"Representing the Venture Capital and Private Equity Industry in Africa"

Unlocking Venture Capital and Private Equity for Our Common Interest

AVCA response to UK Commission for Africa Report

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About AVCA

"The **African Venture Capital Association** **(AVCA)** represents the private equity and venture capital industry in Africa. AVCA was established in 2002 and its head office is in Yaoundé, Cameroon. AVCA's membership is drawn from across Africa and internationally. AVCA's objectives are to represent the industry within Africa and internationally, stimulate the growth and expansion of the industry throughout Africa, stimulate professional relationships and co-operation, provide opportunities for professional development of industry practitioners, research, publish and circulate industry information and insights, provide policy makers with proposals to improve the corporate, fiscal and legal environment for the industry, maintain high ethical and professional standards and contribute to the management development of investors, investees and other stakeholders. AVCA's activities include an annual industry conference, a quarterly newsletter, research, and training and advocacy programs. For more information visit the AVCA website **www.avcanet.com**."

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Executive Summary

'AVCA welcomes Tony Blair and Gordon Brown's commitment to alleviating poverty in Africa.

We give a resounding welcome to the UK Commission for Africa's Report and appreciate the extensive and comprehensive work behind the recommendations that have been drawn up and we fully endorse its aims.

We do however believe that much greater emphasis needs to be placed on private sector led initiatives and on the positive role that venture capital and private equity can play and suggest a much greater proportion of the financial resources be allocated to this'

This document presents the African Venture Capital Association's (AVCA) response to the Commission for Africa (CfA) report published in March 2005. The CfA report recommends a series of actions to provide crucial support for the Millennium Development Goals (MDGs) for Africa. Central to the CfA's recommendations is a call for an additional $25 billion annually in aid over the next three to five years, with an additional $25 billion annually subject to review.

AVCA gives a resounding welcome to the CfA's report and appreciate the comprehensive work behind the recommendations that have been drawn up and we fully endorse its aims. We do however believe that much greater emphasis needs to be placed on private sector led initiatives and on the positive role that venture capital and private equity can play and suggest a much greater proportion of the financial resources be allocated to this.

AVCA makes four main recommendations to be included in the CfA's recommendations to the EU and G8 governments. These are the establishment of:

- An **African Venture Capital Technical Assistance Fund** (AVC-TAF) to support and improve the performance of SME investors in Africa
- An **African Venture Capital and Private Equity Fund of Funds** (AVC-FOF) as an incentive to further capital provision
- An **African Venture Capital and Private Equity Tax Relief** (AVC-TR) scheme to encourage more private investment in African Private Equity
- **Capacity Building for AVCA**, which as the only pan-African representative of the African venture capital and private equity industry, is well positioned to promote and stimulate the industry

The contribution of the private sector to Africa's continued development requires further emphasis and in this response, AVCA draws attention to a direct relationship between private sector investment and poverty alleviation in Africa. Enterprises backed by venture capital and private equity are confirmed as key drivers of growth and sustainable development. The investors' local expertise and flexible approach to financing have resulted in significant growth and profitability for the companies involved. The consequent impacts these companies have had on their local communities (and the wider economy) cannot be overstated. They provide employment, education, skills, healthcare, infrastructural development, housing, security and are an enduring source of opportunity and empowerment to Africa's most needy.

This view is echoed by industry guru Alan Patricof (co-founder of Apax Partners, a leading international venture capital and private equity firm). His recent article published in the Milken Institute Review (second quarter 2005) is featured in the section titled "The case for venture capital" and makes several recommendations for the improvement of the private investment climate in poor countries.

AVCA also draws on the insights of the UN Millennium Project Task Force on Science, Technology and Innovation, who support the use of public resources to encourage and leverage private investment into venture capital.

AVCA would like to thank all contributors to this report including Emerging Markets Partnership (EMP) and Aureos Capital for providing case studies originally published as part of their respective Social and Development Impact reviews. These case studies illustrate the important contribution of private sector investments to poverty alleviation in Africa.

AVCA sincerely hopes the Commission, EU and G8 government's responds to this opportunity to unlock and maximise the development impact of venture capital and private equity in Africa.

Introduction

'AVCA therefore gives a resounding welcome to the Report… We do however believe that much greater emphasis needs to be placed on private sector led initiatives and on the positive role that venture capital and private equity can play and suggest that a much greater proportion of the financial resources should be allocated to this'

Poverty, conflict, the AIDS pandemic, environmental damage and economic stagnation are the problems that cripple the development of Africa today. Action is urgently needed to address these problems and the UK Commission for Africa has drawn up a list of hard-hitting recommendations which call for action on the part of African governments and on support from developed nations to halt the continent's further decline.

