How Africa Can Embrace Venture Capital

By Edwin Obonyo , Strathmore University, and Claudia Zeisberger , INSEAD

Education, local perspectives and stronger networks can help unlock the continent's investment potential.

According to the **African Development Bank**, 11 African countries currently feature in the top 20 fastest-growing global economies. The organisation's latest **Outlook Report** estimates that real GDP (gross domestic product) growth for the continent is expected to average 3.8 and 4.2 percent in 2024 and 2025 respectively. That compares favourably to projected global averages of just 2.9 and 3.2 percent in the same time periods.

By actively seeking out and supporting African-led start-ups, investors can tap into the region's vast potential while contributing to the long-term growth and development of this dynamic continent.

Slow to invest

The big question is whether Africans have fully embraced the potential of venture capital (VC) investment. Existing data suggests a positive upward trend. The 2024 **Africa Venture Capital Association (AVCA) report** showed that the continent attracted US$4.5 billion of VC investment in 2023, with a 23 percent year-on-year increase in investors participating in VC funding in Africa between 2014 and 2023.

But despite these positive signs, 2023 recorded a dip in investments, coming in at US$2 billion less than the previous year. While this slowdown reflects global investment trends, the US$4.5 billion invested across 603 deals on the continent is still small when compared to the US$78.1 billion invested in Asia or the US$144.3 billion invested across more than 11,000 deals in North America in the same period.

It's clear that more work is required to overcome obstacles and fully unlock the potential of VC investments in specific regions and business sectors within Africa. Indeed, the reality is that the VC model is still somewhat of an unknown entity in many African business ecosystems, which still rely on foundational principles and practices. Traditional business models predominate and have been honed over decades of refinement and adaptation. For many, they offer stability, predictability and a proven track record of success.

The Central Bank of Kenya's **MSME Access to Bank Credit survey report 2022** found that banks were by far the biggest funders of small and medium enterprises (SMEs) in Kenya, reflecting the dominant model in most African countries. For example, leading African banks, such as Nigeria's **Access Bank** and South Africa's **Absa Group**, often look to work closely with SMEs by actively facilitating credit and training.

Context and local know-how

While VC investments often target innovative models, the current investment ecosystem may not fully support the form of innovation inherent in Africa. Across the globe, innovation springs from various sources. However, in Africa, necessity often serves as the primary catalyst, inspiring Africans to invent resourceful solutions that are uniquely tailored to their continent or an individual country's context and culture.

From innovative agricultural practices to resourceful methods of addressing healthcare challenges, African entrepreneurs have demonstrated remarkable ingenuity in finding solutions tailored to the specific needs of their communities. These solutions may be highly effective and impactful within their local contexts **but may not resonate** with investors from the United States or Europe, who are traditionally the majority source of funding in Africa's start-up scene.

Take **Drop Access**, a Kenyan start-up that developed a creative solution for small-scale dairy farmers. Traditionally, farmers would use bicycles or donkey carts to deliver fresh milk to collection centres, but they faced an issue with keeping the product chilled. Drop Access developed solar fridges that could be installed onto motorcycles, allowing for a faster and more hygienic delivery method. Their innovative solution meets a very important need and offers potentially huge supply chain benefits that are also relevant and scalable across the continent. However, it is a need that may not be obvious to an overseas investor. It's also a relatively low-tech solution that may appear less ”sexy” to investors who are fixated on the latest technological breakthroughs.

The point is not that only Africans can solve African problems; rather, it is essential to understand and embrace local behaviour and perspectives in order to find truly relevant and impactful solutions. Foreign investors may prioritise innovations that align with their own experiences and perspectives, which can lead them to overlook the potential of African-led or African-focused start-ups.

A lack of relatability can create barriers to funding and hinder the growth and scalability of viable innovations. Equally important, it may stifle the development of solutions that could be truly transformative within the African context.

Lack of networks

An additional challenge is that the majority of VC money still goes to European and American founders. **Local reports** show that a significant number of the start-ups invested in by VCs are led by white male founders of American or European descent, such as leading finance app **Branch** and solar energy company **Sun King**.

