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RWANDA

A textbook example of pro-business policy makes for strong investment case

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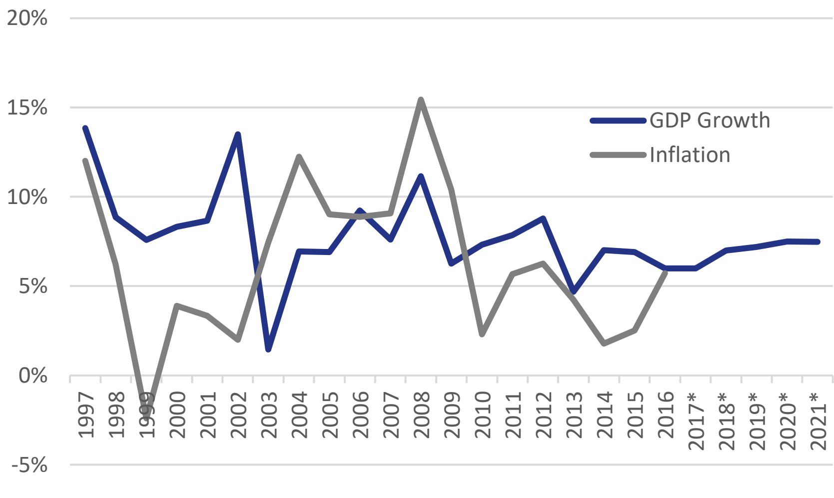
Rwanda is often described as the Switzerland of Africa – small, landlocked, mountainous, and meticulously well-run. But the better comparison might be with Singapore. The country is being driven down a development path under the strong hand of Paul Kagame, president for 14 years and de facto leader since the end of Rwanda's genocide in 1994. It is strongly reminiscent of Singapore under Lee Kuan Yew, that country's founding prime minister who took the country from third to first world during his 31 years of leadership: small, densely populated with almost 12 million people, and presided over by a dominant figure. Singapore was one of the countries Kagame studied before launching a development plan for his country in the late 1990s, aiming to turn Rwanda into a middle income country by 2020. On many measures, he is succeeding.

Among the reforms Kagame has pushed is a much improved business environment. That has seen Rwanda rocket up the World Bank's Ease of Doing Business rankings to 56th in the world, now placed only behind Mauritius (49th) in Africa. This was not a by-product of other reforms – Kagame appointed a team in government specifically to improve the ranking. It gives a flavour of how things work in the country. A disciplined civil service boasts an array of development initiatives targeting improvements in everything from foetal health to the numbers of science and technology graduates. It has also leapt up the rankings on Transparency International's 2016 Corruption Perception Index, now ranked 50th out of 176 countries in the world, ahead of South Africa and Ghana. The Rwanda Development Board is tasked with investment promotion which it pursues with zeal, plying the world's trade fairs and offering a one-stop-shop for foreign investors, who face much encouragement to invest in priority sectors including tourism, ICT and financial services.

