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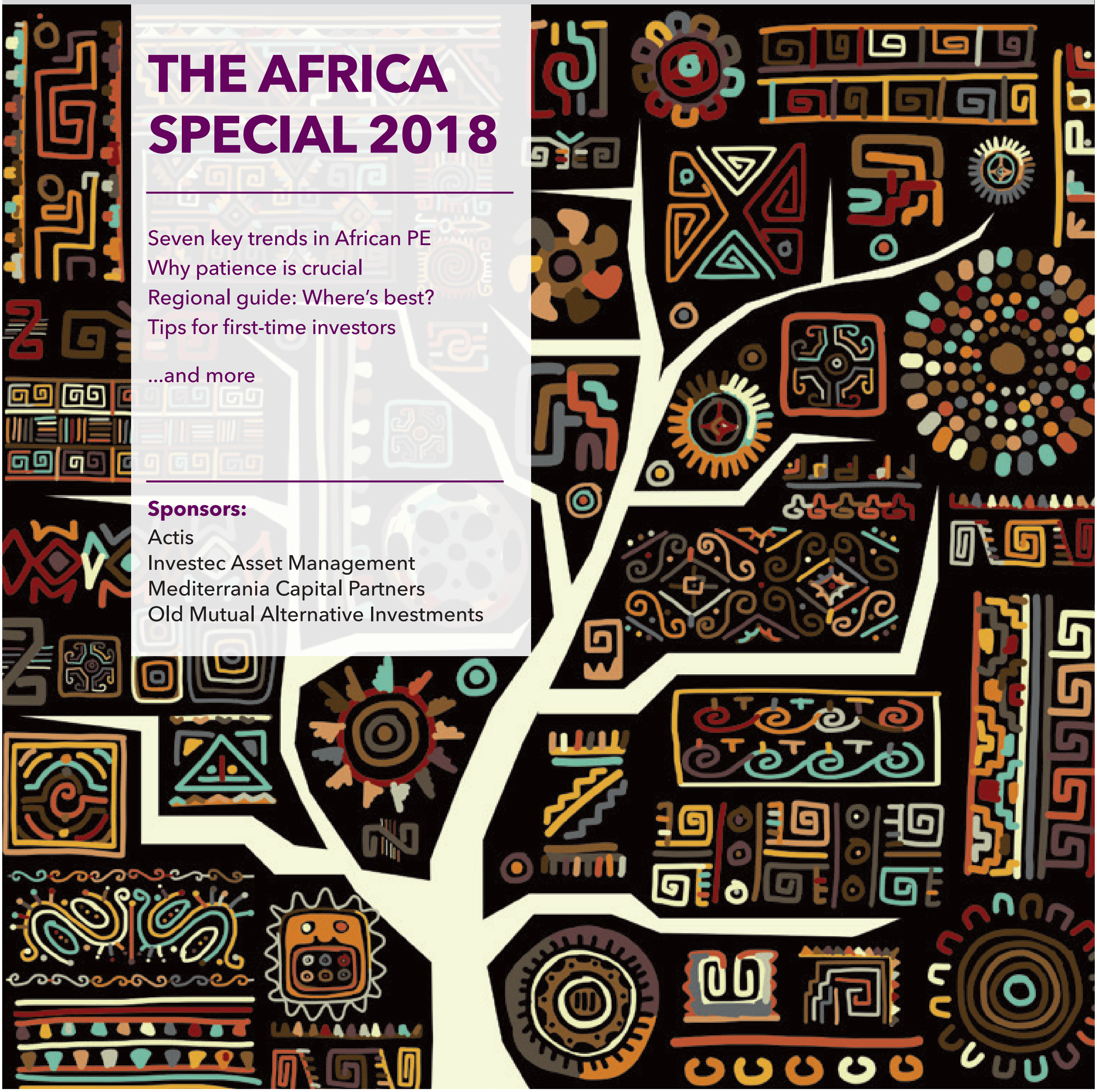

THE AFRICA SPECIAL 2018

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Through the macro lens

GRAEME KERR
EDITOR'S LETTER

Just how much have Africa's macro woes hit the private equity industry? There's little doubt currency devaluations in the major markets and political uncertainty have damaged the investment climate.

A survey published by the African Private Equity and Venture Capital Association last November found 75 percent of GPs believed currency risk had a detrimental effect on their realised investments and 67 percent considered political risk management when constructing their portfolios.

But talk to any of the GPs investing in Africa and you soon learn that it is possible to make solid returns if you have the patience and the local know-how to build a business, as we outline on p. 4. Currency fluctuations come across as one of the key threats to returns but even those can be weathered if you have pricing power and market share.

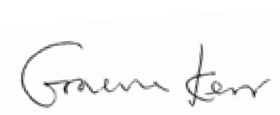
The theme of how to build regional champions comes across strongly in our keynote interviews where we talk to some of the leading figures in African private equity.

Actis's global head of private equity Natalie Kolbe and head of Africa Rick Phillips discuss how investors can find openings in both good times and bad (p. 9). Paul Boynton, the CEO of Old Mutual Alternative Investments, says the creation of a new free trade area could prove a boon for South Africa (p. 18) and Albert Alsina, founder and CEO of North Africa-specialist Mediterrania Capital, explains how diversification is the key to managing the macro risks (p. 23). Meanwhile, Peter Baird of Investec Asset Management explains why he believes the stage is now set for attractive private equity investments and – importantly – exits (p. 29).

So where is best to invest? We ask some leading LPs for their tips on where to commit capital in the continent on p. 12, and on p. 14 we present our annual regional guide which scours the continent for the countries with the most attractive private equity prospects. Kenya, boosted by strong GDP growth and a stable currency, is fast emerging as one of the most promising markets, helped by its more stable political outlook as we detail on p. 21. And countries as diverse as Algeria, Ivory Coast and Ethiopia also have strong potential, according to market participants.

No one is claiming that investing in Africa is anything less than challenging. Local know-how is key, ESG is an important consideration (p. 26) and the macro environment can be brutal, but solid returns are possible if you know where to look in this most diverse of continents.

Enjoy the supplement



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PERFORMANCE

In search of a solid 3x

From rising to falling star, Africa rewards those with discipline, patience and the skills to build a market leader, writes Nathan Williams

When the world was struggling to emerge from the financial crisis, Africa was a beacon of light. In 2013, with Europe in recession, gross domestic product growth in sub-Saharan Africa peaked at over 5 percent. In North Africa the picture was similarly rosy, with Egypt, Tunisia and Morocco all recording growth between 4 and 9 percent. Africa was the rising economic star, coming second in EY's 2014 survey of the most attractive global investment destinations.

In a separate report that year the advisory firm confidently stated that the "growth momentum will continue". Even the rapid fall in commodities prices through 2015 didn't change the narrative much. In January 2016 the IMF forecast sub-Saharan Africa growth for the year at 4 percent and said it expected Nigeria – one of the engines of performance – to exceed that.

But then the reality. In 2016 growth across the region fell back to a little over 1 percent and Nigeria and Angola – two of the three largest economies in sub-Saharan Africa – plunged into recession. As a result, 2016 became the worst year of growth for the continent in 20 years. As Florent de Boissieu, a principal at sub-Saharan private equity firm Adenia Partners puts it: "Some of the stars have fallen. We still see strong interest from LPs but Africa has been through some turbulent times over the last three years. Certain countries such as Nigeria are now regarded as much more risky."

The commodities rout continued through 2016 and had a profound impact on growth as well as some private equity investment strategies. Africa-focused private equity firm Helios Investment Partners cancelled a $300 million oil and gas sidecar it had planned for the continent. LP interest fell away and hasn't picked up to its old levels since, says Holger Rossbach, a senior investment director at Cambridge Associates. "After the financial crisis investors were seeking additional pockets of opportunities globally and the interest level in Africa then was at its highest point."

De Boissieu says: "It's never been easy to raise funds in Africa compared to other countries worldwide, but it is proving to be more challenging at the moment." Some funds have dropped out of a market they had rushed into only a few years ago, while others are struggling. "Many funds have been unable to deliver the outperformance lined to the risk premium expected from LPs," he adds.

The numbers bear this out. The African Private Equity and Venture Capital performance benchmark produced by Cambridge Associates shows a five-year average IRR generated by 51 Africa-focused funds of 2.85 percent, which lags a long way behind the advisory firm's US private equity performance indicators, as well as all MSCI indexes.

Investors say the slowdown has changed dealmaking in Africa. "In this new atmosphere we need to be extremely disciplined about picking the right opportunities. Previously some players thought private equity in Africa was about capital deployment, but this is absolutely the wrong way to think about private equity, especially in Africa," says de Boissieu. "Some firms selected bad investments thinking that to be number three or four in the market will still get them a return, but this is wrong."

He says the key to investing in Africa is market position. "You need to be the leader. When you are the leader you have pricing power, you can out-invest your competitor, you can buy better, you can execute better."

Rossbach echoes de Boissieu, saying expectations around performance have been too high. "It took African managers longer to implement changes and drive value creation in the underlying companies than they originally thought when they made these investments. Reaching those target multiples took longer," he says.

And the performance numbers suggest investors need to be more patient, with a nine-year return clocking in at 5.39 percent. "Exit markets are about timing and

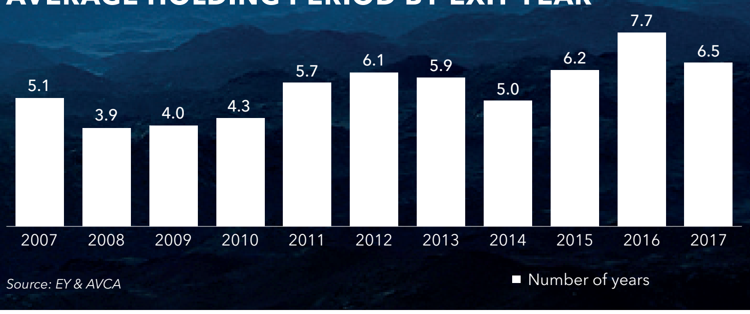
UNCERTAIN RETURNS

Private equity and venture capital returns over 10 years

Notes: The index is a horizon calculation based on data from 51 Africa and private equity and venture capital funds, including fully liquidated partnerships, formed between 1995 and 2015. Private indexes are pooled horizon IRR calculations, net of fees, expenses and carried interest.

Source: Africa Private Equity & Venture Capital Index, Cambridge Associates

AVERAGE HOLDING PERIOD BY EXIT YEAR



Source: EY & AVCA

in Africa we have seen periods of time where companies were ready for an exit but the overall market conditions meant you couldn't get the EBITDA multiple so managers had to wait another two or three years," Rossbach says. From 2008 to 2016 holding periods went from less than four years to nearly eight years.

Patience is critical. Private equity investors say there are opportunities to build market leaders and secure strong returns in a way unique to Africa – by creating a company from scratch. "Because economies are less well formed in sub-Saharan Africa you have white space where there is a need to build and create a business because no company is meeting a certain need," says Alykhan Nathoo, a partner at Helios Investment Partners. "We've done this in telecom towers and student accommodation. In sub-Saharan more than in north Africa as an investor you need to think about the creation of a business."

The key, he says, "is not finding the white space. The key is finding the right team to build a business to fill that space".

GO MODULAR

Nathoo says this 'white space' opportunity necessitates a particular style of capital investment. "When building a business from scratch the key is to find a business model that's proved itself elsewhere and then take a modular investment approach. What that means is you don't put all the capital in upfront. For example on the telecoms towers business (in 2009 Helios created Helios Towers, one of Africa's largest telecommunications infrastructure businesses) we invested in a modular fashion ie, $10 million first, then when concept was proven another $10 million and then when further milestones were hit another $10 million. This leads to a feedback loop that helps fine-tune the parameters for the next tranche of investment."

