Catalyst

SA's quarterly Private Equity & Venture Capital magazine

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SEPTEMBER QUARTER 2021

Private equity finds (renewable) energy

PE builds antifragile companies

Date is the new leverage in buyouts

FROM THE EDITOR'S DESK

At the time of writing this note, just over half of the local government election's votes had been counted, but the predictions were being proffered by the psephologists, with high degrees of certainty that the ANC would see its share of the vote nationally fall below 50% for the first time in our young democracy's history.

In conversation with political analyst Moeletsi Mbeki, he characterised this as "the beginning of the end of an era" for the ANC. "For me as a businessperson," he stressed, "we now have an opportunity for new economic policies."

The bottom line is, can those coalitions that emerge post this local government election, and indeed into 2024, as is now being predicted, provide the kind of stable, better quality and more honest and responsive political leadership and government that the country is clearly yearning for? That is the big question.

The irony, according to Mbeki's incisive observation, is that business has increasingly leaned left of the centre of South Africa's politics.

"They are the ones who are very concerned about poverty levels; they are the ones who are casualties of the July riots. They want the population to be better housed, better fed, to become an effective real market for them," he points out.

It seems to me, though, that the country and the ANC have far bigger problems to worry about than who to form partnerships with, in which municipalities. The ANC is now facing a slow death as it is being abandoned by the black working class in the country's core commercial heartland of Gauteng. I suspect that the black middle and upper class in the private sector, who live in former white suburbs, are also not voting for it.

This leaves the ANC dependent on rural and urban poor, public sector middle and upper class, and traditional leaders. This is what happened to the ZanuPF, who eventually had to be kept in power by the army. Aren't these the real issues, rather than coalitions, that the country, and especially business, should be talking about?

Interestingly, Cyril is making the army more and more active and visible in national life. He had an army guard of honour at his inauguration, he uses it to police elections, to enforce lockdowns, et cetera. Maybe he and his advisors know something the rest of us don't know? ◆

Michael Avery

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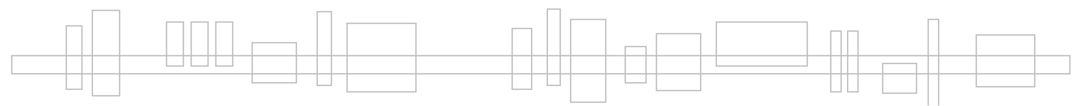


ITSMO of the same – as Eskom expects to miss DPE Roadmap date for transmission unbundling

Technically insolvent state power utility, Eskom, revealed in its 2021 integrated annual report that it is projecting to miss the target date for the proposed unbundling of its transmission division as part of the Department of Public Enterprises (DPE) Roadmap, which promised to oversee the unbundling of Eskom into three separate stand-alone businesses.

Tucked away on page 48 of the Report it states that"[r]egrettably, a number of delays are being encountered in preparation for the legal separation of Transmission. A number of dependencies are lagging behind, and this puts the finalisation of the separation by 31 December 2021 at significant risk. Guidance is awaited from DMRE regarding licensing and internal market operations of the Transmission entity. **At the moment, our projection is that separation will not be achieved by the target date**. Our intention remains to comply with the timelines set out in the DPE Roadmap, despite the obstacles encountered."

DPE's Roadmap sets out timelines for the restructuring of Eskom from a vertically integrated utility into an unbundled state, with three wholly owned separate legal entities in the form of Transmission, Generation and Distribution, as follows:

- Divisionalisation by March 2020
- Functional separation by March 2021
- Legal separation of the Transmission entity by December 2021
- Legal separation of the Generation and Distribution entities by December 2022

Eskom's debt remains unsustainable, attracting a net finance cost of R31,5 bn, turning an operating profit of R5,8 bn into a loss of R18,9 bn after tax. It reduced its gross debt by R81,9 bn – a 16,9% reduction – to an outstanding debt of R401,8 bn.

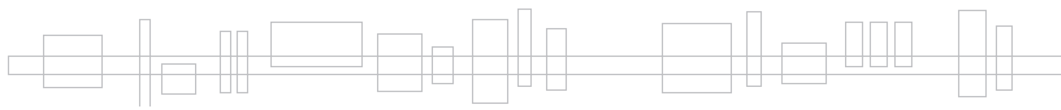
The utility's finances have been a binding constraint on economic growth since load shedding first started in 2008.

As part of the country's economic reconstruction and recovery in the wake of the pandemic, Busi Mavuso, CEO of Business Leadership SA, revealed that finance minister Enoch Godongwana told the Business Unity SA annual general meeting that the state was working to strengthen the security of supply, including the unbundling of Eskom into three separate units, while implementing a just energy transition towards a low-carbon economy. "These developments pose serious policy questions about the future of the electricity supply industry," he said. "This will effectively introduce competition in the sector."

The delay poses serious questions about the urgency with which government is trying to tackle the problem.

Anton Eberhard, a University of Cape Town (UCT)

Anton Eberhard



professor who heads its Power Futures Lab, called it "a very disappointing statement".

"I don't see any impediments around NERSA transferring the licence to a Transmission subsidiary," said Eberhard. "Of course, there are a number of issues around the internal market, for example, the novation of IPP contracts, setting up contracts with Eskom generators, etcetera, but one would have expected more progress on this by now."

It is a requirement, and key dependency, that bondholders and financial instrument holders approve any unbundling of Eskom.

While Eskom's Annual Report states that, "[b]ased on engagements with investors, they question the ability of the business separation to bring about financial sustainability for the company", Eskom bondholder, Futuregrowth says that it has not had any discussions with Eskom about the unbundling yet.

Olga Constantatos, Head of Credit at Futuregrowth, says it's not clear to her what is meant by "engagements with investors".

"Certainly, to our knowledge, Eskom's unbundling has only been discussed in results presentations and other general market updates. There has not, to our knowledge, been a specific engagement with investors to discuss any plans or proposals for the unbundling and the resolution of the debt problem, nor to discuss any concerns we may or may not have on these issues."

"The issue of negotiations with lenders is, of course, tricky," says Eberhard, "but not impossible. 106 countries around the world have unbundled transmission."

