INSIGHTS FOR THE QUINTESSENTIAL INVESTOR

momento

NIGERIA - MENDING THE DEEP CRACKS

BEATING THE STARTUP FRENZY

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EDITOR'S NOTE

We are halfway through the year guys, and I am sure a few people are checking off their to-do lists. It feels like we just wished each other a happy new year yesterday, knowing this was six months ago could put some pressure on you especially if your year has not been eventful thus far. But do not sweat it, all your aspirations will be met at the appropriate time because "what God cannot do does not exist".

The month of June has been dismally eventful for Nigeria though: the further unification of exchange rates, the Twitter ban, and the violence meted out on peaceful protesters on the country's democracy day celebration.

We will all agree that years of policy errors have contributed greatly to the deteriorating socio-economic situation that has left the government helpless, and the people frustrated with arms akimbo. I weighed in on this in **Nigeria- Mending the deep cracks** (Page 05), suggesting – through data analysis – a possible route from the current economic quagmire.

The economic implications of the policy errors have been far-reaching, causing Nigerians to throw caution to the wind in their quest to augment their incomes. In **Risk & reward - The Siamese twins of investing** (Page 07), **Yusuf Ogunbiyi** stresses the importance of looking beyond ridiculous returns and ensuring returns on investment are commensurate with their underlying risks.

In the same vein, **Ife Ojobanikan** in **Beating the startup frenzy** (Page 10), emphasizes investor due diligence to avoid being caught up in startups with flawed models. Lastly, **Adedamola Ojo** in **Improving employee value proposition** (Page 12), proposes that having inclusive company policies – across all employment levels - can improve employees' value proposition.

As we begin the second half of the year, there is a possibility that the excitement and optimism that come with new beginnings can be thwarted by the frustrating realization that your goals are either not what you imagined or will take much longer to achieve. But you should not despair because even failures can be a fun way to learn.

For me, my goal is to keep filling these pages with content that will be worth your attention, and I hope you continue to enjoy them. And if you have any questions, queries, or comments, do not hesitate to drop me a mail at **info@mosopearubayi.com**.

I wish you a cake-filled (cake holds a special place in my heart) H2'21 and hope you are inspired to explore and expand. And if at first, you fail, dust yourself up and try again.

Mosope Arubayi

NIGERIA-MENDING THE DEEP CRACKS

BY MOSOPE ARUBAYI

If recent indicators are anything to go by, Nigeria's economy is in shambles. The Naira is trading at N500/$ at the open market, inflation in double-digits, unemployment at a record high, uninspiring debt levels, and deteriorating welfare indicators. The past few years have been such a downhill ride. But should you expect much from an economy coordinated by policymakers who live in ivory towers? Nigeria may very well just be a victim of inappropriate policies and malinvestments i.e., misallocation of resources, not just in the present but also in its past.

De facto, Nigeria's economy is bifurcated into oil & non-oil sectors. While there is sufficient evidence to back up the macroeconomic volatility precipitated by natural resource wealth, resource windfalls-if properly managed- can also serve as buffers for the economy, especially in downturns. Unfortunately, the country's pro-cyclical fiscal structure amidst expensive costly energy subsidies has dried up previous savings. Nigeria's economy is clearly in dire straits, but how can the country build back better?

There have been recent talks about reining in subsidies to create fiscal space so the government can accommodate more productive spending. But there is no doubt that mispricing of energy in the country eased cost pressures on a population whose income has been crimped for years and weaning the people of their only government-sponsored benefit is unpopular in the political sphere. But by just how much will subsidy removal bolster economic health?

A personal study I embarked on to assess the multi-scenario impact of different plausible policy actions suggests that subsidies are unhealthy for economic wellbeing (-0.12), and interventions amid subsidies come at a higher economic cost (-0.47). While it is established that the removal of subsidies bodes well for the economy, the removal of power subsidies seemed to be of a more beneficial effect to the economy (+1.32) than the removal of fuel subsidies (+0.77) if investment in the manufacturing sector is scaled up further by 50%.

However, complete removal of both subsidies is likely to yield a less optimal economic outcome (+0.94) when compared with eliminating only power subsidies (+1.32) but higher than the outcome obtained when only fuel subsidies were removed (+0.77). This suggests that while the removal of power subsidies is beneficial, the economy could still need some form of support via fuel subsidies to produce the best outcome.

Power subsidies are not necessarily pro-poor as poor people are less likely to afford access to electricity. This suggests that subsidy payments on electricity tend to benefit the non-poor more than they do the poor. Unlike power subsidies, fuel subsidies tend to support the poor to some degree especially since they rely on road transport to access markets and earn a living. Hence, complete removal of power subsidies could be beneficial, but it is economically prudent to roll back only some (50%), not all the fuel subsidies.

A plausible scenario for utilizing the freed funds is investing the 50% fuel subsidy roll back in power infrastructure to scale up the country's power generation capacity, improve electrification infrastructure, and/or renewable energy access. This culminates in a near-optimal outcome (+1.58) while simultaneously increasing investment in the agriculture sector by 50%, just like the manufacturing sector gives the best outcome (+1.62).