While strong return stories exist, investors caution even these can be threatened by an unstable macro environment, especially the currency fluctuations of recent years. "Currency is one of the key killers," says Rossbach. "Entry and exit valuations in a number of African markets are very competitive and the macro environment is strong but currency fluctuations impede deals."

Nathoo says "macro stability in terms of currency stability is an impediment – necessitating the need to think very carefully about investing in businesses which have some explicit or implicit currency hedge to protect against this volatility."

Size, de Boissieu suggests, is one of these hedges. "We have experienced tremendous depreciation in some countries. Those who can survive have to be able to pass part of the increase to the customer, and this depends on the pricing power and on the market share you have."

In such a complex and varied investment landscape, and with GDP growth across Africa not forecast to rise much above 3 percent in the coming years, what does good performance look like? "We typically look at deals with strongly covered downside and cash-on-cash multiple of 3x or so," says de Boissieu, who warns that promises of blockbuster returns come with a sting in the tail: "When I see people talking 5x or 10x money I don't understand where they see this in Africa and I am worried about the level of risk they are accepting." ■

OVERVIEW

Seven key trends in African PE

The private equity industry is finding its feet again in the continent after a series of macro shocks. Graeme Kerr looks at what's driving the market

While it's a little too early to talk of Africa Rising again, there are definite signs that the continent's private equity industry is in a more confident frame of mind.

Take South Africa, the traditional powerhouse of the African private equity industry, with more than 40 percent of all the exits in the last decade.

When private equity executives gathered for the Southern Africa Venture Capital and Private Equity Association's 2018 Conference in February, the mood was glum. "There was a lot of pessimism and negativity," says SAVCA's CEO Tanya van Lill.

Six months on, there's a clear sense that South Africa is starting to put recent political and economic uncertainties behind it. "The business confidence indicators are starting to pick up," says van Lill. "There's a definite sense that the private equity industry is moving in the right direction."

It's a similar story elsewhere with GPs optimistic the continent is finally emerging from its recent setbacks. As they look to the future, what are the factors likely to set the direction of the African buyout industry over the coming years? *Private Equity International* sifted through the fundraising and deal data and talked to the major players to find out.

1 MACRO STILL MATTERS

How important are macro factors to the growth of the private equity industry in Africa? Very. A survey published in November 2017 by the African Private Equity and Venture Capital Association found two-thirds of general partners consider political risk management when constructing their portfolios and 90 percent perceive currency risk as being either important or very important.

"Overall the private equity landscape is looking very different from four years ago when there was all this macro momentum, and everyone was caught up in the narrative of the expanding middle class and the idea that topline economic growth would continue for some time," says Jeff Schlapinski, director of research at EMPEA.

The Africa Rising narrative came to an abrupt halt with the slowdown in commodity prices since 2015, currency devaluations in Egypt, Nigeria and South Africa – private equity's three leading African markets – and political upheaval in key nations.

"There's been a lot more stress the subsequent years. Fund managers have been put to the test across the continent to shore up their portfolio companies, build some kind of resiliency and really create value so they can bring companies along to exit," says Schlapinski.

Unsurprisingly, perhaps, most GPs (60 percent) named currency and commodity price volatility in the AVCA survey as the macro factors that have had the largest impact on their portfolios over the past three years.

2 FUNDRAISING HAS STALLED

Talk to any of the major players in Africa and it's clear the fundraising environment has been one of the major casualties of the macro upheavals. The four Africa-focused private equity funds that closed in 2017 raised just $500 million, down from $1.95 billion in 2016 and

$4.41 billion in 2015, when 14 funds closed.

Half of the funds failed to reach their targets in 2017 and the average fund size fell to $125 million from $315 million at the recent peak in 2015.

But there are grounds for optimism. One of the leading firms, Development Partners International, went back into market in May seeking $800 million for its third fund and industry sources expect at least one of the other big players to begin a new fundraise by the end of the year.

Meanwhile, North Africa specialist Mediterrania Capital Partners raced to a first close of $103 million on its third fund after just six months in November 2017, suggesting there remains an appetite for Africa.

3 INTRA-AFRICAN TRADE IS SET TO GROW

One of the most exciting developments, according to Paul Boynton, the CEO of Old Mutual Alternative Investments, is the creation of a new free trade area. South Africa became the latest country to signal its intention to join the African Continental Free Trade Agreement.

"The opportunity for African countries to trade among themselves is enormous," Boynton says. "Intra-African trade is about 15 percent compared to within Europe where cross-border trade is 40-odd percent."

So far almost 50 countries have signed the initial framework and six have ratified the deal. The agreement takes effect once it has been ratified by at least 22 African nations.

> ***The business confidence indicators are starting to pick up. There's a definite sense that the private equity industry is moving in the right direction***
>
> **Tanya van Lill**

4 CHINA IS BECOMING A KEY PLAYER

One of the more intriguing developments in African private equity is the rise of Chinese investment in infrastructure projects. "Although Chinese investment in Africa is relatively small at about $40 billion in 2016 (around 2 percent of the continent's gross domestic product), it has grown to 5 percent of total foreign direct investment in Africa in 2016 from just 0.2 percent in 2003," Moody's said in a recent report.

"If this growth persists at half of the current rates, China's investment position would reach $100 billion by 2020, or around 4 percent of African GDP," Moody's estimated.

Seventy percent of Chinese investment between 2000 and 2015 was focused on infrastructure, which could help address the continent's deficit in this area, especially in energy and transport, and boost economic growth.

However, Africa's rising reliance on Chinese funds – the country's banks accounted for 80 percent of loans received by African governments between 2010 and 2015 – leaves the continent exposed to political risks. "Future investment in Africa will be significantly affected by any policy changes in China," the report's authors warned.

5 GROWING RECOGNITION OF GOOD GOVERNANCE

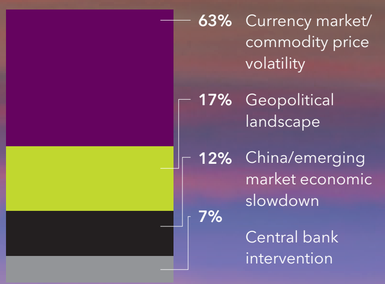
African investments have always had a focus on environmental, social and governance issues because of the crucial role played by development finance institutions in drawing up standards. The message seems to be getting through to the owners of businesses, says Johannesburg-based Natalie Kolbe, the head of private equity at Actis.

"One of the big developments over the last few years is a growing desire for »

RISK FACTORS

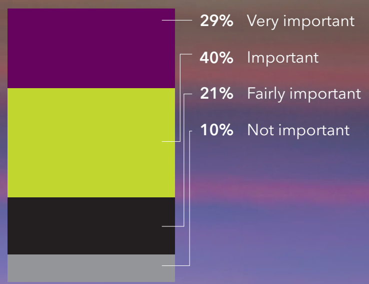
Two-thirds of GPs consider political risk management when constructing portfolios and 90 percent say currency risk is either important or very important

Which macro factor had the biggest impact on your portfolio over the last three years?



Source:AVCA

Beyond a basic need for stability, how important is political risk to your firm?



Source:AVCA

» good governance among businesses in Africa," she says. "There is a growing recognition that strong governance is good for companies and industries. We used to have some difficult conversations with business owners and it used to be quite a struggle to find deals where we could align on governance issues; now, people really understand the importance of this and actively ask us how they can improve."

6 THE RISE OF SECONDARY BUYOUTS

Exit activity has remained resilient despite the challenging macro environment, thanks partly to the growing number of sales of portfolio companies to private equity and other financial buyers. Secondary buyouts are now the most common route with 37 percent of all exits in 2017, up from 16 percent in 2015 and just 8 percent in 2008. "We have seen a great increase in the number of large international funds buying assets from smaller PE firms through secondary transactions as generally these assets are of high quality and can be easily taken to the next level," says Albert Alsina, CEO of Mediterrania Capital Partners, a North African specialist.

7 DEAL TERMS ARE BECOMING MORE FAVOURABLE

One advantage of the challenging economic times is that it has made deal terms more attractive, says Peter Baird, head of private equity at Investec Asset Management. Investors who are still in the market are "able to negotiate more favourable terms".

"I think it's possible to find great businesses at lower valuations in African countries," Baird adds.

Holger Rossbach, a senior investment director at Cambridge Associates, agrees: "Businesses have more imperfections and there is more untapped value in many of the underlying assets than in the US or Europe. There is more low-hanging fruit." ■

DEALFLOW

Looking beyond the headlines

After a difficult macro period for some of Africa's markets, there are signs of greater stability in key economies. Actis's Natalie Kolbe and Rick Phillips discuss how investors can find openings in both good times and bad

Following the highs of the period leading up to 2015, when the 'Africa Rising' narrative was at its peak, the last two years have been rather more challenging for some of Africa's private equity investors. The region's largest markets experienced volatility: both Egypt and Nigeria have seen significant currency devaluations, while South Africa faced a political crisis that resulted in the ousting of President Zuma.

Actis has been one of the most active investors in Africa. The firm has a heritage tracing back 70 years on the ground across the continent and has committed $4.5 billion since spinning out of CDC 15 years ago. We spoke to two Actis partners Natalie Kolbe, who is global head of private equity based in Johannesburg, and head of Africa Rick Phillips about how to source high quality investments and generate value in, sometimes, unpredictable markets.

Q How has recent volatility in some African nations affected private equity dealflow?

Natalie Kolbe: I'd say it did affect dealflow in certain instances, although we're seeing greater stability now as currencies have found a level. In West Africa, in particular, there was a period where deals were paused. When you have such a significant currency devaluation, such as in Nigeria, investors and business owners need a little time to recalibrate their expectations. If you are a business owner, for example, and the currency devalues by 50 percent, you may have lost half your wealth overnight.

That meant that conversations we had been having in Nigeria stopped for a period – we kept talking but we put our pens down until the currency stabilised. Meanwhile, businesses needed a little time to recover and close the perceived gap.

> ***When things go wrong, it's usually less about the business itself and much more about the call on the person or people involved***
>
> Natalie Kolbe

In South Africa, the story was a little different. People didn't move away from deals completely, they simply wanted to wait and see the outcome of the political situation. It just meant deals were on hold for a while – owners saw little point in sending sales memoranda six months ahead of a political change.

Q To what extent can you continue to invest under those circumstances?

Rick Phillips: In the event of a significant currency devaluation, as a prudent investor, you do have to reassess. Yet more generally, our view is that long-term investors should continue to invest through cycles and political events. In South Africa in 2017, for example, we continued to deploy capital – we acquired distance learning businesses Management College of Southern Africa and the Regent Business School through our Honoris United Universities platform. Our long-term strategy with Honoris is to create a pan-African tertiary education business and expansion into Anglophone markets is a key element of this.

Our experience is that political events may come and go – we've seen plenty in our time – but that in certain sectors in Africa, demand continues to grow both as incomes increase and for secular reasons. This is true for university education, both among students and employers. In »

» many African countries, fewer than 10 percent of 18-23-year-olds are enrolled in tertiary education.

Q You mention education. What other sectors do you see as being attractive across Africa?

RP: We back sectors in which the drivers for growth are underpinned by secular trends. So, education is one such sector. Financial services and healthcare are two others. In financial services, there is low banking penetration among local populations, but changing technology is making the security and convenience of electronic payments available even to the unbanked population. In healthcare, increasing urbanisation is improving access to healthcare providers, and increasing connectivity is improving health awareness. Secular changes in demographics, lifestyles and diet are driving growth across Africa's healthcare sector.

NK: If you focus on specific sectors that benefit from secular trends, where market penetration is low, you can look beyond the headlines and continue to invest through cycles. That doesn't mean we are oblivious to issues arising in our markets, but it does mean we can cut through noise and look to the long term.

Q In your experience, does that mean there are sectors to avoid?

