High Growth Start-Up Ecosystems in Sub-Saharan Africa: Initiatives, Challenges, and Policy

Summary Insights from the
Oxford Entrepreneurship Policy Roundtable – May 2021

Executive summary

In May 2021, the Oxford Entrepreneurship Policy Roundtable (OXEPR) convened a group of entrepreneurship experts from different parts of Africa, Europe, and North America, to discuss the emergence of high-growth start-up ecosystems in Sub-Saharan Africa. Buoyed by recent success stories, there is a growing sense that tech-enabled start-up ecosystems are finally emerging in select parts of Africa. The Roundtable focused on new initiatives, current challenges, and public policy implications. It identified four key themes for ecosystem development: talent, acceleration, funding and policy. The discussion generated ideas and recommendations for specific actions to further advance these emerging ecosystems.

In summary, eight calls for action emerged:

1. Develop managerial skills for starting and scaling ventures
2. Focus business training on problem solving skills
3. Improve the business networks of African tech hubs
4. Design new acceleration programmes for scaling internationally
5. Encourage African institutional investors to invest in African venture capital
6. Launch an African Investment Fund
7. Develop a scorecard for tracking start-up ecosystem performance
8. Create organizations that link up key ecosystem players with policy makers

Background

The Oxford Entrepreneurship Policy Roundtable (OXEPR) on “Start-Up Ecosystems in Sub-Saharan Africa: Initiatives, Challenges, and Policy” was held online in May 2021, convened by Gilles Duruflé,[1] Thomas Hellmann,[2] and Karen Wilson.[3] This is a summary of the key insights that emerged from the event.

As background, OXEPR is an annual event which convenes entrepreneurship experts, around a different topic every year. Prior Roundtables examined a variety of ecosystem challenges, including the scaling of tech start-up (Duruflé et al., 2018a), the emergence of student

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entrepreneurship (Duruflé et al., 2018b), and the role of foreign venture investors (Bradley et al., 2019). This prior work provides frameworks for analysing the development of entrepreneurship ecosystems. With the help of Oxford students, the authors gathered publicly available data and reports on tech-enabled start-ups in Sub-Saharan Africa.[4] Furthermore, the authors identified and interviewed a diverse group of experts prior to the Roundtable, most of whom also participated in the Roundtable. The Roundtable was attended by over 40 experts from different parts of Africa, Europe, and North America. The backgrounds of participants included entrepreneurs, investors, academics, policy makers, and managers from philanthropic organizations and multilateral development agencies.[5]

Recent trends in ecosystem development

In recent years there have been clear signals that entrepreneurial ecosystems are emerging in several parts of Africa.[6] We briefly review the most salient trends.

Africa currently has 1.3B people and is projected to double by 2050 (The Economist, 2020). Africa has a very young population with a median age 20 (Worldometers, 2020), half of the UK (ONS, 2019). While Africa is believed to have the highest entrepreneurship rates in the world, a report by the African Development Bank (2017) suggests that only 20% of these entrepreneurs are introducing new products and services; and 33% of all African entrepreneurs start business because they can't find other jobs.

One key measure of ecosystem growth is the amount of venture capital funding, and related angel investments. Different data providers estimate different amounts, due to alternative definitions and data sources. Estimates for the amount of venture capital invested in Africa range from $700m to $1.4M for 2020 (Disrupt Africa, 2020) (Partech Africa, 2020) (Briter Bridges, 2020) (AVCA , 2020). Importantly, all data sources show a clear upward trend, with 2020 amounts representing a three- to fivefold increase over 2015 amounts.

The dominant sector for venture capital is Fintech, capturing 25% of investment amounts. It is followed by E-commerce with 14%, E-health with 10%, Logistics with 7%, and Energy with 6%. While Fintech is clearly leading, there are clear signs that other sectors are also beginning to emerge. The geographic distribution of venture capital is highly concentrated. Nigeria, Kenya, Egypt, and South Africa account for over 80% of all investments. Within these countries a few cities attract the majority of funding, especially Lagos, Nairobi, Cairo, and Cape Town. Despite this concentration, other centres such as Accra, Dakar, Kigali, or Abidjan are also witnessing a rapid growth in venture capital funding, albeit starting at a much lower level.

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[4] We would like to thank Lyly Hangula, Jacob Murphy, Kusal Ranawaka, Maria Rotilu, Emily Tormey, and Adriana Vitagliano for their excellent research support.
[5] Any views expressed here are those of the authors, and not of any institutions they are affiliated with. They also cannot be attributed to any specific interviewees or Roundtable participants.
[6] While some of the data is for all of Africa, the focus of our discussions and call to action was on Sub-Saharan Africa.