While the analysis postulates that investment in power infrastructure - rather than electricity consumption subsidies and isolated interventions to farmers and manufacturers - could bolster the economy to a healthy state, excessive investment could also result in inefficiencies as the outcome (+1.59) of plowing back all the subsidy roll back into power sector investment suggests.

The current economic crisis that is bedeviling the Nigerian economy is clearly a consequence of misguided government interventions in preference sectors that, in isolation, do not have the capacity to catalyze economic transformation. These misallocations of resources have culminated in unintended consequences, including stubbornly high inflation, more frequent recession episodes, and rising income inequality that threatens both social and political stability.

Nigeria needs to improve its production function to gain economies of scale so the industrial sector can be more competitive and, in turn, improve the volume of exports. This will have multiple positive knock-on effects on the economy. Electricity is a major input for any industrial unit and re-directing consumption subsidies to investing in the power sector can help Nigeria's industry achieve cost-efficiency, with trickle-down effects to the agriculture sector and service providers.

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RISK & REWARD: THE SIAMESE TWINS OF INVESTING

BY YUSUF OGUNBIYI

Over the course of my career, there are no two words that I have heard as frequently as "Risk and Reward". The reason these Siamese twins appear inseparable is simple, "you cannot have your cake and eat it". The investment world rings this in the ears of everyone that cares to listen, and it serves as the hallmark of the decision-making system built into the industry. The importance of this set of Siamese twins has been reflected in the Nigerian investment landscape over the years, and we have witnessed the impact of the mismatch of the risk and reward profile (i.e., the ratio of the risk-to-reward for every investment). Each investment has its peculiar risk-reward ratio, and investors make their investment decisions based on this.

The ratio varies across a wide spectrum of investment opportunities. The golden rule has always been to match the reward sought with the risk of the investment being considered i.e., investments matched with high risks should also offer high yield and vice versa. Across the investment industry, the Private Equity/ Venture Capital industry offers some of the most lucrative returns with PE/VC funds returning multiples beyond 10x sometimes. Deep down the massive returns posted by this industry sometimes is a pool of failures and risks and at the end of the day, 7-8 out times out of 10, the investments made by these funds fail and do not perform well. On the other of the spectrum, we have the fixed income instruments that offer guaranteed returns; hence they are deemed risk-free. However, they also offer the lowest returns in the industry.

Investors in Nigeria have been awash with ridiculous investment options - with some offering returns of 30% per month (Brisk Capital) or even 50% in 6 months (H.O Corn) - that have gone bust, with huge sums of money involved. These investment opportunities have come from multiple sources; recognized or unrecognized, structured, or unstructured, but there have been several characteristics that have simply served as the base rock of all these opportunities; high fixed returns and less than a year in tenor. The preponderance of these type of investment vehicles gives off two crucial characteristics of Nigeria's investing population:

- a very low appetite for risk.
- make as much money as possible, and quickly too.

Investors that are easily swayed by the promise of higher returns on short-tenured instruments, oft times are not consciously evaluating the risks involved in the fundamental models of the opportunity.

A mismatch in the risk-reward appetite of an investor is a precursor to disaster. Investors that are easily swayed by the promise of higher returns on short-tenured instruments, oft times are not consciously evaluating the risks involved in the fundamental models of the opportunity. This has caused Nigerians - in hundreds and thousands - to lose huge amounts of money to these schemes. Worst still, more people are still falling prey, daily, to such schemes.

The antidote to this chaos is clear; evaluate the risk and reward of every investment and ensure that they fundamentally match to avoid "God abeg" scenarios. This, however, does not mean that well-thought-out investments do not also go bad, but the chances of losing your money due to poor investment advice or investment management are slimmer.
A word, they say, is enough for the wise.

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BEATING THE STARTUP FRENZY

BY IFE OJOBANIKAN

S4E2 In the series Bull opens with Whitney Holland (the founder) pitching her water desalination technology to an audience of potential investors. She promises that work is ongoing to scale the technology to cater to municipalities. She concludes the pitch with, “my tech team tells me we are only 90 days away” and then proceeds to drink water filtered during the live product demo - on stage. The investors never stood a chance. They were in.

The story of Theranos, is one that is over flogged but reminds us of the importance of due diligence and the inevitable consequences that come when we do not carry out a thorough investigation before investing in businesses. Even though the company raised $700M (some sources quote >$1.1B) at a peak valuation of $9B, it failed because the product did not work. At uBiome, people in the know also point to the use of certain “growth hacking” techniques and fundamental flaws in the science as responsible for the company’s downfall.

In what is probably the most dismal startup story, 1 of 3 Roadstar.ai co-founders reportedly got payola during fundraising, deliberately secreted codes (bear in mind this was a self-driving start-up), and falsified records. He was fired, but in an interesting turn of events, the investors fought back stating that he was fired without their consent and letting him go would be detrimental to the interests of the company. The board went on to discharge the CEO and replace him with CTO.