NK: We prefer to be protected from external events that are beyond our control and that fundamentally affect companies in a given sector. So, for example, we won't invest in oil & gas and mining, as success here is too dependent on commodity prices and agriculture is too dependent on weather.

RP: My experience of investing in Africa began 25 years ago when I moved to

PAYMENTS IN THE DIGITAL AGE

By the time Actis successfully sold Emerging Markets Payments in 2016, its pan-regional payments business had grown from a single office in Cairo to hubs across Africa and the Middle East operating in over 40 countries, providing services to 130 banks and 30,000 retailers and processing more than six transactions a second. Actis had to surmount a number of macro challenges including currency devaluations in key markets and the Arab Spring, says Rick Phillips.

Q What do you need to develop a pan-Africa business?

Creating pan-regional businesses of scale from a single country is difficult. You have to have a clear sector vision of what you want to create and you have to create the right culture that enables individuals spread over different countries to work together. You have to have a local presence to understand nuances and different market dynamics and it helps to have past experience of building similar businesses in similar markets.

Q EMP grew out of a small Cairo-based card processor that you acquired in 2010. How did you cope with the Arab Spring uprisings and currency devaluations?

We looked past these short-term events because we had a long-term vision for EMP. We wanted to build a large, top quality payments business that operated in a number of vertical spaces – we knew this would be attractive to buyers.

Kampala and I have learned this the hard way. There are sectors to avoid, you have to draw lessons from that kind of experience – it makes you better at reading and assessing risk before you invest and at managing it during the investment. Focusing on specific sectors with high growth potential that are less subject to external shocks is one of the ways of mitigating risk in what can be quite a volatile region.

Q So what would you say is the most important lesson drawn from these kinds of experience?

NK: I think we'd both agree that, when things go wrong, it's usually less about the business itself and much more about the call on the person or people involved. This clearly is not unique to Africa. You have to be very circumspect about who you invest with and our local presence is key to knowing who we're dealing with – if there is any hint of misalignment between us and the team we are looking to invest with, we'll walk away.

If a business underperforms and you are aligned with the management team, you can work with that – the partnership can bear the strain and you can work together to improve the business. If it underperforms and there is misalignment, a decent investment can quickly become a poor one; the downward spiral can be very fast indeed.

RP: I'd also add that, with the right people as partners, volatility can provide attractive opportunities for investors.

Q Can you give an example of volatility creating opportunity?

RP: CIB in Egypt is a good example of this. We invested just after the global financial crisis in 2009. It was Egypt's leading bank and had a solid commercial loans business. We saw an opportunity for CIB to expand,

"With the right people as partners, volatility can provide attractive opportunities for investors

Rick Phillips

using its excellent brand in the consumer space, particularly as bank penetration was low in Egypt. Eighteen months in, with CIB ahead of budget, the Arab Spring erupted and Egypt underwent a revolution.

The company and the market as a whole went backwards, but we'd invested with good people and we decided to throw our full weight behind them. We revisited our original business plan and could see that the secular trends of the move towards electronic payments and increased demand for financial services among consumers remained robust, even as the corporate sector was under pressure. So we doubled down on our plans to build up the consumer side of the business. It took three years of rebuilding, but CIB increased its market share, doubled its profits and delivered a strong return on our investment – we managed this because we kept our eye on the long-term goal rather than being distracted by external events.

Q And finally, what about exits in Africa? To what extent are we seeing routes develop?

NK: The main exit route continues to be trade sales. There is still appetite among international acquirers, with interest growing particularly among Chinese, Indian and Japanese corporates. Local strategics are also important as regional consolidation and growth continues. As the private equity market has matured in Africa, we see a handful of players on the continent that are actively acquiring in our exit size bracket. And IPOs are clearly becoming more important and viable as exchanges develop. We've completed a few IPOs over recent years – Edita, IDH, Alexander Forbes and Umeme, for example – and there are a few of our current portfolio companies that may look to public markets listings in the future. ■

INVESTING IN AFRICA

LPs on success, risk and ‘thinking micro’

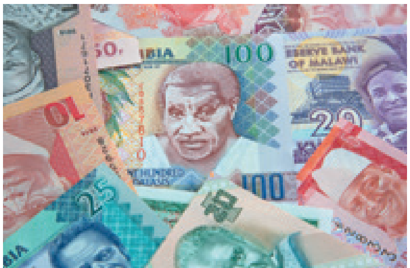
With many global investors yet to set foot in Africa, we asked some leading LPs for their tips on where to commit capital. By Graeme Kerr

What’s your advice for first-time investors in Africa?

Charles Groom: “Expect to commit resources or spend substantial time on the ground to develop local relationships, best practices and to help your investees drive their growth. Consider how to mitigate against currency risks and to manage political risks, but think and act micro.”

Matthew Hunt: “The key ingredients to a successful African private equity recipe are local presence and execution. A first-time investor should ensure that its GP has an investment strategy and team that is well suited to its markets. Most important of all, it is crucial to choose a GP that has boots on the ground so that it can follow through on its plans with hands-on execution.”

Stephen O’Neill: “Africa is no different from any other region – you need to do your homework before committing capital. It is important to construct a detailed map of the investment opportunities and to analyse the capabilities of the GPs. Africa is a unique blend of 54 countries with profound heterogeneity and risks that are different from other places we operate. Our top-down process assesses around 40 factors which we incorporate into algorithms that help us to quantify and mitigate these risks.”



What’s been your most successful investment in Africa?

CG: “From a commercial perspective African Development Partners I (vintage 2008), managed by Development Partners International has performed very strongly. In early 2017, DPI concluded their fourth exit from the fund, from CAL Bank, one of Ghana’s leading independent banks. CAL Bank reported profit after tax growth of 77 per cent per annum from 2011 to 2015.”

MH: “In 2010, we invested in Vivo Energy, alongside one of our GPs. At that time, we concluded that the company offered multiple value enhancement options and was linked to attractive macro growth drivers. Earlier this year, Vivo Energy was listed through an IPO in London, making it the first UK listed entity with operations wholly within Africa and was the largest African IPO on the LSE since 2005.”

SO’N: “The most successful transactions have been in the mobile sector. More broadly, we have successfully committed to regional funds, and work with those GPs to deploy capital to the mid-market. In addition, our market position has provided a compelling pipeline of co-investments and we are optimistic that these may ultimately be our most successful transactions.”

What are the most interesting trends in the African market?

CG: “For generalists, to capture the opportunities arising from building regional businesses across fragmented markets. For the emerging set of venture capital fund managers, the ability to identify and grow high calibre and motivated talent in African cities.”

MH: “I think that digitisation will play a catalytic role in Africa in the coming years and allow the continent to leapfrog other regions in certain sectors through the use of mobilising technologies. Digitisation has already revolutionised the financial services space, in particular retail payments system and the payments infrastructure. Online retail is still nascent in Africa, but there are already unique and attractive applications across the consumer goods spectrum including in healthcare and education.”

SO’N: “The region is evolving in terms of the range of PE strategies that GPs are credibly pursuing and increasingly includes sector strategies (eg, financial services, consumer and healthcare), credit-related strategies, infrastructure-related strategies, and even an emerging venture capital community. As in a number of other regions, we have been most focused on some of the sectoral funds.”

How does Africa fit into a global portfolio?

CG: "Aside from the obvious benefit of diversification, investing in Africa has the potential to deliver strong returns through careful selection of management teams and partners to invest alongside. Successful investments will also often deliver significant development impact."

MH: "African PE is predominantly a growth opportunity and is unlevered, in contrast to more developed markets which tend to have higher leverage levels. In addition, Africa offers a unique geographical diversification to a portfolio of developed and emerging market exposures. African listed markets have less of a correlation with developed markets than emerging markets do. This is partly due to growth being domestically led, low debt levels and the relatively low levels of foreign ownership."

SO'N: "Our approach is more as an opportunistic investor than as an allocator. As such, we have no bucket for Africa. We evaluate opportunities on a risk-adjusted basis against those elsewhere. We have had consistent and increasing exposure to Africa over the last few years. It yields compelling and differentiated opportunities, but has complexity and a range of unique risks."

How do returns in Africa compare with those in the rest of the world?

CG: "Whilst individual transactions have exhibited strong returns, there is a large dispersion of returns in the market as a whole and financial performance has been hurt by significant currency depreciation more recently. Furthermore, returns in Africa suffer from a lack of leverage during a period of all-time low costs of debt."

MH: "Realised returns have not yet lived up to the expectations, driven in part by the recent macroeconomic challenges in Africa, in particular currency depreciation and lower commodity prices. However, the last 12 months have seen rising commodity prices, a changing political climate and more stable currency regimes which should all serve to create a more positive environment for exits."

SO'N: "Top quartile private equity returns in Africa compare well with those for many other regions and can contribute usefully to a global strategy designed to optimise both diversification and positioning relative to the efficient frontier of optimised risk and reward."

What's the key risk of investing in Africa?

CG: "Currency. Then execution risk."

MH: "Currency depreciation remains a significant risk in Africa, as has been witnessed with the recent devaluations of the Nigerian naira and Egyptian pound. We have seen GPs partially protect their investment through deal structuring as well as through thoughtful portfolio construction techniques. This is a welcome development, but ultimately the best defence is diversification."

SO'N: "Similar to other regions, in Africa it is important to assess the legal, regulatory, and political framework, as well as macroeconomic and currency conditions. These factors are not homogeneous across the region but vary widely from market to market." ■

OUR INVESTOR PANEL

Charles Groom, Africa portfolio director, **CDC Group**

Matthew Hunt, director, **South Suez Capital**

Stephen O'Neill, managing director, **57 Stars**

AFRICA

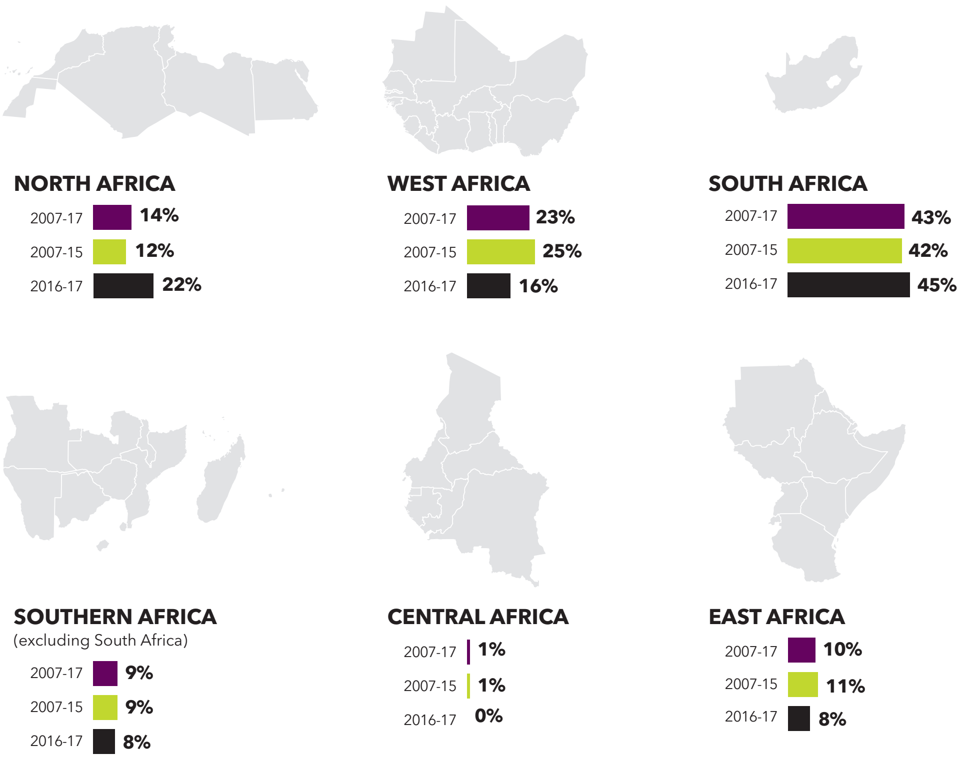
REGIONAL GUIDE

From droughts in the north to currency drops in the south, Africa has endured some tough times over the last three years. **Graeme Kerr** casts his eye over the continent to see which private equity markets performed best

