic will impact growth to decelerate to between 1.8% and -4.1% in 2020
- Growth in Africa is projected to rebound to 5% in 2021, supported by the effective implementation of COVID-19 response measures and global economic recovery.
- Refer to Figure 1.1 for data on Global Economic Growth.

COVID-19: Africa depends on imported medicinal and pharmaceutical products. In 2020, spending on health will increase as governments set aside funds to sustain their health systems and absorb costs related to the COVID-19 lockdowns. In a best-case scenario, $44 billion would be required across Africa for testing, personal protective equipment and treatment of COVID-19 patients requiring hospitalization and intensive care treatment (p.20). Due to the resources being redirected to COVID-19, Africa's existing health challenges will face spillover costs, as happened in the Ebola crisis. Thus, non-COVID-19 health issues should be kept in view (p.4).

The impact of the pandemic will push between 5 million and 29 million people below the extreme poverty line of $1.90 per day, compared with a baseline 2020 African growth scenario, according to ECA projections (p.11).

Moreover, reduced demand due to COVID-19 has depressed the prices of agricultural commodities such as coffee, tea and cocoa, which is expected to affect vulnerable small-scale farmers in Africa (p.11).

INVESTMENT: Investment is key to build infrastructure and foster innovation. Despite Africa's growth, many economies remain unsophisticated or undiversified (Figure 1.5), due to low levels of innovation, limited productive capabilities, low investment and poor quality of education. Building capabilities will require investments in human and physical capital (p.8).

FINANCING GAP: A new estimate suggests a financing gap of $2.5 trillion for all emerging and developing countries and $200 billion–$1.3 trillion for Africa. Because Africa's population is expected to grow by 43% over 2015–2030, the gap could reach $19.5 trillion by 2030 (p.20). Check out "THE ROLE OF FINANCIAL REGULATION" on p.21.

CLIMATE CHANGE: Increasing seasonal variability, frequency and intensity of droughts and floods, and shifting habitats and agro-ecological zones due to climate change can cause food insecurity, lower trade balances, raise inflation pressure and fiscal imbalances. For instance, cyclone Idai, which hit Mozambique in March–April 2019, weakened the economy, took 1,000 lives and caused $700 million–$1 billion in damage (p.5).

CHAPTER 2: THE PRIVATE SECTOR IN AFRICA

A robust and vibrant private sector is vital for inclusive and sustained economic growth. Indeed, the private sector is the engine of economic growth. In Africa, the private sector has an immense potential to contribute directly to Agenda 2030 of the Sustainable Development Goals (SDGs) and the African Union Agenda 2063—the Africa We Want (...). (p.28).

FINANCING INNOVATIONS by banks and non-bank financial institutions, including financial technology (fintech) firms, are needed to respond to private sector financing challenges (p.29).

AGRICULTURE: The agricultural sector in Africa accounts for 20–40% of the continent's GDP. Africa is still at the first stage of mechanization (p.30) (...) Agriculture-based African countries should prioritize mechanization to double agricultural productivity and eliminate hunger and malnutrition in Africa by 2025. This 21st-century mechanization must affect the entire agricultural value chain. It should be private sector–driven, environmentally compatible and climate smart and economically viable, particularly for small-scale farmers. (p.30) (...) Although under the Maputo Declaration of 2003 African governments committed to allocating 10% of their national budgets to agricultural development, few have done so. (p.31)

EXTRACTION: Geological databases at the national geological surveys are inadequate since Africa has not fully been geologically surveyed at an appropriate scale. Basic geological information, particularly in digital format, is essential to attract investments in exploration. Refer to the case study "Mining value addition in Australia". (p.32)

INDUSTRIALIZATION: Fast growth in Africa's labour force and widespread poverty make job creation in high-productivity sectors a top priority. Transforming African economies through industrialization will be key to economy-wide productivity improvements, job creation and sustained progress in growth and poverty reduction. (p.35) (...) In Africa as in China (see BOX 2.3), policies to encourage foreign direct investment can speed industrial development, so African governments should promote them. Foreign investment and foreign firms can allow African countries to improve their trade logistics and increase the knowledge and skills of local entrepreneurs. (p.35)

THE ENERGY CHALLENGE: The high cost and unreliability of electricity in Africa debilitates private sector development in several ways. (...) Energy demand in Africa is expected to increase dramatically due to population growth, a growing middle class, urbanization and climate change. Such challenge can be overcome, since the continent has sufficient resources and limitless opportunities to develop clean or renewable energy. (p.39)

ECA recently developed a methodology to assess the energy sector regulatory environment's effectiveness in Africa and trained officials from member states on energy modelling to improve energy performance. ECA also conceived the SDG7 Initiative for Africa, which brings together countries' financiers and clean energy project developers to align their interests, combine scale and speed, and fast-track private sector financing for deploying clean energy projects. (p.39 - 40)

GOVERNANCE: Corruption deters private sector development and hence economic growth by discouraging foreign investments, increasing the cost of doing business, reducing the quality of services, distorting competitive markets and encouraging the misappropriation and misallocation of scarce resources. (p.41).

CHAPTER 3: ACCESSING FINANCING FROM THE CORPORATE BANKING SECTOR IN AFRICA

Most financing mechanisms in Africa are bank-based, and banks are a major source of innovative financing in Africa.

ASSETS: The retail and corporate banking sector in Africa holds more than 90% of the assets in the financial sector, but it is comparatively underdeveloped when benchmarked against those in emerging market economies in Asia and other industrializing countries. (p.58)

GROWTH: Though still small, the African banking sector is one of the fastest growing and most profitable in the world (FIGURE 3.2), making it one of the key sectors propelling economic growth on the continent. (p.61)

Inclusion Although financial inclusion is low in Africa (35% in 2017), the bancarization rate, defined as the proportion of the population that uses banking services, is projected to rise to 48% in 2022, with more than 450 million banked Africans - see FIGURE 3.3. (p.63)

FINANCIAL LANDSCAPE: During the past 20 years, the African financial sector has changed dramatically. The financial liberalization policies of the early 1990s greatly increased cross-border financial flows, which became an important component of the African financial landscape p.63 (see FIGURE 3.4, see page 64).

RISKS: As financial markets open, risks of contagion and the transmission of financial instability increase, requiring prudential regulation and other preventive measures to avoid or mitigate financial crises. (...) Striking a healthy balance between safeguarding the economy from financial contagion and allowing financial institutions to conduct their business will depend on a careful weighing of macroprudential measures and an arm's length approach to financial service trade transactions. (p.65)

AGRICULTURE: Increasingly, African countries are developing and adopting innovative financing mechanisms to support the Agricultural sector (read more on p. 67). Traditional banks may not be able to close the financing gap in the agricultural sector alone but may need to coordinate with the public sector, as in the European Union. (p.68)

GOVERNANCE: From a policy perspective, a regulatory framework that strikes an optimum balance between ensuring financial stability and offering innovative financing schemes for all is key to developing a strong and robust private sector and ultimately to accelerating economic development. (p.70)

INVESTMENT: Investment is key to build infrastructure and foster innovation. Despite Africa's growth, many economies remain unsophisticated or undiversified (Figure 1.5), due to low levels of innovation, limited productive capabilities, low investment and poor quality of education. Building capabilities will require investments in human and physical capital (p.8).

A new estimate suggests a financing gap of $2.5 trillion for all emerging and developing countries and $200 billion–$1.3 trillion for Africa. Because Africa's population is expected to grow by 43% over 2015-2030, the gap could reach $19.5 trillion by 2030 (p.20). Check out "THE ROLE OF FINANCIAL REGULATION" on p.21.