"Lenders, in general, look forward to a separate transmission company. It's a well understood, stable and easily regulated business with a predictable, steady income. What lenders are worried about is generation, which carries most of Eskom's debt. Again, we need more leadership and urgency in resolving these issues."

Olga Constantatos

"We welcome the idea of Eskom's unbundling as a move to a decentralised, competitive and efficient energy ecosystem for South Africa," says Constantatos, "but recognise that the detail of how this is done, and the allocation of assets, cashflows and debt to the generation, transmission and distribution subsidiaries is important to understand. The unbundling on its own is not going to restore Eskom to financial and operational sustainability – Eskom's debt problem needs to be urgently resolved, as well as its high cost base addressed, and these are key determinants of Eskom's return to financial sustainability. As regards the ITSMO unbundling – from an investor's perspective, we would need to have a degree of certainty that this entity is indeed

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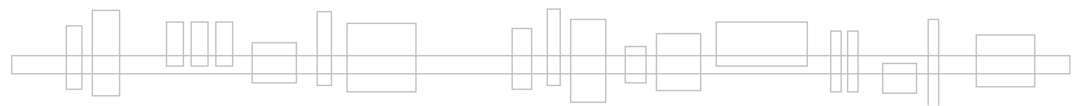


"independent" of Eskom – and that it will buy electricity on a least cost basis from any electricity generation provider, regardless of who the electricity generator may be – be it Eskom, an IPP or some other generation entity. We cannot have a situation where the ITSMO is favouring Eskom's generation capability as a means to 'cross subsidise' a sister subsidiary."

Eberhard points out that transmission accounts for roughly 10% of Eskom's total assets.

"It's really not a big deal, taking an Independent Transmission System and Market Operator (ITSMO) out of Eskom. Lenders will agree and welcome new opportunities for funding much needed new transmission assets," says Eberhard.

Constantatos says there are two concerns though.

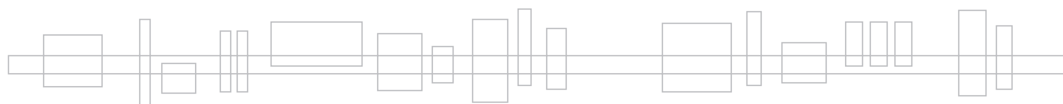
"The first is that any material transaction, and we would argue that fundamentally changing Eskom's operating model and group structure is material, that effectively strips assets and cashflows out of the entity we as investors have lent money to, has the consequence of degrading our investment and increasing our credit risk. There needs to be protection for our clients' money (the nations' savings) against this."

"The second concern is in the ITSMO's ability (or not) to buy electricity at the cheapest cost, regardless of the identity of the generator of that electricity. In a decentralised energy world, the generation of electricity would be done by any one of a number of entities (Eskom, the IPPs, big industrial companies that set up self-generation and sell back excess electricity to the grid etc) and the role of the ITSMO is to procure that electricity "blindly", as it were – on a least cost basis and with no preference to anyone. We cannot have a situation where Eskom's generation subsidiary is being subsidised by some sort of preferred arrangement with the transmission entity – that would be a conflict of interests; is inefficient. It goes against the very idea of decentralising the energy eco-system and providing electricity as cheaply as possible to the nation."

What does the Eskom bondholder make of this revelation of yet further delays around this critical unbundling process?

"To be frank, it is to be expected," says Constantatos in an almost nonplussed fashion. "We're used to plans and dates being published to much fanfare, and then experiencing significant slippage on the actual execution of the plans. This is a general problem and not isolated to Eskom. Furthermore, this is a complex matter requiring a cohesive and dedicated response, and likely requiring significant corporate finance, tax and legal advice. The unbundling is but one of the problems that needs to be solved – it goes hand-in-hand with resolving the debt problem which has not yet (to our knowledge) been meaningfully addressed with investors."

But, more generally, at a 'status-of-the-system' briefing in late October 2021, Eskom COO, Jan Oberhlozer, provided a worrying overview of the utility's poorly performing generation business. He acknowledged that Eskom's weak performance had already resulted in 32 days of load-shedding so far in the current financial year, a concerning trend compared with 47 days for the entire previous financial year. Eskom again emphasized that to eliminate load-shedding and stimulate the economy, there is an urgent need for additional capacity. But where are we going with all these promises and with Eskom's poor performance taking longer and longer to fix? It's a question that sits uncomfortably with an administration trying to sell South Africa to investors on a reform ticket. ◆



Revego stays private, for now

South Africa's power crisis was the subject of intense focus during another period of incessant rolling blackouts in October, as the economy started to open up from the pandemic induced lockdown levels.

But there is some light at the end of the dark loadshedding tunnel. Mineral Resources & Energy Minister Gwede Mantashe, who has been under fire, has breathed new life into the long delayed Renewable Energy Independent Power Producer Programme – six years have elapsed between bid window 4 and 5 – with the awarding of 25 new renewable energy projects that will deliver wind and solar energy at record low prices for the country. A further R50bn will be invested adding to the roughly R200bn that has already been invested to date.

However, the new projects will take roughly 36 months to deliver power to the grid and are therefore not expected to alleviate the supply shortfall any time soon. Once connected, they will add 2,583MW of capacity. Each stage of load-shedding is equal to 1,000MW.

The average cost for wind power was 49c/KWh and for solar 42c/KWh. The low prices put paid to any claim that renewable energy is expensive and that it is threatening Eskom's sustainability and costing customers high prices. Eskom's coal costs alone are 42c/KWh, excluding the cost of maintenance and refurbishment of power stations.

It is within this context of a reborn and growing renewable energy market – if the IRP is anything to go by – that the story of Revego Africa Energy Ltd. (this year's biggest IPO that never was) is a real loss not only for retail investors, but also the JSE, which sorely needs some IPO energy. It makes for a compelling investment case.