The Commission's Report (published in March 2005) represents a bold commitment to Africa which should support and give a much-needed boost to the implementation of the Millennium Development Goals (MDGs) for Africa which have fallen far behind their proposed schedules. In fact, the Report calls for a programme of action that will make sure the Millennium Development Goals do not "perish as yet another pious action".

AVCA therefore gives a resounding welcome to the Report. We appreciate the extensive and comprehensive work behind the recommendations that have been drawn up and we fully endorse its aims. We do have considerable reservations, however, on the way in which the Report has made so little financial provision for the promotion and encouragement of venture capital and private equity – both vital components of economic growth. But before we expand on this, it is useful to look at a summary of the Report.

Case 1: Brookside Dairy Ltd.

CfA recommendations

'… in Strengthening the Quality and Use of Data, the Report points out the vital need for improved information systems which make possible the implementation of all the above recommendations.'

The Report addresses the following areas.

Getting Systems Right looks at Governance and Capacity Building. The main issues here are the **Capacity to Deliver** – which includes an examination of the role of professional skills, incentives and the improvement of infrastructure. **Accountability** is concerned with national justice systems and the role of local governments, constitutional and traditional leadership structures in guaranteeing rights and upholding the law for all sectors of society. **Transparency** covers the role of the international financial institutions and the management of revenues from natural resources, pointing out that increased openness about policies and decisions reduces the scope for inequitable allocation of resources. **Corruption** addresses the problem of bribes, corrupt government procurement of goods and services, and stolen (public) assets. The Report recommends that export credit agencies insist on higher standards of transparency in their support for projects in developing countries. Finally, in **Strengthening the Quality and Use of Data**, the Report points out the vital need for improved information systems which make possible the implementation of all the above recommendations.

The Need for Peace and Security. Good governance and economic and social development are impossible during war - and over the last 40 years, Africa has experienced more violent conflict than any other continent. The Report therefore, in **Building Peaceful Societies**, looks at the way that aid, arms' control, the management of natural resources and corporate activity can promote security and reduce violence. In **Regional and Global Capacity to Prevent and Resolve Violent Conflict**, it calls on other nations to ensure external support for African security and the strengthening of the mediating and preventative role of the United Nations. When fighting ceases, the Report sees the importance of immediate measures towards planning, co-ordination and financial assistance in **Building Peace.** This includes the creation of a permanent $250 million Peace-building Fund, expanding the World Bank's current fund which stands at only $30 million. An adequate financial commitment to post-conflict development is crucial.

Leaving no-one Out: Investing in People. Education, disease prevention, basic sanitation and the problem of social exclusion are tackled in this section of the Report. The poorest

CfA recommendations

‘… the aim is to alleviate widespread poverty by concentrating on the drivers of growth… the private sector has a central role to play in driving growth...’

people in Africa are now excluded from the most basic services of the state; and a healthy and skilled workforce is a vital building-block of economic growth. The first step is **Eliminating Preventable Diseases**: this means new priorities for delivering healthcare, a more co-ordinated approach to donor-funding and improved methods of disbursing funds. There will be a major drive towards **Expanding Water Supply and Sanitation**. The **HIV and AIDS** pandemic will receive nearly half the extra aid that the Report recommends should be spent on the priorities outlined by this section – using existing systems rather than introducing confusing parallel new ones. There needs to be increased support for the growing number of AIDS-orphans and a drive towards the promotion of sexual education. The Report refers to a recent study suggesting that “in countries with an adult prevalence over 20 per cent, GDP will be reduced by 67 per cent after 20 years due to the impact of AIDS”. In these countries, unless urgent measures are taken, economic performance will grind to a standstill – outpaced by the increased costs of the AIDS pandemic.

In **Going for Growth and Poverty Reduction**, the aim is to alleviate widespread poverty by concentrating on **The Drivers of Growth**. The goal is to increase the average growth rate to 7 per cent by the end of the decade and to sustain it. Challenges include **Urban Development**- making African cities (housing the fastest growing urban population in the world) engines of economic development rather than simply unstructured migration centres for the dispossessed rural poor. This means that they need to attract international investment. In **Agriculture and Rural Development**, the Report recommends the encouragement of local and regional markets and the fostering of small enterprises, acknowledging that the private sector has a central role to play in driving growth. “The challenge for sub-Saharan Africa is to unleash its entrepreneurial potential by improving its **Investment Climate**”. Currently 80 per cent of Africa’s investment comes from Africa – but improvements in the domestic climate will also make that climate more attractive for overseas investors.