The exit environment in 2017 was challenging but the number of PE exits was only just below the 2016 peak

EXIT ACTIVITY

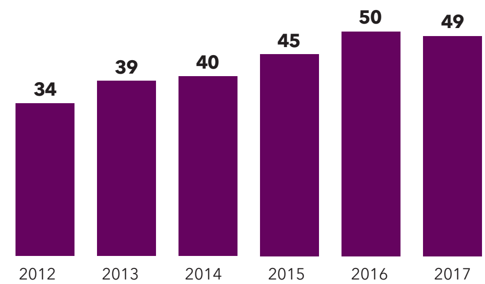
The proportion of exits for each region over a 2-, 8- and 10-year timeframe



Source: EY/AVCA

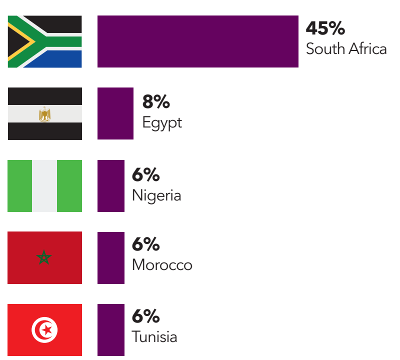
CLOSE TO RECORD LEVELS

Number of exits per year (2012-17)



Source: EY/AVCA

TOP COUNTRIES FOR EXITS 2016-17

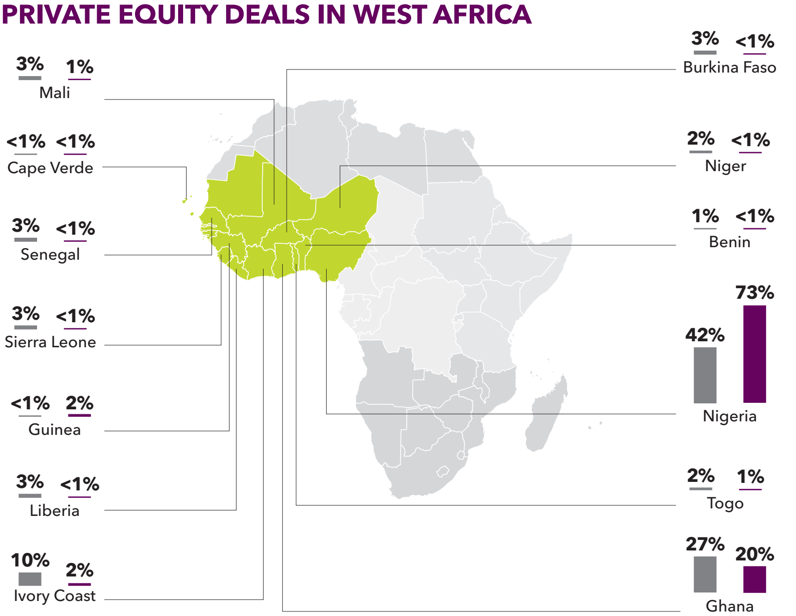


Source: EY/AVCA

West Africa

Nigeria remains 'difficult to ignore' but the francophone region is growing fast

PRIVATE EQUITY DEALS IN WEST AFRICA



% share of PE deals by volume in West Africa, 2012-17 % share of PE deals by value in West Africa, 2012-17

Source: AVCA

35

Number of reported PE deals in 2017

$663m

Value of reported PE deals in 2017

29%

West Africa's share of African deal value

Source: EMPEA

West Africa's share of African deal value hit 29 percent in 2017, up from 25 percent in 2016 and 16 percent in 2011. Nigeria is still dominant, but the francophone countries are the ongoing theme, says Enitan Obasanjo-Adeleye, the African Private Equity and Venture Capital Association's head of research. "The currency situation is much improved, as is the macro environment with Nigeria officially exiting recession in the second quarter of the year. It's such a sizeable market that it's difficult to ignore."

KEY SECTORS: Consumer and financials are traditionally strong, but there's a growing emphasis on energy, as illustrated by African Infrastructure Investment Managers' acquisition of a 44 percent stake last year in Albatros Energy Mali, West Africa's first independent power project to feed into the national grid.

GROWTH AREAS: "In West Africa we see significant opportunities in countries like Ghana and Nigeria, where emerging consumers, the future middle class, will increasingly access financial and healthcare services as they move up the income scale," says Karima Ola, a partner at LeapFrog Investments. Mali is also picking up with its share of deal value growing from 1.4 percent in 2012-14 to 5.8 percent in 2015-2017, according to AVCA.

FUTURE PROSPECTS: A lot is dependent on the strength of Nigeria's recovery. "The big question for the next 12 months is whether Nigeria has returned to a more normal place and fully emerged from the recent recession and seen deal activity returning," says Jeff Schlapinski, director of research at EMPEA.

IVORY HOPES

RISING STAR: The biggest expansion has been in Ivory Coast, a popular base for North African GPs looking to expand into sub-Saharan Africa: "A decade ago were there were just three GPs based in Ivory Coast, now there are around 20," says Mariam Djibo, Abidjan-based principal at Adenia Partners.

Southern Africa

The dominant force in African private equity is recovering after a bout of macro uncertainty

Has South Africa turned a corner? The big beast of African private equity, responsible for 43 percent of all African exits over the last decade, has been mired by currency problems and political uncertainty. But optimism is mounting that a series of reforms by new president Cyril Ramaphosa designed to attract foreign capital may be boosting PE prospects, with "green shoots" appearing, according to Paul Boynton, the chief executive of Johannesburg-based Old Mutual Alternative Investments. Deal value across the region fell from $618 million in 2015 to $359 million in 2017, according to EMPEA.

KEY SECTORS: The retail and service sectors both showed strong growth in 2017: "It's all about the rise in consumers," says AVCA's Obasanjo-Adeleye. Commercial property, and housing and student housing in South Africa also attracted investors. The restarting of the South African government's stalled renewables programme is boosting the energy sector.

GROWTH AREAS: "South Africa is still the dominant market but there's a lot of interest in countries like Namibia and Mauritius as South African PE firms start to look at neighbouring countries," says Obasanjo-Adeleye.

Investec Asset Management sees strong regional prospects for Botswana-based retailer Kamoso, which it bought in October 2017 from Standard Chartered Private Equity and is expanding across Southern Africa.

SOUTH AFRICA: BRIGHTER TIMES AHEAD?

The buzz is back: *there are signs of recovery in South Africa*

FUTURE PROSPECTS: "We've recently seen business confidence picking up in South Africa. There are a lot of new funds being established and also highly experienced individuals breaking away to set up their own funds, with more specialist funds targeting agri, infra, and impact investing," says Tanya van Lill, CEO of Southern African Venture Capital and Private Equity Association.

PRIVATE EQUITY DEALS IN SOUTHERN AFRICA

28

Number of reported PE deals in 2017

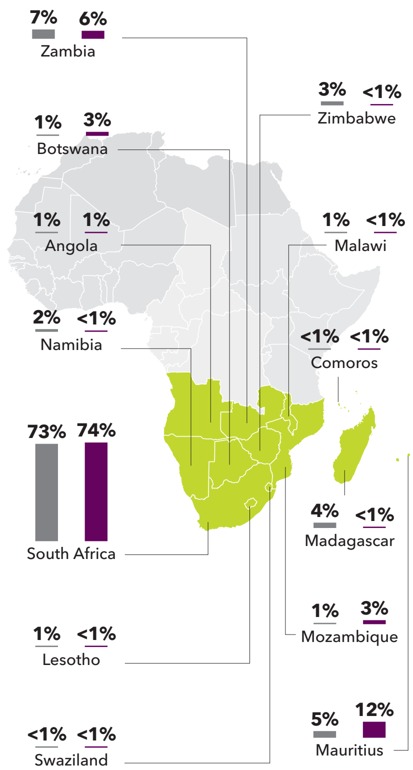
$359m

Value of reported PE deals in 2017

16%

Southern Africa's share of African deal value

Source: EMPEA



% share of PE deals by volume in Southern Africa, 2012-17

% share of PE deals by value in Southern Africa, 2012-17

Source: AVCA

SOUTH AFRICA

'Enormous opportunity' for free trade

Political reforms in South Africa and the creation of a new free trade area will prove a boon for the continent's biggest economy, says Paul Boynton, the CEO of Old Mutual Alternative Investments

***Boynton**: free trade pact could transform economy*

Africa edged a step closer to frictionless trade in July when South Africa became the latest country to signal that it wants to join the African Continental Free Trade Agreement. Nearly 50 countries have signed the initial framework and six have ratified the deal, which takes effect once ratified by parliaments of at least 22 countries.

AfCFTA could help transform the South African economy after a period of stagnant growth, says Paul Boynton, chief executive of Old Mutual Alternative Investments, whose parent company Old Mutual Limited listed on the Johannesburg Stock Exchange in June.

Q How would you describe the investment opportunity in Africa today?

Different parts of Africa are trending positively. In Nigeria, the oil price has recovered. There's been positive political change in South Africa, Angola and Zimbabwe. The AfCFTA agreement [signed in March] is a further positive development for Africa. South Africa has been through a slow patch but there is evidence of green shoots. Infrastructure is a standout for us at the moment, which is our principle activity in Africa.

Q What impact will the new free trade area have?

South Africa has just signed. Nigeria has yet to come on board, although we understand that is a matter of time rather than principle. The opportunity for African countries to trade among themselves is enormous. Intra-African trade is about 15 percent compared to within Europe, where cross boarder trade is 40-odd percent. With rising consumption expenditure over the next decade in Africa, there is an enormous growth opportunity across sectors, for example, in manufacturing. For OMAI, it presents significant opportunities in consumer facing business, manufacturing and infrastructure: logistics, roads, rail and ports.

Q South Africa is a key economy. What is the new government doing to boost growth?

South Africa has been through a period of low growth and uncomfortably achieved procurement activity. Consumer and business confidence has been muted. The previous government was quite profligate in spending and we need to work down the credit card. As a result, it has been a somewhat challenging space to find new investments and manage existing ones.

Looking forward, confidence is lifting. Some key decisions have been made over the past six months by the government of President Cyril Ramaphosa, which position the economy well over the longer term. When the president spoke at the opening of Old Mutual's new building, he reiterated South Africa's need to build strong institutions and encourage foreign capital. He has launched an initiative to attract $100 billion into the country to facilitate this.

Q What do these reforms mean for you?

Now is a very good time to put capital to work in the country. There is some catching up to be done in many portfolio companies. South Africa's stalled renewable energy programme has been restarted. Since the new president came in, we have signed a number of PTAs [preferential trade agreements], reached financial close on a number of new renewable projects to which we've committed several billion Rand. OMAI has invested a

COMMUNITY ENERGY

Dean Alborough, head of ESG at OMAI's African Infrastructure Investment Managers, describes the impact of environmental, social and governance initiatives at Umoya Energy Wind Farm

"By its nature, the Umoya wind farm built in the Western Cape addresses climate change issues. The farm became operational in 2014 and generates 176,600 MWh a year – enough to power 49,000 low income homes – and offsets 183,00 tonnes of carbon emissions annually.

From the beginning we applied a robust ESG risk management process, including due diligence and impact assessments. All renewable energy investments in South Africa must include socioeconomic development and/or enterprise development initiatives. Through the Hopefield Home Improvement Project, we were able to succeed in both.