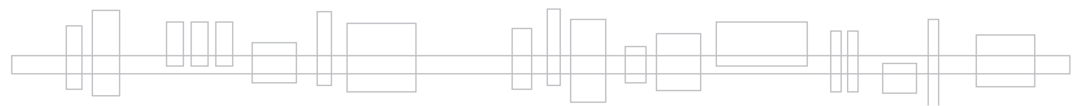
If we consider that renewables are set to lead the global electricity sector and that cost reductions and sustained policy support are expected to drive strong renewables growth beyond 2022, it is evident that we need to fast track wider liberalisation in Africa's electricity generation sectors. While governments can justifiably retain control over the transmission grid to ensure equitable access to electricity, Africa requires a favourable environment conducive to public-private partnerships that can bring additional generation projects online in a short period of time. Enabling policies and financing from the public and the private sectors, along with new business models, can work in tandem with official development finance to play a catalytic role in Africa's clean energy transition.

Catalyst sat down with Reyburn Hendricks the CEO of Revego Africa Energy (Rael) to talk about the listing false start and his vision for Revego.

Rael is the sole limited partner in the Revego fund, a private equity fund and is structured as an *en commandite* partnership, which is a yield-focused specialist BEE investment vehicle that will participate as an equity investor in, predominantly, operational renewable energy assets in sub-Saharan Africa (SSA), with a track record of generating stable cash flows.

"Effectively, a permanent capital vehicle with the aim of giving institutional investors long-term access to the underlying cash flows," explains Hendricks.

"The fund manager of the Revego fund is called Revego Fund Managers and they are responsible for sourcing deals recommending these to the investment committee, and the



ongoing management of the fund. Revego does have in its mandate the ability to invest a portion of its funds in development assets but, for now, it tends to operate in the secondary market and not the primary market."

It is for this reason that the fund offers an attractive dividend yield through a quality initial portfolio of assets that are currently operational, which lowers exposure to development risk.

The underlying investments are renewable assets in unlisted project companies, with minimum correlation to traditional asset classes. This provides a further diversification benefit to investors.

Ongoing economic expansion in the SSA region has made governments more aware of the need for increased electricity generation, leading to a shift towards attracting private investment.

With an increasing focus on the energy sector locally, the company is well placed to take advantage of opportunities, as electricity demand continues to exceed Eskom's supply capabilities.

Given the high levels of sunshine and wind throughout the year, coupled with vast open land, the SSA region provides great opportunities in the renewable energy space.

The fund's BEE status allows it to acquire stakes from BEE partners in these projects as well as other private equity players.

Hendricks says the targeted return is a 9% to 10% dividend yield with a yield to maturity or IRR in the range of 12% to 14%.

The secondary market is heating up for a host of reasons, from the primary investors looking to realise their investments after the initial three year lock in periods have expired, to funds like African Infrastructure Investment Managers, the Old Mutual Infrastructure fund, following their pre-emptive rights, Globeleq has entered the market and Hendricks says one is seeing some of the South African

"I think there are going to more players in time. Already through rounds 1 through 4 you've seen roughly R100bn capital raised in debt and equity has been allocated in this space and that is 6,400 MW and the IRP calls for approximately 20,000MW of renewables up to 2030 and that's excluding the 2,400MW in the RFIPPP (the emergency procurement process running parallel to the IRP)."
Reyburn Hendricks.

Reyburn Hendricks

construction firms sadly exiting their equity to raise liquidity to deal with their own balance sheet issues as a result of the broader construction malaise.

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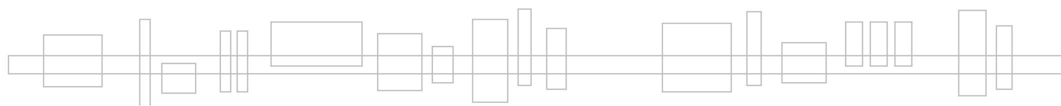
The cornerstone shareholders in Rael are Investec Bank, UK Climate Investments (UKCI) and the Eskom Pension Fund (EPPF) which have collectively committed R1,5bn to the fund already.



"UK Climate Investments also recently marked the delivery of its latest project in South Africa – Kruisvallei Hydro – a run-of-river hydropower facility which it part-financed alongside majority black-owned renewable energy investor, H1 Holdings," says Hendricks. "The project takes the total capacity of renewable electricity financed through the partnership in South Africa to 254 MW.

UK Climate Investments LLP is a joint venture between the Green Investment Group and the UK Government's Department for Business, Energy and Industrial Strategy. It forms part of the UK's aid-funded International Climate Finance, which is a UK Government commitment to support emerging markets and developing countries to respond to the challenges and opportunities of climate change.

Managed by Macquarie Asset Management and supported by the wider GIG team, UK Climate Investment's has committed approximately £70m of UK International Climate Finance over three years, to support the development of clean energy and green finance markets in sub-Saharan Africa.

UK Climate Investments fulfilled its cornerstone commitment of R500m (£25m) on the 18th of August 2021, to help establish Rael as Africa's first dedicated renewable energy yieldco.

And the fund manager has also invested in the fund to show skin in the game.

The fund acquired stakes in a number of leading wind assets in August, all of which are helping to build South Africa's clean energy future.

The acquisitions include the Mainstream wind assets, Loeriesfontein 2 Wind Farm, Khobab Wind Farm and Noupoort Wind Farm, situated in the Northern Cape.

Loeriesfontein and Khobab (completed in December 2017) each have capacity of 140 MW and Noupoort (completed July 2016) has a capacity of 80 MW. The assets were built as part of Bid Window 3 of the Renewable Energy Independent Power Producers Procurement Programme (REIPPPP), led by sponsors Mainstream Renewables SA, a leading developer of wind and solar PV projects.

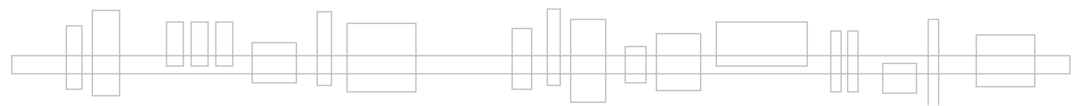
Eskom is the sole off-taker for all power produced by the three wind farms through a 20-year Power Purchase Agreement (PPA) as part of the REIPPP. The PPA is backed by the Government Support Framework Agreement (GSFA), whereby the South African government provides support to Eskom in an event of default.

