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Private Equity as a Developmental Catalyst: A Three-Level Framework for Inclusive Entrepreneurship in Africa

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Abstract

Private equity (PE) is increasingly positioned as a vehicle for entrepreneurial development in Africa, yet its reach and impact remain uneven. This paper proposes the Three-Level Developmental Private Equity (3LD-PE) Framework to analyse how PE catalyses or constrains entrepreneurial growth under conditions of institutional fragility, financial exclusion, and enterprise informality. The model employs Agency Theory, Resource-Based View (RBV), Financial Constraint Theory (FCT), and Institutional Theory to conceptualise PE as a multi-level actor that operates at the firm (micro), financial system (meso), and institutional (macro) levels. The model presents five empirically testable propositions which focus on governance, strategic capability, capital access, institutional engagement and business resilience. The paper focuses on distributional dynamics to illustrate how gender, geography, and enterprise form determine who benefits from PE interventions and who remains excluded. The paper proposes a research and policy agenda for more inclusive, accountable and context-responsive PE strategies in African entrepreneurial ecosystems.

Keywords

Private equity, entrepreneurship, informal enterprise, governance, development finance, business resilience, inclusive growth

1.Introduction

1.1 Background and Context

Private equity (PE) investment serves as a transformative financial tool that enhances business expansion, promotes financial inclusion and Innovation, and drives governance improvements throughout Africa's entrepreneurial ecosystem. The investments typically take the form of capital investments, such as equity shares in the business (Knickerbocker, 2022). PE provides enterprises with financial support that traditional banks or lenders find challenging to provide. In addition, it also delivers managerial expertise, supports innovation adoption, aids operational efficiency improvement, along with governance frameworks enhancements and strategic guidance, which traditional banking institutions often cannot offer.

The number of PE investments in Africa has experienced significant growth over the past twenty years, expanding into sectors such as technology, healthcare, Fast-Moving Consumer Goods (FMCG), and infrastructure. The growing investor trust in African markets is driven by macroeconomic diversification and the expansion of the middle class (Jha, 2024).

1.2 Problem Statement and Structural Gaps

The growing interest in PE activity in Africa does not translate to widespread PE investment across the continent because most PE activity focuses on formal high-growth sectors, which exclude numerous microenterprises and survivalist ventures that make up the majority of African entrepreneurship.

The majority of African economies consist of numerous informal and necessity-based enterprises, which create a structural problem because PE investment models do not match the actual characteristics of local enterprise ecosystems. Informal firms face challenges in capital absorption and institutional engagement because they lack audited accounts, effective governance structures, and scalable business models.

1.3 Purpose and Scope of the Study

This paper aims to go beyond synthesising existing scholarship by offering a novel conceptual framework and a set of testable propositions on how PE catalyses enterprise transformation in Africa under conditions of adversity. It integrates four theoretical perspectives, namely Agency Theory, Resource-Based View, Financial Constraint Theory, and Institutional Theory, to examine the mechanisms through which PE fosters resilience, Innovation, and inclusive governance in African businesses.

1.4 Contribution to Knowledge

This paper offers a conceptual contribution by proposing a new framework for understanding how PE supports enterprise development under financial and institutional adversity in Africa. Anchored in the four theoretical perspectives highlighted above, the paper integrates theoretical insight with context-specific dynamics to generate original propositions on PE's developmental role. In addition to offering a conceptual model, the paper articulates five testable propositions to guide future empirical inquiry. It also engages critically with the limitations and risks of PE in African markets, including elite capture, the exclusion of informal ventures, and structural exit challenges. While highlighting PE's enabling functions, it also interrogates its constraints, especially in reaching survivalist and necessity-driven enterprises. The framework and propositions contribute to developmental entrepreneurship scholarship by reframing PE as a systemically embedded actor operating across firm, financial, and institutional levels.

2. Literature Review

PE is increasingly portrayed as a catalytic force in Africa's entrepreneurial development, often credited with expanding access to finance, enhancing governance structures, and driving Innovation among investee firms. Dominant scholarly narratives celebrate PE's role in strengthening managerial capacity, operational performance, and market competitiveness, particularly within formal, high-growth enterprises. PE is also positioned as a contributor to inclusive development through targeted investments in youth- and women-led ventures.

Yet this largely affirmative literature often under-theorises the structural exclusions, systemic risks, and contextual constraints that shape PE's functioning in emerging economies. Critical questions remain insufficiently explored, especially regarding the uneven distribution of PE across geographies, firm types, and socio-economic contexts. Investment practices continue to prioritise scale, compliance, and exit viability, effectively marginalising the vast informal and necessity-driven enterprises that define much of sub-Saharan Africa's entrepreneurial ecosystem.

Despite recorded successes, PE's broader developmental impact remains constrained by persistent institutional and market-level challenges. Regulatory opacity, bureaucratic inertia, and market fragmentation inhibit deal flow and long-term engagement. Heightened risk perceptions and shallow local capital markets further undermine investment sustainability. These structural bottlenecks reveal a deeper theoretical and practical gap, i.e. the need to interrogate not only what PE enables, but also where, why, and for whom it fails to deliver inclusive outcomes.

The literature also fails to adequately account for the disjuncture between PE investment criteria and the enterprise profiles that dominate African economies. Informal, subsistence-based businesses, especially in urban and peri-urban areas, are structurally misaligned with the risk-return expectations and governance standards demanded by PE investors. Empirical studies, e.g., reveal that such enterprises often lack formal registration, audited accounts, and scalable models, rendering them effectively invisible to most PE funds. This misalignment raises urgent questions about the inclusivity of PE as a developmental mechanism. As Kaplan & Strömberg (2009) and Lerner et al. (2007) note, PE inherently favours firms with robust governance and transparent financial records, criteria that most informal or survivalist ventures cannot meet. Without the integration of flexible instruments such as blended finance, revenue-sharing models, or community-based intermediaries, PE risks reinforcing existing capital inequalities rather than bridging them.

Against this backdrop, the following section critically synthesises the evolution of PE in Africa, examining both its contributions to governance, Innovation, and financial sustainability, as well as the persistent limitations that constrain its developmental potential.