CfA recommendations

'…the Report urges a sea-change in the way the business community engages in the development process – and recommends measures which will facilitate business and private investment working in partnership with national governments, donors, and civil society

Among international investors' key concerns are policy unpredictability and macro-economic instability – as well as complicated strangleholds of red-tape and regulations and, for example, a lack of access to property rights. The Report recommends identifying the obstacles to investment and taking action to make the investment climate favourable. It also makes a commitment to "double **infrastructure** spending" in Africa with an initial increase in donor funding of $10 billion per year up to 2010 and, subject to review, a further increase of $20 billion in the following five years. Rural roads, transport, power-projects and small-scale irrigation systems are just a few of the areas of infrastructure that need to be improved in order to attract private equity investment to towns and regions. The Report also urges a "sea-change" in the way the business community engages in the development process – and recommends measures which will facilitate business and private investment working in partnership with national governments, donors, and civil society. Finally, it suggests the establishment of a **$100 million Africa Enterprise Challenge Fund** to support private sector initiatives that contribute to small enterprise development.

More Trade and Fairer Trade. Here the Report examines how African producers can be helped to break into world markets. At the moment, indefensible trade barriers impose punitive tax restrictions on the continent's goods as they enter the markets of developed countries. Among the preconditions of growth in trade is a **reduction** in **Commodity Dependency**, a **reduction** in the burden of **Debt** and improvements in infrastructure, good governance, **Regional Co-operation** and an increase in private sector participation. It acknowledges that excessive bureaucracy, corrupt public servants and tangled red tape must be streamlined or weeded out. "It must make it easier to set up businesses". All this creates an **Enabling Environment for the Private Sector**. But, quoting Brazilian President Lula's description of the "new geography of trade and economics", the Report also issues a powerful challenge to rich nations: to dismantle the barriers they have erected against African goods and to abolish trade-distorting subsidies to their own agriculture and agribusiness which gives them an unfair advantage. They must not only **lower tariffs** and other barriers to African products but they must demonstrate their commitment by completing the current world trade talks in Doha and by not there demanding reciprocal concessions from poor African nations.

CfA recommendations

‘AVCA welcomes the Report’s encouraging faith in Africa’s entrepreneurial potential and the wide-ranging beneficial economic impact made by private investors throughout the continent’

Furthermore, Africa must be provided with funds to help it adjust to the new opportunities of a changed international trading regime.

In the final two chapters - **Where Will the Money Come From: Resources**, and **Making it Happen** - the Report answers the question: **Can Africa Finance a Big Push without Extra Aid?** To support the changes necessary for growth in Africa, the Report calls for an additional $25 billion in aid a year – to be implemented by 2010. Subject to review, a second $25 billion a year would be forthcoming by 2015. To ensure that the money is spent as productively as possible, it is necessary that good governance in Africa prevails and that the quality of aid and the means of its delivery are improved. It is important that donors are harmonised both with other donors and the priorities, procedures and systems of individual African governments. The Report goes on to recommend not only that rich nations should commit to a timetable for giving 0.7 per cent of their annual income in aid, but that in order to provide aid urgently needed now, it should be **front-loaded.** The Report recommends that “the best way” is to “**put aid into African government budgets** and let them prioritise the spending of it. The direct budget support ensures that aid goes most effectively to the government’s agreed development priorities’. And for poor countries the objective must be “**100 per cent debt cancellation**” – to be implemented as soon as possible. AVCA welcomes the Report’s encouraging faith in Africa’s entrepreneurial potential and the wide-ranging beneficial economic impact made by private investors throughout the continent**.**

Case 2: Mount Elgon Orchards.

The case for venture capital

It is necessary however to put the case more specifically for venture capital and private equity investments. Enterprises, including Small and medium-sized enterprises (SMEs), supported by venture capital and private equity investment are vital in bringing economic growth and sustainable development to African economies. Venture capital and private equity financing can add significant advantages to the investment recipient, such as access to a national and international networks of suppliers, producers and consultants, gain of critical mass, attraction of world class management and facilitation of regional and international business expansion.

'It is necessary however to put the case more specifically for venture capital and private equity investments…vital in bringing private sector led economic growth and sustainable development to African economies'

By way of example, in *Investing for the Future*, the Social Impact Review, AVCA member EMP (Emerging Markets Partnership) Africa highlighted the social "ripple effect" that their African portfolio companies have instigated.

