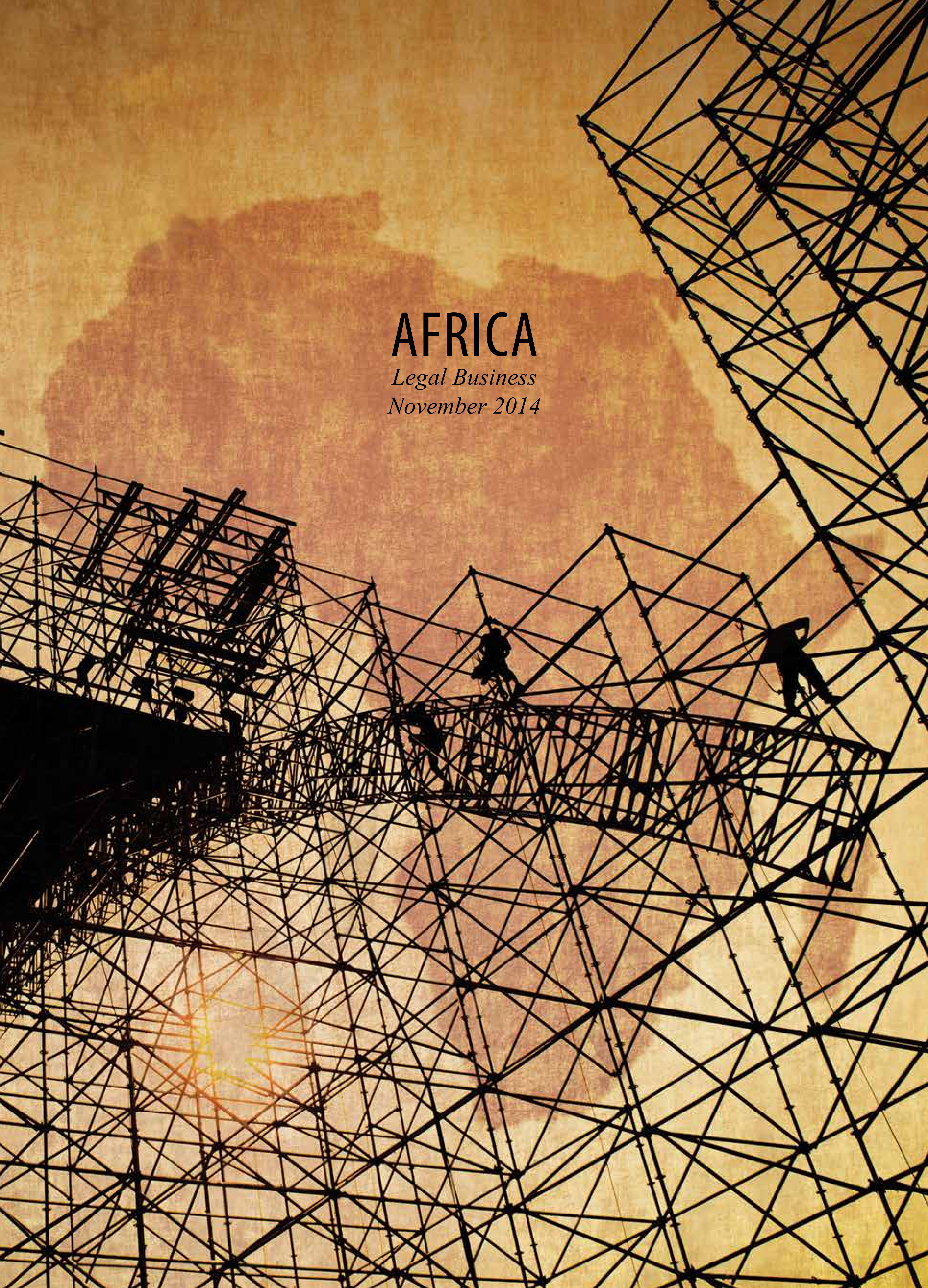
AFRICA

Legal Business
November 2014



Constructing continents

With a huge infra deficit and investment flooding in, *Legal Business* assesses the bellwether projects – and their advisers – defining Africa's infrastructure market