2.1 Growth of Private Equity Investments in Africa

PE activities in African markets have experienced significant growth over the past two decades due to investors' growing optimism, sectoral Innovation, and institutional reforms that have taken effect. The growth of PE serves as a fundamental investment tool which Development Finance Institutions (DFIs), along with impact investors and regional funds, use to expand their exposure to emerging African markets. However, a closer analysis reveals significant variation in the depth, spread, and consequences of this capital. The following section examines the historical development of PE in Africa through three interconnected elements. There are the scale and sectoral composition of investment flows, the geographic and institutional barriers shaping distribution, and the structural dynamics of capital sources and their implications for development.

2.1.1 Capital Inflows and Sectoral Trends in PE Investment

PE investments in Africa have expanded substantially over the past twenty years, characterised by growth in deal values and increased fund sizes, driven by more active participation from global and regional investors. The positive macroeconomic trends and urban market growth, combined with demographic advantages and the adoption of digital technology, have all contributed to this trend in Africa (Ernst & Young, 2022; McKinsey Global Institute, 2016). The African Private Capital Activity Report (AVCA, 2023) indicates that PE deal values reached USD 7.6 billion in 2022, representing a 21% increase from 2021, while the number of transactions increased from 429 to 626. The data indicates that capital availability has increased, while investors demonstrate greater confidence in the region's future economic growth.

The majority of PE investments stream into only a few "investment-ready" sectors. Technology, financial services, healthcare, and renewable energy have received the majority of investments because they offer strong scalability potential and both resilience and developmental value alignment (Dalberg, 2018; International Finance Corporation, 2020). Startups in fintech fields from Nigeria, Kenya and South Africa received substantial PE funding, reflecting investor interest in digital financial inclusion solutions (GSMA, 2022). The private capital sector has also begun to finance off-grid solar power, as well as agri-tech and logistics, because these sectors bridge development service gaps and offer profitable investment opportunities.

The increase in sector-focused investments demonstrates a broader trend among Development Finance Institutions (DFIs) and impact investors use PE vehicles to achieve blended value creation by merging financial returns with measurable development results (Bugg-Levine & Emerson, 2011). However, the distribution of these investments remains unbalanced between different geographic areas and enterprise categories, a concern explored in the following subsection.

2.1.2 Uneven Geographies and Institutional Constraints

The headline statistics in 2.1.1 above clearly indicate that capital distribution across geography and structure remains highly unequal. PE flows are concentrated in a few middle-income urban economies, such as South Africa, Nigeria, Egypt, and Kenya, where legal predictability and investor protection frameworks are more developed (Mbeng Mezui & Hundal, 2013). In contrast, markets with high entrepreneurial density but weak regulatory environments, such as those in under-capitalised, informality-dominated markets, continue to be marginalised. These markets are not attractive to most PE funds despite the significant developmental needs due to the lack of mature exit pathways and sufficient institutional infrastructure (Hainz & Kleimeier, 2012).

The problem is further complicated by the fact that exit constraints persist due to limited liquidity in local capital markets and underdeveloped exit infrastructure. Lerner et al. (2007 explain that these conditions force PE firms to adopt shorter holding periods, maintain risk-averse investment strategies, and select firms with pre-existing global value chain integration. The literature rightly points out the upward trend in PE inflows, but it often fails to account for how these structural exclusions shape investment behaviour. Growth narratives often overlook the fact that a substantial portion of Africa's entrepreneurial economy, particularly in underserved areas, remains inaccessible to formal capital. In doing so, they risk overestimating the developmental impact of PE and under-theorising the institutional barriers that limit its transformative potential.

2.1.3 The Political Economy of PE Capital

Capital investment by PE firms in Africa has grown, which is a sign that investors are more confident in the opportunities the continent offers. One key concern, however, is that most of this capital comes not from actors on the continent but from institutions based outside of Africa. These foreign institutions include development finance institutions, which are at the forefront of this investment story. Their capital comes with external returns, including environmental, social, and governance (ESG) considerations, as well as geopolitical expectations and objectives (Agbloyor et al., 2014).

Inflows of investment often fail to align with local development needs. This is due to structural financing asymmetries and weak institutional frameworks across much of the African continent (Bracking, 2016). In this regard, African economies are not benefitting from investment that seeks to achieve sustained, inclusive local growth (Mawdsley, 2018. These observations are supported by recently published data from AVCA, which reveals that over 70% of the PE capital invested across Africa is from investors based outside the continent. For the most part, these investors have exit timelines that do not align with the long-term investment strategies required to support the establishment of sustainable African enterprises (AVCA, 2023).
This results in risk-averse investment strategies focused on urban hubs and high-yield sectors such as fintech and renewable energy, while under-capitalised, informality-dominated, and institutionally underserved sectors remain excluded (Bracking, 2016; Mawdsley, 2018).
The dominance of offshore listings, foreign acquisitions, and profit repatriation has led to significant capital outflows, undermining local reinvestment, capacity-building, and financial resilience (Fofack & Ndikumana, 2009, 2010; Hill et al., 2025). An example of this is seen in some East African cases, where firms relocated control and exit proceeds abroad to align with fund priorities. Additionally, structural weaknesses in domestic capital markets further limit local exit options. In Kenya, for example, over half of PE exits between 2007 and 2014 were through share buybacks, with no IPOs recorded, highlighting the limited local liquidity (Divakaran et al., 2018). These patterns highlight a critical issue: while PE aims to support development, its impact may be limited due to its operation within unequal global financial systems. Without local capital mobilisation, blended finance tools, or structural reforms, PE may reinforce exclusionary dynamics rather than disrupt them. Addressing the political economy of capital is essential for making PE genuinely developmental.

2.1.4 Probing the Limits of PE Inclusion: From Ecosystem Structures to Firm-Level Impacts

The preceding sections established that Africa's PE environment, while growing in capital volume and sectoral breadth, remains structurally exclusionary. Investment flows continue to favour formalised, scalable ventures, leaving out the vast majority of informal and necessity-driven enterprises (Charman et al., 2017). This exclusion is not incidental but reflects the architecture of most PE funds, which prioritise risk-adjusted returns, regulatory clarity, and clear exit pathways. The dominance of foreign capital further complicates alignment with local developmental objectives, raising concerns around value extraction, reinvestment deficits, and the social equity of PE-led growth.

Understanding the developmental implications of PE requires a shift from broad trend analyses to the interrogation of investment effects on enterprise dynamics at the firm level. The subsequent section dissects core areas, including governance, Innovation, inclusion, financial access, and resilience, all of which are crucial to PE's developmental effects, critically interrogating whether it enhances Africa's transformative capacity or reinforces structural constraints in the entrepreneurial landscape.

