

South Africa - challenges and opportunities in the year ahead

By [Morne van der Merwe](#) and [Wildu du Plessis](#)

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South Africa is experiencing a period of prolonged political and economic uncertainty, but the country's commitment to improving the local investment environment, combined with signs of future economic improvement, have resulted in increases in M&A value and volume predictions in South Africa in 2021 and 2022. In addition, shifting global trade patterns are resulting in the formation of new trade relationships in Africa, which is good news for the entire continent, including South Africa.



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According to Baker McKenzie's Global Transaction Forecast, produced in conjunction with Oxford Economics, South Africa's M&A market will remain weak in the near-term, with the projected strengthening of the economy in 2020-21 likely to support a modest recovery in deal-making activity in future years. Merger and acquisition value in South Africa was US\$10.1 billion in 2019, but is expected to drop to \$5.2 billion in 2020, before rising to \$9.4 billion in 2021 and \$12 billion in 2022.

Investor uncertainty

International investors and South African dealmakers often feel discouraged by the current South African business and socio-economic environment. They are currently not experiencing South Africa as "open for business". Dealmakers in South Africa often comment about the uncertainty created by BEE laws and regulations, which they experience as being too complex, not consistent and unpredictable. The risk of being found guilty of "fronting", and facing criminal sanction as a consequence, raises a dark red flag when making investment decisions. This is especially in light of the considerable challenges investors face in not falling foul of anti-bribery and corruption laws.

Further areas of concern include the labour market related issues - including costs, productivity and the legislative framework; currency volatility; bribery and corruption; and inadequacies in the justice system, which raises concerns about the rule of law. Investors are also worried about the support and performance of SOEs, including Eskom and Transnet; as well as the socio-economic mandate of the Competition Authorities and the inconsistencies and unpredictability caused by the manner in which this might be applied. Land expropriation without compensation, uncertainty about security of property rights and security of tenure have further eroded business confidence.

Over-regulated

South Africa has a highly regulated business environment which also results in uncertainty and inconsistency. Too much regulation can also cause interference in free market economy and can lead to an unfavourable business environment that is difficult to navigate.

Despite all this, we believe the country is on the right track for future growth and recovery, although there is still a lot of work to do. For the country's investment environment to improve there has to be an acknowledgement of the fact that we should and could do better, and visible action needs to be taken to address the areas of concern. All stakeholders, including government, labour and business, must work together to address these issues and contribute to creating a sustainable and well-functioning and vibrant economy.

International economic ripple effect

The recent escalating global trade tensions, such as the China-US trade war and Brexit have been adding to the uncertainty of investing in Africa in general. However, there are strong signs that the shifting global trade patterns are good news for the continent, and particularly South Africa, as the major players turn to Africa for new avenues for trade and investment.

The Southern Africa Custom Union countries, with Mozambique, (SACUM) recently announced the agreement in principle of a new Economic Partnership Agreement (EPA) with the UK, which will govern bilateral trade between the SACUM countries and the UK if the UK leaves the EU. The new EPA benefits South Africa as it will allow for the continued preferential access to the UK market for certain important sectors in the event of Brexit.

Further, it would not be unreasonable to expect that Africa will be a geopolitical priority for the EU in the near future and that the EU will position itself as a close ally of Africa, including doing more trade deals with the continent.

China has also noted that it is looking for new opportunities to trade and to be a responsible investor in Africa. As one of South Africa's largest trading partners, the country plays an important role in infrastructure investment, having pledged to invest \$14.7bn in South Africa in 2018. China's Belt and Road Initiative (BRI), a multi-billion dollar plan to link Asia, Europe and Africa, will result in further increases in infrastructure investment across Africa in future years. According to Baker McKenzie's BRI & Beyond Forecast, one of the models for likely BRI investments predicts an estimated \$910 billion in BRI investments in the 2020s, with sub-Saharan Africa receiving the biggest share - 25%.

Also in 2018, the US outlined its Africa strategy by reiterating its commitment to strong partnerships with African countries, including South Africa. The US said it would seek to promote intraregional trade and commercial ties with its African allies, shifting its focus from "indiscriminate aid" to one of trade and investment.

AfCFTA

Notably, South Africa is also expected to be a key beneficiary of the African Continental Free Trade Area (AfCFTA). If fully

implemented, AfCFTA will unlock significant but uneven growth opportunities on the continent, according to Baker McKenzie's research with Oxford Economics, *AfCFTA's \$3 trillion Opportunity: Weighing Existing Barriers against Potential Economic Gains*. The research found that some countries are currently better placed than others to reap the rewards of intraregional trade and that South Africa stands to maximize the benefits of AfCFTA due to its existing strong connections across the continent and well-established manufacturing base.

South Africa is next to chair the African Union, starting in January 2020 and will be keen to facilitate progress in free trade on the continent under the agreement, especially as it is one of the nations with the greatest opportunities for growth through AfCFTA. So while the short term looks challenging, a very exciting picture is forming for Africa in the long term.

ABOUT THE AUTHOR

Morne van der Merwe, Managing Partner and Head of Corporate/M&A, and Wildu du Plessis, Head of Africa, Baker McKenzie Johannesburg.

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