MICHAEL WEST

In August this year, President Obama hosted the largest US-Africa leaders' summit ever, with the heads of nearly every African nation gathering in Washington DC. As well as working on governance and leadership issues, Obama talked to a business forum hosted in the Mandarin Oriental, with 90 US firms and over 100 major African companies attending, in an attempt to broker deals and build relationships across the Atlantic.

The summit came after 18 months that have seen increasing numbers of US institutions committing money to the continent and stoking opportunities for law firms. But the US is late to the game with Asian, Middle Eastern and European players having an established presence while local developers have become increasingly prominent.

Thomas Laryea, chair of Dentons' Africa executive committee and ex-International Monetary Fund assistant general counsel, observes: 'US companies in the past have been relatively behind the investment trend into Africa, but given the size of the US economy, a small shift makes a significant change and we are seeing more private sector and government initiatives.'

Symbolic of this drive was Blackstone-backed Black Rhino and Dangote Industries, one of the largest industrial conglomerates in west Africa, pledging at Obama's summit to jointly invest $5bn into sub-Saharan

Illustration SHUTTERSTOCK

Africa energy projects over the next five years.

The memorandum of understanding between the two companies, drafted by Jones Day and Kirkland & Ellis, touted the development impact while also eyeing the pent-up demand of 589 million people lacking access to electricity. As Weyinmi Popo, partner at Jones Day, says: 'That's real money. I understand there was some cynicism over some of the announcements that they were just repackages, but this is a definite new investment.'

The demand Popo sees is, of course, potentially huge. The continent's lack of infrastructure remains a major problem, with many countries lacking adequate transport links, power connections, schools and hospitals. Despite the economic revival that has seen Africa over the last decade shake off its image as a poverty-stricken region to post some of the fastest economic growth rates in the world – lack of investment outside of commodities and energy remains a major issue. Filling that gap remains a huge challenge in a region with a sprawl of various languages, legal systems, levels of development and cultures, but a growing number of firms are moving in.

While corporate America has only begun to seriously look at the continent in the last 18 months, Chinese investment has grown hugely since the 1990s with sponsors and financial institutions entering the region. The investment is spread across the continent, but sectorally 'in Africa,' says Luís Filipe Carvalho, partner at Portuguese-firm ABBC, 'I would say real estate, infrastructure, finance, energy and industrial operations provide the most substantial volume of work from Chinese investors.' But it remains a challenging market to service or establish a reputation in.

'The fact that we have a sizeable presence on the ground in Beijing is obviously pretty helpful as that is where most people are based.'