There are 32,000 employees in EMP's Africa Fund 1 (US$407.6 million) of which 97 per cent are African. Twenty two per cent of those are women and this percentage is rapidly increasing. The employment effects are magnified by examples of indirect employment. Several thousand smallholder rubber farmers, for example, sell raw rubber to SIPH (an EMP portfolio company) through an outgrower programme which provides technical assistance, credit and access to rubber markets – and a transparent pricing mechanism. Tens of thousands of shop-owners in 14 countries make a profit on the pre-paid phone cards sold by Celtel. And the Moroccan fertiliser company Charaf gives seasonal employment to hundreds of truckers in the peak planting time.

But the impact of EMP's portfolio companies extends far beyond job creation and training in the country the investment was made. One hundred per cent of their companies provide comprehensive health benefits to their employees and/or their dependants. Fifty four per cent have formal pension plans for employees and 63 per cent offer educational and training opportunities. Seven companies offer benefits that include provision for religious holidays and transportation.

The companies have played an important part in the expansion of the private sector in Africa, freeing companies from often restrictive state ownership and monopolies and contributing to the liberalisation of a range of sectors. Celtel, for example, has purchased the Tanzania

The case for venture capital

'By introducing new standards of transparency, fairness, accountability and honesty, they have made their portfolio companies more attractive to investors.'

Telecommunications Company from the Tanzanian government. Air Ivoire, formerly the state-owned national airline of Cote d'Ivoire, had stopped operating in 1999. It was re-launched in 2002 as a joint venture between Africa Fund1 and Air France. Charaf, one of the first privately-owned fertiliser companies in Morocco, broke the monopoly of a state-owned firm – therefore giving local farmers greater choice.

High standards of corporate governance are expected from EMP companies. By introducing new standards of transparency, fairness, accountability and honesty, they have made their portfolio companies more attractive to investors.

The charitable donations made by private sector companies are crucial to the building of schools, hospitals and other facilities in local communities. Celtel spent $5 million in charitable donations – mainly to the refurbishment of schools and clinics. Globaleq spent $1 million on several local projects including the provision of drinking water and a new jetty for villagers on Songo Songo Island, Tanzania.

EMP requires all its investee companies to undertake an assessment survey to evaluate the environmental effects of its operations. Veolia Water Maroc, for example, is to invest $370 million in a comprehensive waste water system which will prevent the discharge of sewage into the Bay of Tangier.

A single example from Aureos – also a member of AVCA – in their *Annual Development Impact Review 2004* is instructive. The Nairobi-based fast food business Hoggers was founded in 1985 by two brothers, Abdul and Farid Mohamed, who initially opened four outlets. Their turnover was disappointing and in 1996, they sold the outlets and with an injection of capital from an independent investor, purchased the franchise of a South-African fast-food chain and opened several branches in various parts of Nairobi.

By 1997, the Mohamed brothers wanted to extend outside Nairobi and sought financing. They considered commercial debt to be too expensive and they did not have adequate collateral, so they invited Acacia (an Aureos Fund) to take an equity stake in Hoggers. Acacia had a major influence on the management and governance of the company, instituting a board of directors and focusing attention on rigorous financial analysis. Hoggers has now returned 70 per cent of Acacia's invested capital and the

The case for venture capital

‘In the UK, the venture capital and private equity industry supports close to one in five private sector jobs. In the US, venture backed companies employ one in ten jobs…..the African venture capital industry has the potential to generate one in ten required jobs in Africa’

Mohammed brothers are working with Acacia to plan a long-term strategy to promote further growth.

Hoggers’ staff levels have climbed from 210 in 1998 to 276 in 2003. The average age of employees is 26 and remuneration is above the minimum wage. All staff receive meals while at work and medical benefits. The company’s emphasis on high standards of training and hygiene has led Hoggers’ competitors to raise their own standards.

The main components in Hoggers’ food products are chicken, beef and potatoes. Ninety per cent of these are sourced in Kenya. The chicken comes from Kenya’s largest chicken producer and accounts for roughly 15 percent of their entire sales. Beef represents 7 percent of the output of a local beef supplier. And 12 local farmers supply the potatoes – in the case of one of the farmers, Hoggers accounts for 90 per cent of his crop.

From the micro to the macro…

In the UK, the venture capital and private equity industry **supports close to one in five** private sector jobs. In the US venture capital backed companies **employ one in ten** jobs. With the right policies, incentives and investment, the African venture capital and private equity industry has the potential to create and support one in ten required private sector jobs in Africa. AVCA is determined to unlock this potential.