2.2 Private Equity Strategies and Entrepreneurial Success

Functional international PE investors in Africa operate as partners, not just financiers, because they help to implement governance controls, lead in making key strategic decisions, and professionalise the management of their portfolio companies (Hearn et al., 2018).

In nations like South Africa, PE funds employ methodical risk-management structures such as EV/EBIT analysis, stress tests, and co-investments to ensure that the companies in which they invest grow in a way that meets the funds' return expectations (Zerihun & Affedjou, 2025). This is not just influence at the top level, it is PE's hands-on, strategic way of managing the operational levers within the companies it invests in.

PE funds are now also focusing on young and women entrepreneurs, a result of the impact-oriented strategy of many funds that target sectors such as agriculture and renewable energy. The research by Watts & Scales (2020) reveals that PE and social impact investors are intentionally targeting rural and gender-inclusive agriculture in sub-Saharan Africa, employing deliberate strategies to support women farmers and climate-resilient models. In addition, the research by Adjei-Mantey et al. (2025) reveals a direct correlation between expanded access to renewable energy for females and their empowerment. This shows the potential of clean energy to serve as a pathway to female empowerment in Africa. These interventions create employment opportunities while developing business models that include everyone, helping companies expand their operations in accordance with African development requirements.

However, these developmental advantages primarily benefit a specific entrepreneurial group of formalised high-growth firms that maintain strong internal controls and record-keeping systems. The investment logic demonstrates rationality, but it strengthens existing financial inequalities. The majority of business operations in African urban and peri-urban communities function as survivalist or informally structured enterprises, which, due to these characteristics, are excluded from PE Investment opportunities (Charman et al., 2017; Cunningham & Bodewig, 2023). These firms remain hidden from conventional PE investment vehicles because they lack financial documentation, scalability and governance capacity. Most PE funds claim to support inclusivity, but they do not modify their financial instruments or investment systems to reach a broader range of entrepreneurs. The development impact of PE remains restricted to a small number of formal businesses, which hinders its potential to create extensive systemic transformations. The difference between PE's declared developmental purpose and its actual operational methods raises doubts about its effectiveness in developing local economies through community-based entrepreneurship (Chen & Alter, 2012).

To understand the scope and limitations of PE in Africa, it is necessary to disaggregate its contribution across different operational variables or levers. These include improvements in governance empowerment through inclusion, access to capital, innovation acceleration, sustainability alignment and crisis resilience. The following subsections examine these mechanisms, drawing on empirical literature to demonstrate both the practical advantages and structural barriers that PE creates when operating across the African continent.

2.2.1 Governance and Organisational Change

Entrepreneurial resilience in emerging markets requires robust governance frameworks, as weak oversight and opaque decision-making, combined with informality, pose significant threats to business survival and sustainability. PE investors resolve these gaps by implementing professional management systems and strengthening accountability measures and internal control mechanisms. The involvement of PE in sub-Saharan African SMEs, particularly those with family management and informal governance practices, brings essential organisational structure and disciplinary practices.

Lin et al. (2019)reveal that PE-backed firms implement advanced governance practices primarily through active investor participation on the board. Through these roles, organisations make strategic decisions, fulfil financial obligations, and establish long-term plans that prove essential for managing volatile markets. PE engagement also helps to resolve principal-agent issues, which builds investor trust and organisational trustworthiness (Montchaud, 2014).

The governance enhancements exist only for companies that fulfil the fundamental formal requirements. The governance benefits of PE investments are often unavailable to microenterprises and early-stage ventures, which operate informally due to a lack of transparency and low absorptive capacity. PE governance impacts show selective results because they only affect specific businesses (A. Charman & Petersen, 2014; International Finance Corporation, 2024).

2.2.2 Empowerment and Inclusion

Providing targeted financial support to businesses run by women and by other groups that have been marginalised in the entrepreneurial sphere makes PE an inclusionary force. Today, PE firms are making gender-balanced investments their priority. These firms recognise that such investments can pay off economically and socially (McAdam, 2023). Historically, women and minority founders have faced persistent structural barriers to accessing growth capital.

However, recent PE-backed initiatives have demonstrated that firms led by women often outperform on key development metrics such as job creation, network mobilisation, and community reinvestment (Nulleshi & Kalonaityte, 2022). By championing diversity and inclusion, PE can transform Africa's entrepreneurial ecosystem through targeted support that enables businesses to access capital while also receiving mentorship, operational expertise, and market linkages that might have been otherwise unavailable.

Yet, the transformative potential of these strategies is frequently limited to a narrow segment of the entrepreneurial population. Without formal investment mandates that institutionalise inclusion priorities, many PE firms continue to focus on scalable, formalised businesses, leaving informal, gender-marginalised, or community-rooted ventures at the periphery of investment flows (Robino & Jackson, 2022). Systemic approaches to inclusion are more effective than treating it as incidental because the latter risks maintaining current inequalities instead of eliminating them (Naudé, 2010)

2.2.3 Bridging the Funding Gap

Access to finance remains one of the most cited constraints to business growth across Africa, particularly for SMEs, youth-led startups, and women entrepreneurs. Traditional lenders often impose stringent collateral requirements, short repayment terms, and high interest rates, all of which act as barriers that exclude most early-stage or informal businesses from formal capital markets.

PE offers an alternative by providing patient capital, often accompanied by strategic support. For example, Dalberg (2018) observes that PE not only fills financing gaps but also enhances investment readiness by supporting business planning, compliance, and reporting functions. This dual financial-strategic support positions PE as a development-oriented actor, especially in underbanked sectors. Robino & Jackson (2022) further argue that impact-focused PE investors increasingly target ventures with both growth and social return potential, thereby addressing historically underfunded demographics. However, without adapted funding structures, such as revenue-based finance or tiered equity models, the reach of PE remains limited. Many promising but informally structured ventures remain under the radar, pointing to the need for more inclusive capital instruments (Charman et al., 2017)

2.2.4 Driving Innovation

PE serves as a key driver of Innovation and technological advancement throughout African economies, particularly in high-growth sectors such as fintech, agritech, and healthcare. PE investments deliver capital alongside strategic guidance, which helps businesses accelerate product development, technology adoption, and market expansion. Research shows that companies backed by PE tend to file more patents, launch new services at a faster pace and achieve better market competitiveness than unbacked companies (Link et al., 2014).

