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# Catalyst

**Actis: Boldly into Africa**

**SA private equity breaches R100bn**

**Accurate valuations needed now more than ever**

**TouchStone Resources' electrifying prospect**

**SA's Private Equity & Venture Capital**  
**magazine**



## From the Editor's desk

The second quarter of 2009 ushered in the eagerly anticipated KPMG and SAVCA: *Venture Capital and Private Equity Industry Performance Survey of South Africa* covering the 2008 calendar year. Expectation in the market was that deal flow and value numbers would show a dramatic decline. However, and to the collective sigh of relief of many within the industry, the numbers weren't all that bad.

South Africa's private equity industry penetrated the R100bn mark for the first time during 2008. In addition, R29,2bn in commitments remain undrawn and can be used for further investment.

Another positive can be drawn from the significant growth in BEE private equity deals from R11,8bn in 2007 to R16,3bn in 2008, an increase of 38,1% from 2007.

Considering the dearth of the large public-to-private deals, as seen in 2007 (for example: Edcon, Alexander Forbes, Primedia and Consol), it came as no surprise to see private equity investments falling in 2008 from R26,1bn in 2007 to R21,3bn in 2008.

More worrying though must be the

decrease in fundraising from R15,4bn in 2007 to R7,2bn in 2008. This is a trend that looks set to worsen according to Peter Schmid (see Actis Profile p1).

Schmid issued a cautionary warning saying that the local industry would struggle during the next round of fundraising and that the subsequent shakeout would forever alter the private equity landscape in South Africa.

And this alarming trend is being experienced worldwide. A recent report published by McKinsey Global Institute, entitled *The new power brokers: How oil, Asia, hedge funds, and private equity are faring in the financial crisis*, makes for sobering reading.

McKinsey found that "Funding for the 'megadeals' (greater than US\$3bn) that accounted for most buyouts has disappeared. And new fundraising has dried up as private equity investors assess their portfolio losses and face large capital commitments to the industry."

McKinsey's base-case scenario sees total private equity industry assets under management rise to US\$3,4 trillion in 2013,

at a compound annual growth rate of 4%. However, the report goes on to note that assets under management of leverage buyout funds will decline from 1,2 trillion to \$1 trillion over the same period. Therefore, buyout funds will represent a shrinking share of the global industry's total assets under management over the next five years, decreasing from 44% in 2008 to less than 30% in 2013.

McKinsey isn't all doom and gloom, however, and offers some words of encouragement for the industry as a whole.

..."[T]he rest of the private equity industry is retooling and evolving, seeking opportunities in new forms of investment and in new regions. Therefore, while buyout funds' influence will wane, the broader private equity industry will grow."

Looking ahead, SAVCA, in conjunction with the DBSA, is conducting an economic impact assessment of the South African private equity industry. The survey is due for release in August and industry insiders and analysts will be awaiting the outcome with keen interest.

## Catalyst

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## Profile

**Emerging markets focused private equity house, Actis, last year walked away with the DealMakers/Catalyst Private Equity Deal of the Year award for its R5,16bn acquisition of Alstom South Africa.**

# A pure private equity player

**Catalyst** caught up with the Head of Actis's Africa private equity business, Peter Schmid, to gain an insight into the industry leader's African investment philosophy and strategy during times of economic uncertainty.

Schmid doesn't mince his words when it comes to assessing what makes Actis so successful in Africa and other emerging markets. He stresses the importance of local knowledge and presence along with a strong sectoral focus as the key drivers underpinning successful emerging market investments.

"Our strategy has been, first, to become a pure private equity player. Number two, we've got a third party fund model."

Actis's main offices are based in Johannesburg ("our hub"), Lagos, Nairobi and Cairo and it covers the Maghreb region which is Morocco and Tunisia. These regional centres represent Actis five major areas of focus from which it can assess deal opportunities across the African continent.

"And this ties into our key differential," explains Schmid, "and that is on-the-ground

presence. We just do not believe that you can execute private equity deals if you are not on the ground. We've seen some of our competitors do that and we've seen the deals they're doing and if they knew what we knew, they wouldn't be doing those deals."

Particularly, for Schmid, "it's all about the people you partner with. Unfortunately you can't build that skills base overnight but we've inherited some good people and we're fortunate for that considering it takes about ten years to be able to train someone to operate at that level especially when dealing with the complexities of the African market."

