Toward the end of 2018, the United States merged existing development agencies into the new US International Development Finance Corporation (IDFC). With a financing capacity of $60 billion in equity and debt – more than twice that of its predecessors – the new agency, which is scheduled to become operational by the end of this year, represents a major step in US development policy, particularly regarding Africa. It may also reflect rising global awareness that a huge investment-financing gap poses an existential threat to Africa's future.

The continent's potential is beyond doubt. Over the past two decades, Africa has entered a phase of structural change that is about to accelerate. Progressive – if uneven – political stabilization has allowed a number of African countries to rely less on raw-material exports and start becoming consumer economies. McKinsey, for example, forecasts that African consumer spending will increase by $645 billion between 2015 and 2025.

Yet massive challenges remain. The IMF recently forecast that Africa must create 20 million new jobs per year until 2035 – twice the current rate – just to absorb new labor-force entrants. This will require huge investment. But the three main existing sources of non-state financing in Africa are unable to meet these needs.

Official development assistance (ODA) to Africa declined between 2014 and 2016 and has since remained relatively flat. The local financial sector, including large African banks, suffered from the commodity-price downturn and is still constrained. And international banks retreated significantly from the continent after new regulatory standards increased the costs and capital consumption of operations in non-investment-grade countries. Surprisingly, this aspect of the collateral damage caused by the global financial crisis has not sparked much debate.

As a result, the African financing gap continues to widen alarmingly. Whereas Africa's annual financing needs have been conservatively estimated at $130 billion for infrastructure alone, available resources cover less than half of this amount. According to McKinsey, actual capital expenditure in Africa amounted to $415 billion in 2015. With average annual GDP growth on the continent forecast to exceed 3%, Africa would need to finance a further $750 billion of capital spending over ten years.

None of the major existing sources of financing can rise to the challenge by themselves. Even the IDFC, which aims to counterbalance Chinese influence and compete with European institutions, will not significantly change the pattern of

international financial flows to Africa.

What Africa needs is a new type of investor. The good news is that alternative sources of funds have been accumulating like never before. PwC expects the value of assets held worldwide by pension funds, insurance companies, sovereign wealth funds, and high-net-worth individuals to rise from $115 trillion in 2012 to $195 trillion by 2020.

These investors obviously have not been satisfied by the very low yields available in European and US markets in recent years. Furthermore, liquid assets remain extremely volatile. A number of these investors are now distancing themselves from the standard view of African transactions as “high risk,” to be compared only with high-yielding US dollar or euro investments.

This change of perception has statistical support. In 2016, Moody’s released a report showing that the rate of project-finance defaults in Africa between 1983 and 2015 was the second-lowest in the world at just 2.7%, which reflects the relatively higher strategic importance of these projects. As a result, the idea of investing in Africa through more conservative instruments, rather than “high risk, high return” private-equity deals, is gradually gaining ground.

Private-sector debt funds would be the best vehicle for such investments. Such funds total almost $640 billion worldwide, but the market remains mostly North American and European. Although private-debt funds raised more than $100 billion in 2017, almost none of this went to Africa.

The potential for these funds to invest in Africa is therefore huge. Even if only one-third of Africa’s estimated $750 billion in additional investment needs over the next decade were debt-financed, that would still amount to a $250 billion requirement. This indicates a unique opportunity to align investors seeking to finance real assets offering long-term stable returns and projects that need financing.

But even if their perception of African default risk has evolved, potential newcomers to the continent remain paralyzed by its reputation and image. They can hardly be blamed, either, given incessant media coverage of African countries’ rankings in global indices of governance, ease of doing business, and corruption.

This is where development finance institutions could play a key role in reassuring new investors who are still deterred by “Africa risk.” Annual ODA to Africa exceeds

$50 billion, is invested in the public and private sectors of most of the continent's 54 countries, and often involves world-class industrial sponsors. DFIs also have been instrumental in promoting private-equity investment in Africa, which totaled nearly $24 billion between 2012 and 2017, in sectors as diverse as infrastructure, telecoms, banking, and consumer goods. Clearly, doing business in a decent environment in Africa is possible.

The Africa investment-financing gap is a major threat to the continent's future. Growing international recognition of this is welcome, as are additional billions of development dollars from the US and elsewhere. But Africa needs new investors, and in particular private-sector debt funds, in order to close the gap and realize its enormous potential.

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