Miyamoto et al. (2022) demonstrate how PE facilitates innovation commercialisation in European markets, a trend now becoming evident in Africa's developing entrepreneurial clusters. PE's support enhances the market readiness of startups and SMEs, making them more attractive for future acquisitions or stock listings, thereby contributing to the diffusion of Innovation across sectors.

However, these innovation benefits tend to concentrate in formal, urban-based, tech-enabled firms. As with inclusion strategies, these innovation pathways essentially bypass the informal and survivalist ventures that dominate much of Africa's entrepreneurial landscape. Despite sector-specific advances, the majority of these enterprises remain structurally disconnected from PE-led transformation due to their limited absorptive capacity, inadequate record-keeping, or limited scalability potential (Abor & Quartey, 2010).

2.2.5 Sustainable Development and Social Impact

The Sustainable Development Goals (SDGs) are becoming increasingly pertinent to Private Equity (PE) through investments in renewable energy, healthcare, education, and infrastructure. Impact-oriented PE firms have as their principal aim the creation of both financial returns and demonstrable social value. Their strategy is to invest in businesses that deliver enhanced service or that foster greater economic participation. The ultimate goal is to generate substantial returns for investors while also achieving significant social impact.

The research by Fox et al. (n.d.) demonstrates that PE is now playing a bigger role in SDG financing through blended finance vehicles that combine private incentives with public outcomes. Nachemson-Ekwall (2023) explains how PE strategies now combine financial returns with sustainable social and environmental objectives, including job creation, poverty reduction, and green Innovation. However, the implementation of environmental social governance (ESG) metrics in PE investment mandates shows inconsistent patterns. Most funds pursue impact through opportunistic means instead of using established, enforceable frameworks. Standardised reporting and third-party verification, as well as outcome-linked performance metrics, are missing from the current system.

2.2.6 Entrepreneurial Resilience During Crises

Political instability and climate shocks have long made African enterprises vulnerable to disruptions. The vulnerability of African businesses became even more pronounced during the COVID-19 pandemic. Research shows that firms backed by PE show a better capacity to endure and innovate during disruptions. They have better systems for managing liquidity and conduct scenario planning more effectively, making their operations more adaptable Gompers et al., 2022).

PE investors actively manage their portfolios during crises, according to Gompers et al. (2022), by assisting firms in restructuring debt, reconfiguring supply chains, and maintaining employment levels.

Interventions from PE-backed firms lead to improved business continuity and faster post-crisis recovery compared to those from non-PE-backed firms.

However, such resilience remains inconsistently distributed between different groups. The majority of formal and large enterprises receive PE support, but informal and subsistence-level businesses, which face maximum external shock exposure, lack such protective measures. The developmental inclusivity of PE becomes a concern because PE does not provide sufficient protection to all businesses during times of economic vulnerability (Beck & Cull, 2014).

2.3 Toward a Broader Theoretical Lens

The literature demonstrates that PE can be a potent and effective tool for nurturing entrepreneurial growth in Africa. However, its impact remains limited and shallow, affecting only a small group of firms, mainly formal, growth-oriented businesses that meet the particular investment criteria of the private equity industry. In contrast, the vast majority of enterprises, including those that operate in the informal sector, survivalist businesses, and community-based firms, find themselves excluded from the focus of the apportioning of PE, as well as from potential access to PE investments, which results in exclusion of a large number of potential beneficiaries from what could be a transformative vehicle.

To address this gap, the paper proposes the Three-Level Developmental Private Equity (3LD-PE) Framework, which integrates four foundational theories. These are Agency Theory, the Resource-Based View, Financial Constraint Theory, and Institutional Theory. The framework positions PE as a multi-level actor operating at the micro (firm), meso (financial system), and macro (institutional) levels, simultaneously enabling and limiting entrepreneurial transformation under adverse conditions. Section 3 presents the theoretical basis, and Section 4 introduces the integrated model along with five empirically testable propositions for future research.

3. Theoretical Foundations of the 3LD-PE Framework

This paper adopts a conceptual approach to understanding how PE catalyses entrepreneurial transformation under conditions of institutional fragility, financial exclusion, and enterprise informality. The 3LD-PE Framework is an original model that integrates four theoretical lenses, namely Agency Theory, the Resource-Based View (RBV), Financial Constraint Theory (FCT), and Institutional Theory, to explain how PE operates across micro- (firm), meso- (financial system), and macro-level (institutional environment) layers to generate developmental outcomes. This section presents each theory, clarifies its relevance to PE in African contexts, highlights both its beneficial and limiting aspects, and examines it through an adversity lens to ensure it aligns with African entrepreneurial environments.

3.1 Agency Theory: Governance Reform and Its Boundaries

Agency Theory, introduced by Jensen & Meckling (1976), addresses the misalignment of interests between principals (e.g., PE investors) and agents (e.g., managers) by proposing mechanisms such as incentive alignment, performance monitoring, and board control. In African SME contexts, often dominated by family ownership and informal decision-making processes, PE's intervention through board representation, audit enforcement, and managerial accountability is especially critical.

Yet, these governance improvements are frequently limited to enterprises that have already achieved fundamental formalisation. Most micro-enterprises and informal firms across Africa remain beyond the oversight of PE because they do not have audited financial statements or formal board structures. The

Agency Theory explains PE's governance professionalisation role, but also reveals a selection bias that restricts its impact on the broader system.
Under conditions of adversity, marked by weak enforcement institutions, informal managerial norms, and volatile accountability frameworks, the assumptions of agency alignment are less predictable, and PE's capacity to impose governance discipline is restricted.

3.2 Resource-Based View (RBV): Capability Enhancement and Exclusion
The RBV Barney (1991) explains competitive advantage as emerging from a firm's access to valuable, rare, inimitable, and non-substitutable (VRIN) resources. PE contributes to this by injecting strategic resources, such as operational systems, skilled talent, market access, and digital infrastructure, into its portfolio companies.
However, PE's contribution to firm capabilities is concentrated mainly in scalable, urban-based, and tech-enabled enterprises, where such resources can be leveraged to generate financial returns. In contrast, the majority of African entrepreneurs, particularly those in rural, community-based, or survivalist ventures, remain excluded from these upgrading pathways. RBV, therefore, helps explain how PE drives firm-level Innovation and expansion, but also reveals its structural blind spot in reaching marginalised segments of the entrepreneurial landscape.
In the face of adversity, where firms operate with minimal structure, limited absorptive capacity, and social capital serving as a substitute for VRIN assets, RBV must be interpreted more flexibly. Resources such as informal trust networks or subsistence-level adaptability, while not traditional VRIN assets, are critical for survivalist entrepreneurs. PE's inability to recognise or integrate these informal resources constrains its developmental reach.