Revego has purchased the wind assets from Metier, one of Africa's leading private equity fund managers, and Lereko, who jointly manage the Lereko Metier Sustainable Capital fund. The acquisition fits in with Revego's strategy to take stakes in operational renewable energy assets in sub-Saharan Africa that have a track record of generating stable cash flows, and that deliver an above-inflation dividend yield over an extended period.

John Hannig

Metier's Sustainable Capital practice targets investments in energy efficiency, renewables, water and waste management businesses, as well as projects supporting Africa's development objectives and environmental commitments.

"We are pleased to have played a part in three of the largest wind assets in South Africa and their contribution to building a thriving renewable energy sector in the country" said John Hannig, a principal in Metier's Sustainable Capital practice.



Revego's portfolio now consists of three wind and one solar asset, and it has secured a wind and a solar asset, all of which have 20-year PPAs with Eskom, thus providing the long-term, stable cash flows that investors seek. In addition to the three mainstream wind assets noted above, Revego's assets will include:

Aurora Wind Power – a 94MW wind farm located in the Western Cape, built as part of Bid Window 2 of the REIPPPP, and led by sponsor, Engie Energy International, one of the largest energy players globally, with extensive experience in developing and operating renewable energy plants. Aurora became operational in June 2015 and has a PPA with Eskom until June 2035.

Kathu Solar Park – a 100 MW concentrated solar power thermal energy project located in the Northern Cape. It was built as part of Bid Window 3 of the REIPPPP, led by sponsor, Engie Energy International.

The project became operational in February 2019, with a 20-year PPA, valid until February 2039.

Bokpoort CSP – a 50MW concentrated solar power (CSP) thermal energy power plant located in the Northern Cape. It was developed by Metier and built as part of Bid Window 2 of the REIPPPP, led by sponsors ACWA Power, one of the largest energy players globally with extensive experience in developing and operating renewable energy plants. The project became operational in March 2016 with a 20-year PPA, valid until March 2036.

"We are pleased to have rapidly built up scale within Revego in some of South Africa's most important renewable assets, and to be able to provide our investors with the basis to meet their sustainability and return goals," concludes Hendricks.

Hendricks reveals that the reason that the IPO, which was planned for April 2021, was cancelled at the eleventh hour was due to engagements with large institutions indicating that Revego had yet to achieve the sort of scale that would assuage any liquidity concerns that larger institutional investors were expressing reservations about.

But the interest from the market was substantial, according to Chantal Marx, who heads equity research at FNB Wealth and Investments.

Despite the risk of policy uncertainty and regulatory delays to the development of further power capacity in South Africa and in SSA generally, much of the company's success depends on the quality and cash-generating capability of assets acquired; therefore, the risk of making poor investments exists. However, with the quality of the team behind Revego, this is hardly a concern for the market, and investors will be eager to get their chance to invest in this exciting and growing new asset class, hopefully via a JSE listing in the not too distant future. ◆

What's Happening in M&A?

SA's top financial advisers & industry players weigh in.

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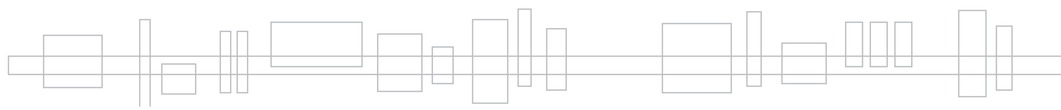


Four Quick Fixes to Spur SA's Entrepreneurial Growth & Job Creation

The recent meeting between President Cyril Ramaphosa and representatives from the South African entrepreneurial community, including start-ups, to discuss issues relating to enabling entrepreneurial growth, holds potential.

Alison Collier

By proactively reaching out to the community, our government is taking a positive step towards the goal of making South Africa a place where entrepreneurship is celebrated and encouraged, rather than being tangled up in red tape. It could also be the antecedent to unleashing latent growth potential and job creation in the economy.

While expectations regarding the implementation of a complete Start-Up Act should be managed – gazetting a new Act is a multi-year process – prioritising a few of the policy amendments proposed in this will achieve the majority of the impact and are implementable in a few months.

Indeed, government has proven that quick and radical change is possible. June's announcement that the threshold for private power generation is increasing from 1 MW to 100 MW caught the sceptics off guard, and a hopeful sign of more actions to come. Similarly, there are four interventions that the government could make that would constitute quick wins and big impact.

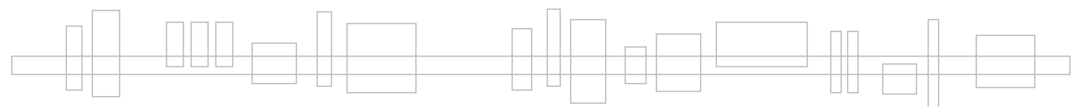
These four amendments are by no means the only remedies needed, but they could quickly mediate a number of problems that entrepreneurs and start-ups are experiencing, specifically those in the high growth, high impact, tech space.

1. Provide tax breaks and incentives to all VC investors – making SA the most attractive VC destination globally

Current macros aside, South Africa is far from the preferred destination for venture capital (VC) investors. One of the main reasons is because other countries offer investors massive tax breaks and incentives. South Africa needs to do the same to make us more attractive for VC investors, relative to the best start-up locations globally, such as the Netherlands, Ireland and the US (Delaware). Global VC liquidity is abundant, but South African VC has not been a prime recipient. Provide favourable tax incentives, and it will come.

2. Remove barriers that inhibit skilled talent nationals

These days, few countries can boast all the talent needed to build a company of international standards, especially in the tech space. While the vision is there for exceptional products, South African start-ups often require the skills and expertise only available from foreign nationals. By allowing a small number of highly skilled visas per company, South African start-ups can tap into international know-how



from markets that are far more developed than our own. We need a global 'ubuntu' mindset when it comes to talent.