FIGURE 1: RWANDA GDP GROWTH AND INFLATION

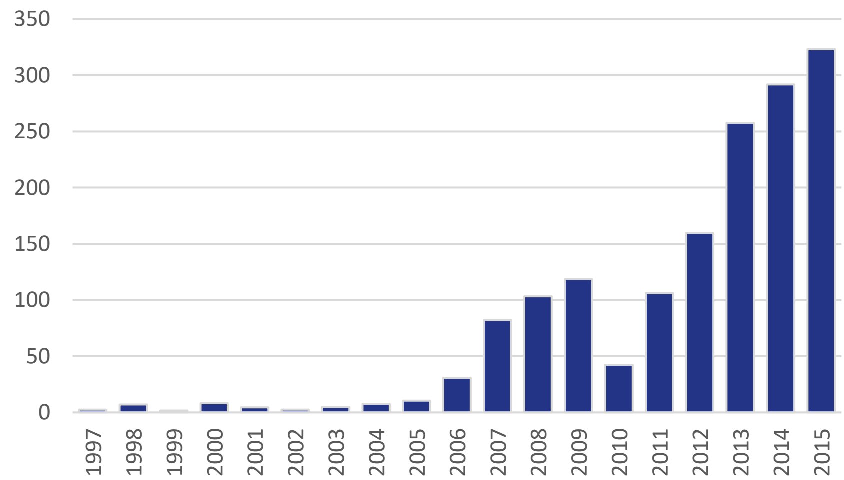


**Forecast* *Source: World Bank/International Monetary Fund*

On many measures, the programme has been a stunning success. From 1997 to 2016 the economy grew 8% on average per year. It is forecast to grow at 7.2% this year, rising to 7.5% by 2020, making it one of the six fastest growing economies on the sub-continent. Between 2002 and 2015, life expectancy rose from 50 to 64 and the number living in extreme poverty fell from 35.8% in 2005 to 16.3% in 2014. The country also has the highest proportion of women MPs in the world at 64%, and the leaders of many businesses and public institutions are women. The Vision 2020 plan sets out the steps Rwanda is taking to achieve its goals and the whole government is regularly assessed against those targets.

Given the government's strongly pro-business stance, opportunities for foreign investors abound. Government has prioritised sectors from tourism to mining for foreign investment. It switched the language of education from French to English in 2008, to make the country more internationally focused. The focus is on attracting investors willing to commit for the long term and to adding value within the country. The Rwanda Development Board is proactive in assisting foreign investors and maintains a comprehensive list of available projects. But Rwanda's growing entrepreneurial business sector is also eager to find foreign partners to join them in exploiting opportunities.

FIGURE 2: NET FOREIGN DIRECT INVESTMENT ($m annual)



Source: World Bank

The pitch is persuading many. Foreign direct investment has steadily increased, reaching a net $323m, or 4% of GDP, in 2015, the latest available figures. But the opportunities remain relatively under-exploited, with Kigali's streets still mostly uncluttered by big international brands despite a massive surge in development.

The key risk investors have to assess is the political stability of the country. The development effort has been driven by the horror of Rwanda's 1994 genocide, and overseen by a regime which tolerates little political opposition. Without the stability of free political activity and entrenched democratic institutions, investors must rely on credibility of the government to remain on course. Rwanda therefore represents a difficult calculation: will the country be able to deliver on its promise to develop into a sophisticated and wealthy politically stable economy, emulating Singapore, or will it lose track and fall victim to lingering tensions domestically and in the region?

BORN OUT OF TRAGEDY

In just 100 days in 1994, 800 000 Tutsis and Hutu moderates were killed in Rwanda's genocide while many escaped into neighbouring countries. The killing was quelled when the Rwandan Patriotic Front (RPF), led by Kagame, gained control of the country, having steadily advanced from its base in Uganda, throughout the period. Reprisal attacks were widely reported, and some 2-million Hutus fled the country.

The physical and economic infrastructure was destroyed, with half of GDP lost, banks collapsed and the government simply unable to function.

The legacy of the genocide is felt with a deep pain that is invisible to outsiders at first, but slowly comes out as one gets to know Rwandans. It is an ever present subtext to the country's political and economic development. Nothing makes sense without understanding the genocide and its aftermath. The 100 days of the genocide is marked every year with a period of mourning and reflection.

The government vigorously pursues an anti-ideology programme to quell what remains of the hatred that sparked the genocide. Much of the post-genocide political process is focused on that objective. The government sees itself as not just the engineers of an economic transformation, but also of a social and ideological transformation. The RPF is completely committed to this responsibility and too often sees contrary voices as dangerous. The distinction between Hutu and Tsutsi has been removed from all government documents and with no physical or language differences between the groups, it is hoped the distinction will dissolve with time in favour of the common Banyarwanda culture and language. "Divisionism" is a criminal offence and political opposition figures are often accused and charged with sowing it. While opposition politics is technically legal, Kagame's RPF wins most elections with 90% of the vote. In late 2015 a referendum to amend the constitution to allow Kagame to stand for a third term was approved by 98% of voters.

The genocide was followed by the pursuit of justice in the context of a shattered country. Two thirds of the country's 750 judges had been murdered or fled. Jails were forced to hold eight times their capacity as some 130 000 alleged perpetrators were arrested. In 1997, the judicial system had only 50 lawyers. The United Nations presided over a tribunal system for high profile genocide leaders, but this only focused on a small proportion of those accused. Given the slow progress of cases, in 2001 the "Gacaca" court system was developed in which villages elected leaders to preside over cases locally in a form of transitional justice that aimed to achieve community healing. Over 1-million people were tried by such courts for aiding or abetting crimes during the genocide, with 800 000 convicted – equivalent to one quarter of everyone over the age of 16 in 1994. The system was praised for bringing out information about victims and healing communities, but also criticised for the sometimes arbitrary punishments and lack of due process for the accused.