The largest source of African venture capital funding comes from the US, accounting for 40% of total investments (AVCA , 2020). This is followed by South Africa (9%), UK (8%), and Nigeria (4%). Many venture capital backed companies are run by expat and foreign founders, not local founders. Bayen (2019) examines companies raising over $1M in venture capital: while over 50% of companies had purely local founders in Nigeria and South Africa, in other countries, such as Kenya or Ghana, less than 15% were purely local founders. Note, however, that in South Africa and Kenya approximately one quarter of all companies included a mix of local and expat founders. Other data sources observe similar patterns. Village Capital (2017), for example, finds that only 10% of Fintech investment in East Africa goes to ventures with purely local founders.

Probably the most important signals are the recent successful exits and success stories. According to Digestafrica (2019) there were 51 exits ($435m in total disclosed investments) and 56 exits ($647m) in 2018 and 2019, respectively. Some of the most celebrated ones include Interswitch (acquired for $200M by VISA in 2019) and Paystack (acquired by Stripe for $200M in 2020). Equally exciting are some of the scale-ups that have not yet exited, but have raised large later stage rounds, including Flutterwave (which raised a Series C round of $170M at a valuation over $1B) and Tala (which raised over $200M and is valued at $560M). While these are all Fintech companies, it is also worth mentioning Andela, an EdTech company, that raised $180M and is currently valued at $700m. (Pitchbook, 2021).

Overview of Challenges

The Roundtable was structured around four key challenges of African start-up ecosystems: Talent, Acceleration, Funding, and Policy. The discussion generated numerous ideas for improving ecosystem conditions along these four themes. Below is a summary of the key calls for action that were proposed by various participants. This is not an exhaustive list of all the ideas that were mentioned, let alone the ideas that could be pursued. Instead, the goal here is to draw attention to key ideas that played a central role in the Roundtable.

The summary below identifies 8 calls for action that emerged across the four subthemes. Each action calls on different sets of players that could potentially make a difference. Key players include entrepreneurs (founders, managers), investors (angels, venture capitalists, institutional investors, a.o.), policy makers, established corporations (local, multinationals), academics (educators, researchers), foundations, multilateral organizations, and others, within and outside of Africa.

Talent

There is no shortage of entrepreneurial talent in Africa. In recent years there have been many efforts to improve technical skills. Data by Quartz Africa (2019), for example, shows that Africa has the fastest growing pool of software developers. Our interviews also suggest that technology expertise is growing more broadly. However, there is a marked lack of managerial business talent. Of particular note is the difficulty to find mid-level business managers with experience of managing growth and scaling across multiple markets.

Key Action #1: Develop managerial skills for starting and scaling ventures

The first key action focuses on business skills for potential founders and managers. This clearly goes beyond the current emphasis on technical skills, which also often lead towards careers at more established corporations. These business skills can be imparted through practical on-the-job training, within local and multinational established corporations. Such business training is valuable not only for potential start-up founders, but also for potential non-founding managers who join later-stage scale-ups.

Key Action #2: Focus business training on problem solving skills

A surprising large number of Roundtable participants emphasized the importance of experiential learning and problem solving skills, over traditional teaching methods that focus on knowledge acquisition. Traditional business training for entrepreneurs and managers can easily be misguided, especially if local business conditions differ from those assumed in the training materials. Moreover, it is argued that entrepreneurial talent manifests itself through on-the-job problem solving. Therefore, entrepreneurial training methods should focus on problem solving skills.

The emphasis on problem solving skills matters especially in light of the fact that African schools and universities tend to be severely underfunded, and that alternative training methods already play a larger role in talent development. New alternative training programmes based on online learning, bootcamps, internships, and corporate training programmes therefore have a chance to be designed from the outset on imparting problem solving skills. An example is to create internships for African managers, not only in local or multinational companies, but also in high-growth scaleups in North America and Europe.

<u>Acceleration</u>

One sign of ecosystem growth is that by 2019 there were across Africa 643 tech hubs, where 41% of them had incubators, 39% co-working spaces, 24% innovation hubs, and 14% accelerator programmes, with some hubs hosting multiple activities across categories (AfriLabs & Briter Bridges, 2019). Interestingly, nearly half of these hubs were not-for-profit organizations, receiving grants from corporations, NGOs, and philanthropic institutions.