The local community next to the wind farm identified low income homes that required upgrading through the installation of water geysers, electrics, sinks and new roofs. In phase one of the project, 19 local residents trained on the job alongside outsourced contractors to complete the upgrade of 591 buildings. At the end of the first phase, all 19 had acquired a new skill set and had established three businesses. They alone are now completing phase two of upgrading 351 homes.

Our relationship with the community is paramount. We have a team that communicates with residents and other stakeholders on an ongoing basis. A non-profit community company is a shareholder in Umoya, so it holds a beneficiary interest. To date the feedback from the community has been very positive, but we are not complacent. The relationship is something we continuously strive to better and uphold."

significant amount of capital in renewable assets over the past five or six years. Our portfolio is in excess of 2,000 megawatts. We have invested in solar, wind and CSP [concentrated solar power] and also in a small amount of hydro.

Q Currency and political risk are prevalent in any investment in Africa. How do you manage them?

Africa is highly diverse: 54 countries with 54 different risk environments. We work from the bottom up. We find a project of interest and then look at the jurisdictional risk, the operational, legal and regulatory frameworks. Even though we are local to some extent, for example, in Nigeria, with an office in Lagos staffed by Nigerians, we would ordinarily also look for a local partner to mitigate risk. We would also look for political risk insurance cover on projects.

The dominant risk in many investments is currency, both in terms of the exchange rate and ability to remit. If we invest dollars into a project in Ghana, we want to know, if we can link our revenue line in some way to the dollar or leverage the project in a way to mitigate currency risk.

As an investor in South Africa, where we are investing principally domestic capital into our funds, currency and political risk are elements we don't look at as a sovereign issue. We do, however, consider the credit risk around any payment guarantee that we may have received.

Q How easy is it to find African GPs to invest in for your fund of funds business?

The landscape in Africa has diversified over the past few years. There are 200-odd GPs in Africa and more sector-focused or niche funds. The Africa PE ecosystem has matured significantly in recent times having historically struggled to perform over a long period of time compared to the global private equity space, particularly the US. We believe that Africa on a relative basis constitutes an attractive investment proposition in the next five years as global asset prices are pretty challenging and the macro view for Africa has improved.

Q How do you manage ESG?

Each business unit in OMAI has a fit-for-purpose ESG management system that fully integrates ESG into the investment process. From initial screening to detailed due diligence and to active asset management, we look to ascertain whether it is a suitable business and if changes can be achieved for positive outcomes. We have implemented an ESG framework that allows us to run the ESG management systems, align with United Nations Sustainable Development Goals and measure impact at ground level. We push hard in areas where we can make a difference. We assess a portfolio company both 'longitudinally' over time and we also compare it 'horizontally' or laterally to its peer group. We aggregate this information both at the fund level and as a manager to determine our impact footprint. ■

East Africa

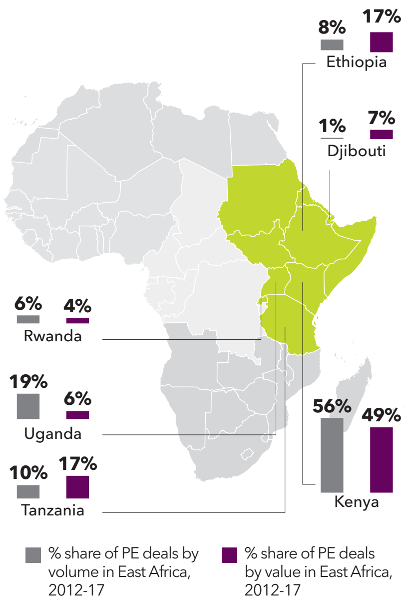
Buoyed by a booming tech sector, East Africa is set for a bumper year in 2018

PRIVATE EQUITY DEALS IN EAST AFRICA

38
Number of reported PE deals in 2017

$396m
Value of reported PE deals in 2017

18%
East Africa's share of African deal value



Source: EMPEA

Deal value in East Africa has gradually expanded from just 3 percent of all African deals in 2008 to 18 percent in 2017, according to EMPEA. "There has been a lot of momentum in East Africa especially the tech activity that is concentrated there," says the association's director of research Jeff Schlapinski. The region boasts three of the world's fastest growing countries in terms of gross domestic product – Ethiopia, Kenya and Tanzania – and 2018 looks set to be a bumper year, with East Africa receiving the most capital of all the African regions so far this year, much of it venture capital, says EMPEA.

KEY SECTORS: Lots of interest in social infrastructure – healthcare and education – buoyed by the emerging middle class, says AVCA. Tech is especially strong in Kenya and the finance sector has seen some notable deals: Kibo Capital Partners bought a stake in Rwanda's largest bank I&M Bank Rwanda in 2017.

GROWTH AREAS: "The one that everyone gets excited about is probably Kenya. There's a community there from early stage right through to traditional infrastructure investments. It has been on something of a political rollercoaster but has calmed down a bit," says Schlapinski.

FUTURE PROSPECTS: "East Africa is the most developed and most integrated economic block in Africa," says Paul Kavuma, CEO at East African investor Catalyst Principal Partners. "It's the one where you have the most harmony in terms of policy and macroeconomic management and even socio-economic patterns are relatively similar across the region. The mobility of talent and convergence of policy has meant the ability to extend businesses, services and products across the region has increased."

EMERGING ETHIOPIA

RISING STARS: "Ethiopia is one to watch. It has a population of over 100 million, a big market and a lot of tightly held assets by government. There is also talk of privatisation. It's a name that always crops up in our LP surveys," says AVCA's Obasanjo-Adeleye.

One to watch: *Ethiopia is a promising market*

EAST AFRICA

The tailwinds behind Kenya's PE growth

Investor confidence in the country is growing thanks to renewed political stability, writes Victoria Robson

The handshake in March between Kenya's president Uhuru Kenyatta and opposition rival Raila Odinga marked a turning point for East Africa's largest market. It brought to a close a period of heightened political tension and violence that followed Kenya's disputed general elections last year.

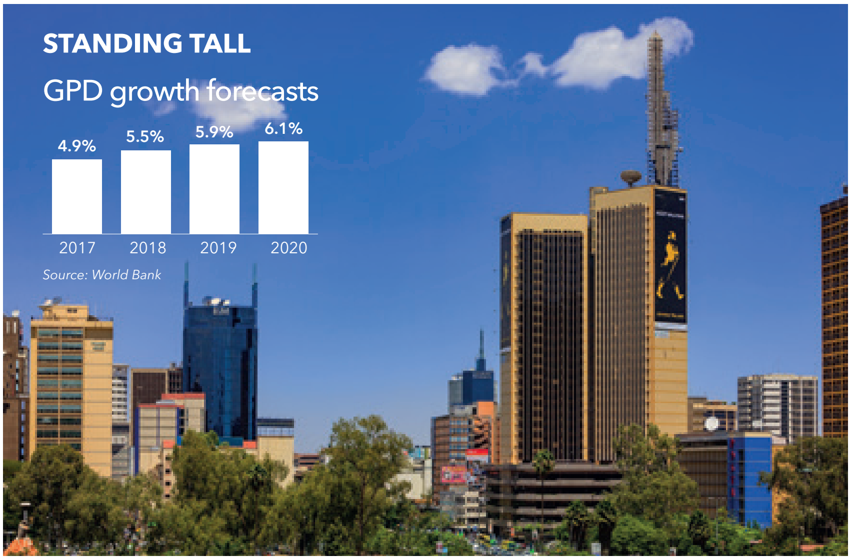
"Business sentiment improved markedly after the handshake," says Paul Kavuma, chief executive of Nairobi-based Catalyst Principal Partners, which seeks opportunities across East Africa. "It was symbolic and had substance. It reduced business uncertainty."

"People are very chipper," says Karim Anjarwalla, managing partner at Nairobi-based law firm Anjarwalla & Khanna. "Our M&A team has never been busier."

Kenya's underlying economic fundamentals bolster the mood. The World Bank forecasts the economy will grow by 5.5 percent this year, up from 4.9 percent in 2017. "This creates a tailwind for top-line growth," says Takudzwa Mutasa, principal at pan-African investor Development Partners International, which is actively looking for deals in Kenya.

The market presents other advantages such as sizeable businesses with the scope for regional growth; a deep pool of human capital; and a sophisticated financial services sector, says Kavuma, who notes the weight of his firm's investments "naturally" falls in Kenya.

It is also an open market thanks to an absence of capital controls and foreign investment caps – bar certain sectors like insurance where a third of shares must be Kenyan-owned, says Anjarwalla. And the stability of the shilling means in terms of currency risk, over the past few years, Kenya has compared favourably to commodity-dependent economies, where currencies have been volatile.



Connected city: *Nairobi's expansion has been supported by its tech businesses*

"We are seeing an increase in dealflow for transactions of $20 million-$100 million," says Mutasa. "There are a lot of family businesses looking for capital. They are starting to see the value of private equity to the capital structure and to expanding beyond Kenya," he says, adding sellers are a mix of founders cashing out and those wishing to take on a new partner.

BIG FOUR

Sectors drawing GP interest include healthcare, which is a pillar of the government's Big Four development agenda (alongside manufacturing, affordable housing and food security). Per capita expenditure on healthcare is rising and pharmaceutical retail chains and clinics are emerging, says Mutasa.

Fast-moving consumer goods is where "we'll continue to see strong growth", Mutasa adds. "The Kenyan consumer is becoming wealthier. Established brands will do well." Within financial services, Anjarwalla highlights insurance as a particular area of opportunity, seeing deals such as the $55 million investment in May in listed financial group Britam Holdings by a consortium of pan-African manager AfricInvest alongside German, Dutch and French development finance institutions.

Technology-enabled businesses reliant on broadband connectivity such as payment solutions and internet-based video also have potential supported by the country's growth in internet penetration, adds Mutasa.

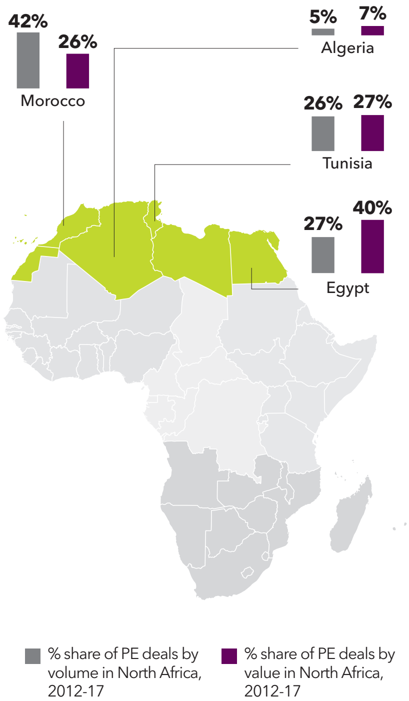
However, valuations are high relative to neighbouring markets, buoyed by the growing availability of alternative sources of capital, such as bank debt, says Anjarwalla.

But the market is not overvalued, says Kavuma. The rise in prices has occurred in tandem with improved corporate performance, scalability and liquidity. "The quality of businesses has improved, the capital markets have deepened and investor interest has risen." ■

North Africa

GPs in the region, traditionally bracketed with the Middle East, are looking southwards

PRIVATE EQUITY DEALS IN NORTH AFRICA



Source: AVCA

14

Number of reported PE deals in 2017

$101m

Value of reported PE deals in 2017

4%

North Africa's share of African deal value

Source: EMPEA

North Africa's strength has traditionally been its proximity to Europe and the Middle East, but GPs based in the region are increasingly looking to move southwards and expand in sub-Saharan Africa, especially to the francophone region of West Africa. Dealflow was an unusually lacklustre $101 million in 2017, but has rebounded in the first half of 2018, according to EMPEA.

KEY SECTORS: Industrials, consumers and financials, with the mid-market – deals of between $10 million and $30 million – the biggest opportunity, according to North Africa specialist Mediterranea Capital Partners.