CHAPTER 4: TAPPING INTO THE POTENTIAL OF AFRICAN MARKETS

In other parts of the world, financial markets complement bank finance as another source of financing to the private sector, but in Africa they are small and underveloped, largely dominated by commercial banks.

CHALLENGES: The underdevelopment of African financial systems constricts credit for firms and produces low investment rates. (...) The low level of credit in Africa shows the limited services financial institutions provide the private sector. (p.74)

STOCK MARKETS: They allow domestic firms to raise funds in developed economies and mobilize domestic savings by offering a variety of instruments for investors to diversify their savings. In developing and emerging economies, two constraints of stock exchanges are the limited diversity of financial instruments and the limited number of listed stocks. (p.75)

OBSTACLES FOR STOCK MARKETS: High transaction costs and fees, lengthy listing procedures, binding and difficult listing conditions, lack of knowledge about stock markets and, in some exchanges, lack of transparency (p.77). In many developing markets around the world, transaction costs are below 1% of the value of the trade, but African exchanges usually charge well over that. (p.76)

BOND MARKETS: There is a growing local currency bond market in Africa with increased appetite among local investors. Local currency bonds make up 78% of outstanding debt in Africa (including government and corporate bonds). In South Africa, the biggest bond market on the continent, local investors hold 62% of government bonds (p.81).

CHAPTER 5: LONG-TERM FINANCING FOR SUSTAINABLE DEVELOPMENT IN AFRICA

The cost to achieve the SDGs by 2030 in Africa is estimated at about $1.3 trillion a year, according to the United Nations. That could increase to $19.5 trillion as a result of population growth— projected to be 43% over 2015–2030.

INVESTMENT GAPS: A central challenge for Africa to meet the SDGs and achieve sustainable and inclusive development is to mobilize the investment needed in key sectors such as health, energy, transport, construction, agriculture, education and manufacturing (p.98). The continent's infrastructure needs amount to $130-$170 billion a year until 2025, with a yearly financing gap of $67.6-$107.5 billion. Refer to p.106 for more information.

CLIMATE CHANGE: An estimated $18-$30 billion a year will be needed over the next two decades for climate action and climate change adaptation in Africa, with nearly $1 trillion worth of investments and projects ready to be financed (p.98).

GREEN BOND MARKET: Sovereign ssuers are typically financing the greening of public infrastructure, including energy, water and transport, including major emerging economies such as Brazil, China and India, as well as smaller countries such as Fiji, Seychelles and Thailand. (p.101). The African green bond market emerged in 2010 - South Africa and the African Development Bank (AfDB) took the lead, followed by Morocco, Nigeria and Seychelles. Refer to "Box 5.1 - Examples of green bonds programmes in Africa", on p.102.

SUSTAINABILITY FINANCING: Private non-foreign direct investment cross-border capital flows to Africa being dominated by high risk-high return investors, such as private equity funds, and investors with a longer-term investment horizon, such as sovereign wealth funds or non-traditional bilateral investors (for instance, China), (p.103).

DOMESTIC FRAMEWORKS: Regulatory and governance frameworks for green, social and sustainability bonds are critical to developing the market. Several African governments have recognized this and have introduced green bond governance frameworks, including independent certification and monitoring of proceeds, that align with international best practice. (p.104)

PUBLIC-PRIVATE PARTNERSHIP (PPPS): In Africa, as in many other developing countries, the infrastructure sector does not attract much private investment and funding. Private financing accounted for only 11% of infrastructure funding in Africa in 2018 (p.107). Check out "figure 5.3 - Infrastructure investment by international lenders and donors, national governments and the private sector in Africa" on p.108. Only a few African countries have embarked on PPPs to tap private capital for fi¬nancing infrastructure. Kenya, Nigeria, Uganda and South Africa account for almost 50%. (p.109)

DEVELOPMENT BANKS: African regional and national development banks are pivotal in supporting infrastructure finance, including by catalysing private finance. They should expand in countries where they are active (adding infrastructure finance to their business if they are not already participating in that sector) and should consider going into new countries. (p.110)

INVESTMENT: Investment is key to build infrastructure and foster innovation. Despite Africa's growth, many economies remain unsophisticated or undiversified (Figure 1.5), due to low levels of innovation, limited productive capabilities, low investment and poor quality of education. Building capabilities will require investments in human and physical capital (p.8).

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CHAPTER 6: LEVERAGING GLOBAL INNOVATIONS IN FINANCIAL TECHNOLOGY IN AFRICA

The global fintech revolution is expected to triple access to financial services in Africa, creating a new market of 350 million customers. In Africa, fintech is reducing costs and risks, as well as extending service to unbanked populations.

DIGITAL PAYMENTS: The biggest component of fintech transactions In Africa, with mobile money transactions accounting for close to 10% of GDP, compared with 7% in Asia and less than 2% in other regions. Africa accounts for more than 60% per cent of mobile money transactions in the world—more than $450 billion in 2019 (p.121).

MOBILE FINANCE: With the spread of COVID-19 and its impact on economies, the use of fintech, including mobile money, is expected to increase even more. For instance, one study estimated that the spread of COVID-19 and related government lockdowns have led to a 24–32% increase in the relative rate of daily downloads of mobile finance applications in 74 sampled countries around the world (p.121).

MOBILE MONEY: Among fintech innovations, mobile money and digital payments are areas where Africa has made significant inroads. Almost half of total global mobile money accounts are in Africa, which had 396 million registered users and 1.4 million agents serving them in 2018. (p.125)

FRAUD CONTROL: Growth projections and forecasts for alternative financing and other crowdsourcing instruments in Africa are very promising, but the market faces a major challenge: controlling fraudulent activities. Crowd-based financing for business activities benefits markets only if borrowers and investors trust one another. Establishing binding rules and guidelines is essential to securing that trust. (p.121)

CROWDFUNDING: Africa accounts for less than 1% of global crowdfunding activities and reasons for that include low internet penetration rates, high internet service cost and weak regulations and standards (p.123).

CHAPTER 7: REGULATIONS TO SUPPORT FINANCING IN AFRICA

Africa needs to rethink its financial services regulation so that innovation is fully functional, the environment enables innovatok

ion, transparency is enhanced, and financing for private sector development is delivered.

CRISIS PREVENTION: African countries need to regulate their bank sector to limit the possible harm from banking crises or from more general system-wide misallocation of resources. For the sake of private sector development, the regulation of banks and other sources of capital for funding private industry—such as equity and debt capital markets and digital platforms— needs to be strengthened. (p.136)

CONFIDENCE FOR BUSINESSES: Appropriate, effective and enabling regulatory frameworks for all financial intermediaries operating in Africa will give confidence to a new breed of fit and proper entrepreneurs. The frameworks will introduce new financial service platforms and innovative products, whose competitive arena will become more transparent and will open up to new players. (p.137).

BANKING REGULATIONS: Financial sector reform has had three distinct phases across Africa, and the evolution of the sector has shown a number of key trends. Read more about that on p.137.

MARKET REGULATORS: African countries also need sound and appropriate regulatory environments and frameworks to enable the development of stable and resilient capital markets. All countries with established securities markets or stock exchanges have appropriate rules, regulations and regulatory bodies. (p.140)

REGULATORY CHALLENGES: Regulations that concern the banking sector alone may be insufficient to safeguard the financial system against some of the risks fintech services pose, such as data privacy, money laundering, mismatched risk and return, and systemic risk. These new risks call for financial regulation to be reviewed to provide a flexible environment for fintech to develop that is strict enough to limit the risks. (p.143)

COVID-19 CRISIS: Some African countries have limited fiscal space and international reserves and thus lack the necessary resources to implement COVID-19 responses (p.149) (...) According to IMF data, African countries will record fiscal deficits averaging 5.8% in 2020 and 4.4% in 2021, compared with 3% in 2019. (...) However, African policymakers' and regulators' experience with the 2008-2009 financial crisis and use of various measures to cushion its impact give them an advantage in rapidly responding to the COVID-19 crisis (p.151).

