POWER ON: AFRICA WORKS ON SOLVING ITS ELECTRICITY DEFICIT.

The slow pace of electrification is the Achilles' heel of the African growth narrative, writes Johan Steyn, Africa Fund Manager at Prescient Investment Management

Electricity in many African countries is still inaccessible, unaffordable, and highly unreliable. About 90% of the rural population in Sub-Saharan Africa has no access to electric power, with Ethiopia, Kenya, Mali and Sierra Leone among the most severely compromised. Many frightening statistics are bandied about to illustrate the dire need to increase electrification, including that Spain with its 50 million odd population has roughly the same power generation capacity as the whole of the African continent, which is home to more than a billion people. Across Africa about 640 million people lack access to electricity.

According to a report by the Africa Progress Panel, more than 600 000 Africans are killed every year by air pollution caused by the use of firewood and charcoal for cooking, where women and children are the primary victims. In nine African countries more than 80% of primary schools have no electricity. To make matters worse, 50% of Africans will be living in cities by 2030, placing a huge strain on energy infrastructure. Africa's energy needs are indeed massive.

The slow pace of electrification is the Achilles' heel of the African growth narrative. Africa's true potential is significantly curtailed as economic growth is hampered by a lack of a sustainable and affordable power supply. Industrialisation, jobs, business, agriculture and social development all depend on energy becoming a more important priority in Africa. Not only does the pace of electrification need to be increased, the scale needs to be enlarged as well. It's a mammoth task, but not an impossible one. Indeed, good progress has been made on a number of fronts and there are quite a few positive trends.

The speed of adoption and development of renewable energy has been remarkable. Even though growth has come off a low base, there has been a clear push for low-carbon power development across the continent. From solar power in South Africa and Morocco, to hydro and geothermal power in Kenya, the willingness to embrace the revolution in clean energy has been encouraging. Africa is rich in renewable resources and could benefit from the increasing use of renewable energy.

Across Africa, hydropower is responsible for 84 per cent of all non-fossil fuel energy use, and in a continent rich in lakes and rivers, the opportunities for expanding hydropower are huge. There is arguably enormous potential for geothermal energy in the East African Rift Valley which is roughly 5,900 kilometres in length and spans several countries in East Africa including Eritrea, Ethiopia, Djibouti, Kenya, Uganda, and Zambia. Other renewable sources that haven't even scratched the surface of their potential include energy from wind, biomass, and biofuel.

It's important for African countries to continue to set ambitious targets for renewable energy developments to avoid the pitfalls of a high reliance on power from fossil fuels. Countries like China are currently struggling with major air pollution problems due to a dependence on coal power to drive its historic industrialisation. Although it would be unrealistic to expect fossil fuels not to play an important role in the overall energy mix given its rich resource endowment, Africa can avoid the harmful effects of dependence on dirtier energy sources.

Other encouraging trends include the increase in independent power producers (IPP), mini-grid and off-grid energy solutions. Africans are rapidly adopting and adapting them, particularly to meet the needs of areas that are remote or neglected by the grid. By allowing diversity in the way electricity is generated and distributed, African countries could leapfrog to a model where power is no longer solely delivered through a complex and expensive grid of base load generation and fixed cables, but through a mix of renewable technologies that are more affordable, smaller and decentralised.

Utilities in Africa still have an important role to play. At the core of Africa's power system, the utilities that manage the national grids are becoming more efficient and accountable. In some cases, there has been a separation of the generation, transmission and distribution functions, opening the way for private capital to play a larger role in addressing financing shortfalls. This, together with the improvement in regulatory frameworks and the amendment of electricity laws, has resulted in governments paving the way for greater investor involvement.

However, it must be mentioned that this course of action hasn't always been a roaring success. When Nigeria embarked on a privatisation drive a couple of years ago there were lofty expectations of dramatic improvements, but inappropriate policies around pricing as well as infrastructural impediments have meant the expected benefits have not been realised. This experience has perhaps highlighted the importance of having the appropriate legal, financial and technical frameworks in place. In this regard, greater international energy cooperation has a role to play.