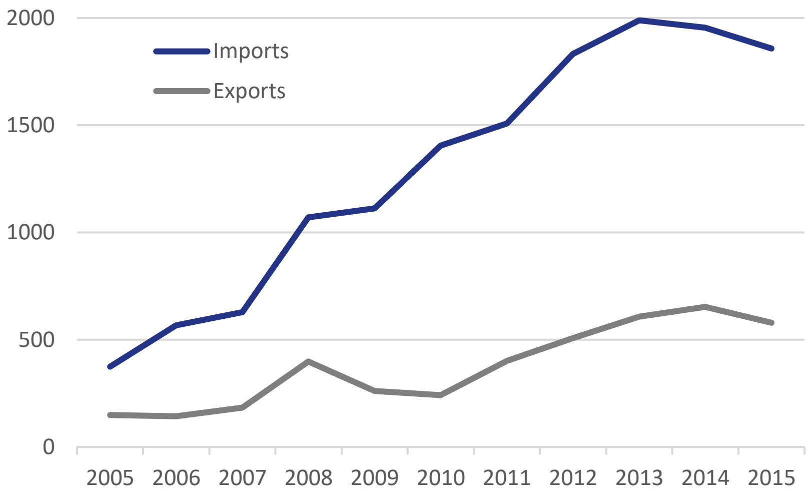
The genocide also looms large in Rwanda's international relations. Its military forays into neighbouring states are often motivated at least in part by the pursuit of Rwandan Hutus who remain outside of the country. They are feared to be refuges of genocidal intent. Rwanda has been accused of backing the M23 Tutsi rebels in the DRC's long-running civil war despite being accused of war crimes, leading some donors to suspend aid to Rwanda in 2012. That quickly forced Rwanda to pull back from its neighbour. The region remains a complex security challenge for Rwanda, especially given the unstable security situation in the DRC and Rwanda remains highly militarised.

It is also alleged that Kagame's government has assassinated opposition figures, particularly Patrick Karegeya, who was murdered in Johannesburg in 2014, an allegation the Kigali government has vigorously denied. The incident has meant relations between Rwanda and South Africa are frosty.

Ideally, Rwanda would seek to resolve this legacy through openness and transparency, gaining legitimacy across the population. There is certainly widespread support for Kagame's tough approach to peace and security. He is also credited for performing an economic miracle, particularly among the middle class. It is difficult, however, to determine how robust and sustainable government's authority is in an environment with limited free media or notable domestic opposition voices.

ECONOMIC DEVELOPMENT

FIGURE 3: IMPORTS AND EXPORTS ($M)



Source: World Integrated Trade Solution

Rwanda's 12-million people are squeezed into an area smaller than Lesotho. Some 90% of that population is rural, working increasingly smaller and less efficient plots of land in a country consisting of hills and valleys and almost no plains. A primary objective of the country's development trajectory has been to migrate labour from agriculture to manufacturing and service activities while also boosting the productivity of farming. This has resulted in a substantial shift in economic activity – between 2006 and 2011, 90% of the increase in labour productivity was driven by shifts from agriculture to other sectors. In the decade to 2010, the share of employment in agriculture fell from 89% to 72%, according to the World Bank. The shift is particularly prevalent among Rwanda's young who have given up farming in favour of seeking out non-farm employment, often in the cities. Education is highly correlated with movements to wage employment, so as Rwandans become more educated, the economy will become less rural, subsistence-based, and agricultural.

Even as it shrinks in terms of employment numbers, agricultural productivity is increasing, though some reforms may be unpopular. The ambition spelled out in Vision 2020 is to boost agricultural productivity and linkages with manufacturing and export markets. Policies include attempting to combine the fractured country side into cooperative production units that can function at scale. That has been politically difficult with the country's frequent refugee inflows and outflows complicating historic property rights. Farming units must now have a minimum size of one hectare, so they can no longer be split among the next generation as in the past. These moves have occasionally met strong opposition. Productivity has been boosted by state-sponsored initiatives to improve terracing, irrigation, mechanisation, better seed and farming techniques, and increased use of fertiliser and pesticides.