During the Roundtable it was noted that while there has been a dramatic increase in the number of these tech hubs, the real issue was quality. Especially since many tech hubs are not-for-profit organizations, a focus on the commercial performance of ventures is key. Several experts expressed concerns that many African accelerator programmes were not guided by experienced entrepreneurs who themselves had built successful businesses. Many programmes also lacked the buy-in from local investors, and strong connections to established large corporations.

Key Action #3: Improve the business networks of African tech hubs

Roundtable participants argued that the key to improving the quality of tech hubs was to build stronger business networks. Acceleration programmes and tech hubs need to be led by experienced entrepreneurs who understand what it takes to build real companies. Moreover, they need to be closely connected to market participants, especially investors and established corporations. They can help entrepreneurs with product development, market access, and business development. Ideally, tech hubs also include regulators and policy makers in their networks too.

Key Action #4: Design new acceleration programmes for scaling internationally

Many African accelerator programmes are geographically isolated and find it difficult to build meaningful Pan-African or global connections. This limits their ability to support start-ups that want to pursue ambitious international expansion strategies. Several Roundtable experts noted the opportunity to build new acceleration programmes that focus specifically on the scaling challenges of tech-enabled start-ups. African startups often find it difficult to scale beyond their home market and build business models that reach across multiple African countries and/or to larger global markets in the US, Europe, or Asia. New acceleration programmes could convene networks of mentors, investors, and corporations across these geographies. To be most effective, such programmes might also have a thematic focus, such as E-Commerce, Fintech, Health, Energy, Agtech, or other. And again, these acceleration programmes need to be guided by seasoned entrepreneurs who have first-hand experience building significant businesses themselves.

<u>Funding</u>

Despite the recent rise in angel investment and venture capital, there remain large funding gaps across sub-Saharan Africa, both at early and later stages of venture development. There are concerns that funding is dominated by foreign investors and that many local investors lack a proper understanding of the venture investing process.

The data above highlights the large role played by foreign investors, especially from the US. Foreign investors are viewed as a mixed blessing.[7] On the one hand there is a clear benefit to attracting foreign capital. Moreover, this capital typically comes with valuable expertise on how to successfully scale ventures, and powerful networks to support foreign expansion strategies. On the other hand, there is a concern that returns flow to foreign investors who may not necessarily reinvest into the local ecosystem. Related to this, it is worth noting that most venture-backed start-ups operating in Africa are incorporated outside of Africa.

There is a related concern about the willingness and expertise of potential local investors. Roundtable participants expressed concerns that local African investors, particularly institutional investors, have limited interest and understanding in local venture investments. It

[7] In this context it should be noted that there is a parallel debate in Europe and Canada about the role of US investors. We discuss this in Bradley et al. (2019).

was also remarked that, relative to foreign investors, local investors tend to offer lower valuations and tougher investment terms.

Key Action #5: Encourage African institutional investors to invest in African venture capital

A recurring argument of the Roundtable was that if more of the financial returns from investing in African start-ups are to flow into local ecosystems, African investors must be the ones to invest in those start-ups in the first place. As a consequence, African institutional investors need to step up their commitments of investing in their own venture capital industry. The current reality is that African pension funds, and other institutional investors, are largely avoiding this sector, presumably because there is no proven track record of above market returns. Any purely data-driven backward-looking investment approach is bound to miss path-breaking investment opportunities. Yet it is precisely those investments that are needed to create long-term economic growth.

Key Action #6: Launch an African Investment Fund

One bold idea that emerged from Roundtable is the creation of an "African Investment Fund" (AIF), loosely modelled after the European Investment Fund (EIF). Launched in 1997 as part of the European Investment Bank (EIB) Group, the EIF is widely acknowledged to have played a central role in the development of the European venture capital industry. It is not only a source of funding, but it also helps to disseminate best practices. It acts as a source of industry research which helps to attract private sources of funding.[8] Over the years, the role of the EIF has expanded to support business angel investments. It also develops regional and sector specific initiatives in partnership with European countries.[9]

An African version of the EIF, call it AIF, could play a key role in mobilizing African institutional investors, as suggested under key action #5, and eventually partner with Pan African or International Funding Agencies to play a similar role for the development of the African VC industry and business angel investment activity.

Such an AIF could also focus on first-time fund managers. Private limited partners often balk at the lack of track record, yet there is a strong economic rationale for supporting new fund managers who bring novel investment ideas.[10] An AIF might also be well-positioned to develop a training programme for a new generation of African venture capitalists. Specifically, there is an opportunity to develop training programmes to help talented young Africans to become professional venture investors. There are clear role models for such training programmes in the US with the Kauffman Fellows programme, or in the UK with the Newton programme.[11]

[8] "See EIF VC Survey 2018 Fund managers' perception of EIF's value added", EIF Working Paper 2018/51
[9] https://www.eif.org/who_we_are/index.htm
[10] Several Roundtable participants questioned whether the standard US venture capital structure is suited for African venture investments. One issue is whether the 10-year fund horizon is appropriate when liquidity is limited. There are also questions whether venture investor should be allowed to invest in alternative securities, possibly some variants on venture debt, and possibly some revenue sharing arrangements.
[11] See https://www.kauffmanfellows.org/ and https://newtonprogram.vc/.