Also, if a business is investing in local digital apprenticeships, then that business should be given a tax break. These digital apprenticeships are already happening on a small scale, and are helping to correct the digital skills gap in our country. Incentives can be a powerful way to address both youth unemployment and the digital skills shortage.

3. Right size the threshold for B-BBEE level 1 status to R100m

Under current circumstances, small businesses that surpass a revenue of R10m and/or R50m need to adhere to many of the B-BBEE codes, slowing their growth due to increased administrative complexity, amongst other burdens increasing their costs. This is particularly challenging for small businesses in their growth phase. To boost entrepreneurial growth, and thereby job creation, we propose that the government increases the revenue limit to R100m turnover for automatic Level I B-BBEE status.

Collier

4. Remove regulatory barriers that hamper globalisation

Currently, for many high-growth start-ups, there comes a time when the company's intellectual property needs to be moved overseas in order to maximise investment and growth. Recent loop structure reforms to exchange control have helped, but two concerns need to be addressed further.

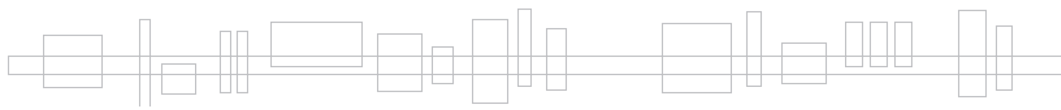
Firstly, the length of the process to find out if your company qualifies for the move takes too long – anything from three months to up to a year. Many VC firms that are contemplating investing simply cannot wait that long, which leaves many South African start-ups unfairly out of contention. The waiting period for qualifying start-ups must be no more than 30 days.

> "To boost entrepreneurial growth, and thereby job creation, we propose that the government increases the revenue limit to R100 million turnover for automatic Level I BBBEE status."

Secondly, when moving IP overseas, the asset is revalued after transfer, which triggers a capital gains tax. The revaluation doesn't mean that the founder is now cash rich, but it leaves him/her with a burdensome tax bill that is barely payable. This capital gains tax needs to be deferred to when the investment is eventually sold.

With these interventions noted by the Presidency during the meeting, alongside the open reception displayed in initiating the meeting, there are grounds for hope. The private sector must continue to organise itself to work with government and come up with very clear goals for the short, medium, and longer term. And whilst these suggestions may be quick fixes, the reality is that they can provide the medium and longer term secret economic ingredient – business confidence. ◆

Collier is Managing Director, Endeavour South Africa.



Private Equity and Venture Capital Regulatory Review

As part of its mandate the Southern African Venture Capital and Private Equity Association (SAVCA), engages with various regulators and policy makers advocating for changes to the regulatory, policy and legal framework with the objective of making South Africa a more attractive investment destination, as well as increasing the capital flows to private companies in Southern Africa.

Shelley Lotz

This is a snapshot of some of SAVCA's focus areas currently impacting the industry.

Twin Peaks Regulatory reform

As part of the wider Twin Peaks regulatory reform, National Treasury published the second draft of the Conduct of Financial Institutions Bill (COFI bill) which seeks to regulate the market conduct of financial institutions in South Africa. The legislative reform aims to harmonise the legislation and treatment of all financial services firms doing similar types of activities, irrespective of whether they are a bank, asset manager, insurer or private equity firm.

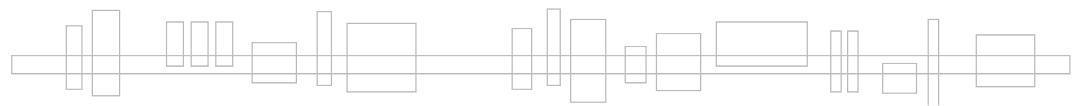
Lotz

The COFI bill, once enacted, is expected to have a significant impact on the private equity industry. Although the COFI bill is not yet finalised, it clearly indicates the regulator's intention in relation to all alternative assets. The explanatory policy paper accompanying the COFI bill clarifies that pooled funds currently regulated under the Collective Investments Schemes Control Act (CISCA), private equity funds and real estate trusts will be licenced under the COFI bill.

SAVCA provided detailed comments on the first and second draft of the COFI Bill, which were followed up by several engagements with National Treasury and the FSCA. SAVCA understands that there will be no further opportunity for public comment on the COFI Bill, and that National Treasury intends to submit the final Bill directly to Parliament for approval by the end of 2021.

Proposed amendments to Regulation 28

National Treasury issued proposed amendments to Regulation 28 for public comment together with an accompanying media statement on 26 February 2021. Regulation 28 is issued under the Pension Fund Act. The main purpose of Regulation 28 is to protect pension fund members from poorly diversified investment portfolios or portfolios which are considered too aggressive or risky. The key aspects covered in SAVCA's submission were as follows:



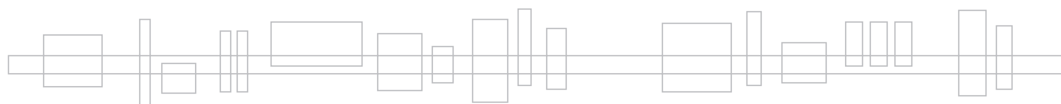
- SAVCA is supportive of the proposed delinking of hedge funds and private equity and increasing the maximum exposure limit of private equity to 15% as set out previously in SAVCA's Regulation 28 position paper.
- The accompanying media statement includes the detailed explanation of why the amendments were considered, and the rationale for the changes. It was, however, unclear how, the proposed changes to the legislation are supportive of these objectives in some instances, and if they will achieve the desired outcomes as set out in the media statement.
- The definition of infrastructure, as set out in the amendments, was limited to projects that form part of the national infrastructure development plan. This plan only includes public infrastructure. SAVCA proposed that the definition be expanded to include both public and private infrastructure, and discussed in detail the anomalies and uncertainty created as to what the amendments were trying to achieve.
- The other item causing confusion is that once infrastructure is defined, the overall exposure to infrastructure through the various asset classes is limited to 45% for domestic exposure and an additional 10% in respect of the rest of Africa. The limits appeared arbitrary and, as the exposure to infrastructure (however it is defined) is currently not monitored, the market cannot assess what impact the proposed changes would have.

