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Consumer Packaged Goods/Retail

Lions (still) on the move: Growth in Africa's consumer sector

Africa remains a high-potential region, but growth is concentrated in a few markets and income segments. To win, companies need a tailored, data-driven approach.

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Just a few years ago, consumer spending in Africa passed the $1 trillion mark. The continent's impressive growth trajectory at that time—in particular, the robust growth in Africa's 30 largest economies—caught the attention of consumer businesses worldwide. Indeed, the consumer-facing sector has been pivotal in Africa's growth story, accounting for almost half of the continent's GDP growth between 2010 and 2014.

But because of the recent slowdown, some executives have begun to question whether Africa's once-roaring economy and burgeoning consumer sector still hold promise. Is Africa truly worth investing in? Can multinational companies succeed in the region? Is the African consumer opportunity still as attractive as it once seemed? Our unequivocal answer is yes—but companies will need to adopt increasingly sophisticated approaches to compete effectively.[1] In this article, we share our latest perspectives on Africa's outlook to 2025 and what it will take for consumer-goods companies to thrive in the region.

A temporary slowdown

Consumer spending across the continent amounted to $1.4 trillion in 2015, with three countries—South Africa, Nigeria, and Egypt—contributing more than half of that total. Food and beverages still constitute the largest consumption category, accounting for as much as one-third of Africa's household spending in 2015 (and close to 40 percent of household spending in lower-income countries such as Ghana, Kenya, and Nigeria), but discretionary categories

already make up a substantial share of consumption. Spending on nonfood consumer goods—including clothing, motor vehicles, and household goods—accounts for a further 15 percent of consumption.

However, due in part to currency devaluations and a sharp downturn in oil-exporting economies, spending growth has slowed. Out of the 15 largest consumption markets in Africa, which constitute 90 percent of the continent's total consumption, 12 experienced a slowdown in consumption growth between 2014 and 2015—the exceptions being Ethiopia, the Democratic Republic of Congo, and Tanzania.

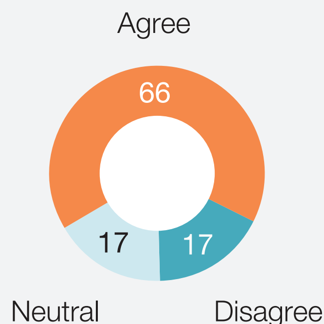
Clearly, the African consumer is under financial pressure. In a 2016 McKinsey survey of consumers in six African countries, two-thirds of respondents said they were worried about their finances and more than half said they've reduced their spending (Exhibit 1).

Exhibit 1 **Consumers in six African countries surveyed are finding it harder to maintain their living standards.**

Results from countries surveyed,[1]
% of respondents, weighted average

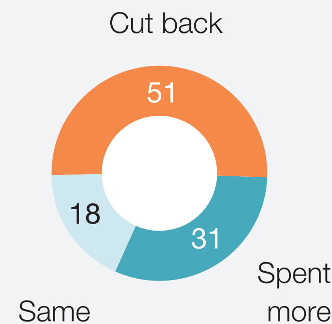
Consumers are worried about their finances…

"I worry about my finances and fear I will be living paycheck to paycheck."



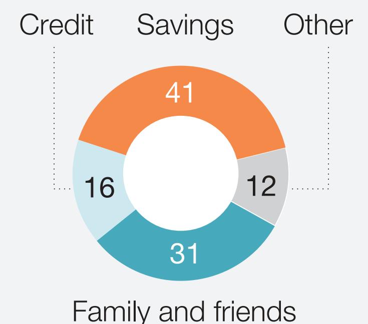
…and as a result have reduced spending…

How has your household's spending changed over the past year?



…using other income sources to supplement.

Other than a job or business, what other source of income do you use for shopping?



[1]The countries surveyed were Ethiopia, Ghana, Kenya, Morocco, Nigeria, and South Africa; 4,600 people sampled.

