



The African Consumer and Retail

Sector Report

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OVERVIEW

Africa is home to more than one billion people, presenting a massive potential consumer market. Moreover, population growth remains rapid, and the United Nations (UN) Population Division forecasts that the continent's population will surpass the 1.5 billion mark by 2026 and the two billion mark 15 years later. In addition, Africans are increasingly moving to cities, making it easier for companies to target certain consumer groups. Although the demographic make-up of the continent is extremely favourable, success is not guaranteed. Firstly, there are vast differences across countries – North Africa is for example far more developed than sub-Saharan Africa (SSA), while the retail market opportunities in countries will differ due to variances in consumer tastes, culture, income, and demographics. Secondly, it is important to distinguish between opportunities at the national and at the city level. Data at the national level can often be misleading, as a city's GDP per capita can vastly exceed the national average due to the greater concentration of wealth in some urban areas. Finally, simply because a country has favourable demographics does not mean that this will necessarily translate into higher levels of economic growth and consumer spending. An increase in the proportion of the working-age population relative to the total population (the so-called demographic dividend) is potentially beneficial for consumer spending as it frees up resources. But this will not happen if there is a high unemployment rate in the working-age population.

Africa's retail sector remains relatively under-developed at present, with most shopping being done at traditional shops. The formalisation of the sector will be a key trend underlying the sector's expansion in the coming decade. The lack of physical infrastructure has been one of the main constraints to the entry of formal retailers, as there are simply not enough shopping centres available at present, while bureaucratic obstacles and land issues further complicate matters. At present, most African consumers – especially south of the Sahara desert – remain extremely poor and spend most of their money on food and other necessities. This makes for a promising outlook for fast-moving consumer goods (FMCG) companies given the large market to cater for. Crucially, an increasing number of consumers are on the cusp of the US\$1,000 annual income level, which will allow for the expansion of consumption beyond just the basics. Retailers will be looking to take advantage of the large market at the low end, while gradually starting to offer these consumers higher-value products.

The aim of this report is to analyse the key drivers of the retail market in Africa, including key demographic and macroeconomic factors, as well as spending patterns. In addition, we consider the broad outlook for the sector and highlight the countries we expect will have the strongest growth rates in the sector over the long term.

KEY DRIVERS

Demographics

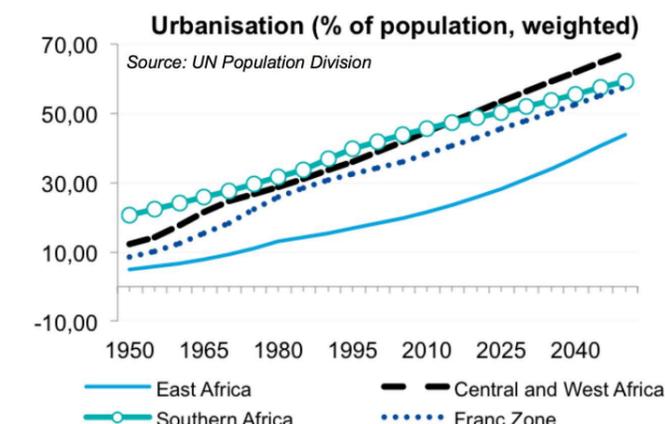
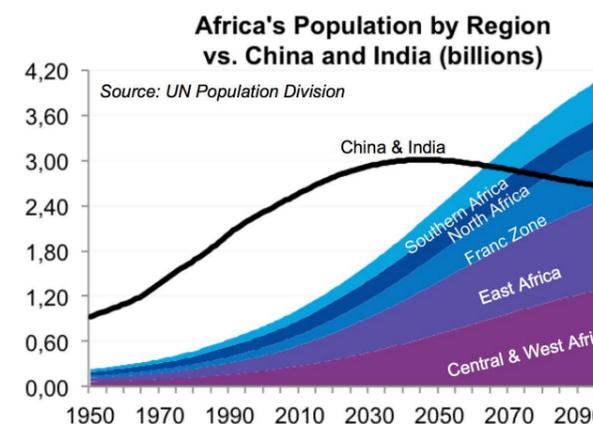
Demographic factors underpinning Africa's retail sector expansion include:

- A large population – estimated at just over 1.1 billion in 2014. SSA accounts for 81 % of Africa's total population, while Nigeria accounts for around a fifth of the SSA total. Other countries with notable population sizes include Ethiopia, Egypt, and the Democratic Republic of the Congo (DRC). These four countries account for 38% of Africa's total population.
- Population growth rates are still relatively high. This trend is confined to SSA countries, as population growth rates in North Africa have already declined significantly on the back of lower fertility rates. In turn, this trend is in line with differences between the stages of economic development that the regions find themselves in.

continent. East Africa's low level of urbanisation can be ascribed to the substantial importance of subsistence agriculture in most of these countries.

- Beneficial changes in the age structure. The composition of the population is crucial, as a large proportion of children and/or elderly in a population (i.e. a high dependency ratio) implies that the working population will have fewer resources to save and spend. The dependency ratio is therefore very important for forming a view on the outlook for consumer spending.

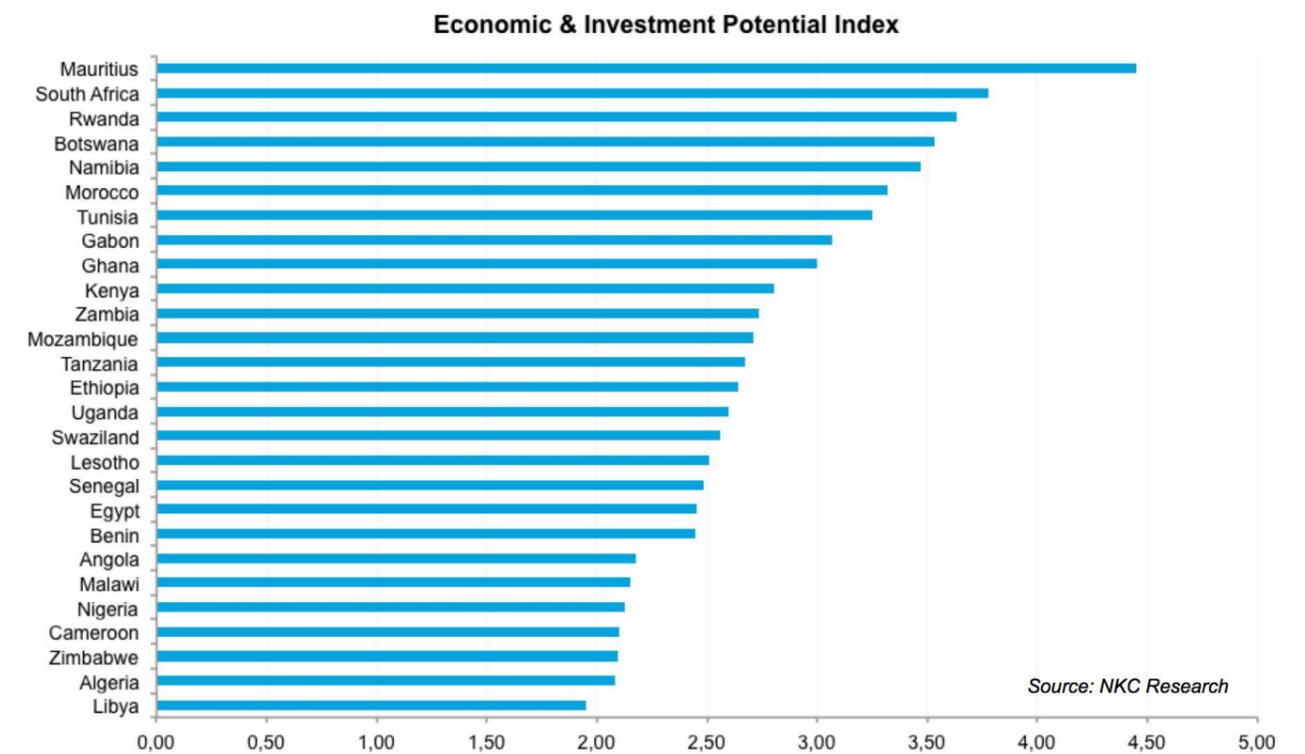
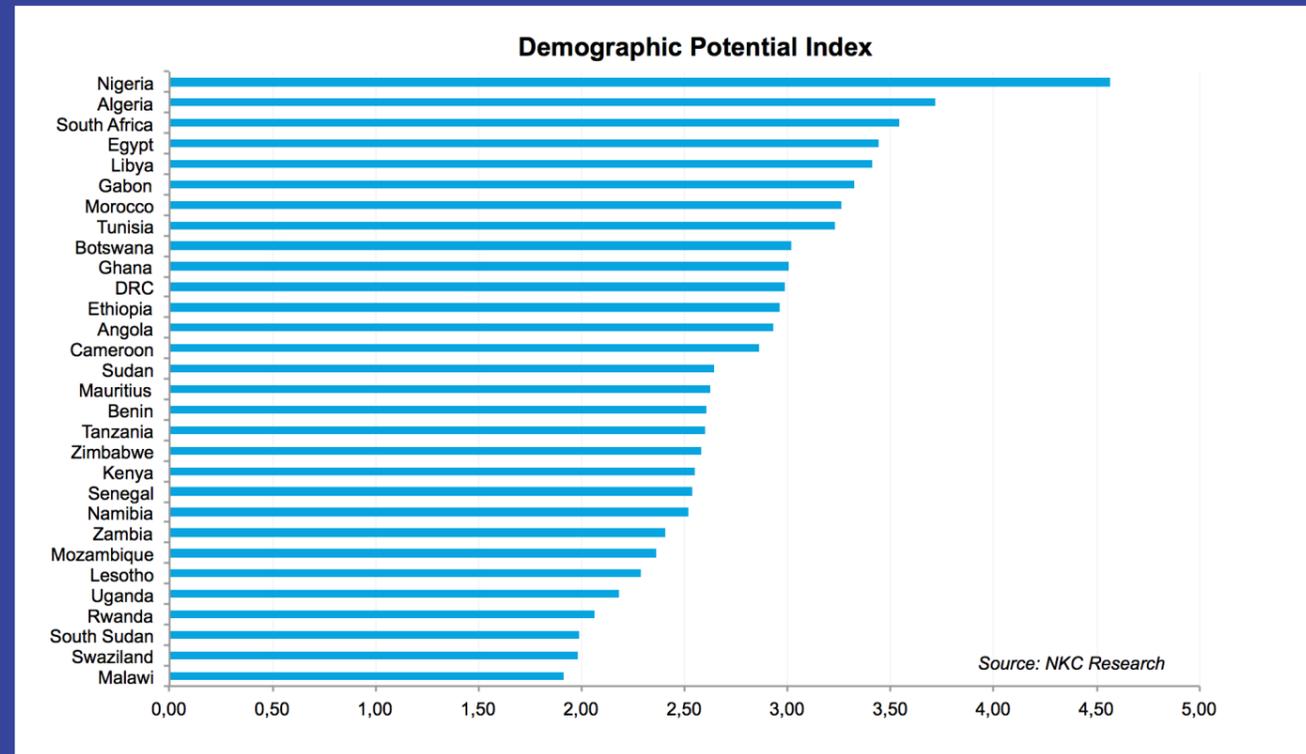
Taking the above factors into account, we have developed a Demographic Potential Index (DPI) for 30 African countries, which is shown in the accompanying graph. The index value can potentially range from zero (worst outcome) to 10 (best outcome). Due to its large population size, Nigeria performs