INVESTMENT: Investment is key to build infrastructure and foster innovation. Despite Africa's growth, many economies remain unsophisticated or undiversified (Figure 1.5), due to low levels of innovation, limited productive capabilities, low investment and poor quality of education. Building capabilities will require investments in human and physical capital (p.8).

A new estimate suggests a financing gap of $2.5 trillion for all emerging and developing countries and $200 billion-$1.3 trillion for Africa. Because Africa's population is expected to grow by 43% over 2015-2030, the gap could reach $19.5 trillion by 2030 (p.20). Check out "THE ROLE OF FINANCIAL REGULATION" on p.21.

CHAPTER 8: CONCLUSIONS AND POLICY RECOMMENDATIONS

This chapter summarizes the key aspects of innovative financing for the development of the private sector in Africa. Five messages are key (refer to Figure 8.1)

1. Financing innovations can arise from multiple sources simultaneously Businesses need to consider leveraging different sources according to their financing needs (banks, fintech, financial markets, capital markets, development banks).

2. A transparent and effective regulatory institution is mandatory to minimize risk and oversee the financial operations of firms and peer institutions.

3. The absence of a sound eco-system can impede firms even when financing is readily available. This affects firms of all sizes, depending on their stage in the growth cycle.

4. Innovative financing of the private sector and business growth generates: firm value added, gainful employment, tax revenue for government, stable investment returns for entrepreneurs, growth of financial institutions.

5. The transformation from innovative financing and from a fully operational financial sector to economic growth, lower inequality and reduced poverty is long term and necessarily involves feedback mechanisms.

COVID-19 CRISIS: To enable economic recovery and reasonable SDG progress, African economies should fully explore innovative financing for the private sector and enhance the eco-system for private sector development. Efforts should include raising investment to 35–40% of GDP, enhancing competitiveness and supporting regional integration. A key strategy is the African Continental Free Trade Area (AfCFTA), signed by 54 African countries - see Figure 8.2 on p.157 and read more on p.158.

REGULATION: The report recommends that public policymakers (including central banks) consider amending banking and financial services legislation to enable innovative private sector funding. The process could lead to lobbying, opening for debate a range of banking and financial service issues. (p.164)

CHAPTER 1: RECENT ECONOMIC AND SOCIAL DEVELOPMENTS IN AFRICA

RECENT NUMBERS:

- Africa is the second fastest growing region in the world, estimated to have grown 3.4% in 2019.
- COVID-19 pandemic will impact growth to decelerate to between 1.8% and -4.1% in 2020.
- Growth in Africa is projected to rebound to 5% in 2021, supported by the effective implementation of COVID-19 response measures and global economic recovery.
- Refer to Figure 1.1 for data on Global Economic Growth.

ENGINE OF GROWTH: **The private sector, as the engine of growth,** will **catalyse investment in infrastructure and industrialization** and so contribute crucially to implementing the The African Continental Free Trade Area (AfCFTA). **The private sector can generate productivity** and **enhance the participation of households and business** firms in economic activity, driving economic growth and prosperity. (p.10)

AVIATION INDUSTRY: Air travel **restrictions and the reduction of air travel routes has affected major African carriers.** The International Air Transport Authority (IATA) projects **a $4 billion drop in revenue for African airlines.** The effect is aggravated for airlines that were weak before the pandemic and will likely end up filing for bankruptcy or seeking bailouts (p.4).

FINANCING: **Bank financing to the private sector remains low,** and usually **does not fit the needs** of the private sector since about **60% is short-term** (with a tenor of less than one year), (p.14).

DIGITAL REVOLUTION AND ALTERNATIVE FINANCING: The digital revolution under way in Africa, mainly based on mobile phone networks, presents **opportunities for sustainably developing finance.** The infrastructure is suitable for developing prepayment systems, and **if telecommunications companies and banks collaborated, prepayment systems could be replaced by bank account transfers** (p.20).

ALTERNATIVE FINANCE, especially crowdfunding, is another **fast-growing market in Africa. Crowdfunding** presents some difficulties, since entrepreneurs must spend time building a base of contacts that will contribute capital and promote the campaign, but it **can have non-monetary benefits**, such as increased credibility and market awareness (p.21).

Check out the case study "DIGITAL SOLUTION AND LENDING: TWO EXAMPLES FROM KENYA" on p. 21.

CHAPTER 2: THE PRIVATE SECTOR IN AFRICA

A robust and vibrant private sector is vital for inclusive and sustained economic growth. Indeed, the private sector is the engine of economic growth. (p.28)

The **infrastructure gap** in Africa not only challenges private sector development but also offers Africa's **private sector an opportunity to invest**. (p.28)

GROWTH: More than **700 private businesses** in Africa are large enough to **generate more than $500 million** a year in revenue. **Large companies** (with 100 or more employees) **generate between $1 billion and $1.4 trillion a year** in profits. (p.29)

Agriculture: the current **financing needs of Africa's 48 million** smallholder farmers are estimated at about $450 billion. (...) Innovative financing mechanisms are needed, such as cooperative groups; value chain frameworks or out grower schemes binding farmers to supply products to a particular firm, which can be linked to public-private partnerships (PPPs); and mobile money for the private sector (...). (p.30)

CHALLENGES TO PRIVATE SECTOR DEVELOPMENT: **Easy, affordable and reliable access to infrastructure** (particularly energy) and finance are **the two most cited obstacles** affecting the operation of businesses in Africa**.** **Access to electricity** is cited by **20.7%** of firms in Africa as the main obstacle, and **finance by 19.6%** (p.38). See figure 2.4 "Main obstacles to businesses in Africa" on p.39, and figure 2.5 "Main obstacles to the operation of businesses in Africa, by company size" on p.42.

ENERGY: **Some 79% of firms in Africa experienced electricity outages** between 2007 and 2018, and the average effective cost of electricity for manufacturing enterprises in Africa is close **to 20 cents per kilowatt-hour**, **about four times higher than industrial rates elsewhere in the world** (p.38). (...) The gap between demand and supply is a chance for the private sector to invest in the energy sector, to power industrialization and to stimulate growth, employment and trade, especially given the prospective benefits of the AfCFTA. (p.39)

COVID-19 PANDEMIC: African businesses expect **a slow recovery** from the crisis and a **drop in revenues by an average of 30–40%**, with small companies expecting to be affected worse. *Read more about the Potential impacts of COVID-19 on African businesses on p. 43 and 44.*

THE AFRICAN CONTINENTAL FREE TRADE AREA (AfCFTA): African firms need to industrially upgrade through participating in global value chains. AfCFTA provides an opportunity **AfCFTA provides an opportunity** for African countries to learn by doing how to **develop competitive regional value chain**s, a much needed step towards participating in global value chains. (p.35) Under the AfCFTA, it is assumed that tariff and non-tariff barriers to trade will be reduced and so reduce the cost of business operations. (p.50)

CHAPTER 3: ACCESSING FINANCING FROM THE CORPORATE BANKING SECTOR IN AFRICA

Most financing mechanisms in Africa are bank-based, and banks are a major source of innovative financing in Africa.