Source: McKinsey African Consumer Survey, September 2016

The outlook to 2025

Consumer spending in Africa is projected to reach $2.1 trillion by 2025.[2] The following strong structural fundamentals are in place to drive the consumer opportunity:

A young and growing population. The continent's population is projected to grow by 20 percent over the next eight years, with Africa's youth making up 40 percent of the total. By 2025, almost one-fifth of the world's people will be living in Africa. This population growth is accompanied by falling dependency ratios and an expanding workforce: the size of Africa's working-age population is expected to surpass both India's and China's by 2034.

Rapid urbanization. By 2025, an additional 190 million people in Africa are expected to be living in urban areas, which means that about 45 percent of the population will be urbanized by then. City dwellers are voracious consumers: per capita consumption spending in large cities in Africa is on average 79 percent higher at the city level than at the national level. Cities in Kenya and Nigeria, for instance, have per capita consumption rates that are more than double the country rates. The top three cities in Ghana and Angola will account for more than 65 percent of national consumption spending in each of these countries.

Rising incomes. Since 2005, increases in spending per household have been responsible for about 40 percent of consumption growth in Africa. By 2025, 65 percent of African households will be in the "discretionary spending" income bracket (earning more than $5,000). Consequently, the profile of goods and services that Africans purchase will shift, from basic necessities toward more discretionary products.

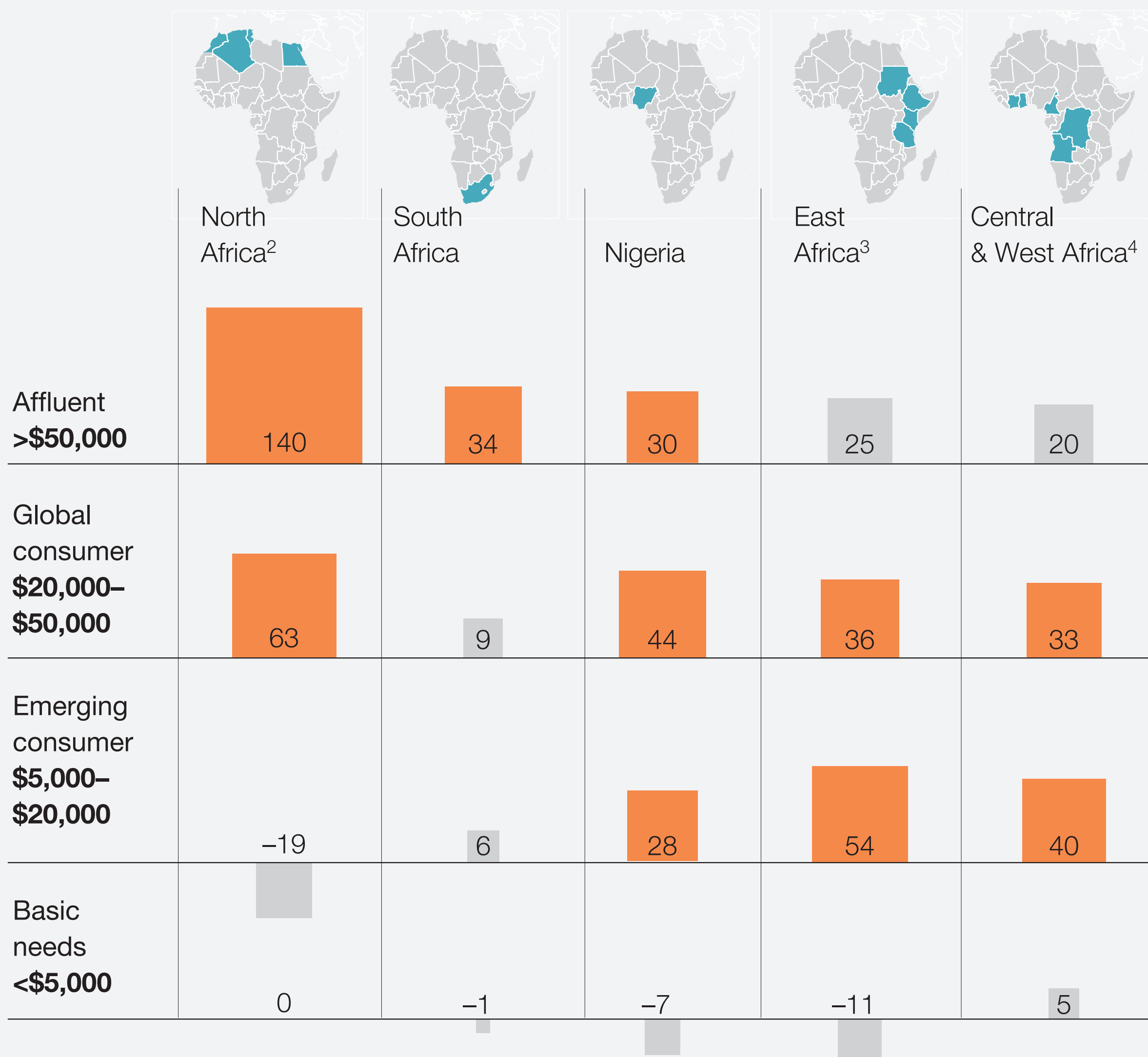
Widespread technology adoption. Technology is opening many new doors for consumers. Mobile money, for instance, is growing five times faster in Africa than in any other region. By 2020, half of Africans—up from 18 percent in 2015—are expected to own a smartphone, which they can use to buy and sell products and services, pay bills, and make remittances. A study in Kenya found that families with M-Pesa mobile money were able to withstand financial shocks (such as illness) without reducing their consumption, because they could borrow money electronically from friends and family. The success of e-commerce company Jumia—colloquially referred to as "the African Amazon.com"—is partly due to the fact that it accepts mobile payments, allowing even Africans who don't have bank accounts to make purchases. E-commerce and m-commerce offerings are partially leapfrogging formal retail, and McKinsey analysis suggests that e-commerce could account for 10 percent of retail sales in Africa's largest economies by 2025.