- Urbanisation rates are rising. The effect of urbanisation on economic growth – or vice versa – is dependent on job creation, the economy's structure, and – crucially – the definition of urban areas. UN figures indicate that in SSA, the urbanisation rate increased from 11.2% in 1950 to 24.1% in 1980, and 36.4% in 2010. (Note that this is a weighted average.) The UN forecasts that SSA's urbanisation rate will reach 45.9% by 2030 and 56.7% by 2050. The urbanisation rate of East Africa is much lower than the rest of SSA. In 2010, East Africa's urbanisation rate was almost 17 percentage points lower than that of the Franc Zone, which has the second lowest rate on the

the best by far. On the other hand, countries that outperform significantly relative to their population sizes include Gabon, Libya, Botswana, Tunisia, and Mauritius. These countries have the potential to benefit from demographic shifts despite having relatively small population sizes, due to either having an urbanised population, or due to the working age population accounting for a sizable proportion of the total. Meanwhile, countries that perform notably worse than their population sizes would suggest, include Uganda, Malawi, Kenya, Tanzania, Mozambique, and Ethiopia. For comparison purposes, note that China's index value is calculated as 8.8.





Macroeconomic Environment

Africa's economic performance has improved greatly since the turn of the century, leading to notable gains in GDP per capita and lower levels of poverty. During 2001-13, the SSA economy grew at an average rate of 6.3% p.a. in real terms, according to the International Monetary Fund (IMF), compared to 2.9% p.a. during the previous 13-year period. This meant that nominal GDP per capita rose from US\$571 in 2001 to US\$1,750 by 2013 after having declined during the previous two decades. The expansion coincided with an improvement in business environments and a reduction in political risk, although a commodity boom also played a significant role in the increase in real GDP. In addition, several African countries are expected to be among the fastest growing in the world over the next decade.

A key question is whether there will be the complementary economic reforms that are needed to ensure that economies benefit from demographic shifts, since a large working age population will count for nothing if unemployment is rampant. Apart from economic policies and reforms, other factors that are crucial to ensure that a country can benefit from demographic shifts are the effective mobilisation of national savings and a relatively skilled labour force.

In order to determine which African countries would be best placed to take advantage of their demographic profiles, an Economic & Investment Potential Index (EIPI) has also been developed. The following indicators were included in the index:

- GDP per capita – a proxy for wealth.
- Real GDP growth outlook.
- Main commodity export product as a percentage of the total – measure of diversity, exposure to shocks, and inequality.
- Ease of doing business.
- Financial market development – ability to mobilise savings.
- Consumer price inflation – measure of macroeconomic stability, and effect on consumers' purchasing power.
- Labour market efficiency – labour market flexibility has an effect on employment levels.
- Political risk with a medium- to long-term outlook.
- Business costs of crime and violence.

The countries that perform the best on the EIPI are generally those with good business environments. Four of the top five countries are from Southern Africa, with the only exception being Rwanda, a country that has made significant strides to encourage investment over the past decade. Apart from a favourable business environment, low political risk, and stable economic policy making, the economy is also not overly dependent on any single commodity for exports, and it is expected to grow strongly. On the other hand, Rwanda still has a very low GDP per capita and it also performs poorly on the DPI. North Africa's performance is highly varied. On the one hand, Morocco and Tunisia perform well thanks to their diversified economic structures, solid business environments and high GDP per capita (by African standards). On the other hand, Algeria and Libya are at the bottom of the rankings (despite high GDP per capita) due to their dependence on oil, challenging business environments, high political risk, and weak economic growth prospects.

Gabon's performance is also quite good – perhaps better than would be expected a priori. This is due to the country's large GDP per capita, although this could be slightly misleading as GDP is inflated by its oil sector. Two other oil-exporters – Angola and Nigeria – languish at the lower reaches of the rankings due to challenging business environments and commodity dependence.

Comparison with the 2014 Index

The top five positions remained unchanged compared to a year earlier. One of the big movers was Morocco, which

surpassed both Tunisia and Ghana to move into sixth position thanks to further improvement in its business environment, and to a lesser extent a drop in inflation. Notably, Nigeria's ranking on the EIPI deteriorated by three positions despite a large increase in its GDP per capita following the rebasing of its GDP. This is because its score deteriorated in almost all of the other components of the index. Further down the rankings, both Mozambique and Tanzania's rankings improved notably. Mozambique's ranking improved by three positions to 12th on the back of an improvement in its World Bank Doing Business ranking and a decrease in inflation. In turn, Tanzania's ranking improved by four positions to 13th. This came on the back of a 47% increase in GDP per capita following a rebasing of GDP, as well as an improvement in the business environment.

Although still having poor rankings, both Egypt and Angola's rankings improved by three places compared to last year. In Angola's case this was due to an increase in GDP per capita. In Egypt's case, there were notable improvements in its business environment and political risk. In the short to medium term, Egypt's consumers are expected to struggle due to large fuel price increases (as the government cut subsidies), high inflation, a weakening currency, and high unemployment. However, if the new government under President Abdel Fattah Al-Sisi sticks to its planned reform programme, then longer-term prospects for the economy are bright. The country that deteriorated the most is Libya, with its ranking slipping from 13th to last (27th). Uganda and Nigeria's rankings weakened by three places each, while Ghana's ranking slipped from seventh to ninth.