Financing: the banking sector is the main source of finance for the private sector in Africa, yet the ratio of bank credit to GDP is very low, less than 30% in 2019, compared with 47% in Latin America and the Caribbean and 94% in Europe and Central Asia. (p.61)

GROWTH: Though still small, **the African banking sector is one of the fastest growing and most profitable in the world** (FIGURE 3.2), making it one of the key sectors propelling economic growth on the continent. (p.61)

EXPANSION: The low levels of financial inclusion in Africa mean that there is **massive potential for growth** if the banking sector can bring financial services to underserved and unserved populations. **Expanding inclusion will lead to rising deposits and to financing** that can increase capacity for businesses. (p.62)

COMPETITION: Deregulation has relaxed entry barriers, paving the way for competition in the banking sector. (...) **If domestic banks are not structured properly** to enable them to compete on pricing, they are **likely to face tough competition from new pan-African entrants**. (p.65)

AfCFTA: With the establishment of the African Continental Free Trade Area (AfCFTA), and liberalization of financial services as one of the priority service sectors, **African banks will have the opportunity to tap into a continental market of over 1.2 billion consumers.** (p.65)

EXTRACTION: **As mining firms continue to grow, traditional banks in Africa may have to forgo financing** for some of these projects because of perceived high risk and limitations imposed by international regulations. Similar dynamics are also observed in oil and gas firms. (p.68)

SMES: As small and medium enterprises (SMEs) scale up production to enter other markets in Africa and engage in cross-border activity, **they will need trade finance and other types of credit to ramp up their business.** (p.69)

CHAPTER 4: TAPPING INTO THE POTENTIAL OF AFRICAN MARKETS

In other parts of the world, financial markets complement bank finance as another source of financing to the private sector, but in Africa they are small and undeveloped, largely dominated by commercial banks.

CAPITAL MARKETS: they provide not only an alternative for additional private sector fund raising, but also an **alternative to regular bank deposits for investors to save and to gain returns.** (p.74)

EQUITY MARKETS: they serve as a **fundraising platform for businesses** that require large amounts of capital to expand and as a sales vehicle to let entrepreneurs lower their stake in the business. Participating in equity markets **provides African investors and businesses** higher **name recognition, access to the public debt markets** and other varieties of **financing instruments, raise funds and diversify their savings.** (p.75)

LISTING REQUIREMENTS: stock exchanges often require that businesses meet **certain thresholds** before being listed. Businesses must also **align their accounting practices with the regulations** set forth by the stock exchange or regulatory authority. **Read more on p.77.** In recent years, African stock exchanges have started setting up secondary boards to offer **not-yet-profitable smaller companies** and **start-ups** an **opportunity to access equity markets** for fund raising (p.78).

INITIAL PUBLIC OFFERING (IPO): With more than 1,200 public offerings completed in 2019, the African IPO market represented **1.4% of the $1.2 trillion worldwide value of IPOs** (p.79). Refer to Figure 4.2: Initial public offerings by selected African exchanges, 2014-2019, p.78.

PRIVATE INVESTMENT MARKETS: In 2019, $106 billion in private capital was raised worldwide, but only $1.1 billion in Africa. **The number of deals in Africa increased** from 158 in 2014 to match its 2013 historic high – **186 deals in 2018.** (p.86). Check out Figure 4.6 “Share of African private investment deals by region, 2013-18” on p. 87.

OPPORTUNITIES: **Africa’s growing population, emerging middle class**, rising food prices and increasing **value of the food market** (projected to reach $1 trillion by 2030) **present investment opportunities** for the private sector in both farmland and agribusiness. (p.89)

CHAPTER 5: LONG-TERM FINANCING FOR SUSTAINABLE DEVELOPMENT IN AFRICA

The cost to achieve the SDGs by 2030 in Africa is estimated at about $1.3 trillion a year, according to the United Nations. That could increase to $19.5 trillion as a result of population growth— projected to be 43% over 2015–2030.

SUSTAINABILITY BONDS: The **integration of environmental, social and governance** (ESG) considerations and sustainability increasingly **attracts environmentally and socially responsible investors**. It also offers Africa a **unique opportunity to mobilize private capital** for financing infrastructure development and large-scale economic activities. (p.99)

THE GREEN BOND MARKET: **The investment opportunity** to address climate change in emerging market cities is estimated at **$29 trillion by 2030**. The **key sectors** of such an investment opportunity include **green buildings, electric vehicles, public transport infrastructure, climate-smart water, renewable energy and municipal solid waste management**. (p.100)

FUNDING: In Africa as in many other developing countries**, the infrastructure sector does not attract much private investment and funding**. Private financing accounted for only 11% of infrastructure funding in Africa in 2018 (p.107). Check out "figure 5.3 - Infrastructure investment by international lenders and donors, national governments and the private sector in Africa" on p.108.

INFRASTRUCTURE INVESTMENT: due to considerable risks, demand must be great enough to cover capital and operating costs, creating risk for those investing large amounts of money in hope of future demand. So, **private investors willing to take the risk will demand a large risk premium for their investment**, or else guarantees, for example, of traffic. (p.110)

DEVELOPMENT BANKS: **they can provide funds to the private sector** through loans or equity; with a diversified portfolio integrating riskier and less risky projects, they can fund their operations through revenues and through funds levied on the market. (p.111)

CHAPTER 6: LEVERAGING GLOBAL INNOVATIONS IN FINANCIAL TECHNOLOGY IN AFRICA

The global fintech revolution is expected to triple access to financial services in Africa, creating a new market of 350 million customers. In Africa, fintech is reducing costs and risks, as well as extending service to unbanked populations.

ALTERNATIVE SOURCES: Africa's financing gap has provided a **unique opportunity for fintech development** to furnish alternative finance sources and investment mechanisms, particularly for start-ups and micro, small and medium enterprises. Two key fintech activities, **crowdfunding and crowdinvesting**, grew over 2017–2019 and **are projected to keep growing** during 2020–2023 (p.121).

CROWDFUNDING: It is currently **more prominent than crowdinvesting in Africa**, though Statista forecasts that crowdinvesting will surpass crowdfunding in 2022. (p.121) Refer to Table 6.1, "Alternative financing in Africa, 2017–2023" on p. 122.

MOBILE MONEY: Among fintech innovations, **mobile money** and **digital payments** are areas where Africa has made significant inroads. Almost **half of total global mobile money accounts are in Africa**, which had 396 million registered users and 1.4 million agents serving them in 2018. (p.125)

DIGITAL PAYMENT SYSTEMS: It is **growing fast in Africa**, along with e-commerce. Major e-commerce platforms offer multiple payment methods on their websites and apps, Table 6.4. (...) while **most e-commerce firms operating in Africa are local,** a **substantial portion of payments processed** on these platforms happen on **foreign-owned card and payment schemes** (p.126). Refer to "Box 6.1 - Regional developments in e-commerce", on p.128.

FUNDING: The emergence of fintech across Africa has opened new avenues of funding for businesses and has led to the emergence of new financial service providers, new financial instruments such as **crowdfunding** and **mobile money services**, **new currencies** such as cryptocurrencies and even new ways of conducting conventional banking such as **online banking** and **electronic payment systems** (p.130).

SMES: Fintech has the **potential to overcome some of the financial constraints** faced by Small and Medium Enterprises (SMEs) as a consequence of the complexity of SME financing. (...) **Fintech,** including data analytics, **is closing the financing gap in the SME sector** through innovation in credit appraisal, underwriting, origination and servicing (p.131).

CHAPTER 7: REGULATIONS TO SUPPORT FINANCING IN AFRICA

Africa needs to rethink its financial services regulation so that innovation is fully functional, the environment enables innovation, transparency is enhanced, and financing for private sector development is delivered.