Ian Coles, Mayer Brown

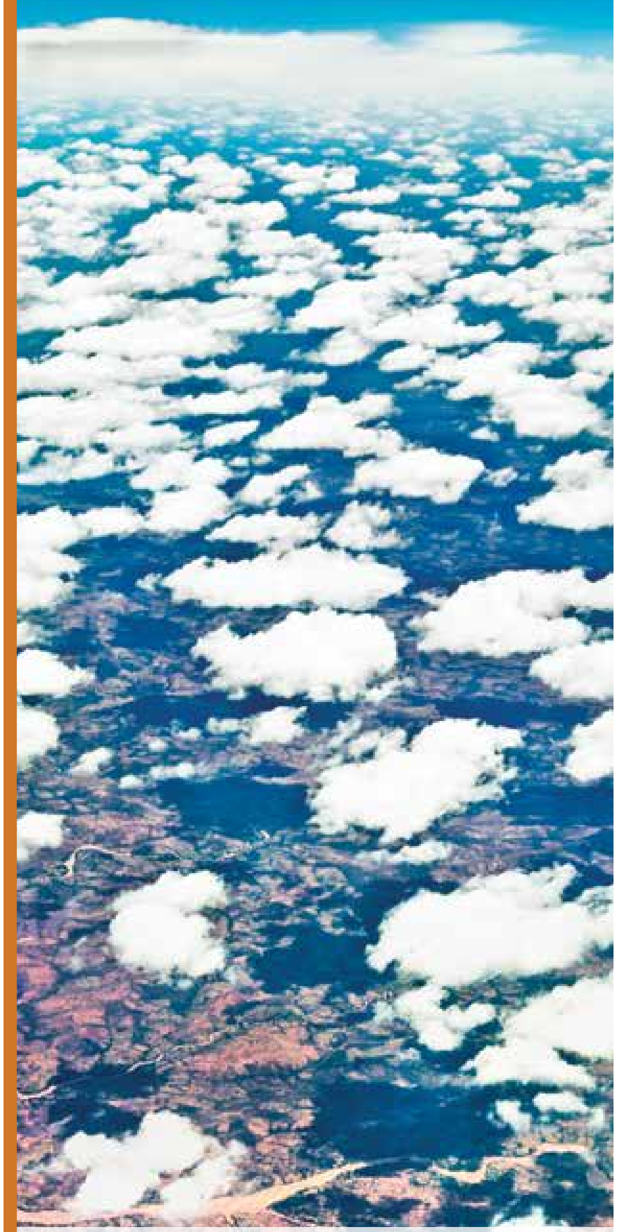
Chinese companies tend to operate alone and carry out complete packages of works, not only mines or wells, but also power plants, roads, railways, staff housing and ports. Few law firms boast of much success in handling leading Chinese companies in Africa, though the Magic Circle and some top-tier US law firms are acknowledged to have made the most headway. The scarcity of mandates stems from the government-to-government style agreements used by many Chinese corporations and the cultural tendency to rely on political problem-solving (or arm-twisting) rather than legal recourse, with many deals being drawn up on only a couple of pages.

Nevertheless, there are opportunities for firms that can find the right angle. Ian Coles, projects partner at Mayer Brown, who heads the US-based law firm's Africa and mining practice, comments: 'It's not easy to get the work, but nowadays no work is easy to get. It's occasionally difficult to figure out who the right people are to talk to, but that apart, once you have found the right people, the Chinese are just as amenable to advice from law firms as anyone else is these days.'

Coles adds: 'The fact that we have a sizeable presence on the ground in Beijing is obviously pretty helpful as that is where most people are based.'

Freshfields Bruckhaus Deringer partner Tim Pick takes up the theme: 'You have to have a credible China presence to land roles involving Chinese sponsors. If you are pitching to a consortium, even if the Chinese sponsor is a minority participant, it is very difficult to get their vote if you haven't significantly invested in the Chinese market. It's about

AFRICA – THE AERIAL VIEW



'Over the last five years we have probably had the most exciting times and growth in the legal market, which coincided with the growth of Kenya and, quite frankly, the entire continent.'
Amyn Mussa, Anjarwalla & Khanna

Africa's economy managed to come out of the financial crisis largely unscathed as the development finance institutions, which provide a large proportion of the continent's capital, avoided the kind of blows that hit commercial lenders in the west. After several years of consistent 5% growth and the International Monetary Fund (IMF) expecting this trend to continue, Latham & Watkins partner Kem Ihenacho observes: 'Africa is in the sights for investors globally like never before. GDP is growing in some of these countries faster than anywhere else – you segment that down and some sectors are growing 20-25% plus year-on-year.'

This growth, although often still based on extractive industries, is raising disposable incomes for the first time in recent history. Combined with increased urbanisation, Africa's consumer classes are growing quickly and attracting investors who want to climb the value chain, whether that is through retail, fast-moving consumer goods, agribusiness, or financial services.