Consumer Demand Potential Index (CDPI)

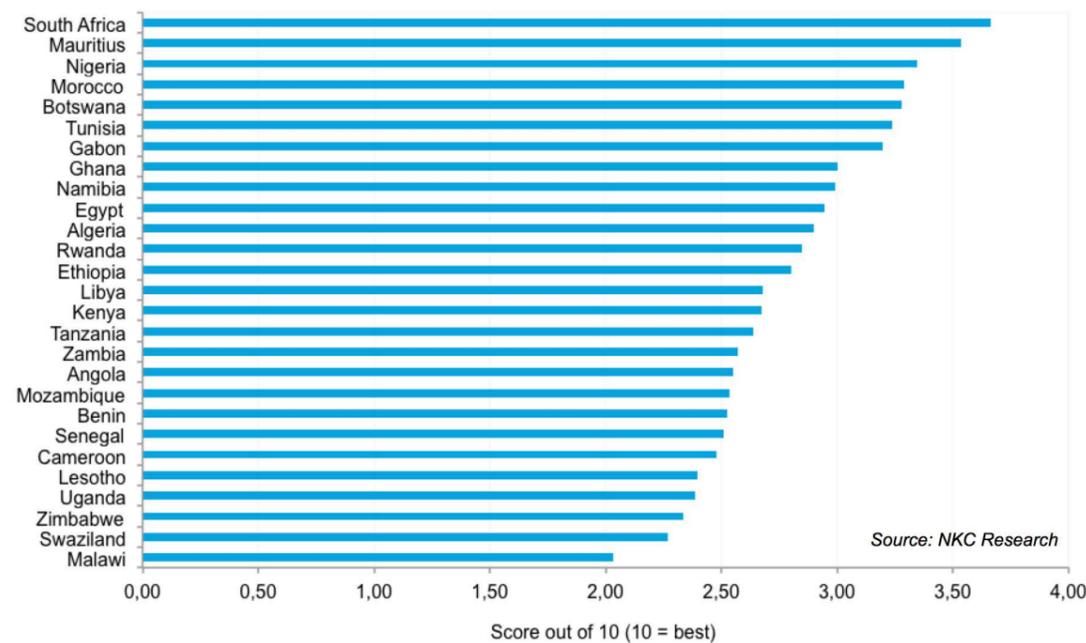
Combined, the DPI and EIPi aim to identify countries with the biggest potential growth in consumer demand. This is shown in the accompanying graph, where the two indices were given equal weight. As in last year's report, South Africa, Mauritius and Nigeria claim the top three positions. These three countries differ substantially from one another. South Africa has the most developed retail sector and has a fairly consistent performance across all sub-indices of the CDPI. Mauritius has one of the smallest populations on the continent, which constrains its DPI, but this is counterweighed by its diversified and well-managed economy and relatively rich population. In stark contrast, Nigeria offers investors with a very large potential market, but with risk, as it also has a very challenging business environment.

In fourth place, and moving up two places since last year, is Morocco. The country's demographic make-up is reasonably favourable, with a young population, rising urbanisation, and

growing middle class. In addition, a marked improvement in the country's business environment is now also making it easier for retailers to enter the market. The country is also becoming an increasingly important gateway to Africa for European companies. Botswana and Tunisia also perform well on the index thanks to its fairly young and urbanised populations, and solid business environments. However, both countries (especially Botswana) have small populations, which reduces their appeal for retail companies.

Gabon has held on to the seventh position, as the country has a good demographic profile combined with a high GDP per capita, which means that there is still a relatively large consumer market to cater for, despite significant drawbacks. Although Ghana has significant short-term challenges (large twin deficits and a depreciating currency), it does quite well in the CDPI since it is generally welcoming to foreign investors, has a favourable demographic profile, and has strong medium-term economic growth potential.

Consumer Demand Potential Index

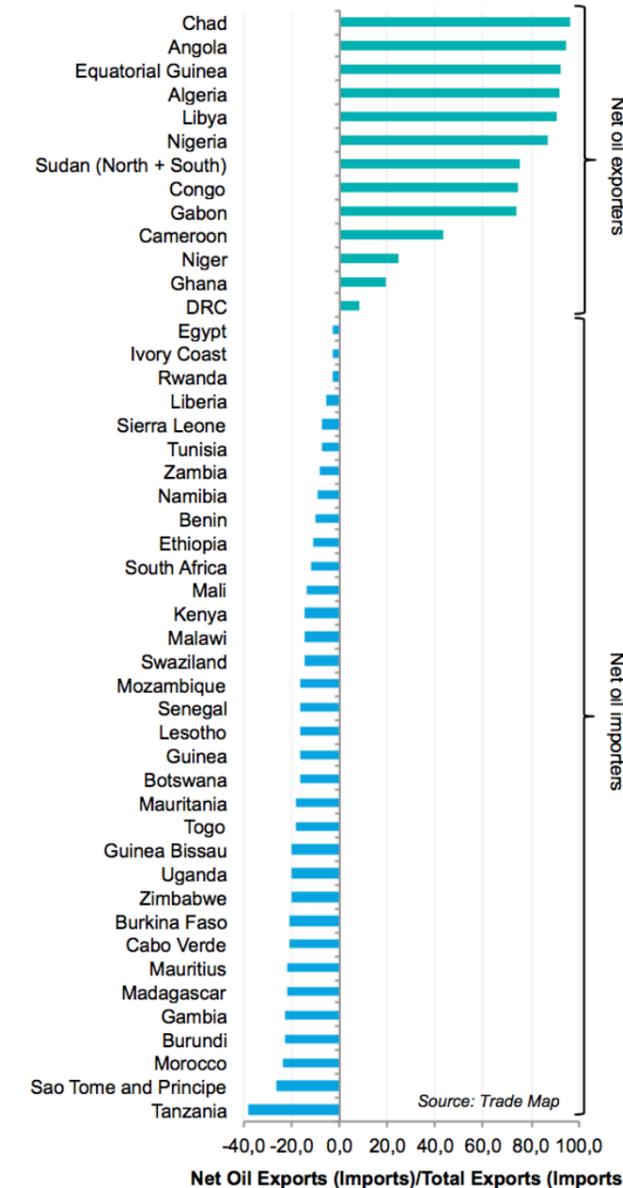


Comparison with the 2014 Index

The countries whose CDPI scores increased the most over the past year were Egypt and Benin. Regarding the latter, its score was boosted by the fact that it was ranked as one of the top 10 best reformers in the World Bank's most recent Doing Business index. Two other countries worth mentioning are Tanzania and Mozambique. Although still only ranked 16th and 19th respectively, their rankings are on an upward trend. These two countries still have extremely low income levels, with Tanzania's GDP per capita at only US\$955 and Mozambique's at US\$647. Therefore, over the short to medium term, retail will continue to focus on the lower-end of the income spectrum with FMCG companies being most prominent. However, both countries have strong economic growth prospects, and the development of their natural gas industries holds exciting long-term prospects due to the additional foreign exchange and fiscal revenues it will bring into the country as well as the opportunity for companies to provide services in the gas-producing regions.

Three countries' CDPI scores deteriorated fairly significantly over the past year, the most severe of which was Libya, which is in the midst of a civil war. The other two were Zambia and Ghana. The deterioration in Zambia's score was mainly due to its Doing Business ranking rising from 83rd globally in 2014 to 111th globally in 2015. In recent weeks, though, there have been signs of improvement, as the Lungu administration has reversed some controversial mining laws and we expect it to follow a more rational and business friendly approach in its dealings with foreign investors than the previous regime. Ghana's score weakened on almost all the sub-indices, with the most important contributors to the deterioration being lower GDP per capita, lower real GDP growth prospects, an increase in political risk, and a weaker rating on the Doing Business index. The core of the problem for Ghana, though, is its weak fiscal finances, which have contributed to a widening current account deficit, a depreciating currency, increasing levels of inflation, high interest rates, and an increase in tax rates. All these factors, in addition to ongoing energy shortages, are likely to keep real GDP growth under pressure over the short term.

Winners & Losers From Lower Oil Prices: Net Oil Exports/Imports as % of Total Exports/Imports (2013)



Impact of Lower Oil Prices

As a continent, Africa is one of the world's largest net oil exporters. Therefore, the sharp drop in oil prices since mid-2014 is expected to have a negative impact on Africa's aggregate economic growth prospects. However, it is worth reiterating that Africa is not one big country; indeed, the majority of African economies will be benefited greatly from the drop in oil prices. The accompanying graph illustrates this by showing the following:

- In the red bars: net hydrocarbon exports (i.e. exports minus imports) as a percentage of total exports for net oil exporters; and
- In the grey bars: net hydrocarbon imports (i.e. imports minus exports) as a percentage of total imports for net oil importers.

The countries at the top of the chart – those that are most dependent on oil exports – will be severely negatively affected by the drop in oil prices. Nigeria, for instance, has already devalued its currency by more than 20% since the start of November and pressure on the currency will remain strong as long as oil prices remain low. In turn, this pushes up the cost of imports, which hurts consumers' purchasing power. Meanwhile, Angolan banks have restricted foreign exchange transactions due to the lower availability of dollars. This has made it difficult for foreign companies to repatriate profits or to import goods. The government has also put import restrictions on a wide variety of products. This has already had a negative impact on consumer goods companies operating in the country, especially those that need to import their products. In addition, the Angolan government (which subsidised fuel products) has raised fuel prices by 50% since the end of 2014 in order to cut subsidies in support of its budget. In mid-February 2015, the government also slashed its budget for the year by 35%.

The top nine economies in the graph (up to Gabon) are all highly dependent on oil, especially their fiscal finances. Therefore, their governments will be forced to respond to the drop in oil revenues by reducing fiscal spending, which could have knock-on effects for employment (especially in the construction sector if the government cuts public investment), wages, and subsidies, all of which will affect consumer spending. (Possible exceptions are Algeria and Libya, who have exceptionally large stocks of forex reserves, which they could use to finance spending.) Although many of these economies will still offer strong long-term opportunities, it is important to take note of the risks that emerge when oil prices are low.