The Commission for Africa has the opportunity to mobilise EU and G8 support to create the specific international policies and incentives, AVCA recommends in this report, to unlock private investment into and strengthen the African venture capital and private equity industry.

The case for venture capital

Alan Patricof, Co-founder of APAX Partners and international venture capital industry guru supports AVCA's call for enabling policies, technical assistance and incentives to private investors ….

In recent articles in the Financial Times and the Milken Institute Review, industry guru Alan Patricof (co-founder of Apax Partners, a leading international venture capital and private equity firm) calls for enabling public policies, technical assistance grants, investment funds and incentives to Diaspora and other private investors to promote equity capital in SMEs in recognition of the development impact of these enterprises.

Writing in the Milken Institute Review (second Quarter 2005), Patricof and Julie Saunderland (a private consultant specialising in small businesses) explain that "Like their counterparts in wealthy nations SMEs – in poor countries are responsible for a disproportionate amount of innovation, growth and employment compared to the resources they consume. Yet… they have little access to the long term capital they need to grow." The following are extracts from their article.

SME: An Acronym for Economic Success:
We see the need for a three pronged approach to encourage the flowering of SMEs in poor countries. First governments must reform their business environments, with the focus on easing regulation and stemming the corruption that feeds on it. Second, access to capital for these enterprises must be expanded, with government- or donor-supported capital augmenting private sources. Third entrepreneurs and managers of SMEs need access to skills gleaned from practical experience and international best practice.

All three concepts are familiar to development specialists. The insight that has been lacking is that all three must be pursued simultaneously; with any component missing, competitive businesses will not take root….success turns on long-term commitment from governments and international organisations as well as investors. Wealthy nations should follow up on the findings of the UN Commission on Capital Flows to Africa (an initiative of the Corporate Council for Africa in the United States, along with the Washington based Institute for International Economics) by making support for small business an explicit objective of development policy.

Access to Capital:
Foreign donors must accept the reality that, in the short term, they need to provide a portion of capital at below-market returns. But market should still rule; programs to deploy below market capital should leverage private investment in the SME sector (through

measures like guarantees, co-financing and tax breaks) rather than crowding it out.

Though governments and international organisations have tried to invest capital directly in small businesses, bureaucrats have neither the information nor the incentives to invest wisely. Programs to finance SMEs have only succeeded where this responsibility stayed in the hands of private investors, even as governments or donors provided incentives to balance the risk reward equation. Local investors are more likely to have the specialized knowledge and connections critical for effective investment decisions. Equally important, if local private capital is at risk in small businesses, the elites are more likely to support government policies that sustain the sector's development …. programs need to be implemented in co-operation with foreign experts, and intensive training and mentoring programs for local investment professionals should be part of the package.

Remittances from expatriates represent another source of capital for the SME sector. To encourage expatriates to use transfers for investments, wealthy countries could provide tax incentives to those who invest in key sectors back home.

Remittances from expatriates represent another source of capital for the SME sector. Indeed, remittances provide an estimated $150 billion annually to developing countries – triple the flow of development aid. To encourage expatriates to use transfers for investments, wealthy countries could provide tax incentives to those who invest in key sectors back home.

Assistance to Small Business:
Access to capital is necessary - but far from sufficient – to exploit opportunities for small businesses. Managers must also acquire the skills to run modern organisations that can compete in export markets. Thus, part of the capital provided by donors on a pure grant basis should be dedicated to training and mentoring. Formal training and consulting can lay the groundwork for acquiring technical skills.

Time for Action:
For a host of reasons, which boil down to enlightened self-interest, we think it is time for the United States to take bold action on the model of the Marshal Plan and Peace Corps. Helping to build indigenous companies that are both capable of competing globally and committed to establishing the institutions of capitalism will create the conditions for growth, stability and equality.

Alan Patricof served as vice chairman of the Commission on Capital Flows to Africa and as a member of the UNDP's Commission on Private Sector and Development.

The case for venture capital

The UN Millennium Project's Task Force on Science, Technology and Innovation explains that "…attracting venture capital and encouraging "angel" (private) investors can increase finance for technological innovation…"

The UN Millennium Project, directed by Professor Jeffrey Sachs, Special Advisor to the UN Secretary General on the Millennium Development Goals (MDG's), Task Force on Science, Technology and Innovation in its recent report on Achieving the MDG's identify the main sources of financing for technological innovation as banks and financial institutions, individual private investors ("angels") and public funds.