CONFIDENCE FOR BUSINESSES: Appropriate, **effective and enabling regulatory frameworks** for all financial intermediaries operating in Africa **will give confidence to** a new breed of **fit and proper entrepreneurs.** The **frameworks will introduce new financial service platforms and innovative products**, whose competitive arena will become more transparent and will open up to new players. (p.137)

MOBILE PAYMENT: The **use of mobile payment systems is growing**, helping to fill the vacuum in the **unbanked segment of communities across Africa.** Domestic transfers through mobile payment platforms pay for a wide range of services, from school fees and rent to utility bills and wages. **The importance and extent of the financial services** provided through mobile platforms **should not be underestimated.** (p.143)

RISKS: Many African economies are dominated by a small number of sectors, normally the **producers of cash crops or natural resources**, such as oil and gas. **Bank lending tends to concentrate on firms and households in those sectors**, so great macroeconomic risks are associated with lending portfolios vulnerable to commodity risk. (p.146)

SMES LENDING: Lending to small and medium **enterprises (SMEs)** has been **considerably affected by regulations**. Read more on the Impact of regulations on small and medium enterprise funding on p.145.

CHAPTER 8: CONCLUSIONS AND POLICY RECOMMENDATIONS

This chapter summarizes the key aspects of innovative financing for the development of the private sector in Africa. Five messages are key (refer to Figure 8.1)

1 - **Financing innovations can arise from multiple sources simultaneously.** Businesses need to consider leveraging different sources according to their financing needs (banks, fintech, financial markets, capital markets, development banks)

2- **A transparent and effective regulatory institution** is mandatory to minimize risk and oversee the financial operations of firms and peer institutions.

3- The **absence of a sound eco-system can impede firms** even when financing is readily available. This affects firms of all sizes, depending on their stage in the growth cycle.

4- **Innovative financing** of the private sector and business growth **generates**: firm value added, gainful employment, tax revenue for government, stable investment returns for entrepreneurs, growth of financial institutions.

5- The **transformation** from innovative financing and from a fully operational financial sector to economic growth, lower inequality and reduced poverty is long term and **necessarily involves feedback mechanisms**.

FINANCING CHALLENGE: Over 2020–2030, **the private sector in Africa** is expected to play **an important role in enabling economic recovery** from the COVID-19 pandemic, increasing economic prosperity and achieving the SDGs. (...) However, **financing is one of the major impediments** to private sector development in Africa. The recent outbreak of COVID-19 is a threat and aggravates the already major challenge in finding financing. (p.159). Financial markets might be expected to complement bank finance as another source of financing to the private sector (p.161).

AFRICAN CONTINENTAL FREE TRADE AREA (AfCFTA): creates **opportunities for internationalization** by supporting the **development of regional** and **global value chains** in which manufacturers that rely on embedded and embodied service inputs can source such inputs locally in the continental market, **creating jobs, adding value and expanding their share of the global market**. (p.158)

CHAPTER 1: RECENT ECONOMIC AND SOCIAL DEVELOPMENTS IN AFRICA

RECENT NUMBERS:

- Africa is the second fastest growing region in the world, estimated to have grown 3.4% in 2019.
- COVID-19 pandemic will impact growth to decelerate to between 1.8% and -4.1% in 2020.
- Growth in Africa is projected to rebound to 5% in 2021, supported by the effective implementation of COVID-19 response measures and global economic recovery.
- Refer to Figure 1.1 for data on Global Economic Growth.

DECLINE ON COMMODITY PRICES: After slight increases in 2019, **commodity prices plummeted** for more than **two-thirds of African exports** in 2020, The price of **petroleum**, which accounts for 40% of African exports and 7.4% of GDP in Africa, **crashed by more than 50% per cent to its lowest level since 2003**. Metal prices fell 20%, while cotton fell 26%. The Economic Commission for Africa (ECA) projects a minimum $65 billion loss to fuel revenue for 2020. (Figure 12, p.3).

IMPACT OF COVID-19: The impact of the pandemic will push between **5 million and 29 million people below the extreme poverty** line of $1.90 per day, compared with a baseline 2020 African growth scenario, according to ECA projections (p.11).

The current health crisis has many adverse social impacts and **Africa is particularly vulnerable, given weaker health systems, difficult living conditions and sparse access to sanitation**. African health systems are weaker than those elsewhere in the world, with lower ratios of hospital beds, intensive care units and health professionals to their populations. **Africa on average has 1.8 beds per 1,000 people**, compared with 6.0 in France and 8.2 in the Russian Federation (p.11).

African governments require additional funds to deal with COVID-19. In a best-case scenario, with suppression of the coronavirus spread and intense early physical distancing measures, **$44 billion would be required across Africa for testing, personal protective equipment and treatment of COVID-19 patients** requiring hospitalization and intensive care treatment (p.20).

INFRASTRUCTURE: By recent estimates, **Africa needs $100 billion a year to close its infrastructure gap** (McKinsey & Company, 2019). That figure aligns with African Development Bank estimates of the continent's infrastructure needs amounting to $130 billion–$170 billion a year, with a financing gap of $68 billion – $ 108 billion (AfDB, 2018). **The gap is about 3–5 per cent of the continent's GDP. Key sectors are energy and transportation**, accounting for about 55% of the financing needs, and **water supply and sanitation**, accounting for about 40 per cent (Table 1.3), (p.20).

CHAPTER 2: THE PRIVATE SECTOR IN AFRICA

A robust and vibrant private sector is vital for inclusive and sustained economic growth. Indeed, the private sector is the engine of economic growth (p.28).

Small and medium enterprises are considered the **backbone of African economies**, since they represent about **90% of all private businesses** and account for more than **60% of employment** in most African countries. (p.29)

CHALLENGES TO PRIVATE SECTOR DEVELOPMENT: Easy, affordable and reliable access to infrastructure (particularly energy) and finance are **the two most cited obstacles** affecting the operation of businesses in Africa**. Access to electricity** is cited by **20.7%** of firms in Africa as the main obstacle, and **finance by 19.6%** (p.38). See figure 2.4 "Main obstacles to businesses in Africa", p.39.

TRANSPORT: Some **3.6% of firms in Africa** identified **transport as the main obstacle** to business. (p.38)

ENERGY: About **590 million people in Africa lack access to electricity**, and for those with access, the quality is generally poor and reliability unacceptably low compared with other regions of the world. (p.38)

ICT: It is estimated that **75% of the population in Africa does not have internet access**, and so does not have access to the knowledge, information and services that the internet can bring. (p.40)

WATER: The **unavailability of clean water and sanitation results in approximately a 5% loss of GDP** in Africa annually, and people spend 40 billion hours a year of otherwise productive time just collecting water. (p.40)

GOVERNANCE: Some **6.3% of firms** in Africa reported that **corruption is a major challenge** to their business operation. (p.41)

Financing: As reported by **19.6% of firms**, **financing is a MAJOR obstacle to business operations**. Almost a quarter of small firms reported it as a major obstacle, as did about 13% of large firms. (p.41)

CHAPTER 3: ACCESSING FINANCING FROM THE CORPORATE BANKING SECTOR IN AFRICA

Most financing mechanisms in Africa are bank-based, and banks are a major source of innovative financing in Africa.

FINANCING: Despite an overall increase in banking activities, **bank financing to the private sector remains low and ill tailored to the needs of private firms**. (p.58). (...) **Most bank loans** to the private sector are **short- to medium-term** in tenor. However**, businesses often need financing for longer-term projects**, such as to purchase fixed assets or property to expand capacity. Common loan types are on TABLE 3.1. (p.59)

FIRM SIZE: it can have pronounced effects on access to financing, as **large companies are more likely to get loans** and favourable terms. However, small and medium enterprises can be effectively shut out of bank financing. (p.59)

INCLUSION: Although **financial inclusion is low in Africa (**3% in 2017), **the bancarization rate**, defined as the proportion of the population that uses banking services, **is projected to rise to 48% in 2022**, with more than 450 million banked Africans. See FIGURE 3.3. The expansion of traditional banks to reach more people and the entry of new banks are expected to create even more opportunities for the banking sector. (p.63)

AfCFTA: With the establishment of the African Continental Free Trade Area (AfCFTA), and liberalization of financial services as one of the priority service sectors, **African banks will have the opportunity to tap into a continental market of over 1.2 billion consumers.** (p.65)

CHAPTER 4: TAPPING INTO THE POTENTIAL OF AFRICAN MARKETS

In other parts of the world, financial markets complement bank finance as another source of financing to the private sector, but in Africa they are small and undeveloped, largely dominated by commercial banks.