Government has also highlighted the agricultural sector for foreign investment, particularly in beneficiation activities. It has earmarked tea plantations and related factories for privatisation. It is pushing for foreign investment into value-adding agriprocessing from coffee roasting to distribution. Rwanda's coffee is world-class.

Investors are responding. US-based Nationwide Group International recently invested $200m in an agriculture equipment leasing business that will support government's ambition to boost farm productivity. Others have invested in everything from cold storage to export-oriented cut flowers.

But the real potential for the country lies beyond its agricultural sector. And the best sign that it might deliver is the massive investment in education. The country now spends 4% to 5% of GDP on education and training. Primary school enrolment is now at practically 100%. A strong push toward STEM (science, technology, education and mathematics) subjects at tertiary level is being supported with government scholarships and loans. Gross tertiary enrolment between 2010 and 2013 rose from 1.3% of those within five years of completing secondary school to 7.5%. Government has strongly encouraged international universities to enter the country with subsidiary campuses (Carnegie Mellon is the most prominent to do so) while also investing heavily in public universities.

Rwanda has taken the view that services will be the fastest-growing economic sector and moved aggressively to build competencies, with everything from new hotel schools to the Kigali Lab, which offers free internet facilities and mentorship for young coders to develop apps and turn them into new businesses. There is a sense of excitement in Kigali that Rwanda will be the birthplace of a future Google or Facebook, and there have already been success stories among start-ups like AC Group, which developed a tap-and-go payments system for public transport.

FIGURE 4: MAIN EXPORT CATEGORIES ($m)

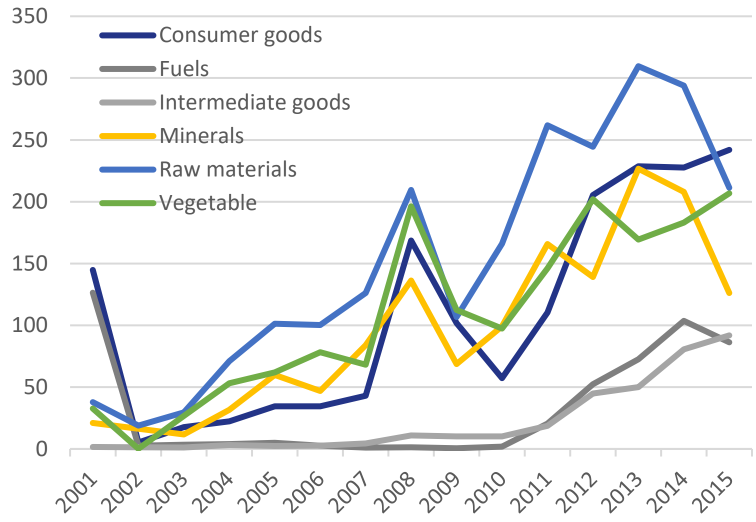
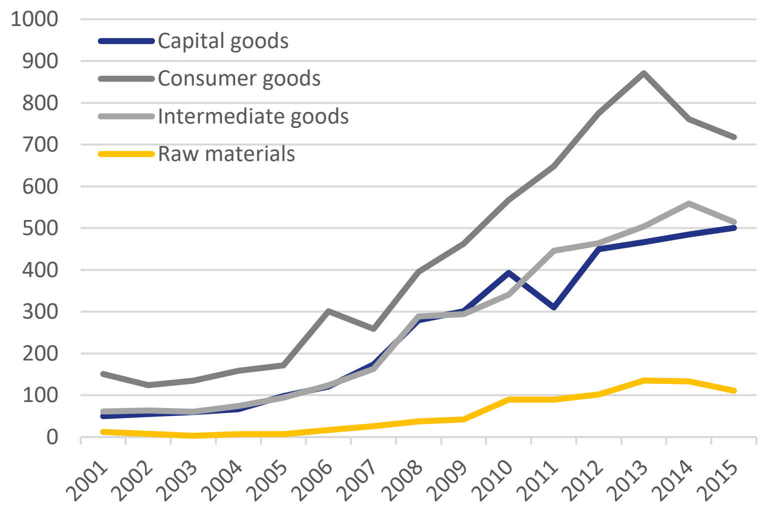