Policy

There are many policy recommendations apply to Africa just like to other places, such as improving the broader business environment, removing regulatory barriers to entrepreneurship, and creating policies to support ecosystem development. In addition, Africa has notable challenges around physical infrastructure (e.g., transportation) and digital infrastructure (e.g., Internet access). To complicate things further, countries across sub-Saharan Africa are at very different stages of addressing these broader policy challenges. While acknowledging these broader policy issues, Roundtable participants focused on policy-related initiatives they thought could specifically help the development of sub-Saharan Africa start-up ecosystems.

Key Action #7: Develop a scorecard for tracking start-up ecosystem performance

A scorecard summarizes key measures to track the performance of a tech ecosystem. It measures the activities of start-ups in terms of founding, funding, employment, growth, and success. Building a scorecard systematizes existing data and also helps to track progress and identify gaps where further action is needed. Roundtable participants thought that more should be done in terms of making data easier to find, organizing it into useful ecosystem maps, and actively publicising it to key stakeholders, including policy makers, to help drive further action towards ecosystem development.

At present there is uneven coverage of entrepreneurial activities across Africa. Ironically, the tech industry should be well-positioned to collect more systematic data about itself - maybe even become a role model for data gathering in Africa. Data on financing is typically easiest to gather, but there is a large need to gather systematic data on company growth (e.g., revenues, exports, employment), ecosystem support (e.g., skills training, accelerators), and policy (e.g., grants, regulation).

Key Action #8: Create organizations that link up key ecosystem players with policy makers

Building a start-up ecosystem requires political consensus and a national strategy. This is best formulated when ecosystem stakeholders speak with a coherent collective voice. A key message from the Roundtable was the need for a sustained dialogue between business practitioners and policy makers. Many experts noted a lack of understanding for start-ups in government circles. There is too little structured dialogue between policy makers and representatives of the start-up ecosystem.

The call for action is to create some type of (non-governmental) organization that provides pertinent information and facilitates policy dialogue between the entrepreneurial sector and key government players. The goal is to have on-going interactions between industry leaders and public administrators, including regulators. The precise structure of such organizations remains a matter of debate. In principle one can think of industry associations, institutes, think tanks, research centres, etc. The optimal structure of such organizations is likely to differ from country to country. Possible role models might include the Kauffman Foundation in the US,[12] the Start-up Nation Central in Israel,[13] Tech Nation in the UK,[14] and many others. These could also be topic specific institutions that help policy makers and regulators better understand fast-moving sectors, such as Fintech or Medtech.

One salient question in the African context is whether such an organization focusses on a single country or a group of countries. Most policy making happens at the national level, suggesting a country-specific focus. However, there might also be some opportunities for cross-country learning, arguing for multi-country collaborations.

Though the details will vary by country, several policy suggestions are likely to apply to a majority of African countries. There will always be an agenda for business-friendly regulations, such as lower taxes, lighter regulation, predictable enforcement, and less bureaucratic red tape. An example of a more ambitious agenda item might be to work on credit rating systems for private companies, or the establishment for entrepreneurship visas that increase the mobility of entrepreneurs (especially within Africa). The list of potential agenda items can naturally be expanded in many directions. In fact, one idea is to work towards national "Startup Acts" that amalgamate all the key policies required to build a cohesive entrepreneurship ecosystem.[15]

Conclusion

There is an emerging sense that several places in Africa are on the verge of building significant ecosystems for tech-enabled high-growth start-up. However, to achieve their full potential, these places still need to create institutional support structures. The roundtable identified a set of 8 key actions in the areas of talent, acceleration, funding, and policy. The first step is to understand the challenges from an ecosystem perspective and identify the areas that require collective action. The next step will be for these actions to be taken up as concrete initiatives, turning ideas into action. The ultimate goal of the Roundtable is thus to encourage building vibrant start-up ecosystems in Africa.

[12] https://www.kauffman.org/
[13] https://www.startupnationcentral.org/
[14] https://technation.io/
[15] This approach has already been adopted by Senegal and Tunisia and has recently be advocated more broadly by Wolken (2020).

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