The other aspect of private equity that Actis has executed differently is its ability to deliver and leverage off its sector focus on its investments. "The world is changing, deep knowledge and experience are now able to add value and to access global best practice is going to be the future of private equity."

"We're focusing on four key sectors. Number one is financial services, second is the consumer markets with the huge and growing middle class in Africa, China, India and South America – I often travel to South America and I can see very similar trends that are happening there as well as South East Asia. Third, is industrials and fourth is business services."

It is interesting to note that the sectors Actis focuses on are common to all these markets.

"There is a huge amount of overlap between these geographically diverse markets," comments Schmid. "I've just had a delegation from China here in South Africa and we are constantly talking to people out of India and Brazil. What's great about our network is that we are able to facilitate this exchange of knowledge, particularly to the benefit of our portfolio companies."

"When we do deals now we bring in the sector experts; they help us assess the busi-

ness, advise the management and we try and get them to sit on the board. It's about being able to introduce the local businesses with the right partners, which is critical. We feel this is great for Africa because it's all about global competitiveness and there is no reason Africa cannot compete on the world stage," Schmid says confidently.

**"... because it's all about global competitiveness and there is no reason Africa cannot compete on the world stage"**

## Fund raising and returns

The South African private equity market appears increasingly twitchy about the next round of fund raising. The mood of a conversation can move quickly south when the issue is broached. But Schmid exudes a bullish optimism for Actis's prospects for the next round of fund raising. This is partly due to a spot of prescient timing as Actis managed successfully to close its US\$2,9bn (R30bn) private equity fund, Actis Emerging Markets 3 (AEM3), before the funding taps ran dry – this was one of the largest dedicated emerging markets private equity funds closed in 2008 and doubles the amount raised by Actis in 2004.

"We were fortunate with the timing of our last fund," admits Schmid, "but I also think that we were offering a compelling investment case as investors were looking



Peter Schmid

to get into emerging markets at that time [just before the wheels came off the global economy].

"Emerging markets are risky but that's where growth is and if you can get a diversification of currencies, countries and sovereign risk then you start to offer a compelling invest scenario."

Schmid says Actis is seeing a very different impact across the various markets in which it operates. "China's consumer industry is starting to recover and so is India, whereas in Africa we are expecting a very tough six to twelve months ahead so we are lagging behind the fallout. Brazil also seems to be recovering while Southeast Asia is also still in the doldrums.

"In other words if we can offer an investor a diversified portfolio they can cherry pick the best deals. When you combine all these factors you have a critical mix that will provide top quartile returns."

*What can private equity investors expect these returns to be now that earnings are plummeting and fear stalks the global economy?*

"Globally, I'm told that LPs [Limited Partners] in the developed world are saying that they will be happy if they just get their money back from the funds they invested in during the last round of fund raising – the 2006 to 2008 funds which most of the private equity houses had as their last funds raised. This will represent top quartile returns for them.



Ngozi Edozien

"My view is that any private equity fund that is going to generate a net 15% return in dollars is going to be in the top performers and that is the target that we are looking at. And I think that the emerging

market funds have definitely got a better chance of achieving that."

Schmid is still concerned about the impending fallout from the credit crash of 2008 and sounds a word of warning to private equity houses that times will get tougher.

"The LPs are very cautious at the moment and the real problem for follow-on fund raising is that there is just no dry powder available for investing. Unfortunately, that affects most of the South African funds and that's not great for private equity and this will most likely lead to a huge fallout because there is just no capital available."

### Changes in West Africa

Actis has recently appointed a new Head of its West African operations. This was an exhaustive process, says Schmid, in order to find the perfect fit for the unique challenges that accompany the position.

Ngozi Edozien joins Actis from her position as the founding CEO of the Equity Vehicle for Health in Africa, established in April 2008 and co-funded by the IFC, the AFDB, the DEG and the Gates Foundation. She replaces Simon Harford, who will move to Johannesburg as the Head of Actis's growing Portfolio Group for Africa and Latin America focusing on Actis's value-add to its portfolio of investee companies.

Edozien will be responsible for all aspects of Actis's private equity business in West Africa including the day-to-day management of Actis's existing investments as well as the development of new investment opportunities in the region. Actis is currently invested in a number of companies in West Africa including: Diamond Bank, Mouka Foam, UAC and Exoro (Seven Energy). In addition, the firm has real estate assets in Ghana and Nigeria as well as infrastructure interests throughout the region. Edozien will report to Schmid.