'Over the past ten years' says Miguel Castro Pereira, managing partner of Abreu Advogados, 'sub-Saharan Africa grew 5% per year and, at this rate, the region's economy should double in size before 2030'. Indeed, averaged across sub-Saharan Africa, the IMF predicts GDP growth of over 5% in the short term as the economies of both resource-intensive countries and emerging markets expand. Though the highest growth will be seen in fragile countries such as Cote d'Ivoire and Mali as they recover from conflicts, it is the developed markets such as Nigeria and Kenya, with large economies, which are still seeing growth rates of 7% and 6% respectively, that are attracting international investors.

While this growth has made many international law firms reassess how they approach Africa, it has also supported growth in the domestic legal market. Amyn Mussa, senior partner at Anjarwalla & Khanna, says: 'Over the last five years we have probably had the most exciting times and growth in the legal market, which coincided with the growth of the country [Kenya] and, quite frankly, the entire continent. We've seen law firms grow in size significantly, including ourselves. If you went back 15 years ago in Nairobi, we were three lawyers – there are now 60 plus.'

The growth of domestic law firms has also seen an increasing specialisation, with leading advisers moving on from being litigation or conveyancing-based enterprises, to take on a greater range of work and more complex deals.

Inevitably, averages hide the diversity of the continent, with some countries seeing rapid development while others suffer civil wars. Nations such as Equatorial Guinea, which are tied to natural resource extraction, are entering recessions or experiencing slow growth as commodity prices weaken, while conflict-riven nations such as the Central African Republic, which is estimated by the African Development Bank to have lost a third of its GDP in 2013, also suffer.

Growth rates are often vulnerable to external events, with neighbouring conflicts spilling over borders or terrorist groups expanding their zone of operation. The latest spectre to stalk the economy is this year's outbreak of the Ebola virus, which has already claimed over 4,000 lives, with major outbreaks in Guinea, Sierra Leone and Liberia. Economists have already warned that the outbreak will impact on the region's economy.

Portuguese law firm Raposo Bernardo's managing partner, Nelson Raposo Bernardo, says: 'The Ebola virus has been a very important limitation in the movement of people and has touched the way to conduct business. Countries such as Guinea Conakry, Sierra Leone, Nigeria and other West African coast countries may register some difficulty in maintaining the pace of economic growth they've experienced in recent years.'

But that won't stop Africa being an interesting prospect for many clients as Dentons partner Thomas Laryea argues: 'The interesting thing about the African continent – there's a market for everyone, there really is; there are people who want to go to South Africa because it has a developed financial sector and diversified economy, and there are people who want to go to Chad and Democratic Republic of the Congo where there's more risk but assets are cheap.'

having people close to their headquarters, having the language skills as well as legal skills, and understanding the business culture and environment.'

Other sponsors from Korea and Japan are easier to gain access to, being more receptive to legal advice and law firms able to leverage established relationships with the large engineering and finance companies. Korea's involvement also dates to the 1990s with support from bodies such as Korea Eximbank, but Japan has recently shown more interest with sponsors backed by institutions such as the Japan Bank for International Cooperation. Arman Galledari, head of Jones Day's global projects and infrastructure practice, says: 'We were in Tokyo in June doing seminars for the trading houses and independently they all asked to talk more about power, renewables and petrochemicals in Africa. They are showing a lot of interest.'

Phillip Hall, head of infrastructure and transportation structured finance for EMEA at The Bank of Tokyo-Mitsubishi UFJ, comments that, in terms of infrastructure, 'the areas we are most likely to look at would be airports, ports or rail, to the extent it's linked to a mining or power concession'.

VETERAN PLAYERS

But, the most-well established players in Africa remain the European nations, with sponsors and commercial lenders often more comfortable with the markets given historic and cultural ties. Finance is also more readily available with European development institutions heavily focused on the region and supporting deals with equity, debt or guarantees.