FIGURE 5: MAIN IMPORT CATEGORIES ($m)

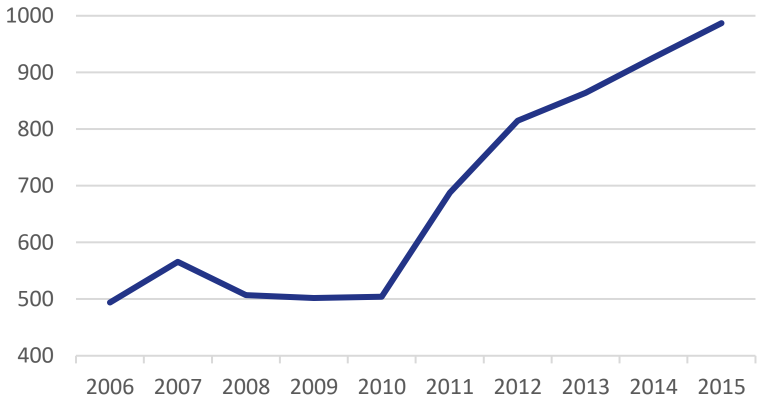


Source: World Integrated Trade Solution

Rwanda's performance in the Ease of Doing Business rankings is part of the push for a new entrepreneurial class. It is particularly strong on measures for access to credit, for which it is ranked joint second in the world. One entrepreneur I met in Kigali told me that being an entrepreneur was easy, it just took a good idea. If you had that, you could find the finance and support all the way to international markets. Services has been the biggest contributor to the GDP growth statistics for the last five years.

While services are a priority, industrialisation is also important. Rwanda has recently instituted a policy of import substitution industrialisation, by erecting tariff barriers on certain imports. This can be interpreted as contrary to Rwanda's free market ethos and is complicated by the presence of firms owned by the RPF and Rwanda's military, who some suggest are given preferential treatment in protecting markets. The main motive for the strategy is a need to reduce Rwanda's substantial balance of payments deficit, which has ballooned as its infrastructure splurge has driven imports. It is notable that capital goods are specifically exempted from any tariffs. Instead the focus is on domestic consumption goods including cement, soaps and detergents, fertilizers, edible oils, sugar and garments. These are being promoted through a country-wide "Made in Rwanda" campaign to boost local consumption of local goods. In part this has been government-led, with major investment in the state-owned cement company expected to soon lead to a six-fold increase in domestic production. However, textiles is seeing substantial foreign interest as government has reduced tariffs on imported textiles and heightened tariffs on second-hand clothes. The strategy makes sense as a means to shift the trade balance, though the country will need to ensure it does not allow inefficient businesses to simply mushroom under the tariff protections, at the expense of consumers. The challenge is whether its relatively small market can achieve the economies of scale needed to compete with far larger producers elsewhere in the region.

FIGURE 6: INTERNATIONAL ARRIVALS ('000)



Source: World Integrated Trade Solution

KIGALI'S INTERNATIONAL CONVENTION CENTRE

Source: Rwanda Conference Board

On the services front, international investors have been significant players in tourism development. Rwanda has a dual strategy: positioning the country as a high-end safari destination, capitalising on its population of rare gorillas, and pursuing the "MICE" market of meetings, incentives, conferences and exhibitions. The latter took a big step forward with the opening in mid-2016 of Kigali's international convention centre. Major hotel brands have also opened in Kigali recently, including Radisson, Marriot, Serena, Sheraton and Protea Hotels. The Rwanda Development Board now has a brief to go after every big international event in the offing. The national airline, Rwandair, has seen substantial investment to improve its fleet and has just introduced a London-Kigali direct route. Rwandair is also often tipped for privatisation.