2021 Draft Taxation Law Amendment Bill ("TLAB")

The 2021 Draft TLAB was issued for public comment on 28 July 2021. SAVCA's main concern in respect of the 2021 Draft TLAB was the proposal to 'restrict the off-set of the balance of assessed losses in determining taxable income' and the impact on SMME's and infrastructure projects. The stated purpose for the limitation on assessed loss utilisation is to broaden the tax base to cater for the anticipated lowering of the overall corporate rate in a tax revenue neutral manner.

"The other item which caused confusion, is that once infrastructure was defined, the overall exposure to infrastructure through the various asset classes is limited to 45% for domestic exposure and an additional 10% in respect of the rest of Africa. The limits appeared arbitrary and as the exposure to infra (however it is defined) is currently not monitored, the market cannot assess what the impact would be for the proposed changes."

Unfortunately, even with the attempt by National Treasury to introduce the assessed loss limitation in the least onerous manner possible, by limiting the assessed loss utilisation in a year to 80%, but still allowing the balance to be carried forward to the following year, would result in start-ups, SMMEs and infrastructure projects being disproportionately impacted. SAVCA included detailed comments objecting to this proposal, based on how it could impact South Africa's economic recovery plans, even post recovery, highlighting the detrimental impact it would have on start-ups and SMMEs and the increase in the cost of capital for infrastructure projects.



SA Start-up Act

The World Bank funded an initial position paper to start the consultation process for a South African Start-up Act (SUA) collaboration. The SUA is looking to provide a framework and legislative support for how start-ups, and scale-ups in particular, operate. It will focus on incentives and the removal of barriers for start-ups, including relaxation of Intellectual Property and exchange control restrictions. The SUA received a recent boost when industry collaborators were invited to engage directly with President Ramaphosa on this and other initiatives aimed at reducing the red tape for entrepreneurs and SMEs to help foster job creation opportunities.

SAVCA and its members are committed to increasing investment and job creation, and supporting South Africa's economic recovery. SAVCA invites policymakers/regulators to attend SAVCA events, and would welcome collaboration to achieve SA's growth ambitions. ◆

Lotz is Head of Regulatory Affairs at SAVCA.

Pandemic evidence that active ownership by private equity helps to build antifragile companies

Private equity investment in South Africa is poised for an exciting few years.

The COVID-19 pandemic, and the unprecedented disruption it has caused, has provided a compelling case for how the active ownership model practised by private equity investment managers can help good companies emerge 'antifragile'.

This is the view of Jacci Myburgh, co-head of Old Mutual Private Equity (OMPE), part of Old Mutual Alternative Investments, who says that the pandemic provided evidence that sound strategy and effective management cannot be overemphasised when navigating a crisis. "While the terms resilience or robustness are considered antonyms of the word fragile, relating to a company's quality to resist shocks or disruption, antifragile companies emerge stronger," he says.

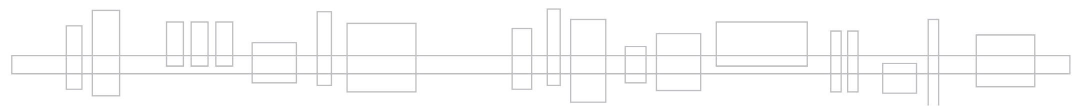
A term coined by Nassim Nicholas Taleb in 2012, "antifragile" companies gain strength from stressors thanks to their leadership's ability to learn, grow, strategise, and execute, explains Myburgh. "Supporting, guiding and counselling company leadership teams is precisely where the active investment approach adopted by private equity managers creates the most value," he says.

While private equity managers don't interfere operationally, they work with management to craft a clear strategy that outlines how a business will compete in a particular market or under certain conditions, he says.

Myburgh experienced this first hand in 2020 when some of Old Mutual Private Equity's most significant investments were severely impacted by the hard lockdown imposed to curb the spread of COVID-19.

"Private equity managers had the immediate advantage of seeing how the impacts of the lockdown and pandemic were playing out across many different portfolio companies," explains Myburgh. "As a result, we were able to develop a sort of playbook to support the company leadership teams across various sectors.

"This involved securing the safety of people, managing costs and working capital responsibly



and engaging with important stakeholders such as lenders and landlords, for example."

At one stage, Myburgh says OMPE was holding urgent board meetings with management teams twice a week. "What the team learnt is that the active ownership model works best in periods of crisis," he says. "COVID forced our management teams to implement sometimes drastic measures – like cutting product inventory by half, for example – to survive."

Myburgh says that this is in sharp contrast to listed companies in the public market, which only meet with its board four times and shareholders twice a year. "Our advantage was acting quickly and decisively, based on current information learnt from across the portfolio, allowing our businesses to weather the crisis very well."

He says that this approach naturally translates into significant results for investors of private equity. "Unlisted equity is proven to outperform listed equity over the long term, evidenced across various markets.

"Rather than trying to elevate private equity over listed, we would argue that allocating a portion of a portfolio to this alternative growth asset class helps to diversify investment risk and smooth out volatility over the long term, over and above the return premium that it offers," says Myburgh.

Given the medium-term outlook of a more stable political and economic environment and a balanced supply of capital, Myburgh is optimistic about the outlook for private equity over the next five to 10 years.

"We don't need the economy to grow at four or five per cent for private equity to do well – one or two per cent will suffice," he says.

Add to this the fact that foreign investors are looking to South Africa for new growth opportunities, and Myburgh's belief that "we are in for an exciting phase in the private equity space," provides an optimistic outlook for what has been a tough few years for the industry. ◆

Data - the new leverage for buyouts

Four years ago, The Economist grabbed our collective attention with the headline: *'The worlds' most valuable resource is no longer oil, but data'.*

Chelsea Wilkinson

Accompanied by an image of oil rigs bearing the logos of Facebook, Google, Amazon, …, we all intuitively nodded our heads.

Sure. Big data was big business for big business.

And then, we went back to our day jobs!