3.3 Financial Constraint Theory (FCT): Alleviation with Thresholds
FCT (Fazzari et al., 1988; Kaplan & Zingales, 1997) holds that many growth-oriented enterprises remain constrained by limited access to capital due to underdeveloped financial systems. PE plays a critical role in addressing this by providing patient, equity-based capital to enterprises that lack collateral or conventional lending relationships.
Nonetheless, this role is primarily confined to firms that meet minimum thresholds of investment readiness. Despite often being high-potential, informally structured ventures, they are typically overlooked due to information asymmetry, governance opacity, or low scalability. While PE mitigates credit rationing for investable enterprises, it does not solve the broader financing exclusion that affects the majority of African entrepreneurs.
In adversity, access to finance is not just a function of capital markets, but also a matter of survival logic. Enterprises may resist formalisation not due to ignorance but because of rational adaptation to volatile or extractive institutional environments. FCT under adversity thus requires rethinking PE's role beyond capital injection to include financial literacy, trust-building, and blended instruments that reduce the risk threshold.

3.4 Institutional Theory: Market Shaping Amid Institutional Voids and Power Asymmetries
The Institutional Theory, developed by North (1990), explains that firm behaviour emerges from formal rules and informal norms, along with their corresponding enforcement systems. PE firms which receive

support from Development Finance Institutions (DFIs) function as institutional entrepreneurs who promote regulatory changes, ecosystem development, and standard setting.

The institutional engagement of PE firms shows inconsistent behaviour while remaining opportunistic. PE firms tend to follow basic institutional standards instead of making efforts to change them. The lack of standardised ESG mandates, combined with inadequate third-party monitoring and limited local policy influence, creates an unbalanced and difficult-to-verify institutional impact of PE. PE in Africa is mainly financed by foreign limited partners who expect high returns and have short investment horizons. These investors have geopolitical concerns that influence their investment decisions. Their priorities often conflict with the types of long-term, stable, and accountable institutions that the continent requires.

3.5 Synthesis: Toward a Multi-Level Model of Developmental Impact

Together, these four theories offer a comprehensive explanation of how PE enables and limits entrepreneurial development in Africa. The 3LD-PE Framework conceptualises PE as a systemically embedded actor that intervenes across three interrelated levels. These are

Micro-Level (Firm), where PE improves governance and builds strategic capacity (via Agency Theory and RBV), but this benefit is primarily confined to already formalised firms and misses informal entrepreneurial logics shaped by adversity.

At the Meso-Level (Financial System), PE addresses capital constraints (via FCT) for investment-ready SMEs but does not extend to informally structured ventures that lack visibility or absorptive capacity. Financial inclusion in the face of adversity requires alternative funding structures.

At the Macro-Level (Institutional Environment), PE can influence market norms and regulatory reforms (via Institutional Theory), especially when aligned with DFIs. However, these efforts are often fragmented, constrained by expectations of foreign capital, and may actually deepen rather than resolve institutional asymmetries.

These levels are interdependent. Improved firm governance enhances financing viability, which in turn increases institutional visibility and legitimacy. The framework highlights feedback loops through which successful PE-backed firms shape institutional change, and vice versa. It also emphasises that PE's development impact remains uneven and exclusionary without adapted funding models, inclusive mandates, and structural checks on capital flows.

This theoretical synthesis provides a foundation for the model in Section 4 and the empirical propositions in Section 5. It positions PE as a selective yet potentially transformative force within Africa's entrepreneurial ecosystems, especially when adversity is considered a core design principle, rather than a background condition.

4. Conceptual Framework: Private Equity and Entrepreneurial Development in Africa

4.1 Overview of the 3LD-PE Framework

The Three-Level Developmental Private Equity (3LD-PE) Framework conceptualises how PE catalyses entrepreneurial transformation in Africa by operating across three interconnected levels these being the firm (micro), the financial system (meso), and the institutional environment (macro). It integrates four theoretical lenses highlighted above to provide a holistic understanding of PE's developmental role and its constraints under conditions of adversity.

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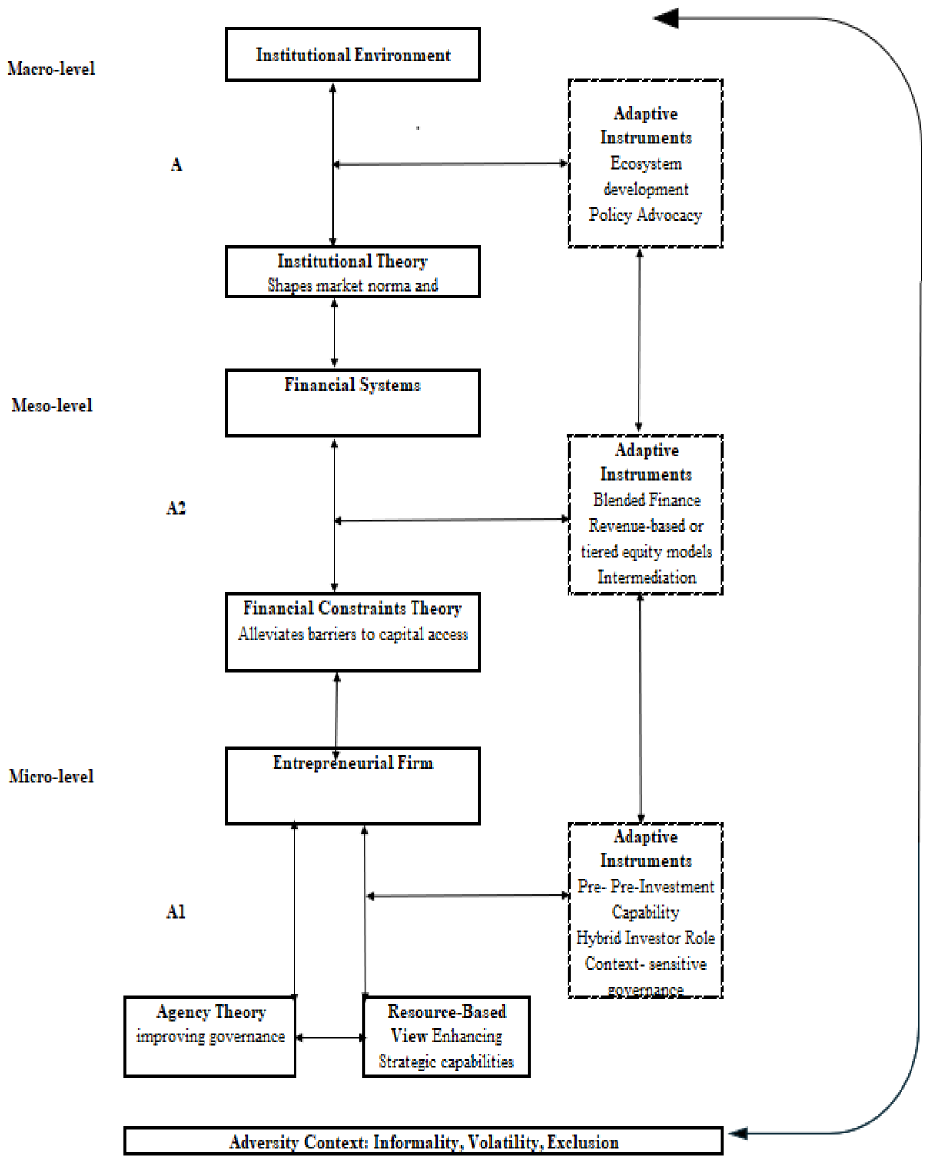
Figure 1: Three-Level Developmental Private Equity (3LD-PE) Framework