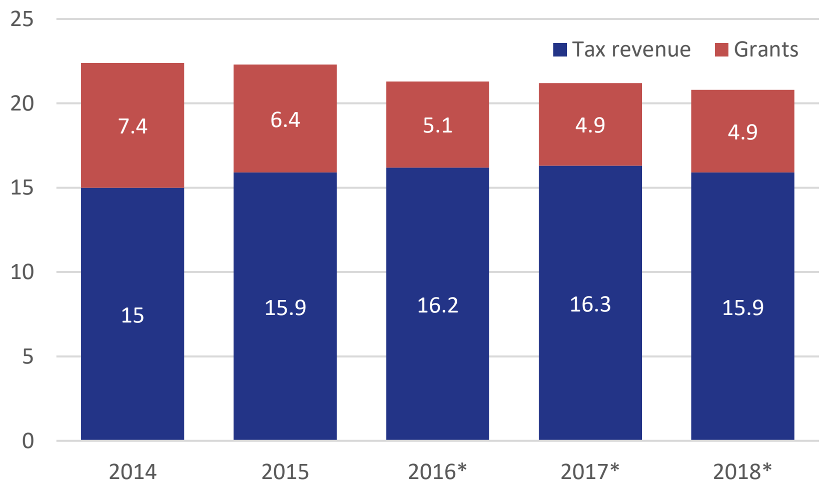
The impact of the tourism strategy has already been substantial, with foreign tourist arrivals increasing from about 100 000 in 2000 to almost 1-million in 2015. Those figures are widely thought to have grown substantially since then. It is already the country's biggest foreign exchange earner. The opportunity for foreign investment is clear. Aside from the urban hotels springing up, One & Only and Wilderness Safaris are developing top-end Safari lodges in the country's parks.

Lastly, Rwanda's minerals industry is not being ignored. Unlike many other sub-Saharan African countries, Rwanda's mineral wealth is minimal, with limited energy and precious metals activity. It does, however, have a vibrant rare earths mining sector like neighbouring DRC, which has grown to supply global mobile phone manufacturing, and some gemstones. Mining has historically been artisanal and the country is keen to attract foreign investors to drive industrial-scale mining. There is some concern that Rwanda can be used as a conduit for minerals mined in DRC in conditions that fall short of international standards, particularly in coltan and tin. That is a reputational risk Rwanda needs to manage.

GOVERNMENT FINANCES

Since the genocide, Rwanda has relied on large amounts of foreign aid to prop up the national budget. The country's development plan, however, sees this reducing as a proportion of the total. About a quarter of the budget is still funded by aid (see figure 7). This has economic, but also political consequences. It means that the checks and balances that might normally be expected of opposition politics and civil society are often provided by foreign donors. The World Bank, IMF and development agencies of many countries have played a critical role in assisting Rwanda to rebuild its institutions of government and infrastructure, but also play a chastening role such as when aid was suspended in 2012 over military action in the DRC. Donors seldom make any public comment but behind the scenes pressure is thought to be common.

FIGURE 7: GOVERNMENT REVENUE (as % of GDP)



*Forecasts

Source: International Monetary Fund

The tax system has been built from scratch and continues to be evolved into a modern and dynamic revenue collection service complete with various economic stimulation measures. There has been impressive growth in tax collection, growing 250% between 2008 and 2015, leading to better-than-expected collections last year. The overall fiscal deficit was 3.5% of GDP in 2015/16, lower than the International Monetary Fund had expected. The IMF is anticipating a deficit of around 4% for the next few years, which will be funded out of borrowing and receipts from privatisation.

The National Bank of Rwanda is well respected in the country though its independence is not entirely guaranteed. Bankers describe it as a vigilant and capable regulator, while it has substantially enhanced its monetary policy architecture. Interest rates are surprisingly low relative to other markets in the region, though this is because Rwanda's large state-owned pension administrator injects masses of liquidity into the banking system through deposits. The banking system is constrained by its capital levels, and dominated by the main local bank, Bank of Kigali. Several regional banks including Kenya Commercial Bank and Ecobank operate in the market but there is no presence from international majors like Barclays or Standard Chartered. The bank supervisor says it has discussed deals with international banks in the past, but none have come to fruition, though it is now creating a new rep office category to allow entry without a full licence. Banking liquidity makes it difficult for the central bank to control interest rates and the development of a domestic market for public debt to ensure a more stable monetary sector is a priority.

In many respects, Rwanda's government finances are exemplary. Almost 40% of total expenditure is directed into capital expenditure while salaries and wages make up only 14% of total spending, far lower than the likes of South Africa where the wage bill accounts for 36% of spending. The efficiency of that spending is also maximised by a tough public financial management framework. An unambiguous commitment to stimulating the private sector ensures that spending is focused on creating the right enabling environment. And it is that which is seeing a dramatic upswing in private sector activity.