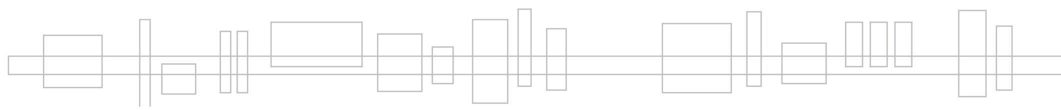
But the reality is that data is everyone's business, big and small. None more so than in the private equity sector.

Yet, on the face of it, GPs have been slow to harness the transformative power – and value – of data and advanced analytics. However, momentum is building, driven by heightened competition for capital, deals, regulation, and reporting requirements. Plus, of course, the quest for alpha.

What are the benefits of advance analytics and data science for GPs?

Clearly, there are many approaches and tools which can improve the operations of GP themselves: from origination to due diligence to investor reporting.

For example, EQT Ventures (the venture arm of Swedish parent EQT Partners) have built a



proprietary machine learning platform to support their origination. Aptly named 'Motherbrain', it pulls the structured and unstructured data of over 10 million companies, from multiple sources, into a centralised system – enabling deal and operating teams to identify patterns and themes useful to target investments. Motherbrain has been pivotal in the sourcing of several successful investments, including Peakon, which EQT Ventures sold to Workday for US$700m earlier this year.

Likewise, many GPs are using advanced analytics within their due diligence, to assess a target company's organisational capabilities, customer behaviour, product portfolios, and brand awareness as they seek pre-deal valuation validation.

Furthermore, as more companies and Information Memorandum claim: *'proprietary AI-backed decision making'* and *'advanced automation'* – savvy investors are also diving more deeply into the data ecosystems, datasets, and algorithms themselves to determine reality – and then pricing and value creation strategies.

During these deep-dive data due diligences, prospective investors are asking the killer question: *How effective is the target company at leveraging data and analytics to power its business and operational models?*

Portfolio company optimisation & value creation through data

Data – be it a client list, production line feed, vehicle tracking application, ERP, inventory, or workforce management system – can frequently be leveraged beyond its current use, thanks to data-science techniques. For many private equity-owned businesses – which have been heavily optimised using traditional operating methods – leveraging this data might very well be their 'last mile' in efficiency.

And I use the word *'leveraging'* deliberately. Because opex or capex or both have typically been spent implementing the incumbent system and collecting the data. So, the *leverage* here is that you are using the same data again, just for a different purpose[1]; there's a compounding effect.

In fact, this is one of the extraordinary characteristics of data (as opposed to other assets) – it can be used again and again, without deteriorating or depreciating. In fact, its value multiplies with each new use and use case.

Of course, it's easy to assume that these *mystical* datasets and *alchemic* data-science techniques are the exclusive domain of sexy start-ups or the deep-pocketed giants on our Economist cover. But the benefits hold true for *traditional, analogue* business, too. Arguably, the multiplier potential is greater and value extraction opportunity higher!

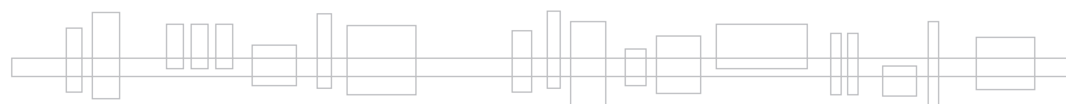
It's revelations like these which normally persuade management teams to cross the *analytics chasm:* shifting from traditional, business intelligence outputs (such as rear-view-mirror reporting) to predictive, data-led insights that can optimise operations, enhance top-line performance, and sharpen competitive edges.

Start with the business problem, not the data

Nonetheless, delivering data's value is hard. Gartner research tells us that 80% of data projects are failing.

One of the chief tactics to avoid becoming this statistic is to *tightly* link data-science projects to the portfolio company's business strategy and KPIs, via a data strategy. At a high level, this strategy must frame:

1. **The Busines problem** – for example: a SaaS business' problem might be to increase ARR
2. **The Analytical solution** which solves it – in our SaaS example, this might be a combination of churn, cross-sell and upsell modelling
3. **The Data sources and resources** required – which might be (i) SalesForce and online customer behaviour data sources, and (ii) domain experts from the portfolio company



sales and marketing teams, plus data scientists to build the analytical models
4. **A well-defined roadmap** – comprising the infrastructure, investment required, quick wins, decision making forums, and success measures.

One of the most sophisticated data-science-led GPs, UK-based HG Capital, has published a case study which powerfully demonstrates the outcomes gained by SaaS portfolio company Access, following the roll out of just such a cross-selling algorithm. After only four months, the project delivered a 25% increase in sales pipeline creation and 30% lift in sales conversion – resulting in a 60% uplift in converted sales orders.

Of course, results like this are never guaranteed. But you'll be considerably closer to achieving them if you link your portfolio company data projects to business outcomes.

This is the true unlock of data.

Building data & advanced analytics capabilities

It's true, HG Capital have over 30 in-house data scientists embedded into their investment team! I concede that most GPs don't have the capacity to build such internal capability. Rather, many firms are testing the analytical waters by using specialist data science consultancies to build out their proof-of-concept projects and manage the medium-term outputs, whilst transferring skills.

However, GPs *do* need to build the skill base of their teams to embrace and embed these new techniques.

After all, consider the new data opportunities arising from (radically) accelerated digital transformation at portfolio companies, following the COVID pandemic. As business models were disrupted and digitally recast, IT systems and customer platforms morphed – almost overnight.

And what do all these digitally evolved systems and processes have in common?

They facilitate the collection and curation of more and more data. Meaning, as the volume, velocity, variety, and veracity of company data increases, so does its potential value.

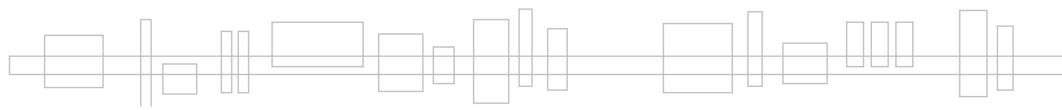
So, assess it. And realise it. ◆

Wilkinson is Co-founder | DataDiligence

1 (You're not having to pay for it twice – though you may require new investment into a data infrastructure and skills).