In 2015, the New Partnership for Africa's Development (NEPAD) established the Africa

Power Vision, and the African Development Bank launched its New Deal on Energy for Africa. Both reflect the increased commitment to ensuring universal access to modern energy, and adequate power to enable economic growth and prosperity. The African Development Bank has made energy one of its five top priorities, committing $12 billion of its own resources to the energy sector over the next five years.

This is significant because institutions like the African Development Bank help in many ways, including raising ambitions to solve Africa’s energy challenges, mobilising domestic and international capital for innovative financing in Africa’s energy sector, and supporting African governments in strengthening energy policy, regulation and sector governance.

With the power sector in Africa set-up for solid long-term growth, the question becomes how investors can participate in this growth.

One way is by participating in the direct debt financing of power related projects. However, there tend to be size and liquidity constraints that make this option unsuitable for the typical investor. In this regard Prescient has established the Prescient Renewable Energy Fund to take advantage of opportunities in the renewable space, and make it more accessible to investors.

Another way to get direct exposure to the power sector in Africa is to invest in companies that operate in the industry. These include the JSE listed Consolidated Infrastructure Group which has ambitions to be Africa’s leading supplier of high voltage turnkey electrical substations, overhead power lines and renewable energy. With a footprint across 21 African countries, it is the largest high voltage turnkey solutions provider in sub-Saharan Africa. Other power sector plays include Elswedy Electric in Egypt, and the Ugandan electricity distribution company, Umeme, which is listed in Kenya and Uganda. Kenya also has its power generation company (Kengen) and the distribution company (Kenya Power and Lighting) listed on the Nairobi Securities Exchange.

The investment case for direct power sector plays may differ, but the indirect benefit of having a reliable and affordable electricity supply will impact many different listed companies. Telecommunication companies, for example, will be beneficiaries through massive fuel related cost savings. About 60% of operator network costs for mobile-phone operators are spent on diesel fuel. Banks with large branch networks could face similar savings if they can cut down on the amount spent on diesel fuel to run costly generators. Savings in operating costs will feed through to the bottom-line and enhance profitability. In the consumer and manufacturing sectors it is difficult to even estimate the investment in new projects and capital expenditure that will result from projects that become viable due to lower projected operating costs. Benefits will accrue to brewers, retailers and other consumer-focussed companies operating and listed across the continent.

While the African power sector faces many challenges, there are a number of reasons to be optimistic about the future. There is an increasing international willingness to support and help solve Africa’s energy problems. Private sector involvement is essential to effectively delivering new capacity. There are an abundance of opportunities for investors and growing interest from financiers. Governments will need to play their part by establishing the regulations and capabilities needed for the sector to thrive.

Success will propel the economic growth of the continent and greatly enhance the lives of hundreds of millions of people, as well as potentially create a thriving electricity supply industry. As an enabler of entrepreneurial activity, a more consistent and ubiquitous power supply will have a vital multiplier effect in creating jobs and lowering the unemployment rate.

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- Prescient Investment Management is a signatory to the United Nations Principles of Responsible Investing (UN PRI) and pledged to the Codes for Responsible Investing in South Africa (CRISA).
- The Prescient Global Income Fund, now known as the Prescient Global Income Provider Fund, was ranked by Morningstar as the 7th top performing fund for 2015.
- **More recently, the Prescient Income Provider Fund won the Raging Bull Award for the Best South African Multi-Asset Income Fund, Best South African Interest-Bearing Fund as well as a certificate for the Best South African Multi-Asset Income Fund on a risk – adjusted basis over five years to December 31, 2016.**
- Morningstar data also confirmed that The Prescient China Balanced Feeder Fund has been the top performing South African domiciled fund for the second year in a row.
- Prescient Investment Management was the first institution in Africa to be granted a Qualified Foreign Institutional Investor (QFII) licence by the China Securities Regulatory Commission (CSRC).
- Prescient Investment Management was named Overall Investments/Asset Manager of the Year at the Imbasa Yegolide Awards 2011, Absolute Return Manager of the Year in 2013 and Bond Manager of the Year and Responsible Service Provider of the Year in 2015.
- The full details and basis of the award can be obtained from the fund manager.
- For any additional information such as fund prices, brochures and application forms, email info@prescient.co.za or visit www.prescient.co.za
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