GROWTH AREAS: Morocco, still recovering from a drought, is widely regarded as having the most promise, with Northern Morocco "a great market at the moment", according to Peter Baird, head of private equity at Investec Asset Management. "I think it has the potential to become the Mexico of Europe – it has strong expertise in precision engineering and other manufacturing for export to the EU," he says.

FUTURE PROSPECTS: Investors are increasingly targeting the region: 50 percent of LPs regard the region as an attractive destination for PE investment, compared with 11 percent in 2016, according to the AVCA *2017 Annual LP Survey*. The listing of Vivo Energy in London was another boost for the region. "There were more public exits in North Africa in 2017 than we've seen for some time," says EMPEA's Jeff Schlapinski.

ALGERIA: THE BEST RETURNS IN NORTH AFRICA?

***Attractive destination**: Algeria has performed strongly despite the perceived currency risk*

RISING STARS: "Algeria is not a market that people are familiar with, but it has picked up in the last three years," says AVCA's Obasanjo-Adeleye. That is confirmed by Mediterrania Capital CEO Albert Alsina, who says Algeria has provided the firm's best returns in North Africa despite its perceived currency risk.

NORTH AFRICA

Positioned to obtain high returns

Local knowledge and a clear diversification strategy are key to mitigating macro concerns in North Africa, says founder and CEO of Mediterrania Capital Partners Albert Alsina

Alsina: mid-market has the biggest opportunities

North Africa has weathered seismic political and economic shocks over the last few years. The Arab Spring raised fears of social unrest and the devaluation of the Egyptian pound two years ago jolted the region's largest economy, yet North Africa specialist Mediterrania Capital Partners has continued to rack up double-digit returns by investing in the mid-market. The secret, says its founder and CEO Albert Alsina, is to diversify across countries, sectors and deal segments and ensure that you have people on the ground to provide true local expertise.

Q How would you characterise the last 12 months?

The last 12 months have been incredibly busy. Our third fund targeting €250 million hit a first close of €103 million in November after just six months on the road and we are looking at a second close towards the end of 2018 or early 2019. We've already deployed more than 60 percent of the first close with three deals: leading a consortium investing €55 million in Morocco's largest construction company TGCC; investing in Cairo Scan, the leading private provider of diagnostic and interventional imaging services in Egypt; and developing an equity line of which €20 million has already been invested in Côte d'Ivoire-based Cofina, Africa's leading provider of remittance services and mezzo-finance loans for SMEs.

Q Has the focus of your business shifted away from North Africa?

One of the trends in recent years has consisted of North African companies entering sub-Saharan Africa. We originally started our operations with North Africa in mind, but soon we were getting a lot of dealflow from francophone Africa, and so we opened an office last year in Abidjan, Côte d'Ivoire. That's how the Cofina deal came about. With more than 1,000 employees managing 90,000 clients across its six subsidiaries, Cofina services the missing middle of entrepreneurs and SMEs who lack access to financing. The plan is to raise more capital for future development up to an additional €40 million-€50 million. Cofina has an extraordinary team that is delivering double-digit growth on sales and EBITDA while substantially growing the net profit with a very low volume of non-performing loans.

Q How do you factor in the macro uncertainties and political upheavals?

Every emerging market involves political risk, but LPs often overstate this risk – after all, private equity investors don't invest in the country itself but in its companies and in the microeconomy. We insured the political risk in our first fund through MIGA, a World Bank subsidiary, but found we never needed it. Also, the way we manage risks – not just political risks but also macroeconomic ones such as currencies – is through diversification. A clear diversification strategy is very important in emerging markets.

Q How do you ensure diversification?

Firstly, we look at geographical diversification so this is why we invest in many different countries – seven so far. Secondly, we ensure high diversification across sectors, and thirdly we do so by deal type. In terms of sector diversification, we try to balance our investment between sectors with long-term potential such as healthcare and education and sectors that offer larger short-term gains such as fast-moving consumer goods. We also diversify the size and type of deals. We have some large deals, »

» some midsize ones and smaller deals with different financial instruments such as convertible bonds, shareholder loans with a coupon at the end of the year and holding period, or buybacks with call options (rather than pure equity deals).

We have found that having a diverse portfolio of geographies, sectors and deal types helps mitigate the different risks that may arise.

Q What about the fears of currency devaluation?

Currency is a big risk theme in Africa but less than you might imagine in the countries that we invest in. As far as North Africa is concerned, the devaluation of the Egyptian pound in 2016 and its subsequent flotation enabled the currency to reach its true value, so today it's less of a risk. The Moroccan dirham is a basket linked 60 percent to the euro and 40 percent to the dollar, so there's a low risk of devaluation. In the francophone region of sub-Saharan Africa, the common currency is the CFA franc which is linked to the euro due to its strong connections to France and the French Central Bank. The North African country that is perceived to have a higher currency risk is Algeria, which is precisely where we have obtained the highest returns so far. Overall, we can say that in North Africa the currency risk is effectively controlled.

Q How important is local knowledge?

Having a team that understands the local context is very important in order to assess the reality of each country's changes and to find the best opportunities to invest in. Undoubtedly, having a strong foot in the country is crucial for the success of any PE firm in Africa. And you only achieve this by hiring professionals from that country, who over the years can build a strong network and in-depth knowledge of the economies, financial systems and the political environment, as well as having a full understanding of the social trends and needs.

“We have seen a great increase in the number of large international funds buying assets from smaller PE firms

Q What are the main investment opportunities in North Africa?

The reality is that there are opportunities in all segments. For us, however, the biggest opportunity lies in the mid-market segment – with deals of between €10 million and €30 million – because of the lack of capital entering that market. In North Africa, as well as a small number of PE firms focusing on the mid-market like us, you have a few large companies such as Carlyle, DPI, Helios, Actis and TPG among others which are doing €70 million to €100 million-plus transactions. As a result, there's very little competition and lower pricing pressure in the mid-market.

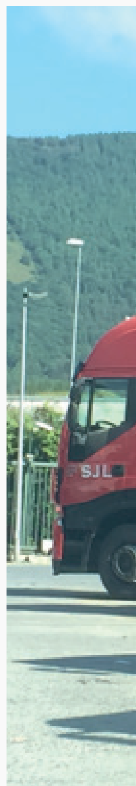
SLEEPING BEAUTY

Under Mediterrania Capital's ownership, Grupo San Jose & Lopez became one of the leading road freight carriers between Europe and North Africa

“SJL Morocco has invested heavily in a new automotive manufacturing plant in Tangier and had huge logistics needs, but when we acquired a stake in international road freight transport company SJL in June 2013, it was totally in dormant mode. It was owned by three Spanish families and had 26 shareholders, with headquarters in Tangier in Morocco and Oiartzun in Spain. The company had a clear governance and direction issue, with excellent services in great demand but flat sales and profits. We initially acquired a 49 percent stake and later on, with a co-investor, we bought the rest of the company.

In the four years of ownership, we more than doubled the EBITDA. We opened offices and warehousing facilities in Tunisia, expanded internationally and changed the governance and the structure. In that time, we managed to transform SJL into a full pan-African/European company with new distribution hubs in France, Germany and Spain, providing just-in-time services to Renault, Nissan, Tyco and many other customers from the automotive, textile and agribusiness industries,

We sold the company to Investec Asset Management in 2017, providing a very good return for our investors, and the company is in very good hands to deliver further growth and expansion.”



Q Are these larger private equity firms stimulating the market for secondary buyouts?

In the last five years, we have seen a great increase in the number of large international funds buying assets from smaller PE firms through secondary transactions as generally these assets are of high quality and can be easily taken to the next level. This is very common in developed economies but relatively new to the African continent. Nearly 40 percent of exits in Africa last year were to another private equity house, compared with 10 percent in 2011 and only 8 percent in 2008.

Q How high are the returns?

Over the last few years, GDP rates in North Africa and francophone Africa have been quite steady with 2.5 to 5 percent growth. That obviously helps ensure good investments with very good prospects.

In this context and also as a result of the right implementation of our value creation model, we are seeing our partner companies achieve double-digit growth, not only in sales but more importantly in EBITDA. Our second fund, MC II holds a portfolio of eight companies that have delivered 25 percent average EBITDA growth for the last four years.

In Africa whenever you have a winning company that delivers double-digit growth for a significant time, anyone trying to enter that market and gain market share will find it very hard. For example, we are part of a consortium that acquired a 49 percent stake in Algeria's leading manufacturer and distributor of generic pharmaceuticals Biopharm in March 2013. We listed the company on the Algerian stock market two years ago and it is doing phenomenally well. When you have a champion asset like that it is very difficult for a competitor to come in and take that position, as Africa is a fragmented continent with little competition for its market leaders.

The favourable environment is enabling leading companies to grow and consolidate their position in the market: in North Africa PE firms that do things properly are able to deliver between 22 percent and 25 percent IRR to investors. That's equivalent to a money multiple of between 2.5 and 3 times depending on the holding period.

Q How would you describe the fundraising environment in Africa today?

Well, there is a lot of competition among mid-cap PE firms investing in Africa. When you look at our rivals, we do not compete in terms of deals, because we often co-invest, but in terms of fundraising instead. Some LPs view Africa in the same way as Latin America and Asia 10-15 years ago. On top of that, the \$150 million or \$200 million investment ticket of big managers, endowments or pension funds is too large for a mid-cap firm like us. So we seek out the smaller investors instead, requiring much more work and a stronger distribution network. But Africa has great momentum and investors can see the benefits of investing here. The challenge lies in educating them about the growth potential and the many opportunities in the continent.

Q Are there any typical concerns for LPs considering investing in Africa?

The main issue is the high perceived risk of investing in Africa. Many investors don't know the actual performance of the individual economies, so they think the risk is higher than it actually is.

A major concern is that many investors see Africa as one region, whereas in fact it is composed of 54 countries with very different economies and political situations. Morocco, for example, offers great prospects for PE investments thanks to a stable political situation, good banking system, favourable demographic trends and a rising middle class with increasing demand for education and healthcare. Algeria too delivers high returns despite it being perceived as a high-risk market. As a result, understanding the real risk versus the perceived risk in each individual country is very important.

The other factor that LPs must bear in mind before investing in Africa is that executing deals takes longer than in other regions. Generally, a typical investment requires a good six months to be fully executed. We are talking in many cases about family-run businesses, meaning that negotiations are highly complex and involve emotional aspects. Exits can take even longer. However, investors who understand the African reality have a lot to gain. ■

RESPONSIBLE INVESTING

Africa 'far ahead' in ESG

Buttressed by a hefty proportion of capital and expertise provided by development finance institutions, African GPs are a force for sustainable change, writes Victoria Robson

African managers are often held up as industry leaders in ESG implementation and innovation. While the accolade is hard to prove relative to other markets, it is clear consideration of environmental, social and governance impacts is imperative for any African GP seeking to invest capital on the continent.

"When we look at our colleagues in other emerging markets, Africa is far ahead of say Latin America or Asia in the discussion of ESG," says Michael Hall, ESG manager at Development Partners International. "It's more common for private equity managers in Africa to be familiar with ESG, the terminology, what it should look like and how to conduct business."

"ESG practice in African private equity meets global best practice in my experience of working within the industry," says Dean Alborough, ESG advisor at African Infrastructure Investment Managers, a member of Old Mutual Alternative Investments. "Given the emerging market context, ESG is naturally going to be a fundamental aspect."

COMMITMENT

Another clear reason for manager focus on ESG is their source of capital. "CDC, among many other DFIs [development finance institutions], have been involved in African private equity funds pretty much since the beginning," says Guy Alexander, environmental and social responsibility manager at CDC, which invests both directly and through funds in Africa as a UK DFI. "In many of the funds that have been raised, a DFI would account for a significant majority of the capital."