IPOS: In an initial public offering (IPO), a private company offers its shares to the public and formally lists itself on a public stock market, connecting it with the wider financial system. A **functioning IPO market requires** investment banks to **help generate interest and connect companies with potential investors**. (...) South African IPOs alone represented more than 65% of the capital raised on African exchanges (p.78).

The **proceeds** raised from IPOs in Africa **between 2014 and 2019 reached $27.1 billion**, **less than 1.4% of global IPO proceeds** during that period. (p.74). With more than 1,200 public offerings completed in 2019, **the African IPO market represented 1.4% of the $1.2 trillion worldwide value** of IPOs (p.79). Refer to Figure 4.2: Initial public offerings by selected African exchanges, 2014-2019, p.78.

SOVEREIGN BONDS: In 2019, **African governments issued** over **$200 billion in sovereign bonds** (denominated in local or foreign currency), **compared with** more **than $700 billion issued by China**, the biggest bond market among emerging markets and the third biggest bond market globally. (p.81)

COMMODITY EXCHANGES: Although African countries are dominant global producers of many agricultural and natural resource goods, **the goods are traded** or have their prices quoted on exchanges **outside of the continent.** So, **opportunities** for price discovery, access to finance, hedging opportunities and market information **are limited for African farmers** and **small businesses** in those sectors. (p.85)

PRIVATE INVESTMENT MARKETS: In 2019**, $106 billion in private capital was raised worldwide**, **but only $1.1 billion in Africa**. **The number of deals in Africa increased** from 158 in 2014 to match its 2013 historic high — **186 deals in 2018** (p.86). Check out Figure 4.6 “Share of African private investment deals by region, 2013-18” on p. 87.

CHAPTER 5: LONG-TERM FINANCING FOR SUSTAINABLE DEVELOPMENT IN AFRICA

The cost to achieve the SDGs by 2030 in Africa is estimated at about $1.3 trillion a year, according to the United Nations. That could increase to $19.5 trillion as a result of population growth— projected to be 43% over 2015–2030.

INVESTMENT GAPS: A **central challenge** for Africa to meet the SDGs and achieve sustainable and inclusive development is to **mobilize the investment needed in key sectors** such as health, energy, transport, construction, agriculture, education and manufacturing (p.98). The continent's infrastructure needs amount to $130-$170 billion a year until 2025, with a yearly financing gap of $67.6-$107.5 billion. Refer to p.106 for more information.

CLIMATE CHANGE: An estimated **$18–$30 billion a year** will be needed over the **next two decades for climate action and climate change adaptation in Africa**, with nearly $1 trillion worth of investments and projects ready to be financed (p.98).

DEVELOPMENT BANKS: African regional and national development banks are **pivotal in supporting infrastructure finance**, including by catalysing private finance. **They should expand** in countries where they are active (adding infrastructure finance to their business if they are not already participating in that sector) and should consider going into new countries (p.110). African national development banks have considerable scope for expanding their scale, which would let them **contribute more to financing infrastructure.** Refer to the case study "Development bank of Southern Africa operations in South Africa (p.111)

PENSION FUNDS: African **pension funds have been expanding in recent years**, though from a low base, thanks to the rise of the middle class and regulatory reforms that bring more people into the social security net (ECA, 2019). **Pension funds in the six largest African markets could grow to an estimated $7.3 trillion by 2050** (from $800 billion in 2014). (p.113)

CHAPTER 6: LEVERAGING GLOBAL INNOVATIONS IN FINANCIAL TECHNOLOGY IN AFRICA

The global fintech revolution is expected to triple access to financial services in Africa, creating a new market of 350 million customers. In Africa, fintech is reducing costs and risks, as well as extending service to unbanked populations.

DIGITAL PAYMENTS: The **biggest component** of **fintech transactions** in Africa, with mobile money transactions accounting for close to **10% of GDP**, compared with 7% in Asia and less than 2% in other regions. **Africa accounts for more than 60% per cent of mobile money transactions** in the world—more than $450 billion in 2019 (p.121).

CROWDFUNDING: Africa accounts for **less than 1% of global crowdfunding** activities and reasons for that include **low internet penetration** rates, **high internet service cost** and **weak regulations** and standards (p.123).

MOBILE MONEY: Among fintech innovations, **mobile money** and **digital payments** are areas where Africa has made significant inroads. Almost **half of total global mobile money accounts are in Africa**, which had 396 million registered users and 1.4 million agents serving them in 2018. (p.125)

INCLUSION: In addition to allowing people to access financial services more easily, the **migration to mobile** and **online banking** has **expanded financial services** to people who have long been unserved by financial institutions, whether because they live in an underserved area or because they lack the documentation to open a bank account. (p.127)

MOBILE FINANCE: With the spread of **COVID-19** and its impact on economies, **the use of fintech,** including mobile money, **is expected to increase even more**. For instance, one study estimated that the spread of COVID-19 and related government lockdowns have led to a **24–32% increase** in the relative rate of daily **downloads of mobile finance applications** in 74 sampled countries around the world (p.121).

CHAPTER 7: REGULATIONS TO SUPPORT FINANCING IN AFRICA

Africa needs to rethink its financial services regulation so that innovation is fully functional, the environment enables innovation, transparency is enhanced, and financing for private sector development is delivered.

CRISIS PREVENTION: African countries need to regulate their bank sector to limit the possible harm from **banking crises** or from more general **system-wide misallocation of resources**. For the sake of private sector development, the regulation of banks and other sources of capital for funding private industry—such as equity and debt capital markets and digital platforms— needs to be strengthened. (p.136)

REGULATORY CHALLENGES: Regulations that concern the banking sector alone **may be insufficient to safeguard the financial system** against some of the **risks fintech services pose**, such as **data privacy, money laundering, mismatched risk and return**, and **systemic risk**. These new risks call for financial regulation to be reviewed to provide a flexible environment for fintech to develop that is strict enough to limit the risks. (p.143)

COVID-19 CRISIS: Some African countries have **limited fiscal space and international reserves** and thus lack the necessary resources to implement COVID-19 responses (p.149) (...) According to IMF data, African countries will record **fiscal deficits averaging 5.8% in 2020 and 4.4% in 2021**, compared with 3% in 2019. (...) However, **African policymakers' and regulators'** experience with the 2008–2009 financial crisis and use of various measures to cushion its impact give them an **advantage in rapidly responding** to the COVID-19 crisis (p.151).

CHAPTER 8: CONCLUSIONS AND POLICY RECOMMENDATIONS

This chapter summarizes the key aspects of innovative financing for the development of the private sector in Africa. Five areas are key (refer to Figure 8.1)

1 - **Financing innovations can arise from multiple sources simultaneously.** Businesses need to consider leveraging different sources according to their financing needs (banks, fintech, financial markets, capital markets, development banks)

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5- The **transformation** from innovative financing and from a fully operational financial sector to economic growth, lower inequality and reduced poverty is long term and **necessarily involves feedback mechanisms**.

COVID-19 CRISIS: To enable economic recovery and reasonable SDG progress, **African economies should fully explore innovative financing** for the private sector and enhance the eco-system for private sector development. Efforts should include **raising investment to 35–40% of GDP**, enhancing competitiveness and supporting regional integration. A **key strategy** is the **African Continental Free Trade Area (AfCFTA),** signed by 54 African countries - see Figure 8.2 on p.157 and read more on p.158.