The task force identify a number of ways that governments can take a variety of steps to increase access to financing for science, technology and innovation including:

- Create sound monetary and financial policies
- Provide additional capital incentives. This could be geared toward venture capitalists through specific policies that support SME's engaged in developing technologies of particular interest.
- Establish a government-funded venture type investment strategy
- Help capital to become professionally managed.

Attracting venture capitalists and angel investors

The task force explains that "attracting venture capital and encouraging the emergence of "angel" (private) investors can increase finance for technological innovation. SME's have flourished in most developed countries because of the critical role that capital markets, especially venture capitalist markets, have played. Venture capitalists do not just bring money to the table, they help groom start-ups into multinational institutions. Bringing venture capital markets into developing countries could help ensure the sustainability of the companies in which they invest. This realisation is forcing developing countries to start reforming their venture capital systems.

The task force concludes that if a developing country is to unlock the potential to turn science, technology and innovation into business opportunities, it needs to undertake a number of core activities. These include providing broader incentive structures to all firms while creating an institutional environment that encourages entrepreneurship, rewards innovation and fosters start-ups, and sustains existing firms with injection of capital.

Case 3: Micro Kenya

Gaps in the current CfA report

‘…the Africa Commissions Report now has an opportunity to adopt the specific recommendations in this report to encourage and enable venture capital and private equity investment in Africa.

Considering the widespread advantages represented by venture capital and private equity investment, the Africa Commission’s Report now has an opportunity to adopt the specific recommendations in this report to encourage and enable venture capital and private equity investment in Africa. As well as recognising the importance of the private sector in promoting growth, the Africa Commission has the opportunity to offer policy and financial incentives to practitioners and private sector investors.

AVCA would like to see more funding commitments and policy incentives to back up the Report’s call for further engagement from the private sector.

Channelling additional aid

In addition, AVCA notes the Report’s recommendation that ALL support in the form of additional aid ($25 billion a year) should be channelled directly into African governments’ budgets (Page 57). The Report states that, where development strategy is lacking and budget systems are not open and transparent, aid should be channelled using a sector-wide approach and where governance is too poor for donors to have confidence in sector-wide approaches, aid may best be paid into specific projects run by aid agencies or other non-governmental organisations”.

AVCA recommends that in all three circumstances (channelling aid through government budgets, sector wide approaches or specific NGO projects), the *delivery* of public services (health, education and public infrastructure) and economic growth should be private sector led, with an emphasis on indigenous private enterprises creating opportunities for venture capital backed growth enterprises. This private sector delivery approach is similar to current UK policy where an increasing proportion of new public infrastructure, including schools and hospitals in the UK, are delivered using the Private Finance Initiative (PFI) and Public Private Partnership (PPP).

AVCA believes that without this emphasis on delivery by indigenous growth businesses there is a risk that channelling all additional aid into government budgets could result in and reinforce a “contract mentality” by which entrepreneurial Africans jostle for their next government contract – in *any* sector. This mentality crushes entrepreneurial motivation and the pursuit, central to the venture capital industry, of growth.

Case 4: An Exemplary Portfolio

AVCA recommendations

AVCA therefore recommends that the Commission look at further incentives that would promote private investment in African enterprises.

Specifically, AVCA recommends the CfA includes in its recommendations to EU and G8 governments, the establishment of the following:

1. An African Venture Capital Technical Assistance Fund (AVC-TAF).

2. An African Venture Capital and Private Equity Fund of Funds (AVC-FOF)

3. An African Venture Capital and Private Equity Tax Relief (AVC-TR).

4. Capacity Building Fund for AVCA

A brief description of each recommendation is provided below.

‘AVCA calls on the CfA to include AVCA’s recommendation to EU and G8 governments to establish a $50 million a year African Venture Capital Technical Assistance Fund, a $500 million African Venture Capital Fund of Funds, $200 million a year African Venture Capital Tax Relief and $1.5 million Capacity Building Fund for AVCA”

1) African Venture Capital Technical Assistance Fund (AVC-TAF)

AVCA wholeheartedly supports the Report’s recommendation to establish a $550 million Investment Climate Facility, a $100 million Africa Enterprise Challenge Fund and additional support for the UNDP Growing Sustainable Business program. However, AVCA also recommends the establishment of a separate African Venture Capital Technical Assistance Fund (AVC-TAF).

The African Venture Capital Technical Assistance Fund will be disbursed as grants to fund training, information systems infrastructure, deal origination, deal selection and other overhead costs incurred by SME venture capital fund managers. These are additional costs that can reduce the performance of SME funds (and their attractiveness to investors) because they choose to focus on many smaller companies who require more “hand holding” as opposed to fewer larger companies – as is typical of US and UK style private equity.