"DFIs are leading the way," says Mariam Djibo, an Abidjan-based principal at Adenia Partners, which closed its latest fund, Adenia Capital IV, on €230 million. The commitments were split 50-50 between DFIs and other investors. "DFIs are our first source of capital and our first constraint. They have stringent ESG criteria from the fund documentation [onwards]. We have to tackle those issues. They want risks managed and impact."

GPs realise "that if you're not going to undertake ESG in a genuine and proper way, you're not going to raise capital", says Alborough. "The more sophisticated LPs become [regarding ESG] the more sophisticated GPs become. Over the last two years, we have seen a dramatic increase in LPs asking about our ESG practices."

DFIs, which exist to promote sustainable development, are themselves evolving. Monitoring of managers' ESG systems and capabilities is well-established. "DFIs have always had a clear view of what they want in terms of reporting," says Hall. "Our DFI partners have been consistent in their approach and work together to streamline the reporting process."

Now "the conversation has moved on from, 'what reporting does the LP need to be confident that GPs are doing their job?', to 'how do we know if we are going in the

> ***DFIs have always had a clear view of what they want in terms of reporting***
>
> **Michael Hall**

right direction, what new contextual risks and themes are arising?" says Alexander.

As African economies grow, industrialise and urbanise, there are new risks to consider. "Regulations and enforcement are weaker in some African countries," says Ritu Kumar, CDC director of environmental and social responsibility, adding that local ESG experts are rare. "That puts the responsibility on an investor like CDC to ensure better ESG practices."

"DFIs are becoming more engaged on what works and what doesn't," says Hall. "Our DFI partners are increasingly looking at technical solutions, providing assistance, whether that's through grants, information sharing or provision of free training."

At the same time, DFI engagement with the investment process is deepening. In the case of first-time or new managers, DFIs are asking to review ESG due diligence and give feedback to the investment committee (on which they typically have a seat), says Djibo. "This is very new," she says, adding that LP scrutiny can extend along the value chain to encompass portfolio company suppliers and customers as investors seek to mitigate investment risk.

LP oversight can stretch to the end of the investment cycle. As DFI focus broadens from purely risk mitigation toward value creation, evidence of ESG-fuelled returns is increasingly important at exit. Demonstrating a track record of positive ESG outcomes "is becoming more valuable for future capital raising", says Alborough. "The more focus LPs give [to ESG], the more value that track record starts to have."

BENEFICIAL INTEREST

However, GP adherence to DFI ESG criteria is more than simply a means to curry favour with investors. GPs see DFIs as a deep wellspring of ideas, experience and support. "There are serious benefits to working with certain LPs and DFIs," says Alborough. "LPs bring to the table a broad line of sight and experience. They've seen a lot of assets globally. When they are asking for something or pushing in a certain direction, you have to take the time to listen." And in problem solving, international DFIs can often help by exercising their local influence, he adds.

"We try to share experiences, and with the resources we deploy help managers »

TAKING ESG TO THE BANK

How a portfolio company in the banking sector gained an edge through sustainability measures

Addressing ESG issues is imperative to build sustainable businesses in the African context, says Mariam Djibo of Adenia Partners. "When you invest in a company in Africa you have a social responsibility that is above the same company in the same sector in Europe, the US or even Asia," she says.

Upgrading business models and processes is increasingly acknowledged as not only a means to mitigate risk but also to create value. In some cases, it delivers direct financial benefit to portfolio companies.

Djibo recalls a conversation she had with the chief executive at a bank in the GP's portfolio about integrating new environmental criteria into its credit committee process. In the absence of regulations that would bind all banks to the same criteria, the CEO expressed concern that adopting these new parameters would slow decision-making and undermine its ability to compete.

"He was probably right," says Djibo, reflecting that it should have been the regulator that imposed the criteria. However, the CEO was persuaded by the fact that including environmental criteria in the bank's credit process meant it was eligible to apply for additional DFI funding to support its lending activities. "Then he was convinced," she says.

Once Adenia wrote the processes and trained the sales agents at the bank to adhere to the new criteria, the bank took the opportunity to access new financing, which ultimately rendered it more competitive. ■

More to lend: *tighter credit checks helped one bank secure DFI loan support*

> ***There is an alignment between LPs and GPs in terms of what we are trying to push for***
>
> **Guy Alexander**

» get the most benefit from the standards we are trying to promote," says Alexander. "There is an alignment between LPs and GPs in terms of what we are trying to push for."

The International Finance Corporation's Environmental and Social Performance Standards provide a "very consistent set of expectations as to what requirements a manager needs to follow", he says. They sit alongside the UN's Sustainable Development Goals and the Principles for Responsible Investment as fundamental reference points for managers.

While collectively GPs understand what is required in terms of ESG, each approaches reaching their goals differently, says Alexander. However, "since there is a consistent set of LPs [invested in African GPs] there are often similar conversations taking place across a number of different managers".

In Africa, where the scope for impact is enormous, the outcome of these conversations can be significant. Relying on veteran DFIs for both capital and expertise, African GPs are well positioned to make headway.

"Progress has been made but there's so much that needs to be done," says Alborough. ■

INVESTMENT OUTLOOK

Why Africa has the edge on Asia

Economies in African markets have been on something of a rollercoaster ride over the last decade, with events in recent years giving many investors pause for thought. But Peter Baird of Investec Asset Management believes the stage is now set for attractive private equity investments – and, importantly – exits

Baird: *Africa is back on track*

It's no secret that many of Africa's large economies – the ones most often targeted by private equity firms – have faced some challenging economic times in the last two years. Hit by a dramatic and sudden fall in commodity prices, many of the region's markets suffered equally dramatic falls in GDP growth. Nigeria, for example, which had been among the fastest growing economies in the world, slipped into recession in 2016 and its currency underwent a significant devaluation. Ghana's GDP growth rate also fell dramatically, while political unrest in countries such as South Africa and Kenya deterred many investors during 2017.

Yet 2018 has been a something of a calmer year across the continent, with many predicting greater stability, at least for the immediate future. One of these is Peter Baird, managing principal, head of private equity at Investec Asset Management. We talked to him about some of the issues faced by investors in his markets and why he believes we are entering a golden age for African private equity.

Q What's your view on the effect of commodity price volatility on African markets?

It has been an interesting decade. Back in 2008 to 2009, it was a time of optimism in emerging markets as developed markets were in turmoil following the financial crisis. We had something of a super-cycle in Africa between 2009 and 2015 as capital flowed here and many people deluded themselves into believing that commodity prices didn't matter anymore – the prevailing view was that endogenous growth and secular trends of demographic growth, urbanisation, and rising middle classes would drive economic fortunes.

That changed when commodity prices dropped. It was quick and deep and that had a devastating impact on some economies, such as Nigeria. If the fall had been more steady and moderate, I think most countries would have managed better, but as it happened, some of the macroeconomic policy responses made a challenging situation even worse.

Q So what would you say has been the biggest impact of this?

For investors with direct or indirect commodities exposure or non-dollar denominated currency, the impact has been significant. Yet it has also trickled through to consumer and government spending and has left a dent in investor confidence. There has been a significant pull-back among investors from emerging and frontier markets. The second and third order effects are still working their way through the economies and capital markets.

Q Yet you believe we are now entering a golden age for African private equity. Why?

The worst is now behind us. Most large economies in Africa are back on track and improving fast. At the same time, business confidence is up. There is a real need and demand for capital for expansion. For private equity firms, this is a great time to be in the market because entry enterprise values have fallen by around two turns of EBITDA. So, when there was a lot of competition for deals, back in 2015, entry EVs were, on average, 9x EBITDA; they're now closer to 7x EBITDA.

The investors who are still in the market – and we are mid-way through investing our $295 million Fund 2 – are now able to negotiate more favourable terms. It's also much more possible to source proprietary dealflow than before – so many of the situations were highly competitive previously, but that has changed. »

Q And how do you think this compares with other emerging markets?

I think it's possible to find great businesses at lower valuations in African countries than many other comparable markets. These are businesses that can achieve the same kinds of growth possible in more popular markets – there are many of the same secular trends – but Africa just isn't getting the same love from investors currently.

Over the last five years, investors have focused much more attentively on markets such as China, Vietnam, Malaysia and Southeast Asia more generally. As a result, there is a lot more untapped potential here in African markets.

Q Given the size of the African continent, and your desire to source proprietary deals, how do you choose where to focus?

We tend to take a regional view and that focuses on four clusters: South Africa and its neighbours; the East African Community countries; Nigeria and Ghana; and Morocco and Egypt. Taken together, these regions represent around 90 percent of Africa's GDP. In each of these regions, there are many high-quality private sector businesses, there is a well-embedded and professional advisory community and debt markets function well.

These clusters also benefit from having markets that are large enough to build and grow attractive regional champions. Our recent investment in, for example, Botswana-based retailer Kamoso, which has expanded across southern Africa, demonstrates this pattern well. It has strong regional growth prospects.

And if you think about the East African Community trade bloc, it has a population of 250 million people, so there's a lot of potential to build substantial East African champions over five to 10 years. That will be highly attractive to strategic buyers.

> *“Business confidence is up. There is a real need and demand for capital for expansion*

Q So how much interest are you seeing among strategic buyers for these kinds of regional champion?

There are some local players large enough to acquire, but in terms of international strategic interest, it's still early days. It's starting to build, but I'm realistic – it will take time for activity to flow through. There's often a lot of talk about East Asian and South Asian buyers looking to Africa, for example. That's particularly the case for East Africa, given the geographic proximity between the two regions. Yet much of that is hypothetical currently and will remain so until investor confidence picks up again. We do see some interest from US and European trade buyers, but secondary buyouts are more common currently as most talks with trade from these regions tend to be more opportunistic approaches or exploratory.

Q What about IPOs – some of these have not gone to plan recently in Africa, have they?

Yes, there were a lot of hopes pinned on a number of large IPOs for 2018, such as mobile communications group MTN, which is under regulatory pressure to list, and a number of telecom towers businesses, such as IHS Towers, Helios Towers Africa and Eaton Towers. Some of these have simply pushed back plans to 2019 and so the general feeling is that, if they do go ahead, they will open up the IPO markets for other companies. I think once we see some successful IPOs get away, listing prospects will become greater for some companies.

Q How can firms return capital to investors in that case? Does this rely mainly on secondary buyouts?

We are very much focused on returning capital to investors early as the long hold periods characteristic of many African private equity portfolios is a source of frustration to some LPs. That's why we focus on cash generative businesses – it means that

TECH TRANSFER

Q African markets have a strong track record for leapfrogging more developed economies in terms of tech – how much does that present an opportunity for you?

We are very focused on this area. We see huge potential for investments taking advantage of new technologies. In some cases, this is industry formalisation, such as in fintech or retail where new technologies can assist in creating regional champions.

In other cases, there's a real opportunity for new industry formation through the adoption and combination of new technologies within existing sectors. In education, for example, mobile communications, the availability of broadband across the continent and new payment systems now enable companies to cater for the almost infinite demand for education among Africa's populations. Distance learning is a rapidly growing sector that meets this demand in very remote locations, for example.

Q Can you give an example of this from your portfolio?

Our investment in Mobisol is a great example of the intersection of technologies creating investment opportunity. It's a company that addresses the need for energy in off-grid households across East Africa through the provision of solar capacity that uses mobile technology. It also recently launched new software that helps pay as you go energy providers (who are often users of Mobisol products establishing businesses to sell energy to other customers) track system performance and payments.

we can sometimes partially exit portfolio companies through dividend recapitalisations. That's quite unusual in Africa, but we have secured two so far.