As shown in the graph, the vast majority of African countries are net oil importers and will therefore benefit from the drop in oil prices. Most notably, consumers will benefit from a sharp drop in fuel prices, which will increase their ability to spend on other products. There will also be a notable decrease in their import bills, which will lead to an improvement in their current account balances and therefore the availability of foreign exchange. Morocco, for instance, struggled with a very large current account deficit in recent years, largely due to its large oil import bill. As a result of this, commercial banks struggled with tight liquidity conditions in recent years, which constrained credit growth. Now with the current account balance set to improve, banking sector liquidity should also improve, thereby facilitating lending, which in turn is expected to boost investment in new and existing businesses, which would boost employment. With a few notable exceptions, countries in Southern and East Africa will tend to benefit the most from the drop in oil prices, while West Africa will be the hardest hit.

INCOMES AND SPENDING PATTERNS

Defining the Middle Class

The African Development Bank (AfDB) estimates that the size of the African middle class was 350 million people in 2010, or 34% of the population. The AfDB's definition of the middle class is daily per capita consumption expenditure of between US\$2 and US\$20. However, there is a lot of criticism against this definition, as it includes people that can barely make ends meet. After all, the World Bank uses the US\$2/day benchmark as a poverty line. One can hardly be considered middle class by spending only US\$720 a year. The AfDB acknowledges as much, referring to people spending between US\$2 and US\$4 per day as the 'floating class' – a vulnerable group that could easily fall back into poverty. According to David Cowan, a senior economist for Africa at Citi, a more realistic definition of middle class in emerging markets is income of at least US\$13.7 per day, which is enough to allow consumers to purchase durable products. This is equivalent to around US\$5,000 per year.

The following table, which is loosely based on the World Bank's classification, provides a breakdown of income brackets, as well as the key characteristics of these groups.

As we discuss below, most Africans south of the Sahara are still clustered within the low income grouping. For these people, the focus is merely on survival. Consumption decisions therefore centre on the fulfilling of basic needs and are only made with a short-term outlook. People in this category usually live a subsistence living, with little left for savings. As people start to move away from a subsistence lifestyle, output per person rises, moving them into the lower middle income group. People in the emerging middle class have usually migrated to urban areas in search of better job opportunities. Once people start to earn more money and move into the middle income group, brand consciousness is awakened and more emphasis is placed on quality. The upper middle income group is categorised by very high purchasing power and increased leisure time. The quality and convenience offered by products and services become increasingly important. Finally, people classified in the high income group have extremely high levels of purchasing power, and quality, convenience, variety, and luxury are valued greatly.

| Income brackets (2012 US\$) | | | |
|-----------------------------|-------------------------|-------|---|
| Income group | Income bracket (\$/day) | | Key characteristics |
| Low income | 0.00 | 2.84 | Subsistence agriculture; fulfilling of basic needs; day-to-day survival. |
| Lower middle income | 2.84 | 6.99 | Output per person rises so that there is less of a subsistence living. |
| Emerging middle class | 6.99 | 11.19 | Usually in urban areas, these consumers have emerged from the previous two brackets and are striving to be in the middle class. |
| Middle income | 11.19 | 18.63 | Brand consciousness is awakened, and more emphasis is placed on quality. |
| Upper middle income | 18.63 | 34.56 | High purchasing power; quality and convenience are increasingly important. More leisure time. |
| High income | 34.56 | - | Very high purchasing power; quality and luxury products are valued highly. |



Spending Patterns

Spending patterns are determined by disposable income per capita, in addition to other factors such as tastes, culture, and idiosyncratic preferences. Despite cultural and regional factors having an impact on consumer spending patterns and trends, one generally finds quite a strong positive relationship between income per person and consumption per capita for various goods irrespective of these other factors. This enables the mapping out of a generalised spending pattern across the income bracket. At the lowest income bracket, there is very little money (if anything) left to spend after basic needs have been met. Therefore, at the bottom of the income bracket, consumption is mainly on food, much of which has been produced on a small plot of land rather than purchased. Any excess production is then bartered or sold in order to pay for other necessities such as clothing and shelter. As soon as people start producing more than they consume, funds become available to spend on more than just the basics. The US\$1,000 income level has been identified as an important barrier that if reached, allows for an expansion in the amount and type of consumer products that can be afforded. The first important trend is

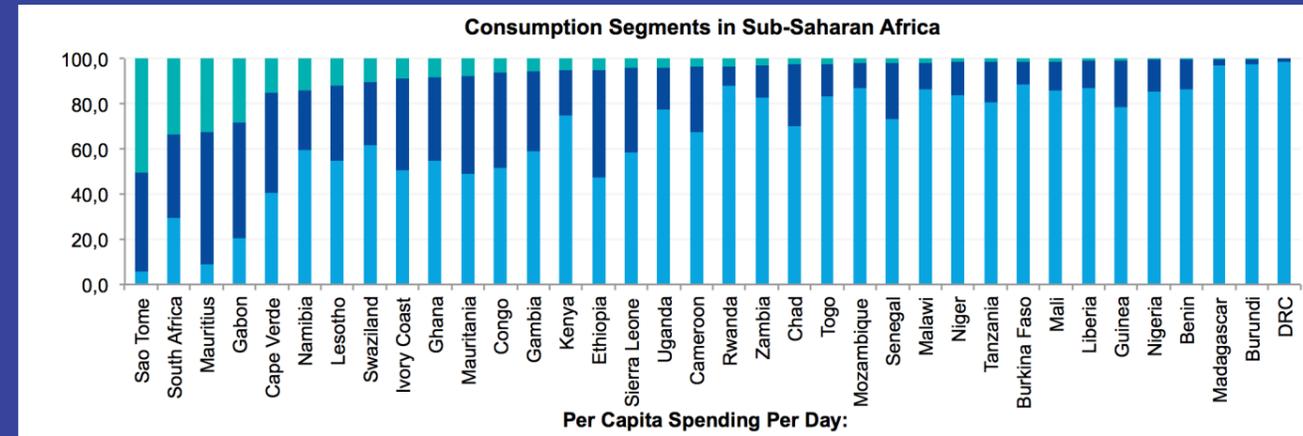
an expansion in the amount of food consumed, in order to boost the daily caloric intake to healthy levels. Following this, a further increase in income will allow for a switch to better quality and/or more convenient foods, for example the gradual introduction of meat and processed food into the diet. Some of the first non-food products to benefit from the expansion of annual income beyond the US\$1,000 level are beer, soft drinks, and prepaid mobile phones.

Moving into the emerging middle class allows for further increases in quantity and quality. For example, consumers will start shifting from unbranded beers to branded beers – first to economy brands, and later on, to premium brands. Eventually, when incomes increase even further, consumers will start shifting away from beer towards products that are viewed to be more sophisticated, such as brandy, whisky, and wine. Even in this consumer bracket, further differentiation is possible, i.e. from mainstream to premium products. The same types of shifts occur for other consumer products, e.g. switching from chicken to red meat or from carbonates to energy drinks.

Breakdown of African Income Groups & Estimating the Size of the Middle Class

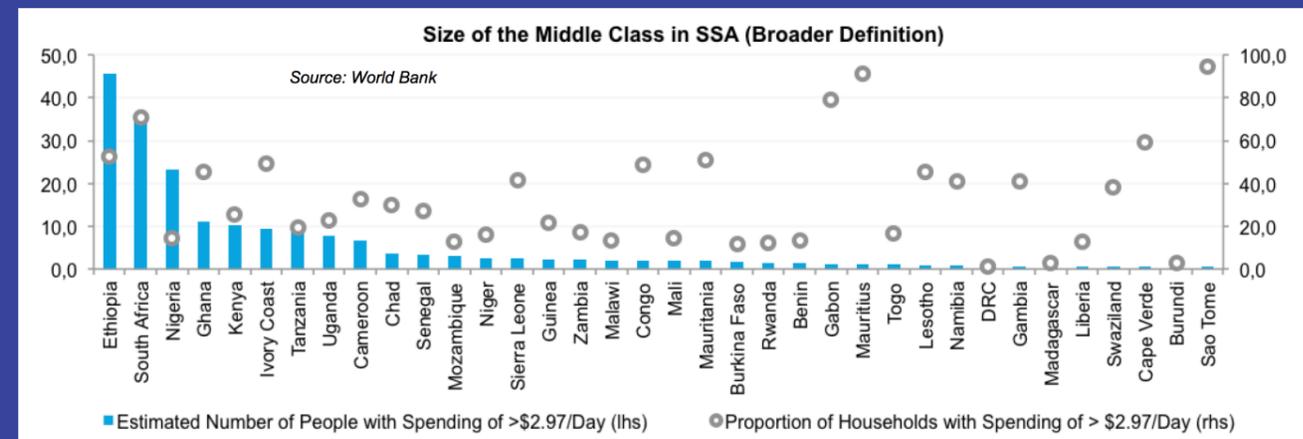
The first graph in this section shows the breakdown of households by their per capita spending (based on the World Bank’s Global Consumption Database). Only a few countries on the continent have a notable proportion of households that spend more than US\$8.44 per day; in fact, this proportion is above 10% of all households in only eight countries. And, of these eight countries, only South Africa has a large population. Furthermore, in 29 of the 36 countries in this sample, more than half of all households have spending per

capita of less than US\$2.97 per day. In most countries, the focus for investors will therefore be the FMCG segment, as most people are not able to afford durable or luxury goods. That said, even though the proportion of middle- to high-income groups is generally low, some of the more populous countries will still have a reasonably large middle class in absolute terms. In particular, there are bound to be opportunities in some of the well-off suburbs of the financial capitals of some countries, including Lagos and Nairobi.