We estimate that a technical assistance fund of $50 million a year for 10 years could support and generate up to $5 billion of venture capital investment over 10-15 years. This would be particularly aimed at SMEs and would encourage further investment in African businesses – particularly by the African Diaspora which represents a large pool of untapped investment potential.

AVCA recommendations

2) An African Venture Capital and Private Equity Fund of Funds (AVC-FOF)

AVCA recommends EU and G8 governments set up a private sector run African Venture Capital Fund of Funds (AVC-FOF) to act as subordinated investment capital.

AVCA propose that the AVC-FOF is run by a small team (3-5) of highly experienced African and International venture capital and private equity practitioners. The AVC-FOF team will identify, select and invest funds in local African venture capital and private equity funds that set targets for the development impact of their portfolio companies.

‘…the Report has missed the opportunity to consider the ways in which successful UK government efforts to support investment in venture capital and private equity (in the UK) might be used to advantage in Africa’

Similar funds of funds have been set up in Israel and other countries to positive effect.

AVCA propose an initial $250 million AVC-FOF expanded to a $500 million fund when it is fully invested and upon review.

The AVC-FOF will also aim to leverage additional private investment into the African funds from local African and international individual, corporate and institutional sources including the African Diaspora.

3) African Venture Capital and Private Equity Tax Relief (AVC-TR)

AVCA recommends that EU and G8 governments implement tax incentives for investors in African private equity.

We believe, for example, that the Report has missed the opportunity to consider the ways in which successful UK government efforts to support investment in venture capital and private equity (in the UK) might be used to advantage in Africa – as well as similar efforts to encourage charitable giving.

Community Investment Tax Relief is used in the UK to stimulate private investment in under-invested communities. A tax incentive, consisting of a form of tax relief, is available to individuals and companies that invest in accredited intermediary organisations, which in turn invest in enterprises that operate within or for disadvantaged communities.

AVCA recommendations

‘Under a British Government tax-relief scheme, the investor’s income tax or corporation tax liability is reduced. The relief is worth up to 25 per cent of the money invested, spread over five years. The scheme can benefit individual as well as corporate investor’

These intermediary organisations are known as **Community Development Finance Institutions** (CDFIs), which specialise in investing in businesses, social and community enterprises within under-invested areas. To keep its accreditation, the CDFI must comply with certain terms and conditions. Among other things, it must report annually to the Small Business Service on its operations and it cannot, for example, hold land with the aim of benefiting from a rise in its value or invest in residential property.

Under a British Government tax-relief scheme, the investor’s income tax or corporation tax liability is reduced. The relief is worth up to 25 per cent of the money invested, spread over five years.

The scheme can benefit **individual** as well as **corporate investors.**

For example: An individual investor has a reduction in his income tax liability. Someone who subscribes £10,000 for shares in a CDFI on 1 June 2004 can claim relief on £10,000 for each tax year. Therefore, tax relief of £500 (five per cent of £10,000) may be claimed for the tax year 2004/5, and for each of the four subsequent tax years.

For corporate investors, the CITR scheme reduces the investor’s corporation tax liability for a) the accounting period in which the date of the investment falls, and b) each of the accounting periods in which the subsequent four anniversaries of that date fall.

The CDFA's 2004 *Inside Out* report, launched on 22 April 2005, shows the sector provides financing of nearly £150m – a 40% growth in portfolios on 2003 – to disadvantaged customers who are unable or unwilling to access finance from commercial sources.

With support from key public and private sector partners this growing and innovative sector has established itself as a credible force for social change. According to *Inside Out*, Community Development Finance Institutions (CDFIs) have so far, financed more than 9,500 businesses and individuals; sustained more than 85,000 jobs; created more than 10,000 jobs; and leveraged another £160,000,000 in additional funds.

AVCA recommendations

'AVCA is an important part of the continued development of the industry in Africa and the association is well placed to promote policy and best practice, hold stakeholders to account, provide industry wide benchmarks, analysis and insights, provide training and capacity building opportunities for practitioners and proactively unlock the development potential of private equity in Africa'

Venture Capital Trusts (VCTs) currently offer another incentive to investment in UK-based companies. They aim to encourage investment in unlisted UK companies by offering private investors tax back for an investment commitment that lasts three years. An accredited list of private equity firms who manage VCTs is available.