The framework, illustrated in Figure 1 (refer to Annexe 1), positions PE as a systemically embedded actor whose interventions at each level are linked through dynamic feedback loops. It incorporates adaptive instruments such as blended finance, trust-building, and capability mentoring to extend PE's reach across formal and informal systems. Adversity is treated not as a static background but as an active structural force that shapes investment viability, enterprise readiness, and institutional effectiveness. Figure 1 visually synthesises the 3LD-PE Framework by mapping the interconnections between institutional, financial, and enterprise-level dynamics.

The vertical arrows represent the core directional flow of influence from macro-level institutions to meso-level financial systems and ultimately to micro-level entrepreneurial firms, as well as feedback loops (A, A1, A2) that enable success at lower levels to inform and reinforce institutional reforms. The horizontal arrows linking adaptive instruments to each level indicate tailored interventions designed to overcome context-specific barriers, ecosystem development and policy advocacy strengthen institutional legitimacy; blended finance and tiered equity expand financial access; and pre-investment capability support equips informal firms for inclusion. This dynamic interplay underscores PE's potential as a multi-level developmental catalyst under conditions of adversity.

The following subsections examine each level of the 3LD-PE Framework in turn, analysing how PE operates within and across these domains and how feedback effects, adaptive mechanisms, and structural constraints shape inclusive entrepreneurial outcomes in African markets.

4.2 Micro-Level: Governance and Capability Transformation

At the micro-level, PE interventions target internal enterprise constraints, especially in governance and strategic capability. Agency Theory emphasises the role of PE in aligning the interests of investors and managers through board participation, performance-based incentives, and managerial oversight. The Resource-Based View (RBV) complements this by emphasising how PE introduces valuable, rare, inimitable, and non-substitutable (VRIN) resources, such as strategic talent, operational systems, and market access, that enhance firm competitiveness and scalability.

However, these benefits are often limited to formalised, high-growth firms that already possess the basic structures necessary to absorb PE interventions. The majority of African enterprises operate in informal, survivalist contexts marked by limited documentation, diffuse control, and volatile market conditions. In such settings, conventional PE practices fail to gain traction.

To address this exclusion, the framework recommends three adaptations. These are pre-investment capability development initiatives to enhance investment readiness, hybrid investor roles that combine capital provision with embedded business development support, and governance models that are context-sensitive and co-designed with entrepreneurs rather than imposed from outside. These interventions strengthen firm-level legitimacy and operational robustness, making enterprises more attractive to investors and enhancing their eligibility for financing at the meso level, as shown by the dynamic captured in feedback loop A1.

4.3 Meso-Level: Expanding Capital Access

At the meso level, PE addresses structural financial exclusion by offering long-term, risk-tolerant capital to enterprises that lack access to traditional banking services. Financial Constraint Theory explains the critical role of PE in easing credit rationing in contexts where high interest rates, collateral demands, and shallow financial markets prevent many businesses from securing funds. In this role, PE acts as an intermediary that links capital supply to entrepreneurial demand in underserved markets.

Nevertheless, PE capital tends to flow toward firms that meet standard thresholds for investability, i.e., strong governance, formal registration, and clear growth potential. This leaves out a vast segment of African enterprises that operate informally or at a subsistence level. As a result, PE's role in fostering inclusive access to finance remains limited.

To overcome this limitation, the framework advocates for the adoption of adaptive financial structures. Blended finance combines concessional and commercial capital to de-risk investments in informal or early-stage ventures. Revenue-based or tiered equity models link investor returns to business performance, rather than to rigid exit timelines, and are thus more appropriate in volatile markets. Engaging trusted local intermediaries helps mitigate information asymmetries and align investments with local entrepreneurial realities. These adaptations expand the investable universe and deepen PE's developmental reach, while simultaneously strengthening firm resilience and reinforcing institutional engagement, as captured in feedback loop A2.

4.4 Macro-Level: Institutional Engagement and Reform

At the macro level, PE can shape the broader regulatory and institutional landscape in which African enterprises operate. Institutional Theory frames PE firms as embedded actors that can influence rules, norms, and enforcement systems through advocacy, ecosystem development, and market-standard setting. When aligned with development finance institutions (DFIs) and impact-oriented mandates, PE has the potential to improve legal protections, regulatory transparency, and capital market depth.

In practice, however, PE's institutional engagement in Africa remains uneven. Foreign capital dominates the sector, and investor mandates often prioritise exit timelines, risk mitigation, or geopolitical interests over long-term ecosystem development. Regulatory fragmentation, elite capture, and weak enforcement mechanisms further inhibit systemic reform. As a result, PE tends to adapt to institutional constraints rather than actively challenge or transform them.