Of course, investors simply wanted out at that point and by 30th March they were looking for new acquirers after procedures to dissolve the company were initiated and a $90M investment fund was frozen. The company’s current valuation is less than 0.1 what it used to be. They had so much potential, but alas.

The startup scene is one that involves a great deal of posturing. With this, subconscious biases quickly become a part of investor decision-making. Amounts raised, talents onboarded, and awards won act as proxies to validate business models, products, and a company's potential to scale. Increasing valuations and fundraising have become de facto indicators of a tech startup's financial wellness, growth, and future success. Startup valuations determine if they are a hectocorn, decacorn, or unicorn, or not. Concealed amounts and your firm is enveloped in mystery. High, and it is assumed you are thriving. Low - or not growing astronomically -, and it is assumed you are bound to crash and burn.

While investors do not have the luxury to move fast and break things, they can do a few things to protect themselves:

- **Run independent due diligence (DD)**: I think everyone assumes the next person has done some due diligence. That X just invested in Y startup or A referred B does not make them foolproof.
- **Have your own investment criteria**: A list of indicators or metrics you personally look out for before investing could go a long way in saving your skin.
- **Voice out issues you may have with the deal or founder to your team**: Even if everyone else thinks you are crazy or if the concern is not a deal-breaker, it helps your team know what to prepare for. Best case scenario, you get to say, "I told you so." Worst case, maybe you are crazy. Sometimes all you have is a gut feeling — get proof to back it up. Tim Ferriss' book, "Tools of Titans", touches on how Marc Andreessen and Ben Horowitz beat up each other's ideas in front of newer hires. This has encouraged newer hires to talk about possible pitfalls they see as well.
- **Post-investment "DD" (More Due Diligence)**: Man up when you discover fundamental flaws. For example, a product that is not working or cannot work at scale, a revenue model destroyed by new government policies, co-founders running amok with exotic automobiles, women, and luxury accommodation on the company's dime. Key questions to ask include:
  > Are they fulfilling orders? (Case in point: Token, Unicorn)
  > Are they hitting a predefined milestone?
  > Is money unaccounted for?
  > Or are they having issues with customer acquisition or building distribution networks?
- **And more importantly, how can you help**: Investors also have skin in this game. The only way to score a major success is if one or more of your portfolio companies outperform. What good is your network if you cannot make asks that give your portfolio companies a better chance at survival? Building a company is hard. Sometimes all a founder needs is for you -the investor - to check on them. Remember how you felt when your (rich) parents did not show up for the open day, PTA, or visiting day? Yeah. Unfortunately, as a parent, the only way to get to know if your child fell ill or is having issues in school is by showing up and asking the right questions.

What good is your network if you cannot make asks that give your portfolio companies a better chance at survival?

IMPROVING EMPLOYEE VALUE PROPOSITION (EVP)

BY ADEDAMOLA OJO

"Everyone talks about building a relationship with your customer. I think you build one with your employees first. "

-Angela Ahrendts (Senior Vice President, Apple)

In the cooperate world, there is a saying 'we just came to work' anything outside that is not necessary to meet my personal goals. Organizations whose employees go with this mantra, tend to underperform organizations that encourage team building and flexibility based on employees' mode of creativity. The pandemic has forced many companies to assess how employees truly feel about their jobs, while many employees have used this past year to introspect and reflect on both their jobs and how they are been treated by their employers.

Traditionally, organizations focus on employees as workers when they define their employee value proposition (EVP). On the contrary, however, building a relationship with your employees or team members will help you understand their areas of strength and weakness, which helps your decision-making process and culminates in greater customer satisfaction. Genuine interest in your employees earns you a lifelong currency of trust and respect but you must get it right from the onset.

Many employees want their organization to see them and treat them as people first, not just employees. As an employer of labour, how do you make people feel: from the recruitment, onboarding to the exit processes? Is your organization's culture designed to value talent? As the CEO/team Lead, do you value people? Do you employ people that value people and align with your organizational culture?

Your employees are the face of your organization; your ambassadors where you do not have your mission and vision displayed. Just the way alumni of Ivy League schools show off their alma mater, your employees should be proud to show they work for you. But this pride does not just manifest, it starts with having a great and inclusive organizational culture that includes treating employees appropriately.

Company size does not really matter when it comes to providing good corporate culture. There are proud employees of seemingly small organizations, just as there are disappointed employees of big organizations, who are not confident to talk about the workplace. Their unpleasant experiences cause them to unintentionally de-market their employers.

Having the right people at the helm of affairs also helps bridge the gap between management and employees. Are your managers and team-leads employee-centric? In the bid to build trust, do not trust blindly; there is a level of emotional intelligence that goes into balancing professional and personal relationships.

The companies of the future are those that can offer flexibility around when and where work gets done and provide employees with opportunities for personal growth. This will not only go a long way in building employees' trust in management, invariably increasing their value proposition in the long term.

Genuine interest in your employees earns you a lifelong currency of trust and respect but you must get it right from the onset.

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OLUKAYODE OLAYEMI