In order to get an idea of the size of the middle class in SSA countries, each country’s population was multiplied by the share of households that have per capita spending of above US\$2.97 per day. There are problems with this method. Notably, the household consumption data are based on survey data, and the World Bank notes that the sample sizes, particularly for the higher consumption segments, “may be very small and not representative.” Nevertheless,

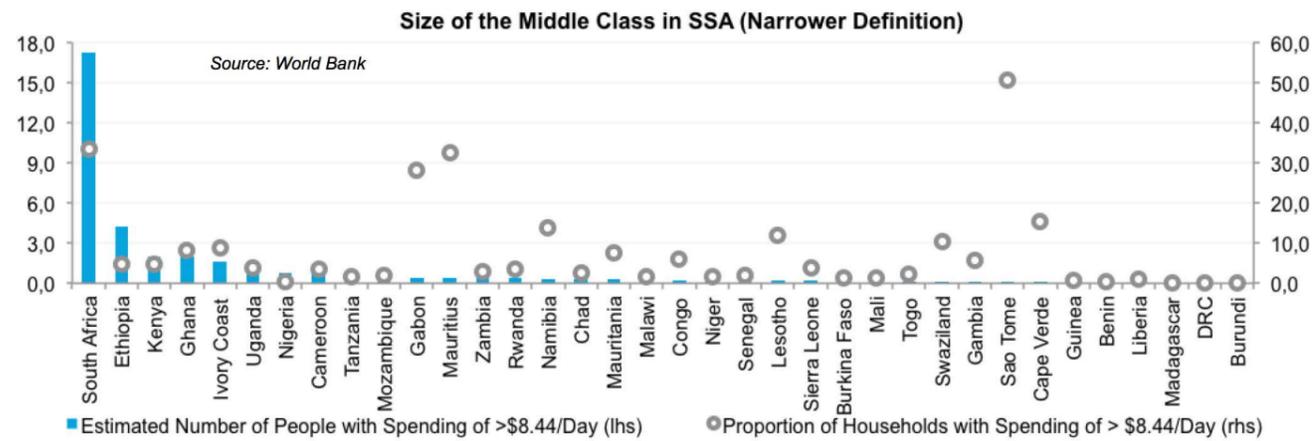
it could still provide valuable insights into the potential market size of SSA countries. In the first of the two graphs, a broader view of the middle class is taken, similar to the one employed by the AfDB study, and all households with per capita spending of more than US\$2.97 per day are included. This gives a total SSA middle class of 200 million people, 63% of which live in Ethiopia, South Africa, Nigeria, Ghana and Kenya.



The above definition is probably too wide for a middle class, though, and therefore the number of people that earn more than US\$8.44 per day is also estimated. Based on this ‘narrower definition’ of the middle class, Africa has 36.2 million people in the middle class, 48% of which reside in South Africa. According to these estimates only five other SSA countries have more than a million people in the middle class. These are Ethiopia, Kenya, Ghana, Ivory Coast, and Uganda. One of the most notable results is that Nigeria’s middle class is relatively small, at only 803,200 people. It is possible that the data underestimates Nigeria’s middle class due to the small sample size; however, the result stands to reason considering World Bank poverty statistics that show that around 70% of Nigerians still live on less than US\$1.25 per day.

Although having relatively small middle classes in absolute terms (400,000 people), there is a relatively large proportion of middle class people in Gabon (28.2% of households) and Mauritius (32.5% of households). Mauritius also benefits significantly from the steady influx of tourists, who are generally well-off and boost the demand for some products, such as souvenirs and clothing. As such, developments like the Bagatelle Mall south of Port Louis, Sunset Boulevard in Grand Bay and Le Caudan Waterfront in Port Louis continue to attract a constant flow of people. All countries in the graph up to Chad have middle classes of more than 300,000 people, thus providing at least some opportunity for retail companies looking to sell more than just the basic products.





Consumer Traits

In a survey done by Nielsen in seven African countries, namely Ethiopia, DRC, Kenya, Nigeria, Tanzania, Uganda, and Zambia, the affordability of brands was found to be the most important factor in influencing consumers' decision to buy, picked by 37% of respondents. Brand loyalty also plays a big role, with 31% of respondents saying they always buy the same brand. (The survey is based on face-to-face interviews with 5,000 urban and peri-urban residents between the ages of 15 and 45 across income groups.) Some interesting results from the survey are listed below:

- Of the seven countries, Ethiopia has the lowest per capita spending on consumer packaged goods (CPG), Nigeria's nominal spending on these products is the largest, while Tanzania has the largest number of CPG categories with a penetration rate of higher than 75%.
- Zambia has the lowest TV penetration (67% compared to an average of 90%), while the DRC has the lowest usage of print media.
- Kenya has the highest penetration of modern retail channels.

The fact that Africa's population is a lot younger than the rest of the world is an important point for retailers to consider. According to the UN Population Division, the proportion of

Africans under the age of 25 is projected at around 55.5% in 2015, compared to 37.8% in South America, 36.6% in Asia, 29.1% in Northern America, and 23.9% in Europe. These young people have significantly different tastes, preferences, and aspirations than older generations, and this would be reflected in their demand for different products.

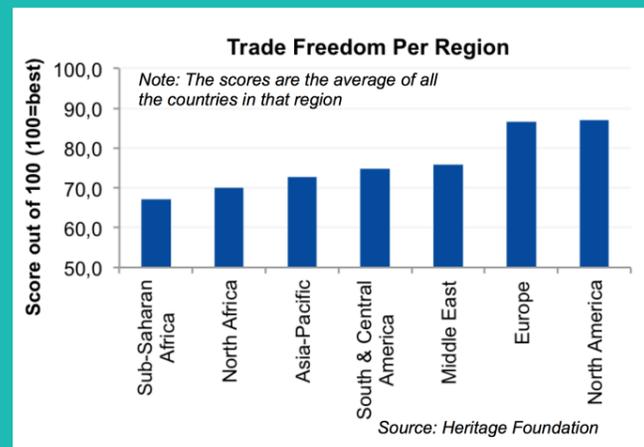
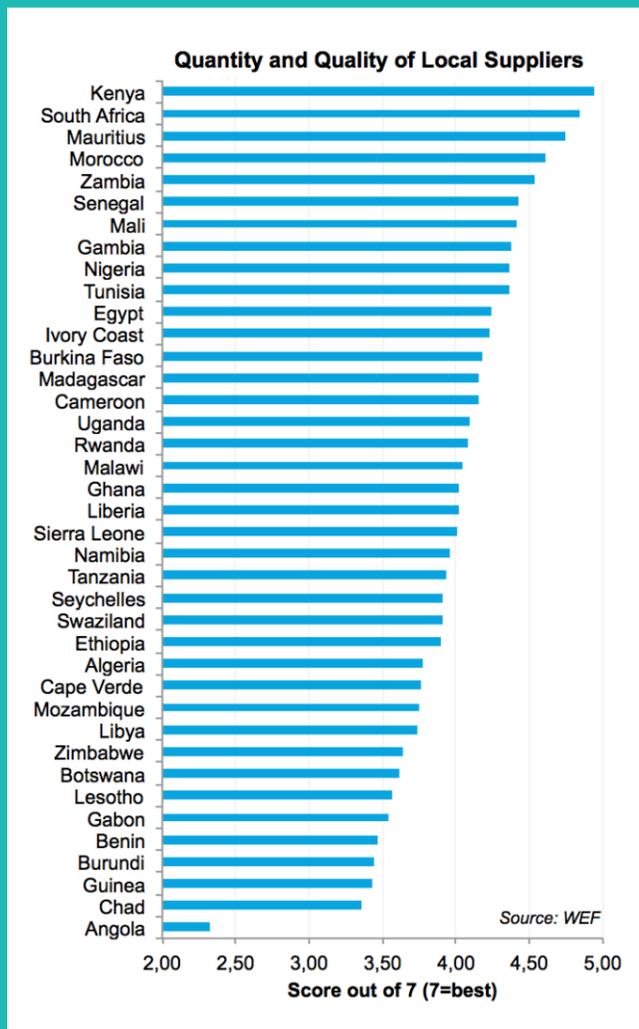
Another important trend to consider is the rise of female buying power. With more and more women earning their own money (and with fertility rates declining), this is an important expanding market for retailers to explore. The reduction in fertility rates results in an increase in time spent on other activities, as well as in an increase in the available discretionary income. With more women having careers, the importance of convenience with regard to the shopping experience has also come to the fore, which might help the development of formal retail in Africa. "The rising middle class has meant that convenience has become important for modern time-strapped consumers, with women in Africa enjoying the mall culture, while wanting instant access to information and technology and staying connected via social networking and mobile phone technology," according to Daphne Kasriel-Alexander, consumers editor at Euromonitor International.