FINANCIAL MARKETS: Africa can **deepen and broaden financial markets** by supporting the digital payment systems and platforms that underlie electronic payments and transfers through two important continental integration initiatives: the **Digital Transformation Strategy and the AfCFTA**.

CHAPTER 1: RECENT ECONOMIC AND SOCIAL DEVELOPMENTS IN AFRICA

RECENT NUMBERS:

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- Refer to Figure 1.1 for data on Global Economic Growth.

COVID-19: The impact of the pandemic will push between 5 million and 29 million people below the extreme poverty line of $1.90 per day, compared with a baseline 2020 African growth scenario, according to ECA projections (p.11). Moreover, in a best-case scenario, $44 billion would be required across Africa for testing, personal protective equipment and treatment of COVID-19 patients requiring hospitalization and intensive care treatment (p.20). Due to the resources being redirected to COVID-19, Africa's existing health challenges will face spillover costs, as happened in the Ebola crisis. Thus, non-COVID-19 health issues should be kept in view (p.4).

CLIMATE CHANGE: The globally coordinated response to COVID-19 provides a template for climate response in Africa. Since Africa's fiscal space has been further constrained by COVID-19, additional assistance such as debt relief and innovations in mobilizing private sector finance are required for African countries to fulfil their nationally determined contributions to climate action. Increasing seasonal variability, frequency and intensity of droughts and floods, and shifting habitats and agro-ecological zones due to climate change can cause food insecurity, lower trade balances, raise inflation pressure and fiscal imbalances (p. 5).

FINANCING: Despite Africa's growth, many economies remain unsophisticated or undiversified (Figure 1.5). The lack of economic sophistication is explained by low levels of innovation, limited productive capabilities, low investment and poor quality of education (p. 8).

A 2019 study concluded that financial inclusion is a promising channel for translating growth into lower inequality (Demir and Murinde, 2019). It found that financial inclusion could increase opportunities enabling firms to develop business, create jobs, increase the incomes of its employees and their households and in turn enable people to increase their investment in education and health. A study in Kenya found access to mobile money services increased savings by more than a fifth among women and allowed 185,000 women to develop business or retail activities (Demirgüç-Kunt et al., 2018), (p.20).

Bank financing to the private sector remains low, and usually does not fit the needs of the private sector since about 60% is short-term (with a tenor of less than one year), (p.14).

CHAPTER 2: THE PRIVATE SECTOR IN AFRICA

A robust and vibrant private sector is vital for inclusive and sustained economic growth. Indeed, the private sector is the engine of economic growth (p.28).

SMALL AND MEDIUM ENTERPRISES (SMES): The productivity gap between SMEs and large firms is explained by the low-value-added and labour-intensive sectors in which SMEs predominantly operate, their limited use of technologies and their low participation in foreign markets (ITC, 2018). Yet, SMEs that export or operate internationally are more productive, contribute more to higher paying jobs, especially in the low-wage segments of the economy, and grow 4% faster than non-exporting SMEs. (p.29)

AGRICULTURE: The financial sector (mainly through bank loans) accounts for about 3% of investments in the agricultural sector, a scantiness explained by the sector's perception as high risk by banks, mainly due to climate risk, and by the low mechanization and weak literacy of farmers, including financial literacy. (p.31)

INNOVATIVE FINANCING: Moreover, these [innovative financial] initiatives should consider World Bank, Food and Agriculture Organization (FAO), African Risk Capacity (ARC) and other development partners' support in risk transfer and insurance solutions to contribute to successful and sustainable climate-risk insurance projects in climate-vulnerable countries. (p.31)

EXTRACTION: Africa is well endowed with natural resources such as minerals, oil and gas (FIGURE 2.2 and FIGURE 2.3). Despite the rich endowments and highly coveted resources, the mining sector has not contributed much to economic development and wealth creation in many countries. Most of Africa's minerals are exported as ores, concentrates or metals without significant value addition, and African countries continue to import inputs the mining sector needs. (p.32)

MANUFACTURING: Although many African countries recognize the importance of manufacturing and industrial development, and have adopted policies to enable those sectors to grow, they are overshadowed by the dark cloud of the lack of investments to implement such policies and strategies. The silver lining is the private sector's potential and the opportunity to attract private investment. (p.35)

SERVICES: Despite its promise, the service sector faces major challenges in moving from consumption-based growth to more durable growth and from subsistence and non-tradable services to services that generate greater value addition and growth (UNCTAD, 2015). Informality, a major feature of the economic and social landscape in Africa, also exists in such service sectors as health, construction, education and agricultural services. (p.38)

FINANCING: The sources of finance can constrain firms. Even if 40 % of large firms have access to credit, 60% of the credit is short-term—that is, with a term of less than one year. (...) Short-term credit is not suitable for infrastructure projects, which require long-term financing. Unless the infrastructure gap can be overcome, firms' financing alone may be insufficient to develop businesses. (p.43)

CHAPTER 3: ACCESSING FINANCING FROM THE CORPORATE BANKING SECTOR IN AFRICA

Most financing mechanisms in Africa are bank-based, and banks are a major source of innovative financing in Africa.

ACCESS TO FINANCING: Access to financing: Large firms tend to benefit more from bank financing than SMEs do, as their track record and scale reduce their risk profile. Smaller, newer companies and those in the informal sector often face higher borrowing costs, if they are able to borrow at all. (p.59)

INCLUSION: The low levels of financial inclusion in Africa mean that there is massive potential for growth if the banking sector can bring financial services to underserved and unserved populations. Expanding inclusion will lead to rising deposits, which banks can lend to retail and corporate customers, enhancing access to housing and assets for retail customers and to financing that can increase capacity for businesses. (p.62)

RISKS: The increasing presence of pan-African banks is driven by the forces of globalization, deregulation and technology. The emergence of a global financial system has opened a wide range of financing options. (...) The 2008 financial crisis did not have a severe impact on African banking sectors, especially in less open economies, but as African banks integrate themselves into the global economy, future global financial crises are more likely to present a severe risk. (p.65)

AGRICULTURAL SECTOR: African farmers are predominantly smallholders who operate in the informal sector and lack financial literacy and legally registered property that they can use as collateral. As a result, banks in Africa view agricultural activities as high risk, and agricultural loans account for only 4 % of bank loan portfolios. To encourage banks to lend to farmers, some governments provide credit guarantees through agricultural development banks or microfinance institutions. (p.67)

MANUFACTURING AND SERVICE: As economies develop and people have more disposable income, domestic consumption rises, spurring expansion of the private sector and a shift from agriculture to manufacturing and service firms. Traditional banks generally step in to meet the financing needs of these new firms. Conventional loans and lines of credit are common among small and medium enterprises (SMEs), but banks can also provide other services, such as trade finance, as firms grow. This can be a critical service for SMEs seeking to grow their business in response to cross-border opportunities (p.68)

POTENTIAL: The SME financing gap remains and unleashing the potential of the private sector to contribute to sustainable development requires strengthening the supporting structures for financial development. (p.70)

CHAPTER 4: TAPPING INTO THE POTENTIAL OF AFRICAN MARKETS

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EQUITY MARKETS: in addition to capital markets, private investments, crowdfunding platforms and other alternative methods of financing are gaining momentum. Currently, Africa represents less than 1% of worldwide private equity markets, but this can be expected to change given the increasing interest of private equity funds in the continent. (p.74)

OBSTACLES FOR STOCK MARKETS IN AFRICA: high transaction costs and fees, lengthy listing procedures, binding and difficult listing conditions, lack of knowledge about stock markets and, in some exchanges, lack of transparency (p.77). In many developing markets around the world, transaction costs are below 1% of the value of the trade, but African exchanges usually charge well over that. (p.76)

INITIAL PUBLIC OFFERING (IPO): With more than 1,200 public offerings completed in 2019, the African IPO market represented 1.4% of the $1.2 trillion worldwide value of IPOs. African markets are expected to experience more capital raising activity as exchanges continue to meet their commitment to capital requirements due to such changes as the Basel III regulatory framework (p.79). Refer to Figure 4.2: Initial public offerings by selected African exchanges, 2014-2019, p.78.