To enhance its institutional impact, PE must go beyond compliance to actively support inclusive reforms. These may include simplified tax structures, incentives for SME registration, and policy changes that enable broader participation in capital markets. PE firms should also invest in long-term ecosystem infrastructure such as professional services, exit pathways, and training institutions. Recognising and addressing the power asymmetries embedded in the regulatory system is crucial to ensuring that reforms benefit not only a narrow segment of elite entrepreneurs but also the broader population. When institutional engagement is inclusive and sustained, it closes the feedback loop between firm-level success and systemic transformation, as captured in loop A.

4.5 Interdependence, Adversity, and Feedback Loops

The 3LD-PE Framework emphasises the interdependence of micro-, meso-, and macro-level interventions, highlighting how developmental effects at one level reinforce or enable outcomes at others. Improved governance at the micro level enhances credibility and readiness for investment; expanded capital access at the meso level fuels Innovation and resilience, and stronger firms gain visibility and influence at the institutional level, contributing to ecosystem reform.

These interactions are not linear but recursive. Feedback loops dynamically link outcomes across levels, reinforcing positive change or exacerbating exclusion depending on the design of PE interventions. Loop A1 reflects how governance improvements increase financial viability. Loop A2 shows that enhanced access to capital drives resilience and credibility. Loop A captures the broader ecosystem effects of successful PE engagement and advocacy.

Adversity, manifested through informality, volatility, exclusion, and weak institutions, is not treated as background noise but as a structural force that mediates these dynamics. It influences risk profiles, enterprise behaviour, and policy responses. Adaptive instruments such as blended finance, trust-building, and capability mentoring function as translation mechanisms, enabling PE to engage productively with both formal and informal systems. By recognising and addressing these structural constraints, PE can become a more inclusive and context-sensitive driver of entrepreneurial transformation in Africa.

5. Empirical Propositions: Testing the Developmental Impact of PE in Africa

This section derives empirically testable propositions from the 3LD-PE Framework, enabling future researchers to explore the mechanisms through which PE fosters or limits entrepreneurial development in African contexts. These are derived from the theoretical basis as outlined in Section 3 and put into practice the multi-level framework developed in Section 4. Each proposition corresponds to a particular level (or intersection of levels) that the 3LD-PE Framework divides into (Figure 1) and builds on the dynamics with each level that is described in Sections 4.2 through 4.5. They are underpinned by a double-headed logic:(a) what PE enables under favourable conditions, and (b) how these benefits are mediated or constrained under adversity.

5.1 Proposition 1: Governance Gains Are Contingent on Formalisation and Absorptive Capacity

Proposition 1: PE investment is positively associated with improved governance outcomes in African enterprises, but this relationship is significantly moderated by the firm's pre-investment level of formalisation and absorptive capacity.

Rationale: Agency Theory suggests that PE can improve managerial accountability, board oversight, and financial transparency. However, these benefits tend to accrue only to firms with some existing governance structure. Informal or survivalist enterprises often lack the baseline structures to absorb governance reforms, limiting PE's influence in these cases. This proposition reflects micro-level dynamics (Section 4.2) and aligns with feedback loop A1 in Figure 1, where internal governance reform enhances financial eligibility.

5.2 Proposition 2: PE-Driven Capability Upgrading Skews Toward Scalable, Urban-Based Enterprises

Proposition 2: PE-backed firms show improvements in strategic capabilities and innovation performance when compared to non-PE-backed firms. However, these effects are concerted in scalable, urban-based ventures with high-tech or export potential.

Rationale: Drawing on the RBV, PE strengthens firm competitiveness by injecting VRIN resources. However, adversity (e.g., informality, limited infrastructure) impedes the transmission of these benefits to underserved areas. This suggests that PE can accelerate capability development only in contexts that meet specific structural prerequisites. This proposition reflects micro-level resource upgrading (Section 4.2) with implications for financial access at the meso level, reinforcing feedback into the broader system.

5.3 Proposition 3: Adaptive Financing Instruments Expand PE Reach to Informal and Underserved Ventures

Proposition 3: The use of adapted PE instruments (e.g., blended finance, revenue-based financing, local intermediary partnerships) increases the inclusion of informal and necessity-driven enterprises within PE portfolios.

Rationale: According to Financial Constraint Theory, traditional equity structures often exclude high-potential but low-compliance firms. In adversity, capital scarcity and lack of documentation block access. Emerging financing innovations offer a pathway to expand PE's reach. This proposition reflects meso-level interventions (Section 4.3) and is directly linked to the adaptive instruments shown in Figure 1, which are designed to bridge informality and expand inclusion.

5.4 Proposition 4: Institutional Engagement by PE Varies with Capital Origin and Investor Mandate

Proposition 4: The extent and developmental quality of PE's institutional engagement (e.g., regulatory advocacy, standard setting) is influenced by the origin of capital (local vs. foreign) and the investor's mandate (commercial vs. impact-driven).

Rationale: Institutional Theory views firms as embedded actors that are shaped by and shape their regulatory context. However, PE's institutional activism is inconsistent. DFIs may promote reform, while commercial PE may adapt to existing norms. Capital origin also affects alignment with local development goals. This proposition reflects macro-level dynamics (Section 4.4) and aligns with feedback loop A in Figure 1, where institutional engagement and reform are both shaped by and reinforce the legitimacy of PE.

5.5 Proposition 5: PE-Backed Firms Demonstrate Greater Resilience During Adverse Shocks

Proposition 5: Firms backed by PE exhibit greater resilience during macroeconomic or sector-specific shocks compared to non-PE-backed firms, particularly in terms of liquidity preservation, employment retention, and operational continuity.

Rationale: Adversity, whether from pandemics, political instability, or climate disruptions, exposes entrepreneurial fragility. The literature suggests PE enhances resilience through capital buffers, scenario planning, and supply chain reconfiguration. This proposition reflects a cross-level dynamic (Section 4.5), integrating the effects of micro-level capacity, meso-level financing, and macro-level stability. It aligns with feedback loops A1, A2, and A in Figure 1.

5.6 Synthesis: The Integrated Developmental Role of Private Equity

The five propositions advance the PE and entrepreneurship literature by incorporating contingency and contextuality into the analysis. They develop a conceptual framework that can be empirically tested using mixed methods, including panel data analysis, case studies, and comparative impact assessments. The ensemble of propositions takes the debate into new turf beyond binary narratives (PE is good or bad) toward a more contextually grounded understanding of when, how, and for whom PE catalyses developmental entrepreneurship in Africa.