Capital flows from Europe still closely mirror the old colonial maps and law firms find themselves adopting configurations to match. Africa's Anglophone countries tend to have a common law system, Francophone states rely on civil law and a version of the French Civil Code and civil law dominates in Lusophone regions. Correspondingly, US and City firms use London to act on Anglophone deals, Paris for Francophone, while Portuguese firms have carved out a niche in Lusophone Africa – though increasingly they are expanding to provide local law advice in other civil law jurisdictions. Rui Amendoeira, managing partner of Portuguese firm Miranda, says: 'Lusphone countries are very integrated and all use civil law, so it is easy to operate between them. We have also started looking at doing work in French civil law countries.'

SOUTH AFRICA – MORE CROWDED BY THE MINUTE

There is no doubt that South Africa enjoys a particular but shifting position in the wider region's legal economy. It has remained by far the largest and most sophisticated law market in the continent, and has continued to see sustained investment from international advisers.

Most prominently, last month Allen & Overy secured its long-expected launch in Johannesburg after recruiting a seven-partner team from leading local practice Bowman Gilfillan, becoming the first Magic Circle practice to launch its own office locally.

South Africa is seen by many as an initial entry point to sub-Saharan Africa, with White & Case making the initial breakthrough in 1995 with an office in Johannesburg. But it has been the last five years that has seen an explosion of interest, with DLA Piper, Baker & McKenzie, Linklaters, Eversheds, Fasken Martineau, Hogan Lovells and Norton Rose Fulbright all entering the market either through mergers or forming alliances. This year has already seen Simmons & Simmons enter with an African alliance with Canada-based Fasken Martineau and Clyde & Co establish an office.

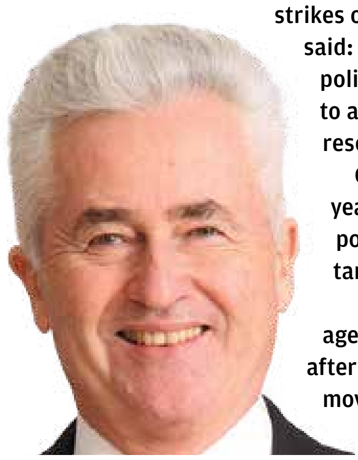
However, many have doubts over whether a South Africa-focused strategy will benefit a broader Africa offering, with some partners being told not to mention Johannesburg in pitches and to instead focus on the London office in order to win mandates.

In addition, the stalling South African economy has arguably seen it lose influence to other fast-growing regional states. The local market also remains heavily lawyered. Werksmans Attorneys chairman Des Williams comments: 'There will probably still be some further activity as global firms attempt to enter the African market through South Africa, but the market is probably close to its saturation point.'

Werksmans is one of a set of leading local firms competing with international firms alongside Bowman Gilfillan and ENSafrica. That competition is putting fees under pressure for international advisers, which are having to cut rates to compete with domestic firms who can do the work cheaper. Jones Day partner, Arman Galledari, says: 'South Africa's market is not as big as some others as it has an evolved domestic market, so there is not as much need for international law firms.'

Herbert Smith Freehills partner Martin Kavanagh agrees: 'The considerations for South Africa are very different [compared to other African countries]. South Africa is already very heavily lawyered and is very competitive, whereas virtually all other markets are absent of international firms.'

Domestic work is also suffering as the economy falters with high unemployment and inequality dragging on growth. The income disparity has held back demand in the country and even led to strikes over pay and conditions in some industries. Williams said: 'Growth has been impeded by labour unrest and political uncertainty. However, South Africa continues to attract investment, particularly in the energy and resources sectors.'



'The market is probably close to its saturation point.'
Des Williams, Werksmans

One of the government's biggest successes in recent years has been a series of solar and wind independent power plant auctions under its renewable energy feed-in tariff programme, which Linklaters helped design.