One driver of this is an overreliance on established networks connecting American and European investors and start-up founders. In turn, investors may have limited understanding of the unique challenges and dynamics of the African market, which can hinder effective decision-making and resource allocation. Ultimately, this impacts the success trajectory of start-ups led by founders from diverse backgrounds.

The good news is that this is changing with the creation of new networks designed to link African innovators with investors. One notable example is the **African Business Angels Network**, which plays a pivotal role in facilitating connections between angel investors and promising start-ups across Africa. Nigeria is an example of a country where investments in unicorns, like payment platform **Flutterwave**, are starting to come from within its own borders.

Another option for developing these networks is to take advantage of existing collaborations, such as current MOUs between international and African universities and business schools. Alumni communities and the sharing of research and knowledge between global institutions can be leveraged to help bridge network gaps. For example, the **INSEAD Africa Initiative** (IAI) looks to collaborate with African universities to develop and disseminate the best of business thought leadership, teaching and research. IAI also leverages INSEAD’s own well-placed alumni community in the African VC space who have rich experience and connections across the continent.

Levelling the playing field

Africa is an extremely diverse continent, made up of 54 countries. At present, only a handful of nations attract the majority of investment, with the **AVCA report** identifying South Africa, Kenya, Egypt, Nigeria and the Seychelles as the top five investment countries by value. The good news is that increased investments mean we are beginning to see start-ups expand their operations. Nigeria’s food tech platform **Orda Africa** is making strides in other countries; Uganda’s ride-hailing company **Safeboda** just relaunched in Kenya; and e-commerce site **Jumia**, founded in Nigeria, now operates across 10 African countries.

One challenge start-ups face is that each country has wildly divergent regulatory environments and economic conditions. A potential solution could be to negotiate a continent-wide legal structure for African VC investments. If this approach proves too optimistic, then it could be possible to explore implementing legal structures through existing regional blocs such as the East African Community (EAC) and the Southern African Development Community.

For example, in the EAC, Kiswahili is the predominant language. A **SAFE (Simple Agreement for Future Equity) note** priced in a common currency to standardise investments could help unlock investment opportunities while reducing the risks of currency fluctuations.

Educating local investors

To further promote African engagement with VC, it is also imperative for local investors to appreciate the potential opportunities this asset class presents for high returns and long-term growth.

Encouraging corporations in Africa to set aside capital to invest in start-ups and support the early-stage ecosystem is another path to explore. An example of how this works elsewhere is Singapore's EDB (Economic Development Board), which has a team that matches corporate dollars allocated to "build" ventures internally on the ground in the city-state.

As local investors become more familiar with this asset class, they will be better positioned to identify investment opportunities that align with their own objectives and risk appetite. By actively participating in VC funding rounds, local investors can contribute to the development of a robust start-up ecosystem and fuel the growth of innovative ventures across various sectors. This also opens up the possibility of African VC syndicates working alongside Western investors, bringing much-needed local expertise to the partnerships.

Learn from experiences

Investors also need to learn from the past mistakes of failed VC-funded start-ups in Africa. With this knowledge, they can build a more robust system based on experiences, networks, familiarity and trust.

To further support growth in this sector, individual governments in Africa could look to follow the model of the **Public Investment Fund in Saudi Arabia** and develop their own sovereign wealth funds with opportunities for VC carve-outs to invest in local start-ups and SMEs.

These funds can provide substantial financial resources and strategic support to emerging start-ups, fostering innovation and economic growth across the continent. They can help bridge the funding gap many African start-ups currently face, thereby accelerating their development and scaling capabilities.

Offering such start-ups VC funding at an early stage can help improve their trajectory of success. This doesn't just help the start-up – it also enables local investors to develop their knowledge of VC investing, underlines the value of local expertise, and strengthens all-important network ties between local and international investors.

Find article at

https://knowledge.insead.edu/entrepreneurship/how-africa-can-embrace-venture-capital

---

About the author(s)

Edwin Obonyo is a PhD student in Strathmore University Business School and lecturer in **Strathmore Center of Value Investing** at Strathmore University.

Claudia Zeisberger is a Senior Affiliate Professor of Entrepreneurship & Family Enterprise at INSEAD, and the Founder of the school's private equity & venture capital centre **GPEI**.