5.7 Operational Mapping of Propositions to PE Mechanisms, Theoretical Lenses, and Developmental Outcomes

The propositions outlined above synthesise the developmental mechanisms of PE across four theoretical lenses and highlight key points of intervention as per Table 1 below.

Table 1: Operational Mapping of PE Propositions to Theoretical Lenses, Developmental Mechanisms, and Measurement Indicators

Proposition	3LD-PE Level	PE Mechanism	Theoretical Lens	Intended Developmental Outcome	Suggested Measurement Indicators & Beneficiaries
P1	Micro	Governance Oversight	Agency Theory	Improved transparency, board structure, and accountability	• Board constitution • Frequency of board meetings • Audit compliance Beneficiaries: Formal SMEs, mid-sized urban firms
P2	Micro	Strategic Resource Transfer	Resource-Based View (RBV)	Enhanced managerial capabilities, innovation, and market reach	• Number of new products/services • Executive turnover • Market expansion Beneficiaries: Urban tech-enabled firms, growth-oriented ventures
P3	Meso	Capital Injection (via Adaptive Financing Tools)	Financial Constraint Theory	Increased access to long-term capital, investment inclusion	• Equity/debt ratio change • Investment size • SME bankability metrics Beneficiaries: Formal startups, women/youth-led ventures with documentation
P4	Macro	Institutional Bridging & Advocacy	Institutional Theory	Policy reform, ecosystem development, and regulatory participation	• Policy changes influenced • Regulatory consultation presence • Legal environment scores Beneficiaries: Firms in DFI-supported countries, formalised SMEs
P5	Cross-Level	Integrated Resilience & Inclusion Strategy	Cross-Theoretical	Increased firm resilience, gender and geographic inclusion	• ESG scorecards • Diversity of investees • Post-crisis survival rates Beneficiaries: Women entrepreneurs, rural enterprises, and underserved firms

Importantly, they provide a structured foundation for future empirical research that can assess not only whether PE works, but also for whom and under what conditions. To address distributional concerns raised in the literature, future research should consider how these effects vary across different firm types (formal vs. informal), ownership structures (e.g., women-led or youth-led enterprises), and geographical contexts (urban vs. rural). Empirical testing may draw on mixed-methods approaches, including matched firm-level datasets, comparative case studies, and regulatory impact analyses. By aligning theory, propositions, and context-sensitive outcomes, this framework advances a more inclusive and empirically grounded research agenda for evaluating the developmental impact of PE in Africa.

6. Conclusion and Policy Implications

6.1 Summary of Key Findings

This paper has proposed the Three-Level Developmental Private Equity (3LD-PE) Framework to explain how PE can catalyse or constrain entrepreneurial transformation in Africa under conditions of institutional fragility, financial exclusion, and enterprise informality. By integrating four foundational theories, the framework conceptualises PE as a multi-level actor operating simultaneously at the firm (micro), financial system (meso), and institutional (macro) levels.

The framework advances current scholarship by moving beyond celebratory narratives or binary critiques of PE, instead offering a grounded, multi-faceted view of PE's developmental potential. It explicitly centres adversity as a structural force shaping both opportunities and limitations and identifies the feedback loops and asymmetries that mediate PE's impact across Africa's diverse entrepreneurial ecosystems.

From this framework, five empirically testable propositions have been developed. These propositions address firm-level governance and capability upgrading, meso-level capital access and adaptation, and macro-level institutional engagement. Each proposition is grounded in the theoretical synthesis and designed to be tested across different enterprise types and policy environments. Collectively, they provide a foundation for future empirical work to evaluate not only whether PE contributes to development, but also who benefits, under what conditions, and with what distributional outcomes.

6.2 Policy Implications

The findings of this study have important implications for policymakers, development finance institutions, fund managers, and ecosystem enablers who seek to make PE a more inclusive and context-responsive development instrument in Africa.

At the micro level, governments and donors should prioritise investment readiness programmes that help informal or survivalist enterprises meet the minimum governance and financial reporting standards required by PE investors. These may include subsidised governance audits, mentorship programmes, or targeted support for women- and youth-led enterprises. Embedding capability development within PE interventions can increase absorptive capacity and reduce the exclusion of high-potential but underserved firms.

At the meso level, financial regulators and DFIs should develop blended finance vehicles that combine concessional and commercial capital to incentivise PE investment in less formalised sectors. Innovative instruments such as revenue-based finance or tiered equity structures can lower entry barriers and align investor incentives with the unpredictable growth trajectories of firms in informal markets. Supporting the growth of domestic PE funds through co-investment facilities or anchor commitments can further reduce dependency on foreign capital and improve alignment with local development goals.

At the macro level, policy reforms should focus on improving regulatory coherence, reducing bureaucratic red tape, and enhancing local capital market infrastructure to create viable exit options for investors. Incentives such as tax relief for long-hold PE investments, inclusive listing rules for SMEs, and the establishment of regional secondary markets can enhance institutional depth and long-term investor confidence. Critically, ecosystem coordination must also address power asymmetries, ensuring that fund structures, mandates, and governance frameworks reflect not only investor interests but also local developmental priorities.

Together, these policy interventions can help reposition PE from a catalyst for selective growth into a broader engine of inclusive economic transformation.

6.3 Limitations and Directions for Future Research

As a conceptual contribution, this study does not empirically test the 3LD-PE Framework; instead, it offers a theoretical synthesis and a set of propositions for future investigation. While the framework integrates multiple theories and draws on extensive literature to contextualise PE's developmental role, it does not capture the full heterogeneity of African markets, nor the variation in PE mandates and fund structures across countries and sectors.

Future research should test the framework using mixed-methods approaches across different contexts, disaggregating outcomes by firm type (e.g., formal vs. informal), ownership (e.g., gender- or youth-led firms), and geography (e.g., urban vs. rural ecosystems). Longitudinal studies would also be valuable in tracking the systemic effects of PE engagement over time, particularly in relation to institutional reforms and the development of capital markets. Expanding the model to consider the role of domestic investors and community-based financing intermediaries may further enhance its explanatory power.

6.4 Final Remarks

As Africa's entrepreneurial ecosystems continue to evolve, PE must adapt not only its capital instruments but also its engagement models to the realities of informal markets, institutional volatility, and social exclusion. The 3LD-PE Framework offers a lens through which these dynamics can be better understood, guided, and evaluated. Future research and policy experimentation should continue to test and refine these mechanisms to ensure that PE scales not only financial returns but also inclusive, sustainable development outcomes across the continent.

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