We've also managed other exits in the last 12 months. For example, we sold a SADC retail business to a local partner, giving us a full exit. We also sold a Nigerian consumer goods business back to the management team – it had been performing well, even despite the troubles there and so we generated a good return. And finally, we negotiated the pre-payment of a South African mezzanine investment. In all, I'd say our experience shows it's possible to exit investments using less common paths than the usual secondary buyouts, international trade or IPO paths.

Q Within the regions you focus on, would you say there are any standout countries for opportunity and why?

There are some very good opportunities in Nigeria now. It's about 12-18 months behind Ghana in terms of recovery (and Ghana is doing very well now), and we're seeing an improvement in Nigeria's macroeconomic policy, which is leading to more foreign direct investment and over time, its reliance on oil for exports will diminish. Yet it's also a market where risk capital is scarce right now and the banking system is in disarray, so there is a lot of opportunity for private equity investors who understand the market well.

Northern Morocco is also a great market at the moment. The economy is booming and the region is seeing high growth in human capital and has a strong geographic location in that it is within easy reach of Europe. I think it has the potential to become the Mexico of Europe – it has strong expertise in precision engineering and other manufacturing for export to the EU. That's why we invested in SJL last year, a cross-border logistics and transport operator in Tunisia, Morocco, Spain and France. ■

LOCAL CAPITAL

The next wave of African PE

An exciting opportunity for global private equity in sub-Saharan Africa lies in its pension funds, writes Alex Lynn

Golden opportunity: *could these Cape Town seniors be a target for private equity?*

We often hear about the vast untapped PE opportunity in sub-Saharan Africa. Proponents of the region will point to steady gross domestic product growth which is outpacing many western markets, and economies that – due in no small part to advances in mobile banking – are developing middle classes with cash to burn. Big-name private equity firms have been acquiring everything from music companies to coffee houses in recent years.

But whether Africa is continuing to deliver on its dealflow promises is up for debate, following the recent slowdown.

An arguably more exciting opportunity for global private equity in sub-Saharan Africa lies in its relatively untapped institutional investors.

Partners Group is among those looking to take advantage. It moved into the region in July with the launch of Helical Capital Partners, which will target $300 million from South African and sub-Saharan LPs for a vehicle that Partners Group will manage and invest alongside its own multi-strategy, multi-regional global value funds.

Private equity has struggled to access African pension funds. A 2015 study from the Commonwealth, the Making Finance Work for Africa Partnership Secretariat and EMPEA – the most recent available – found African pensions had at least $35 billion available for allocation to private equity, of which just $5.7 billion had been invested.

A couple of recent developments have meant that the likes of Partners Group are paying closer attention.

In February, South African finance minister Malusi Gigaba raised the offshore investment allowance for institutional investors from 25 percent to 30 percent and doubled the allowance for investments into the rest of Africa to 10 percent. The country passed legislation in 2011 enabling its pension funds to invest up to 10 percent of their assets in private equity, up from the previous limit of 2.5 percent.

Ghana is also loosening the restrictions on private equity. In April 2017, the country's National Pension Regulatory Authority allowed pension funds to allocate 15 percent to alternative assets, with up to 10 percent of total AUM in any one sub-asset class.

And yet the floodgates have been slow to open.

One obstacle so far has been that many pensions on the continent are simply not geared up to establish relationships with general partners. As one Ghanaian pension trustee put it, there is a "lack of capacity and expertise to do this kind of work".

Perhaps the biggest challenge has been access to international private equity funds. Until now, the majority of Africa's pensions have been unlikely to be able to stump up commitments large enough or have the necessary connections to catch the eye of blue-chip funds.

"We are looking at some of the pension funds in South Africa who may have $5 million or $10 million to invest but maybe not the $50 million that Partners Group will normally accept directly into their fund," Helical co-chief executive Craig Beney tells *Private Equity International*.

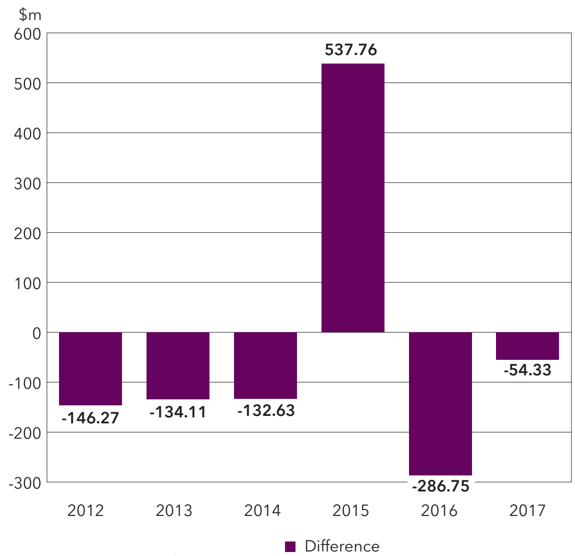
It seems highly likely that a number of African institutional investors are developing the means and the appetite to enter PE. If more blue-chips create a direct line to its funds like Partners Group, the trickle of outbound African LP capital might just become a pour. ■

FUNDRAISING

Shrinking back

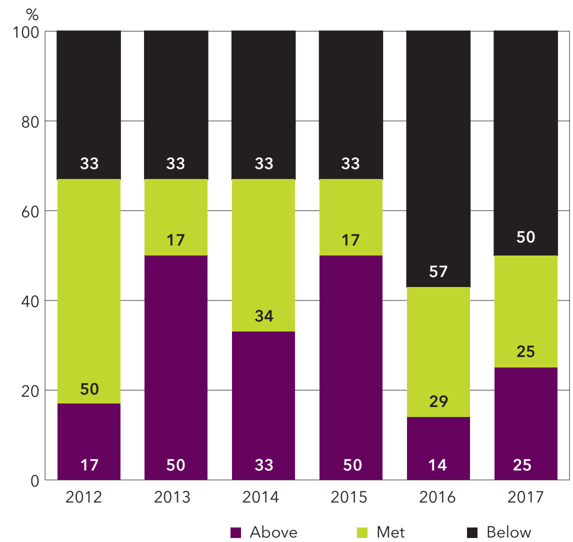
Africa-focused fundraising failed to hit its targets in 2017, according to *PEI* data for funds that reached final close

Amount raised by Africa funds compared with targets



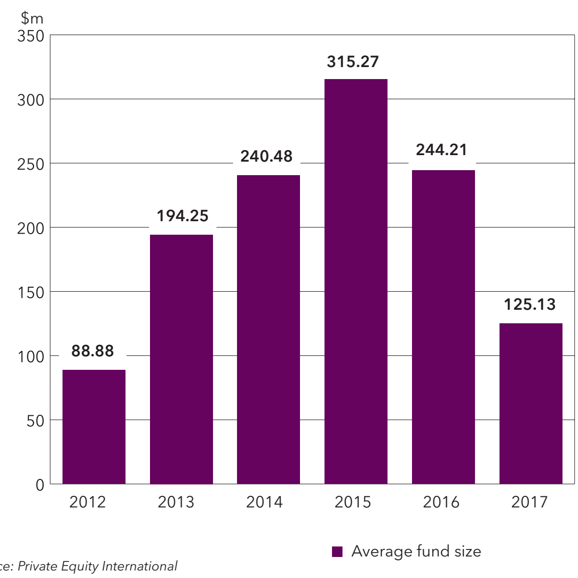
Source: Private Equity International

Percentage of Africa funds that met their targets



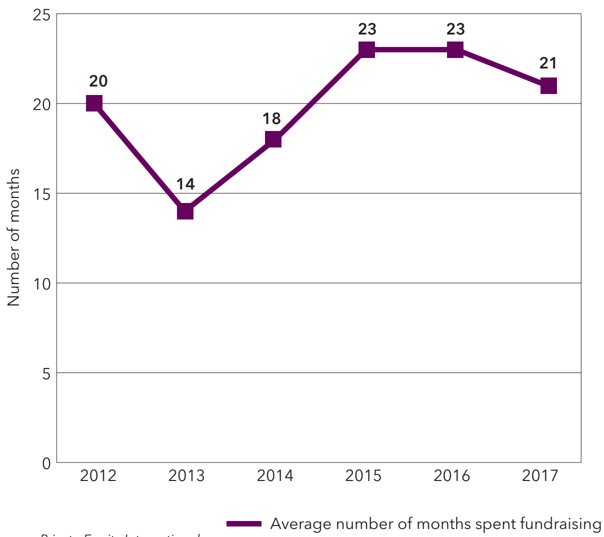
Source: Private Equity International

Average size of Africa-focused funds that closed (2012-17)



Source: Private Equity International

Average time taken by Africa-focused private equity funds to reach a final close (2012-17)



Source: Private Equity International

Ten largest Africa-focused funds to close, 2016-H1 2018

Enko Africa Private Equity Fund
$83m

Fund for Agricultural Financing in Nigeria (FAFIN)
$66m

- Growth equity
- Buyout/corporate private equity
- Fund of funds

4

Number of funds to close in 2017

$500m

Capital raised from Africa-focused funds raised in 2017

21 months

Average time on the road for an Africa fund in 2017

Source: Private Equity International

JOHANNESBURG

Where to eat, drink and raise capital

The main LPs to meet? The most jaw-dropping view? Tanya van Lill, chief executive of the Southern African Venture Capital and Private Equity Association, gives the lowdown for first-time visitors

Where's best to stay?
There are a number of really good hotels in and around the Johannesburg area. To be close to the commercial district of Sandton, Clico Boutique Hotel, Radisson Blu Gautrain, Winston Boutique Hotel or 52 on Bath are all good options. For something more scenic away from the hustle and bustle, consider the Fairlawns Boutique Hotel or Four Seasons Westcliff just on the outskirts.

Which restaurants would impress a client?
For lunch, The Grillhouse Sandton or Café Del Sol in Bryanston are good options. If you want to be seen by the 'who's who' of South African society during lunch, Mastro Antonio in Illovo is the place to be. For something quieter and more private, try the Bellagio in Illovo. For dinner, Qunu at the Saxon or Marble Restaurant in Rosebank are good choices.

Any recommendations for a breakfast meeting?
A lot of the shopping centres in and around Johannesburg, like Melrose Arch or Morningside, offer great breakfast places to meet. Two that stand out that aren't located in a shopping centre are Olive & Plates in Sandton and the View Restaurant at the Four Seasons Westcliff.

Which LPs should I visit?
Two South African LPs worth visiting are the Industrial Development Corporation in Sandton, which gives the DFI perspective on South African and regional deals, and has assets of 137 billion rand ($9.72 billion; €8.49 billion) and Public Investment Corporation in Menlyn, Pretoria with assets of 2 trillion rand.

Johannesburg: *great views and hustle and bustle*

Where should I head for a night out?
Venture to areas such as Greenside, Parkhurst and Melrose Arch. There's a great choice of bars and restaurants, all within walking distance of each other, that offer a different and unique ambience and signature drinks.

Where do you suggest for a morning run?
In and around Johannesburg Zoo offers great running options. For the best sunrise view in the city, try James and Ethel Gray Park near Melrose Arch.

What's the most enjoyable day trip?
Spend a day in Maboneng Precinct near the Johannesburg central business district to catch a glimpse of the buzzing entrepreneurial spirit, explore the sights and sounds of Soweto or venture out into nature at the Cradle of Mankind, a World Heritage Site 50km north-west of Johannesburg.

Which building has the most jaw-dropping view?
The Four Seasons Hotel Westcliff has a stunning hillside panorama. Take a ride up the glass elevator for dinner and drinks at the View restaurant.

What safety precautions should I take?
As with any big city, be vigilant and do not walk around alone with all your valuables, especially at night. Know where you are heading and the best route/mode of transport to get there. The concierge desks at any hotel are a great source of information and assistance.

Which local delicacy should I try?
Local favourite for meat lovers is definitely *biltong* and if you are able to visit the Grillhouse, have the *Boerewors*, a type of sausage, as the starter. ■