These factors bode well for the continued growth of Africa's consumer sector. However, growth will be uneven across countries and income classes, and the geographic spread of consumption will change. Our colleagues at the McKinsey Global Institute have identified four groups of consumers that will drive much of Africa's consumption growth between now and 2025: those earning more than $50,000 a year in North Africa and South Africa, Nigerian consumers, middle-income consumers in East Africa, and middle-income consumers in Central and West Africa (Exhibit 2).

East Africa's share of consumption is projected to rise from 12 percent in 2005 to 15 percent in 2025; Francophone Africa's, from 9 percent to 11 percent. Meanwhile, South Africa's share is projected to decline from 15 percent to 12 percent over the same period, and Nigeria's, from 26 percent to 22 percent. But given that Nigeria will still account for more than a fifth of African consumption, consumer companies can't afford to ignore that market, even amid challenges in the business environment.

Exhibit 2 **Much of Africa's consumption growth is coming from only a few consumer segments.**

Consumption growth by household income segment, 2015–25,[1] $ billion (2015 prices)



[1] These 15 African markets generated 89 percent of 2015 demand and will be responsible for 82%of consumption growth between 2015 and 2025.

[2] North Africa comprises Algeria, Egypt, Morocco, and Tunisia. Egypt will account for 62% of the region's growth in consumption.

[3] East Africa comprises Ethiopia, Kenya, Sudan, and Tanzania.

[4] Central and West Africa comprises Angola, Cameroon, Côte d'Ivoire, Democratic Republic of Congo, and Ghana.

Source: African Development Bank; Canback Global Income Distribution Database (C-GIDD); IHS; Oxford Economics; McKinsey Global Institute analysis

Serving the African consumer

In previous articles, we've discussed some of the imperatives for consumer companies to succeed in Africa.[3] These imperatives—such as taking a city-based view of growth, getting credit for value, tailoring the offer to the local market, and creating bespoke route-to-market models—are as relevant as ever. But the changing consumer and retail landscape has highlighted the importance of several other focus areas: making smart use of advanced analytics across the value chain, adopting sophisticated pricing and assortment strategies, and being selective about distributor relationships.

Understand customers through advanced analytics

Formal retail in Africa is expected to grow by about 5 percent each year over the next few years, bolstered by the aggressive expansion of international retailers such as apparel players Cotton On, H&M, and Zara. However, informal retail channels are likely to continue to dominate the market in sub-Saharan Africa for the foreseeable future.