SOVEREIGN AND CORPORATE BONDS: Although the debt market in Africa is dominated by the sovereign bond market, which accounted for more than 80% of all issuances in 2019, a corporate bond market is timidly emerging, with South African companies accounting for more than 40% of corporate bond issuances in 2019. (p.81)

AGRICULTURAL SECTOR: Despite the increasing interest of private equity funds in investing in African agribusiness, the sector remains underfunded due to various factors that compromise investors' returns, such as corruption, bureaucracy, weak logistics, inadequate infrastructure and limited value addition. (p.89)

FINANCIAL PRODUCTS: The growing African middle class will demand more sophisticated financial products and more innovative ways to save–stocks, bonds and other investments–to help them build wealth. The demand for savings vehicles will especially grow as the world population ages and achieves higher levels of education. (p.94)

CHAPTER 5: LONG-TERM FINANCING FOR SUSTAINABLE DEVELOPMENT IN AFRICA

The cost to achieve the SDGs by 2030 in Africa is estimated at about $1.3 trillion a year, according to the United Nations. That could increase to $19.5 trillion as a result of population growth— projected to be 43% over 2015–2030.

FINANCING GAPS: Encouraging governments to mobilize domestic resources and private sources, ensuring more efficient international development financing, and leveraging climate financing will help bridge the substantial development financing gaps. Advancing the private sector and mobilizing private capital presents a transformative approach for achieving development goals. (p.98)

SUSTAINABILITY FINANCING: Despite global, regional and national initiatives aiming to scale up sustainability financing in Africa, efforts at raising capital and financial investments have yet to accelerate the development of environment-friendly, socially responsible and climate-resilient economies on the continent. (p.103)

DOMESTIC FRAMEWORKS: Regulatory and governance frameworks for green, social and sustainability bonds are critical to developing the market. Several African governments have recognized this and have introduced green bond governance frameworks, including independent certification and monitoring of proceeds, that align with international best practice. (p.104)

PUBLIC-PRIVATE PARTNERSHIP (PPPS): Only a few African countries have embarked on PPPs to tap private capital for fi¬nancing infrastructure. Kenya, Nigeria, Uganda and South Africa account for almost 50%. (...) African countries could also learn from other emerging countries that have unlocked flows of private capital into PPPs, including India, China and Brazil. (p.109)

DEVELOPMENT BANKS: African regional and national development banks are pivotal in supporting infrastructure finance, including by catalysing private finance. They should expand in countries where they are active (adding infrastructure finance to their business if they are not already participating in that sector) and should consider going into new countries (p.110). Many African countries find it more practical to seek finance externally for infrastructure projects and direct their development banks to target less equity-intensive sectors of the economy. African national development banks have considerable scope for expanding their scale, which would let them contribute more to financing infrastructure. Refer to the case study "Development bank of Southern Africa operations in South Africa (p.111)

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INCLUSION: In addition to allowing people to access financial services more easily, the migration to mobile and online banking has expanded financial services to people who have long been unserved by financial institutions, whether because they live in an underserved area or because they lack the documentation to open a bank account. (p.127)

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FINANCIAL INCLUSION: Education and telecommunications infrastructure remain critical to greater financial inclusion in Africa. Higher literacy and educational attainment rates will make participation in the financial system easier and more attractive, increasing demand for more variety in financial services. This demand will open space for new entrants and products in the financial services industry. (p.132)

FRAUD CONTROL: Growth projections and forecasts for alternative financing and other crowdsourcing instruments in Africa are very promising, but the market faces a major challenge: controlling fraudulent activities. Crowd-based financing for business activities benefits markets only if borrowers and investors trust one another. Establishing binding rules and guidelines is essential to securing that trust. (p.121)

CHAPTER 7: REGULATIONS TO SUPPORT FINANCING

Africa needs to rethink its financial services regulation so that innovation is fully functional, the environment enables innovation, transparency is enhanced, and financing for private sector development is delivered.

FINANCIAL REGULATION AND INCLUSION: Two different approaches characterize analysis of how the development of financial regulation affects inclusion and growth. The "growth-enhancing governance" approach seeks direct evidence of financial regulation's impact on development outcomes. A less direct approach studies how regulations contribute to resource mobilization and allocating supporting investments, promoting inclusive development (ECA, 2019). (p.136 and p.142)

BANKING REGULATIONS: Financial sector reform has had three distinct phases across Africa, and the evolution of the sector has shown a number of key trends. Read more about that on p. 137.

MACROPRUDENTIAL REGULATIONS: By emphasizing collective behaviour, they can tighten the link between prudential regulation and development policy. (...) Macroprudential policy can boost economic growth to enhance the financial sector's contribution to a country's development. (p.139)

REGULATORY CHALLENGES: Regulations that concern the banking sector alone may be insufficient to safeguard the financial system against some of the risks fintech services pose, such as data privacy, money laundering, mismatched risk and return, and systemic risk. These new risks call for financial regulation to be reviewed to provide a flexible environment for fintech to develop that is strict enough to limit the risks. (p.143)

RISKS: Many African economies are dominated by a small number of sectors, normally the producers of cash crops or natural resources, such as oil and gas. Bank lending tends to concentrate on firms and households in those sectors, so great macroeconomic risks are associated with lending portfolios vulnerable to commodity risk. (p.146)

MACROPRUDENTIAL MEASURES: A healthy balance between safeguarding the economy from financial contagion and allowing financial operators to conduct their business will require carefully tuning and sequencing macroprudential measures. African central banks and academic economists must study which macroprudential instruments can combat the harm caused by shocks, and what circumstances call for particular instruments, table 7.1, p.147.

CHAPTER 8: CONCLUSIONS AND POLICY RECOMMENDATIONS

This chapter summarizes the key aspects of innovative financing for the development of the private sector in Africa. Five elements are key (refer to Figure 8.1)

1 - **Financing innovations can arise from multiple sources simultaneously.** Businesses need to consider leveraging different sources according to their financing needs (banks, fintech, financial markets, capital markets, development banks)

2- **A transparent and effective regulatory institution** is mandatory to minimize risk and oversee the financial operations of firms and peer institutions.

3- The **absence of a sound eco-system can impede firms** even when financing is readily available. This affects firms of all sizes, depending on their stage in the growth cycle.

4- **Innovative financing** of the private sector and business growth **generates**: firm value added, gainful employment, tax revenue for government, stable investment returns for entrepreneurs, growth of financial institutions.

5- The **transformation** from innovative financing and from a fully operational financial sector to economic growth, lower inequality and reduced poverty is long term and **necessarily involves feedback mechanisms.**

INNOVATIVE FINANCING: Even so, the financial system in Africa needs faster diversification. A full range of financial institutions should offer innovative financial products tailored to the specific needs of the business ecosystem—such as start-ups, marketing, transportation and payment collection. (p.155) Addressing the huge financing gaps will require more innovative financing solutions in retail and corporate banking, plus robust legal, institutional and regulatory frameworks to unlock bank credit to Small and Medium Enterprises (p.160).

REGULATION: The report recommends that public policymakers (including central banks) consider amending banking and financial services legislation to enable innovative private sector funding. The process could lead to lobbying, opening for debate a range of banking and financial service issues. (p.164)