The auctions have warded off potential problems from ageing power plants and generated international interest after investors in Europe were hit by cuts to subsidies, moving them to look elsewhere for opportunities. The government is now looking to turn this success to coal-fired thermal power plants and potentially a hospital building programme.

The financial system has also been a bright spot despite the slowing economy, with South African banks such as Standard Bank remaining well-capitalised and leading investment into other nations, though the collapse over the summer of African Bank has created doubts in some quarters.

As competitive as it has become, there look to be no shortage of international advisers aiming to enter the market.

There are some variations, for instance Ashurst uses Middle East offices to help cover north Africa, while Baker & McKenzie and Mayer Brown handle Portuguese work from their Brazilian offices. Linklaters, meanwhile, uses its Lisbon arm for Lusophone coverage. Most international advisers have expanded and invested in their referral relationships at the same time.

One of the most significant developments in Africa, and especially sub-Saharan Africa, sees local players, such as Nigeria-bred manufacturing and real estate group Dangote, coming to the fore and taking on increasingly complex and ambitious projects. At the end of 2013, Triumph Power Generating Company provided 100% of the equity for an 81MW heavy fuel oil power plant in Kenya, while financing came from Standard Bank, its Kenyan subsidiary CfC Stanbic Bank and Chinese lender ICBC.

This has seen a shift in market dynamics, with local firms being first point of contact for domestic sponsors to either carry out the work entirely themselves, as in the case of Triumph, or to help them find international counsel.

Kem Ihenacho, corporate partner at Latham & Watkins, says: 'Increasingly, deals are being originated locally and even where the client is international, to deliver properly you need to know and be trusted by the local business community. So we spend a lot of time building and maintaining those relationships with local banks, the advisory community and business leaders.'

Anjarwalla & Khanna, part of the Africa Legal Network, advised Triumph on the 81MW power plant deal from the start and on the selection of Norton Rose Fulbright for the lenders. Amyn Mussa, senior partner at Anjarwalla, says: 'It matters to us – our relationship, how they help us build capacity in terms of training, secondments both to and from, and the events they invite us to in London.'

Oghogho Akpata, managing partner at Nigerian firm Templars, agrees on the importance of referral links. 'We look at skillsets and flexibility, but to us it's the ability to call a partner at 10pm and say: "I've got this deal. I need you to give me a fee quote or credentials by tomorrow morning and it will happen."'

RULES OF THE GAME

Although the money going into African infrastructure at the domestic level and flowing from the US has risen hugely in recent years, it still takes time for deals to get done. Freshfields' Pick comments: 'Commercial banks have been through a cycle of retrenching from project finance and then coming back, but large-scale African [project finance] deals can take a long time to close; it can take years before the liquidity available to a project actually gets deployed.'

Even with financing secured, there are still hurdles to overcome and deals are not guaranteed to complete. Legislation and regulatory frameworks are in poor condition across the continent, often because countries have not had to contemplate defined legal and regulatory systems for certain industries before.

Two of the largest projects currently being worked on provide a case in point. Following significant gas discoveries off Africa's east coast, liquefied natural gas (LNG) terminals are being developed in both Tanzania and Mozambique, with each development estimated to cost up to $20bn. The largest is in Mozambique, which is being developed by Eni and Anadarko Petroleum Corporation, as well as Indian and Chinese sponsors, but the country has yet to create a regulatory framework to support large LNG and offshore projects, according to several project advisers. For law firms on the projects, trying to help clients protect their interests, in an environment in which governments are intent on maximising their revenues from natural

'It's the ability to call a partner at 10pm and say: "I've got this deal. I need you to give me a fee quote or credentials by tomorrow morning."'

Oghogho Akpata, Templars

resources, potentially threatening the commercial viability of deals, is a delicate process.

Latham, alongside King & Spalding, and Linklaters are advising the sponsors on the development, while Dentons is working with the government on its framework with Lisbon-based MC&A acting on local law aspects. But time is also a factor. Manuel Santos Vítor, PLMJ managing partner, comments: ‘It is a race against time to develop these legal systems and solidify them while attracting international investment.’