CHALLENGES

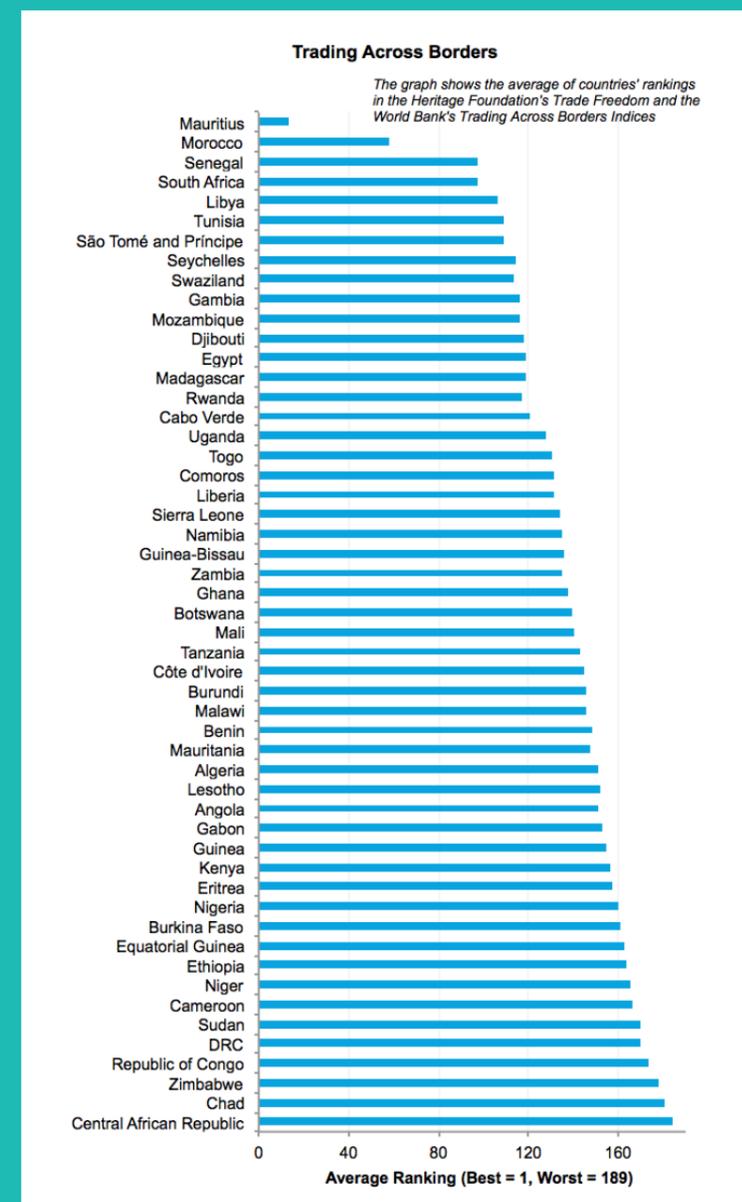
The lack of physical infrastructure has been one of the main constraints to the entry of formal retailers, as there are simply not enough shopping centres available at present, while bureaucratic obstacles and land issues further complicate matters. For example, according to the UACN Property Development Company in Nigeria, Lagos had only three international standard-sized malls (of at least 20,000 m2) as of October 2013, and could easily hold 20 - 25 malls owing to its large population.

The ability to source products locally is an important factor for retailers. Since most African countries lack an established manufacturing base, they are often forced to source goods from overseas, which increase their costs (through high transport costs and import tariffs), while also making supplies less reliable. To make matters worse, poor transport infrastructure makes supplies even more unreliable: not only is road infrastructure very poor across Africa, but there are often bottlenecks at harbours for imported goods. The accompanying graph shows the quantity and quality of local suppliers, based on surveys by the World Economic Forum (WEF). (The scores in the graph are an average of the 'local supplier quantity' and local supplier quality' sub-indices of the WEF's Global Competitiveness Index). Kenya performs remarkably well, especially in terms of the quantity of local suppliers where it is ranked 19th in the world. However, only five countries in Africa are in the top half of the global rankings and most African countries score very poorly on this indicator. Angolan companies in particular seem to have extreme difficulty sourcing products locally. Prospective investors therefore have to take exceptional care to secure reliable suppliers before entering the market across the continent. Thorough research of the logistical and distribution channels will also be needed, given the poor quality of infrastructure.



Another major problem in many African countries are high import tariffs. Since it is difficult to source local products, African countries often rely on imports for a wide range of goods. However, if import tariffs are high, it implies that retailers need to ask high prices for them to sell goods profitably. In some instances, this will lead to traders smuggling goods via informal channels to avoid taxes. In Maputo, Mozambique, for instance, informal traders smuggle goods from South Africa, which enables them to sell their products for up to three times less than formal retailers, thereby making it difficult for retail companies to compete with informal traders on imported goods.

Based on the trade freedom category of the Heritage Foundation's Index of Economic Freedom, Africa (and SSA in particular) lags the rest of the world in terms of trade freedom. As can be expected, though, there are intraregional differences, with Mauritius enjoying a very high degree of trade freedom (ranked ninth out of 181 countries globally) and Rwanda performing fairly well (ranked 68th), but most other countries ranked outside the global top 100. In the accompanying graph ('Trading Across Borders') African countries' rankings in the Heritage Foundation's Trade Freedom and the World Bank's Trading Across Borders Indices have been combined.



RETAIL MARKETS IN A SELECTION OF KEY AFRICAN ECONOMIES

Africa's retail sector remains relatively under-developed at present, with most shopping being done at traditional shops. Much has been said about the prospect for consumer spending in Africa, driven by demographics and rapid economic growth. This has fuelled massive interest from international retailers to establish a footprint on the continent. Given that many Africans tend to be brand-loyal, it is important to enter the market at a relatively early stage, in order to have first-mover advantage and to establish brand loyalty. Five underlying trends are expected to boost Africa's retail sector over the long term, namely:

- Robust economic growth relative to the rest of the world;
- Still-low penetration rates of most consumer goods;
- Saturation levels and lack of further growth in mature markets;
- The expansion of modern retail outlets, and the general improvement in infrastructure; and
- A shift in the preferences of African consumers from informal shopping outlets to modern formal Western-style retail.

An increasing number of consumers are on the cusp of the US\$1,000 annual income level, which will allow for the expansion of consumption beyond just the basics. Retailers will be looking to take advantage of the large market at the low end, while gradually starting to offer these consumers higher-value products. In essence, the key strategy for most

retailers focussed on Africa will be to 1) capture the large low-end market, and 2) benefit from higher margins as these consumers start trading up, e.g. from unbranded to branded beer. By establishing brand loyalty at an early stage, consumer goods companies can benefit from the growth of the African consumer. This is not to say that there is not potential for the luxury goods sector as well, although it remains in its infancy at present in most countries.

Using our demographic and economic potential indices as a guideline, but also taking other factors into account (including the current level of formal retail, penetration rates of consumer goods, the prospect for policy reforms, and the potential for regional expansion), we have identified five countries that we believe show the biggest promise for retail development over the long term. These countries are Egypt, Ghana, Kenya, Morocco, and Nigeria. Since our 2014 report, Algeria has been excluded – despite a relatively poor showing in the Consumer Demand Potential Index, the country was included in the previous report due to its strong demographic potential, which implies that if economic policies improve, the retail sector could truly prosper. However, due to the country's dependence on hydrocarbons, the recent drop in oil prices has weakened its economic prospects. Algeria has therefore been replaced with Egypt, which has excellent long-term retail prospects due to its large, young population, and high population density along the Nile. The economy is also gradually recovering from the political turmoil of the past four years, with economic growth subsequently expected to increase.

| Demographic indicators | | | | | | |
|------------------------|------------------------|-------------------------|--------------------------|--------------------------|-------------------------------------|-------------------------------------|
| Country | Population Size (2014) | Population Size (2030F) | Urbanisation Rate (2010) | Urbanisation Rate (2030) | Working-age population/total (2015) | Working-age population/total (2030) |
| | million | million | % of Total | % of Total | % | % |
| Egypt | 83.4 | 102.6 | 43.4 | 49.6 | 63.2 | 65.7 |
| Ghana | 26.4 | 35.3 | 51.2 | 62.8 | 58.5 | 63.1 |
| Kenya | 45.5 | 66.3 | 23.6 | 33.2 | 55.4 | 59.8 |
| Morocco | 33.5 | 39.2 | 56.7 | 64.6 | 67.0 | 66.2 |
| Nigeria | 178.5 | 273.1 | 49.0 | 60.8 | 52.9 | 55.1 |

Source: UN Population Division

Note: Green shaded areas indicate where countries perform relatively well; red shaded areas indicate where countries perform relatively poorly, while unshaded areas are neutral.