INVESTMENT OPPORTUNITIES

Much of the foreign investment into Rwanda is direct – new hotels, factories, retail stores, construction firms and other infrastructure. This is because Rwanda's capital markets have not yet developed to the point where they offer sufficient liquidity and diversity to support portfolio investors. The Rwanda Stock Exchange, opened in 2011, recently listed its fourth domestic equity when government divested of an interest in I&M Bank. That joined the bourse alongside Bank of Kigali, a Heineken subsidiary and an investor in MTN Rwanda. There are also four counters that are cross-listed from Nairobi's exchange.

Government has at various times flagged several other entities for privatisation and listing in an effort to build available investments on the bourse, including Rwandair, various utilities and agricultural entities. New listings benefit from income tax breaks for five years. The bourse also has a bond sector consisting of government bonds that have been issued to build out a yield curve, which now runs to 15 years. Two banks have also issued bonds.

TABLE 1: RWANDA INVESTMENT PRIORTIES

Priority area	Opportunities
Infrastructure	• Roads • Air transport (new airport at Bugesera) • Railway (two major lines) • Inland water transport (terminal on Lake Kivu) • Public Transport (bus rapid transport system)
Agriculture	• Many opportunities, including: • Rice production and processing • Seed production • Irrigation and mechanisation projects • Coffee: production, washing, roasting, packaging • Sugar cane • Floriculture
Energy	• Methane gas to power project • Geothermal • Peat to power • Micro hydropower • Off-grid solutions
Tourism	• Several particular opportunities have been identified and scoping documents drawn up including • Cable car project • Golf courses • Lake-side resorts
ICT	• Development of an ICT Park
Mining	• Exploration • Tin, tungsten, coltan and gemstones • Value-adding processing plants
Financial services	• Asset and wealth management • Investment banking • Training of professionals • Fintech • Various financing businesses
Real estate	• Housing • Office buildings • Real estate agency operations • Shopping malls • Training
Manufacturing	• Construction materials • Textiles and garments • Pharmaceutical products • Leather processing • Motorcycle assembly • Soaps and detergents

Source: Rwanda Development Board

Developing the capital markets is part of the plan to lessen reliance on foreign aid and funding and mobilise domestic savings. It dovetails with plans to expand private pension fund management and the building of a collective investment schemes industry. The legal framework has now been established, but new entry has been slow. So far the country has just one collective investment scheme, the Rwanda National Investment Trust (RNIT), which is owned by the government, while the institutional sector is dominated by the Rwanda Social Security Board which holds the pension fund and medical insurance savings of the country. The RNIT was set up after years of attempts to attract a private asset manager to establish a scheme failed, but the plan is to sell it to a private asset manager in three years. Rules are now being drafted for exchange-traded funds and real estate investment trusts. A 10-year plan has been drawn up to develop the capital markets which includes outsourcing some of the Rwandan Social Security Board's assets to the private sector to manage, and improving pension regulations to encourage more saving into private pension schemes. Government intends to raise the domestic savings rate from 12% of GDP to 16% in the next three years. There is a clear opportunity for foreign financial services providers to enter.

The more likely entry for foreign investors, however, is through direct investment by opening new businesses or supporting existing ones. The Rwandan Development Board oversees a wide-ranging investment promotion programme that covers almost all economic sectors and includes tax incentives and other support. The Board has detailed many opportunities (see Table 1). Several are in the form of public-private partnerships, while others envisage independent entry into the private sector. The Board even offers to help companies engage with Rwanda's government to shape particular partnerships. It operates a one-stop-centre for foreign investors to streamline all bureaucracy, from work permits to electricity connections.

Further opportunities flow from the East African regionalisation strategy in which Rwanda is a key player. Together with Kenya, Tanzania and Uganda, various integration steps are being made to unite the region into a single economic bloc. As a neighbour to some of DRC's mineral rich regions, it also provides trade linkages across that border.

On the whole, Rwanda presents an exciting investment destination, with a government focused on developing the country into a business-friendly, middle income country within the next several years. Foreign investors are encouraged to be part of that growth. Social stability remains the key risk, but the government has demonstrated its ability to maintain course for at least 17 years. That seems like good reason for confidence. ■