PRIVATE EQUITY DEALS Q3 2021

NATURE	PARTIES	ASSET	ADVISERS	ESTIMATED VALUE	DATE
Investment by	Nedbank, Investec and Compass Venture Capital, with new investors Technova, Grand Bay Ventures, Tahseen Consulting and Kepple Africa Ventures	in Omnisient		$1,4m	Jul 6
Acquisition by	RMB Corvest (RMB Holdings)	equity interest in Insulation Thermal Acoustic Security (ITAS)		undisclosed	Jul 13
Acquisition by	Imbani Private Equity	a stake in Insulation Thermal Acoustic Security Company (ITAS)		undisclosed	Jul 13
Investment by	Enygma Ventures	in Koa Academy		R4m	Jul 14
Acquisition by	Standard Bank from Liberty minority shareholders	remaining 46,3% stake in Liberty plus all preference shares	Merrill Lynch; Standard Bank; Goldman Sachs; Investec Bank; Simonis Storm; Bowmans; Webber Wentzel; Davis Polk & Wardwell London; EY; PwC; KPMG	R10,71bn	Jul 15
Investment by	Expert DOJO, Oui Capital, Basecamp Fund, Soma Capital, Hustle Fund, Future Africa, LoftyInc and some angel investors	in Akiba Digital		$1,1m	Jul 16
Investment by	Launch Africa	in Strove		R4m	Jul 16



PRIVATE EQUITY DEALS Q3 2021 (Continued)

NATURE	PARTIES	ASSET	ADVISERS	ESTIMATED VALUE	DATE
Disposal by	Ascendis Health SA (Ascendis Health) to Acorn Agri & Food	Animal Health Division (Ascendis Vet, Ascendis Animal Health, Kyron Prescriptions)	Absa CIB; Questco; ENSafrica; Webber Wentzel; Werksmans; PwC	R770,19m	Jul 19
Investment by	Knife Capital and Allan Gray E-Squared Ventures	in Kandua [pre-series A]		undisclosed	Jul 20
Acquisition by	Legacy Africa Capital Partners	a 60% stake in Penflex		undisclosed	Jul 21
Investment by	Enygma Ventures	in Feelgood Health		R4m	Jul 21
Acquisition by	Naspers Foundry (Naspers)	investment in Ctrl		R34m	Jul 22
Disposal by	Property Lodging Investments (City Lodge Hotels) to Ukarimu (Actis Africa Real Estate 3 LP)	Hotel portfolio in Kenya consisting of the Fairview Hotel, City Lodge Hotel at Two Rivers and The Tomn Lodge Upper Hill	Nedbank CIB; ENSafrica Kenya	R140,97m	Jul 23
Disposal by	City Lodge Hotels Africa (City Lodge Hotels) to Faraja (Actis)	City Lodge Hotel Dar es Salaam, Tanzania	Nedbank CIB; ENSafrica Kenya	R319,22m	Jul 23
Investment by	Lireas Holdings, the ASISA ESD Fund, E4E, Vunani Capital and the Old Mutual Enterprise & Supplier Development Fund	in Pineapple [Series A]		R80m	Jul 26
Investment by	Dragoneer Investment Group, Breyer Capital, HOF Capital, The Raba Partnership, 4DX Ventures, TO Ventures plus existing investors Partech, Velocity Capital Fintech Ventures, Orange Ventures and Quona Capital	in Yoco [Series C]		$83m	Jul 27
Acquisition by	Imperial Capital (Imperial Logistics) from CSSAF Holdings I (The Carlyle Group), IAFPEF JJ (Ethos Private Equity), Lift Acquisitions, ITL Trustees and founders, certain individuals and key management	51% stake in J&J Group	Rand Merchant Bank; Tugendhaft Wapnick Banchetti; Webber Wentzel; Nortons	R988,5m	Jul 29
Investment by	E Squared Investments	in Khula		undisclosed	Aug 3
Investment by	Edge Growth and the ASISA ESD initiative	in I-G3N		R20m	Aug 3
Acquisition by	Naspers Foundry (Naspers)	investment in Naked		R120m	Aug 4
Investment by	Founders Factory Africa plus some angel investors	in My Health Africa Group	Stratlink	undisclosed	Aug 4
Investment by	The Delta	in Revio		R15m	Aug 5
Joint Venture	Absa Bank (Absa) and African Rainbow Energy and Power	African Rainbow Energy	Absa CIB; UBS; Bowmans	R6,5bn	Aug 6
Investment by	Seed South	myFanPark		undisclosed	Aug 19
Acquisition by	AIH Limited	Kwikspace Modular Buildings		undisclosed	Aug 19
Investment by	Verge Healthtech Fund and angel investors	in VitruvianMD		undisclosed	Aug 20
Acquisition by	Gridworks and New GX	a stake in Sustainable Power Solutions Investments	Webber Wentzel; Addleshaw Goddard; DLA Piper	$22m + $18m	Aug 23
Disposal by	Bidvest Financial Services (Bidvest) to Seriti Capital Partners	Cannon Asset Managers		undisclosed	Aug 31
Acquisition by	African Infrastructure Investment Managers, a member of Old Mutual Alternative Investments (Old Mutual) from Amethis	22% stake in Sodigaz APC		undisclosed	Aug 31
Disposal by	Grindrod Property Private Equity (Grindrod) to Gripon	entire holding in Select Industrial Real Estate UK Fund	Nedbank CIB	£17,39m	Sep 6
Acquisition by	Amethis	a minority stake in Avacare		undisclosed	Sep 9
Investment by	Illumina Accelerator	in BixBio		undisclosed	Sep 15
Acquisition by	One Thousand & One Voices (1K1V)	a minority stake in Digital EcoSystems (DigiCo) [DNI Group]	EY	R200m	Sep 30
Disposal by	Capital Eye Investments to Smollan Group SA	its entire stake in Argility	Cliffe Dekker Hofmeyr	undisclosed	not announced Q3
Acquisition by	Africa Forestry Fund II	an additional stake in Vuka Timbers [will acquire control]	Werksmans	undisclosed	not announced Q3