Egypt

Positives: Youthful population; emergent middle class; continued urbanisation

Sectors: FMCG; clothing; luxury goods

Risks: Purchasing power of consumers under pressure at present due to high inflation; threat of terror attacks by jihadist groups on shopping malls; low economic growth; high unemployment

Traditionally, Egypt is a nation of street retailers, with most Egyptians shopping in local neighbourhoods and at classic souks such as Cairo's Khan el-Khalili. The country's retail sector has been struggling since 2011 due to the uprising and subsequent political turbulence. Furthermore, high inflation has been the norm in recent years and has eroded consumer purchasing power, forcing consumers to cut costs and shop for second hand goods. On the upside, political stability has returned after the 2014 election, with the government committed to promoting economic prosperity. According to Euromonitor, retail (especially in the grocery industry) saw a slight improvement in 2014 because consumers tended to prioritise the purchase of essentials when their incomes were hit hard by inflation.

Western style malls were introduced to the country around a decade ago with the opening of the Maadi City Centre and City Stars. More projects such as the Mall of Arabia and Cairo Festival City followed, but the political upheaval of recent years slowed further progress. Post-2014 optimism has seen major retail pioneers, such as Majid Al Futtaim, announcing that it plans to expand its investments in Egypt by about E£18bn (US\$2.4bn) over the next five years. The new developments include the 455,500 m² Mall of Egypt, which is to be located in Sixth of October City. Mall of Egypt will be host to 420 stores and will include Ski Egypt, the first indoor ski slope on the continent of Africa. Other, notable new mall projects include the expansion of the City Centre Alexandria by another 12,000 m².

Despite, the growing optimism toward Egypt as an investment destination, many malls have vacancy rates of 25% and higher due to retailers remaining wary of the country's political environment.

This phenomenon should abate as longer periods of political stability are experienced, which would create an opportunity-rich environment for retailers wishing to set up shop in future.

As is the case with many of its African peers, **e-commerce** is showing great potential in the Egyptian retail market. Egypt is one of Africa's most advanced markets in terms of internet penetration, with internet users numbering half of the adult population in the country, and still growing. The major online retailer, Jumia, has recently established its first retail hub in Giza in order to capitalise on the growing number on online shoppers in the North African nation.

Outlook – Retailing in Egypt is expected to see a recovery over the coming years, supported by a wide array of factors. These include greater political stability, stronger economic growth and a rising level of disposable incomes. Sales growth in both the food and non-food retail sectors should benefit from increased urbanisation, a youthful population and widening internet access in the North African country. As investment in Egypt's formal retail industry improve, so more people should move towards modern retailing spaces as opposed to the conventional market or neighbourhood retailer. Furthermore, according to yStats, online shopper penetration in Egypt is less than 10% at present, which means that massive potential exists in this market especially as the stable political environment persists. Since Egypt still has around 25.2% of individuals living below the US\$2 per day (2011 dollars) poverty line, and due to higher inflation as well as high unemployment rates, the food and lower-end of the clothing retail sector will dominate over the medium term.

Ghana

Positives: Opportunity to benefit from first demographic dividend; generally accommodating business environment; popularity of shopping centres

Sectors: FMCG; clothing; electronics; appliances

Risks: Purchasing power of consumers under pressure at present due to high inflation and depreciating currency; risk of higher taxes due to the government's weak finances

Ghana's modern retail sector is restricted mainly to Accra, with some recent activity in Kumasi. In addition, most Ghanaians still do their weekly shopping at street markets as the middle class, who typically frequent modern shopping malls, is still small. Although there are currently only a small number of international retailers on the scene, the comparatively accommodative business environment makes the West African country more attractive as an investment destination. Ghana was ranked 70th out of 189 countries in the 2015 World Bank Doing Business survey. Only three countries in Africa are ranked higher than Ghana: Mauritius (28th), South Africa (43rd), and Rwanda (46th). It is also less of a problem to source products in Ghana than it is in some other African countries. Companies that have set up manufacturing facilities in the country include Unilever, PZ Cussons, and Denmark's Fan Milk Group. Retailers can therefore buy a variety of products locally rather than import them.

The West Hills Mall (27,000 m²) on the Accra-Cape Coast Highway, the largest of its kind in Ghana, opened its doors for business on 30 October 2014. The new development boasts two anchor tenants, Shoprite and Palace, as well as 63 line shops. The success of this mall, which has a 100% occupancy rate, has also spurred the developers of the first phase, Delico Investments, to draw up plans for additions to the mall, which will add 12,154 m² of retail space to the facility. The success of developments such as the West Hills Mall, Accra Mall (22,900 m²), A&C Square Mall (10,000 m²) and the Oxford Street Mall (6,230 m²) have prompted further development plans, with Broll Property Group projecting in its 2014 annual report that more than 165,000 m² of formal retail space will come into operation by the end of 2016. The rapidly growing demand for shopping options is outpacing the supply of viable modern shopping spaces in the West African nation, where retail rents have pushed to levels as high as US\$60/m², according to Broll property. Other notable new developments include the Achimota Mall (13,000 m²) and the Kumasi City Mall (27,000 m²).

A number of South African retailers have expressed a desire to expand their presence in Ghana, and to take up space in

new developments. These include Shoprite, Game, Foschini, Mr Price, Spur, Truworths, Woolworths, Edgars, Famous Brands and Pick and Pay. Well-known international retailers have been more reluctant to enter the market, although Zara, Mango, Hugo Boss, Tommy Hilfiger, and TM Lewin have recently shown interest.

Investors, developers and retailers are also monitoring a number of key risks such as the depreciating cedi, high inflation, the recent slowdown in economic growth, the government's large fiscal deficit and the erratic electricity supply. Some of these issues are however being addressed: most notably, the recent start-up of the Atuabo gas processing plant will boost Ghana's electricity-generating ability and the signing of an economic reform programme with the IMF will help to reduce the budget deficit over the medium term, which in turn would also reduce inflation. This will however take a few years to start having a positive impact on the Ghanaian economy, with consumers likely to feel the pinch of a more austere budget (lower wage increases in particular) in the interim.

Outlook – Formal retail space in Ghana is in short supply on the back of increased latent demand from consumers, which has been boosted over the past decade by strong levels of economic growth, albeit slower in recent months. However, consumers are currently under pressure due to high levels of inflation, a rapidly depreciating currency, high commercial bank interest rates, and higher utility and fuel prices. Private consumption levels will therefore be negatively impacted during the coming year, but we remain upbeat about the long-term potential for the sector, which will be supported by a growing middle class and a declining population growth rate. E-commerce should also pick up in Ghana as around five million (almost 20% of the population) internet users are currently active. There is massive potential in this market as stronger future growth prospects should be accompanied by a higher number of internet users with greater disposable incomes.

Kenya

Positives: Strong population growth; growing middle class; educated labour force; dynamic private sector; regional leader – possibilities for regional expansion

Sectors: FMCG; clothing; personal care products

Risks: Risk of terror attacks by Al Shabaab; private consumption dependent on agricultural earnings; risk of inflation and higher taxes; exposure to Europe for export and tourism revenues

Kenya has a well-developed retail sector in an African context, with formal retail market penetration rates at 25% - 30%, double that of Nigeria. The country boasts a growing and sizeable emerging middle class with the New World Wealth report for 2014 reporting that per capita wealth in Kenya has grown by 89% since 2000. The average value of a shopper's basket has risen by 67% in five years, which makes Kenya the continent's fastest growing retail market. BMI estimates that per capita food consumption will increase by 4.2% p.a. over the 2014-19 period in local currency terms. In absolute terms, Kenyans are generally still poor, though. In fact, according to the World Bank, around 45.9% of Kenyans live on less than US\$2 (2005 dollars) a day. As the poor typically spend a greater portion of their income on food, the Kenyan retail market is forecast to be dominated by the food market over the medium term.

The East African nation's grocery retail market has been monopolised by local supermarket chains such as Nakamutt (34 stores), Tuskys (45 stores), Uchumi (22 stores) and Naivas (29 stores), with foreign chains struggling to make inroads due to a general resistance to foreign takeovers. Foreign investors looking to get exposure to Kenya's retail play has therefore been limited to purchasing shares in Uchumi, the only listed Kenyan retailer. Despite this, the French supermarket giant Carrefour is opening two new grocery stores in the Kenyan capital, Nairobi, by the end of 2015. Other notable, foreign retail establishments that have recently made a move on the Kenyan market are the US brands Domino's Pizza, Cold Stone Creamery and KFC in Nairobi and Mombasa.

As in the case of countries such as Nigeria, **e-commerce** has also grown significantly in the Kenyan retail and wholesale market. Kenya is one of the most technologically advanced nations in Africa when it comes to mobile money payments. Nearly 26 million Kenyans make use of mobile money, which represents more than half the adult population. The East African nation's openness to new technology has made it a rich source of business for Amazon-style online shopping sites like Jumia and Kilimall. The online shopping market will continue to present a lucrative investment opportunity in Kenya as the number of mobile internet users will continue to grow in the near future.