If these projects do happen, they are touted as being transformational by the World Bank, providing cheap power to East and southern Africa. Rui Mayer, head of oil, gas and mining at Cuatrecasas, Gonçalves Pereira, agrees: ‘The development of the Rovuma gas reserves, which can be said to be the largest industrial project in Africa, will be a game-changer. When production starts, the revenue generated, if used wisely, will help transform Mozambique into something quite different.’ An initial run of large projects also makes it easier to get sign-off for subsequent deals for lending, raising the investment flows and stimulating the market for projects.

Latham’s Africa practice chair, Clement Fondufe, comments: ‘If you do a project of significant scale and scope, over a tenor of 15 years, then you just open up possibilities of investment in that country because, all of a sudden, a commercial bank that lends $500m to that project reduces the risk profile for the country. As a result, projects of $200m-300m won’t find much difficulty in raising financing.’

WEST COAST VIEWS

While east coast projects are in the initial phase, with greenfield deals dominating, west Africa’s infrastructure market is far more mature. Both Nigeria and Angola have highly developed oil and gas industries, resulting in project and energy lawyers learning to play in different positions, and getting involved in M&A and corporate work. Greenfield is becoming less important as oil majors divest their assets and local companies build their presence. Highlighting the extent of the crossover, Cameron Smith, head of Ashurst’s Africa group, says: ‘Our oil and gas team is primarily focused on M&A work, though they also remain involved in some greenfield developments.’

Andrew Jones, head of Linklaters’ Africa group, comments: ‘Crossover is really strong in terms of what we do. What one day is a projects client is the next an IPO client.’

Nigerian divestments such as Shell’s current sale of its 45% interest in OML 18 to Eroton come as the oil giants have moved to rationalise portfolios. Estimated to be worth $1.2bn, the deal is being handled by Shell’s in-house team while Templars advised Eroton on both the sale and financing with Clifford Chance as ▶

Eroton's international counsel on the lending side, and Hogan Lovells and Strachan Partners acting for the banks. The process will provide a sustainable source of mandates with a secondary market now developing – though local law firms are increasingly taking a portion of that work with domestic sponsors relying on them to carry out transactions.

Some have suggested another rationale for the divestments is a desire to minimise exposure to political risk. This can be one of the more tricky aspects to negotiate for an international law firm, with a certain amount of investor handholding required, but there are opportunities to move up the value chain. CMS Cameron McKenna partner Bob Palmer comments: 'Currently, we're doing a job in Africa, which is not legal analysis as such, but an analysis of the risks associated with the project and what has happened in that country. We're not only looking at past enforcement of laws and what powers the government has, but collating information about corruption, safety and security.'

However, Palmer adds: 'There have been stories about Africa that haven't been good, but you only have to go to other parts of the world like Russia and South America, where there has been very recent expropriation, to see examples of companies and investors being badly affected. Africa gets a bad rap when it comes to political risk. I'm not saying there isn't any, but in terms of political risk it is by no means on its own.'

Kenya is another country which has seen significant development and has confronted another challenge facing projects not tied to commodities: credit worthiness. The Kenyan government has bulked up balance sheets of several state-backed corporations to improve their credit ratings, leading Kenya to become one of the leading jurisdictions for power projects.

After carrying out a restructuring of power distribution monopoly, Kenya Power, which saw the government take majority ownership, complicated deals like Lake Turkana have managed to secure financing. The 310MW wind farm is one of the largest private investments into Kenya, with a capital expenditure of €546m. The lending group, which comprised African Development Bank (AfDB), Standard Bank and Nedbank Capital, alongside the European Investment Bank, was advised by Trinity International with local support provided by Nairobi-based firm Walker Kontos, while Allen & Overy was the international adviser to the sponsor, with Anjarwalla & Khanna on local law.