Because of the highly fragmented nature of informal retail in much of Africa, many consumer-goods companies rely on a passive wholesale model and lack a direct relationship with the retailer, limiting their visibility into retail-outlet performance. But leading companies are now exploiting big data and advanced analytics to take their understanding of their customers to a new level. A consumer-packaged-goods (CPG) manufacturer, to serve hundreds of thousands of small outlets in Africa, equips its sales reps with handheld devices that they use for collecting detailed information about, for instance, an outlet's product range, pricing, in-store execution, and storage space. This information, combined with internal data (such as SKU-level sales and profitability) and external data (such as weather forecasts), helps the company make outlet-specific decisions about which products should be in the assortment, how much stock the outlet should have, what types of promotions will be most effective, and so on. Sales reps then receive specific recommendations based on the analytics. Early results suggest that using advanced analytics in this way can drive a 10 to 15 percent sales improvement within months.

Adopt a more sophisticated approach to pricing and assortment

In the past, companies could offer just a small range of products with a basic pricing structure, all targeting the "average" African consumer. Today, in light of rising income disparities across the continent, the most successful CPG companies are using tiered-pricing strategies to capture price premiums from high-income consumers or special consumption occasions (for example, meals at restaurants or bars) while continuing to provide affordable price points for lower-income consumers or value-oriented occasions (such as family meals at home).

Beer companies have long had tiered brand offerings in Africa. Heineken's brand portfolio in Nigeria, for example, includes Goldberg, a value brand; Star, a

mainstream brand; and Heineken, a premium brand. Soft-drinks players take a slightly different tack: they vary their products' pack formats and sizes. The Coca-Cola Company sells soft drinks in low-cost returnable glass bottles, nonreturnable polyethylene terephthalate (PET) bottles at slightly higher price points, and, at even higher price points, sleek cans or sleeved PET bottles. It sells each of these formats in a variety of pack sizes tailored to specific occasions; it also adjusts pack sizes from time to time to ensure that they remain affordable to the target consumer segments while still being profitable for the company.

Still other companies differentiate their pricing and assortment by region. One CPG manufacturer studies competitor dynamics, cost-to-serve economics, and consumer incomes within micro-geographies so that it can develop region-specific product portfolios and highly localized discounting tactics.

Choose, segment, and manage distributors strategically

Many CPG companies' distributor networks in Africa are the result of long-standing and often unexamined relationships. It's therefore not uncommon for CPG manufacturers to find themselves making big investments (for example, through discounts and other kinds of trade spending) in distributors with poor outlet coverage, shoddy execution, or suboptimal capabilities.

Companies should instead be deliberate about designing their distribution network. They should select distribution partners who can help them achieve strategic objectives such as maximizing outlet coverage or optimizing cost to serve. They should then segment distributors based on criteria such as size and quality of relationship, and then differentiate their treatment of each segment—deploying levers such as trade terms, account planning, capability building, and territory allocation in line with segment needs or challenges. Finally, CPG companies should closely track distributor performance on clearly defined metrics (such as volume, outlet coverage, SKU coverage, and price compliance), establish pay-for-performance parameters, and conduct regular performance dialogues with distributors. A handful of large manufacturers, including Diageo and Unilever, excel at these practices. Other companies would do well to follow their lead.

Africa's economic lions may not be roaring as loudly as they were a decade ago, but they are still undoubtedly on the move. Consumer companies seeking long-term growth would be unwise to ignore the region's potential. ■

[1] See *Lions on the move II: Realizing the potential of Africa's economies*, McKinsey Global Institute, September 2016, on McKinsey.com.

[2] In real 2015 prices.

[3] Damian Hattingh, Karl-Hendrik Magnus, and Sidhika Ramlakan, "South Africa's cautious consumer," July 2016, McKinsey.com, and Yaw Agyenim-Boateng, Richard Benson-Armer, and Bill Russo, "Winning in Africa's consumer market," July 2015, McKinsey.com.

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