*At the moment, Community Investment Tax Relief and Venture Capital Trusts are restricted to investors in UK companies. We would recommend that the restriction be expanded to accommodate **African companies** who would then benefit from further private investment.*

We estimate that based on 25% tax relief, a commitment of $200 million a year towards an African Venture Capital Tax Relief scheme will generate up to $10 billion in investment capital over 10 years.

4) Capacity Building Fund for AVCA

AVCA is the only pan-African business association that represents the venture capital and private equity industry across Africa. AVCA members include fund managers operating in Tunisia, Morocco, Egypt, Senegal, Togo, Ghana, Nigeria, Kenya, South Africa, Uganda and other African countries.

AVCA is an important part of the continued development of the industry in Africa and the association is well placed to promote policy and best practice, hold stakeholders to account, provide industry wide benchmarks, analysis and insights, provide training and capacity building opportunities for practitioners, and proactively unlock the development potential of private equity in Africa.

Current AVCA initiatives include:

- An ***AVCA Benchmark Review of the Tax and Regulatory Environment*** for venture capital and private equity in Africa
- An ***AVCA Millennium Development Goal One-In-Ten*** project to set and monitor targets for the industry to employ one in ten required private sector jobs in Africa
- An ***AVCA Public Private Partnership (PPP) Initiative*** to identify how the industry can support Public Private Partnerships

AVCA recommendations

‘AVCA can play a pivotal role in setting up the African Venture Capital Fund of Funds, African Venture capital Technical Assistance Fund and African Venture Capital Tax Relief scheme’

- ***AVCA How to Develop a Venture Capital Industry*** to help African governments and countries (identify and target stakeholders to) develop their local venture capital industries
- ***AVCA 5th Annual African Venture Capital Conference*** in Mombassa, Kenya on 6-9 November 2005
- ***AVCA Publications*** including the 1st AVCA Annual Yearbook, 1st Annual AVCA Investment Activity Report, Case Studies in African Venture Capital and Private Equity, A Guide to Venture Capital and Private Equity in Africa, Who’s Who in Venture Capital and Private Equity in Africa and an Economic and Social Development Impact of Venture Capital and Private Equity in Africa.
- ***AVCA Training Programs*** including a foundation program for practitioners.

AVCA is currently seeking additional grant funding of up to €1.2 million ($1.5 million) a year to implement a number of its initiatives.

AVCA’s current initiatives can be expanded to deliver the recommendations in this report.

AVCA through its member’s portfolio companies has access to an estimated 1,000 enterprises in Africa and the Association can play a pivotal role in setting up the African Venture Capital Technical Assistance Fund (AVC-TAF), African Venture Capital Fund of Funds (AVC-FOF) and African Venture Capital Tax Relief (AVC-TR) scheme recommended in this report.

AVCA recommends the EU and G8 governments fund AVCA’s Capacity Building to support the Associations efforts in promoting and developing the industry in Africa as a key element of economic growth and poverty alleviation in Africa.

Conclusion

AVCA calls on the UK Commission for Africa to include AVCA's recommendations, to EU and G8 governments, to support the African venture capital and private equity industry…

In conclusion, AVCA sincerely welcomes Tony Blair and Gordon Brown's commitment to alleviating poverty in Africa.

AVCA gives a resounding welcome to the UK Commission for Africa's Report. We appreciate the extensive and comprehensive work behind the recommendations that have been drawn up and we fully endorse its aims.

We do however believe that much greater emphasis needs to be placed on private sector led initiatives and on the positive role that venture capital and private equity can play and suggest that a much greater proportion of the financial resources should be allocated to this.

In this report, AVCA makes the case for venture capital and private equity as an important source of finance for Africa's development that the UK, EU and G8 countries should support.

AVCA calls on the UK Commission for Africa recommendations to include AVCA's recommendations, for EU and G8 governments, to support the African venture capital and private equity industry by establishing the following:

1. An African Venture Capital Technical Assistance Fund (AVC-TAF) comprising $50 million a year for 10 years

2. An African Venture Capital and Private Equity Fund of Funds (AVC-FOF) with an initial capital of $250 million extended to $500 million on review

3. An African Venture Capital and Private Equity Tax Relief (AVC-TR) to provide tax back to investors in African venture capital and private equity

4. Capacity Building for AVCA estimated at €1.2 million a year

AVCA sincerely hopes the Commission, EU and G8 government's responds to this opportunity to unlock and maximise the development impact of venture capital and private equity in Africa.

AVCA welcomes the opportunity to discuss and detail these proposals with the Commission, EU and G8 governments and other interested stakeholders.

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