But while the power sector is clearly gaining momentum, partly thanks to creditworthy counterparties entering into power purchase agreements, it remains far more challenging to attract investment for social infrastructure

‘Africa gets a bad rap when it comes to political risk. I’m not saying there isn’t any, but in terms of political risk it is by no means on its own.’

Bob Palmer, CMS

and transport projects, which lack the secured revenue streams that commodity and energy projects enjoy.

Transport has seen some successes, with toll highways having potential income, while ports and airport have also seen interest as they can impose fees, but the demand for the infrastructure is often linked to commodities being transported rather than for wider economic development.

The Lagos cable car project being developed by Ropeways Transport, with local law advice from Banwo & Ighodalo, could be a break from this and has been cited as a bellwether transport project for the region. The project relies on using cable cars to provide public transport as it is cheaper and quicker than a conventional underground transit system. In addition, shopping centres and housing are being developed around the cable car stations and the project could free up Lagos’ congested streets.

The AfDB is onboard to provide financing, advised by Herbert Smith Freehills (HSF), while the sponsor’s international counsel is expected to be appointed once financing negotiations begin in earnest. HSF partner Martin Kavanagh says: ‘You’d never have thought a project of this type could be financed in Lagos even five years ago. This type of project is much more typical of an emerged economy.'

Social infrastructure has had even less success in attracting investment, with basic facilities such as schools and hospitals low in priority behind the economic infrastructure required to engender growth. David Tinel, International Finance Corporation's principal investment officer, comments: 'Clearly the power sector is where the most critical needs are. Until you can turn the lights on it is very hard to have sustainable developments in any of our client countries.'

Another high-profile project is a public-private partnership (PPP) for Uganda's police force. The project will upgrade the nation's police headquarters, training academy and barracks as Uganda seeks to improve the effectiveness of its police force, while 21 police stations will also be developed to provide modern facilities. The PPP is being advised by local firm Shonubi, Musoke & Co and, in a sign of how long it can take for deals to happen in Africa, it was originally joined by Deneys Reitz before it merged with Norton Rose Fulbright. However, the deal is one of the most progressed in Africa and is the most likely social PPP to succeed.

Outside of traditional projects, there are emerging areas of activity with deals relying on the growing prosperity of consumers. An increasing reliance on mobile phones in Africa as central to e-commerce as well as communications has seen project lawyers working on mast installations and now advising established providers on selling off existing assets to fund further expansion.

Having established mobile coverage, broadband is now also being looked at and one of the first major deals, due out by the end of the year, is being worked on by Baker & McKenzie and Templars. The duo are working with the Nigerian Communications Commission on a policy to create a broadband spine running up the country.

'Increasingly, deals are being originated locally. We spend a lot of time building relationships with local banks, the advisory community and business leaders.'

Kem Ihenacho, Latham & Watkins

Though telecoms is set to be a significant source of work for project lawyers as African companies and consumers increasingly rely on mobile phones to conduct business, the focus on the continent will continue to be extractive projects. In particular, most infrastructure specialists expect Africa's energy market to be transformed over the next decade as the east coast offshore gas discoveries are developed, providing cheap gas to southern and eastern Africa.

While the discoveries will lead to substantial work, even better prospects are in west Africa where the development of a secondary market heralds a sustainable future for energy lawyers acting in the region, with regular deal flow driving the action.

Even after a decade of rising investment, it remains clear why so many infra and project veterans remain increasingly transfixed by the region. It has barely begun to tap its vast economic potential. In comparison to Europe's commoditised, increasingly price-sensitive project sectors – it is easy to see why the lure of carving out bold, ambitious projects from scratch in emerging frontiers is so strong.

As CMS' Palmer concludes: 'The good thing about Africa is that it is a growth area. It has its challenges, partly because it's a massive continent with 54 countries and 54 governments and it's a diverse place to work, but it is very exciting.' **LB**

michael.west@legalease.co.uk