Outlook – Continued strong growth is predicted for Kenya's retail sector, supported by an on-going shift to formal retail, growing levels of urbanisation, and a rising middle class. Retailers are expected to remain innovative in order to hold on to market shares. For example, online shopping sites are creating user incentive schemes to lure a larger number of clients. The strong expansion of formal financial services to the previously unbanked in Kenya – through mobile and agency banking – has opened up an important opportunity to attract new customers, especially through e-commerce. Kenyan retailers are expected to increase the range of their product offerings further over the outlook period in order to build market share. Further potential also lies in the upper end of the retail market as the number wealthy Kenyans is forecast to grow by 73% by 2023, according to the 2014 New World Wealth report. Kenya also has the fourth-highest number of high-net-worth individuals in Africa.

Morocco

Positives: Rising urbanisation; favourable age structure; growing middle class

Sectors: FMCG; clothing; vehicles; luxury goods

Risks: Notable exposure to Europe could negatively affect consumer spending power

Morocco is another African nation that shows promise in the retail sector. New patterns of trade, such as the shift from traditional grocery retailers to modern super and hypermarkets, are emerging in the North African country. Mobile retailing is also on the rise, owing to greater internet connectivity and a higher number of individuals who have become banked. Moreover, we estimate that Morocco falls amongst the top 10 countries in terms of dollar millionaire growth (26% p.a.) over the 2007-13 period, making its luxury brand market ripe for the picking.

According to Euromonitor, the Moroccan department of Trade and Industry implemented the Plan Rawaj (for 2020) to develop modern retail spaces in a nation where the modern mall has not been particularly successful. Amongst the legislative reforms are amendments to a 1955 commercial property law which previously made landlords reluctant to lease retail space, since tenant eviction was very difficult. Four new mall developments, under the auspices of this plan, have occurred since 2011 with the Carre Eden Mall (27,000 m²) in Marrakech being the most recent. One of the exciting new retail developments in Morocco will be the construction of the 540-metre Al-Noor tower in Casablanca. This 114 storey building, which will be built by Dubai-based Middle East Development LLC, will be the tallest building in Africa, housing a seven star hotel, a business centre and a shopping mall.

The Moroccan grocery retail sector continues to be dominated by local players such as Marjane Holdings (33 hypermarkets). The other notable market players in the grocery arena are Label'Vie, Hyper SA, and Ynna holdings. National brands typically benefit from their long existence in Morocco as well as their extensive knowledge of the

North African nation's retail market. Historically, Moroccan brands, due to their market experience, have also tailored their offerings to the purchasing power of social groups within the country, giving them a competitive edge. Furthermore, e-commerce is experiencing a boom in the North African country, with online shopping behemoth, Jumia, and other internet retail sites such as Hmizate and Shoppeos having already established themselves in the market. Much business potential can be unlocked in this industry since Morocco's internet usage is high and rising, according to the Agence Nationale de Reglimentation des Telecommunications (ANRT). The growth in the North African country's e-commerce retail industry could have been even greater if more attention was paid to Arabic translations of online retail platforms, greater promotions on social media occurred and focus was placed on fast growing mobile device usage.

Outlook – The overall outlook for Morocco's retail sector is positive and growth will continue to be supported by a growing urban middle class. The shift from traditional grocery retailers to modern hyper and supermarkets will continue strongly especially as the large grocery chains such as Label'vie and Marjane continue to open outlets in second and third tier cities. Moreover, the tourism industry should contribute to the growth in general retail as tourist arrivals in Morocco are expected to surpass 11 million per year by 2016. The upper middle and high earning income groups present interesting opportunities for retail due to their demand for brand names and quality products. Speciality retailers remain a novelty in Morocco and, given the low number of cars per capita, vehicle retail also presents significant growth opportunities.

Nigeria

Positives: Large market size; youthful population; urbanisation; privatisation of power sector

Sectors: FMCG; clothing; luxury goods

Risks: Risk of naira devaluation, which would raise cost of imported goods; poor infrastructure; difficulty to source products due to small local manufacturing sector; political risk; security risks in northern states

Although Nigeria has experienced high real GDP growth over the past decade, a large share of the growth in income has gone to a small, well-connected group (often political elites) benefiting from oil rents. Consumer goods companies catering to the lower and middle classes have therefore not benefited from high oil prices as much as one would have expected. The recent sharp decline in the international oil prices is therefore expected to have more of an impact on the rich than the poor. Still, the recent devaluations of the naira will increase the cost of imports and thereby weigh on consumers' purchasing power. Moreover, tighter monetary policy due to capital flight and a weaker currency has also impeded access to credit. These negative trends will abate over the medium term and should not derail Nigerian economic prosperity over the long run.

Despite these problems, the Nigerian wholesale and retail industry (which accounts for 16.4% of GDP) remains a lucrative investment opportunity on the back of a large and rising population and an increased rate of urbanisation. The retail market in the West African country has become somewhat more sophisticated from its relatively informal origins prior to 2000. The first modern mall developments in the country were the Ceddi Mall in Abuja and the Palms Mall in Lekki, Lagos. The consequent success of these projects due to the voracious appetite of the up and coming middle class has led to further developments such as the Palms Polo Park Mall in Enugu, the Palms Ilorin in Kwara, as well as the Adeniran Ogunsanya Mall in Surulere and Ikeja City Mall in Lagos. Retail space in the country has therefore grown from an initial 30,000 m² to 227,000 m².

The geographical spread of malls has increased over time as well. In 2006, only two Nigerian cities had malls, whereas there now are 10 cities that have functioning malls. In addition to Abuja and Lagos, Port Harcourt, Ibadan, Enugu and Delta now boast modern shopping complexes. Greenfield Assets Limited and the Abia State government are currently developing the first purpose built Smart Mall in the world and the largest mall in Africa in the city of Osioma Ngwa. This mall will have an impressive 280,000 m² retail space, which roughly translates into 5,830 shops. In addition, the development will comprise a games arcade, petrol stations, climate-controlled warehouse and state of the art cinemas.

The initial retail landscape was dominated by Nigerian and South African firms. Amongst the major South African players in the West African nation are Game, Nandos, Shoprite, Mr Price, Foschini and Barcelos. Recently, the country has also seen an influx of Middle Eastern, American and European brands such as Swatch. Brand diversity remains limited in many of the newly-developed malls and holds great potential for new business ventures in Africa's largest and most populous economy.

Nigeria has also seen the development of a market for luxury goods. The country's burgeoning middle class is expected to have consumer spending in excess of US\$25bn by 2020. This is comparable to spending in Mumbai, India's largest business hub. Furthermore, the West African nation's demand for champagne is expected to more than double between 2011 and 2016. Nigeria is also the world's fastest growing aviation market, with 70 new private jets projected to be delivered in the country over the next four years. However, according to the World Bank, in 2010 about 46% of Nigerians lived on US\$2 or less a day (at 2010 international prices). These stark contrasts further give credence to the fact that the Nigerian retail and wholesale market is highly polarised.

The e-commerce trend also shows no abatement. Major internet sites such as Jumia and Konga have done well in the fashion and mobile devices markets, whereas Supermart.ng and Gloo.ng have made inroads in the order and delivery of supermarket goods. According to Disrupt Africa, the Gloo.ng site had around 7,000 users per month at the start of 2015, up 800% y-o-y. The formal supermarket landscape remains highly fragmented as a population of 180 million people are serviced by only two supermarket chains with 15 outlets countrywide. Should the problems in infrastructure and the difficult business environment receive more attention from Nigerian authorities, both the off and online grocery shopping markets have massive investor potential.

Despite the wealth of opportunities in the Nigerian retail and wholesale market, certain challenges in the business environment make investment difficult. The West African nation is dominated by both high financing costs and very high construction prices. Infrastructure gaps also inhibit the development of effective retail supply chains. Security concerns like the rising insurgency trend especially in the north, also have a major disruptive impact on the business environment. International investors also seem to have misconceived notions about Nigeria such as the absence of a market for luxury goods.

Outlook – The Nigerian consumer may well be under pressure over the next few years as low oil prices put pressure on the Naira and government infrastructure spending plans. However, the retail sector remains an attractive prospect over the longer term. Informal retail channels will continue to dominate. This is despite some

specific measures being implemented by State governments to encourage the formalisation of the sector. The share of modern retail is however expected to continue increasing over the coming years, driven by the development of a number of large-scale modern shopping centres. The low-income consumer by far dominates the Nigerian retail scene, which will provide a lot of opportunities for FMCG companies. In addition, online grocery shopping is becoming ever more popular due to the limited access to formal grocery supermarkets. Brand diversification will also present a good investment opportunity in the future as average household incomes grow. Despite Nigeria's rich investment potential, some serious challenges for retailers to set up shop persist. If the country's infrastructure deficiencies and cumbersome legislative hurdles are not addressed in the near future, the cost of establishment for international brands may remain too high.



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