"Ngozi brings exactly the right mix of experience, drive, insight and regional knowledge that Actis needs in West Africa – her father is a local chief for example. As a critical cornerstone of Actis's pan-Africa network, we see considerable opportunity in this market for us to partner with successful, growing and sustainable private sector businesses in order to deliver benefits to local stakeholders. We are delighted that Ngozi has joined the team. She is ideally positioned to build on the great work done by Simon over the last 3 years."

Edozien started her professional career in investment banking with Solomon Brothers and JPMorgan in New York. She worked for McKinsey & Co. from 1992-1999 in London and Paris, and then joined Pfizer in their US headquarters as Vice-President Strategic Planning and Business Development from 1999-2004. After which, she then moved to Lagos as Pfizer's Regional Director for Anglophone East, West and Central Africa and Managing Director of Pfizer Nigeria from 2005-2008. Edozien holds a BA Honours in Social Studies from Harvard and Radcliffe Colleges, Harvard University and an MBA from Harvard Business School.

Harford will take up his new responsibilities in Johannesburg at the beginning of August.

### Still doing deals

Though most local private equity houses have been fairly quiet on the dealmaking front this year, Actis is powering ahead with the most recent announcement of its US\$244m acquisition of shares in Commercial International Bank (CIB), the leading bank in Egypt.

"CIB is a fascinating business. It's Egypt's leading independent commercial bank and there is an enormous amount of work being done. We're co-investing as part of the Ripplewood consortium run by the renowned Tim Collins from the US," explains Schmid.

Actis is acquiring 50% of the stake held by the consortium making Actis the largest single investor in CIB.

"They [Ripplewood] have done a great job in transforming that bank and bringing global best practise and they are just about to roll out their retail strategy so we hopefully bought in at near the bottom of the cycle. And more importantly they have now got huge growth prospects coming through.

"What's very interesting and just to use as an example of Actis leveraging off the strength of our sectoral focus, we're a major shareholder in the Diamond Bank in Nigeria and we are flying a delegation from Diamond Bank to CIB in order for them to get experience of Diamond's world-class risk management systems," concludes Schmid. ♦

**This transaction was announced in July. Catalyst will take a closer look at the CIB acquisition in the third quarter issue.**

**The results of the KPMG and SAVCA 'Venture Capital and Private Equity Industry Performance Survey' for 2008 concluded that the South African sector remains stronger due to ongoing infrastructure spend and limited 'exposure' to global financial markets**

## Private equity shows growth despite economic down-turn

South Africa's private equity industry breached the R100bn mark for the first time during 2008, despite the global economic meltdown and a slowdown in local merger and acquisition activity. In addition, R29,2bn in commitments remain undrawn and can be used for further investment.

Growth in BEE private equity deals grew 38,1% from R11,8bn in 2007 to R16,3bn in 2008.

These are some of the findings of a joint KPMG and SAVCA (South African Venture Capital and Private Equity Association) survey into the private equity sector released in May.

Private equity has attracted Foreign Direct Investment (FDI) into South Africa, amounting to R23bn over the last three years.

Taking into account the absence of the large public-to-private deals, as seen in 2007 (for example: Edcon, Alexander Forbes, Primedia and Consol), it came as no surprise to see private equity investments falling in 2008 from R26,1bn in 2007 to R21,3bn in 2008. Fundraising also decreased from R15,4bn in 2007 to R7,2bn in 2008.

"These figures are a positive reflection on the achievements of the SA private equity industry," says Warren Watkins, KPMG's head of private equity markets for Africa. "Though SA is not immune to developments in the global economy, we currently appear to be better off than other private equity markets. This could be due to SA's ongoing infrastructure spend and limited "credit crunch" exposure."

Notably, the KPMG/SAVCA Survey also found that funds valued at R68,6bn were under the management of cap-

tives-government or entities that are either black owned, empowered or influenced. This is up 16,3% from R59bn in 2007.

The private equity sector maintained a lingering exuberance from 2007 through the first half of 2008 and then became more subdued in the second half. The net result was overall growth of 19,5% on R86,3bn held at December 2007 to R103,1bn.

There is reason for cautious optimism for South Africa, says Watkins, in particular with respect to the prospect of lower interest rates arising during 2010, and the forthcoming FIFA 2010 Soccer World Cup.

"The scale of activity in our industry continues to outperform most of the major international economies, which bodes well for South Africa's government stated growth targets, as local and international research confirms that private equity investment is a key driver of entrepreneurial activity and growth in any economy," says J-P Fourie, SAVCA executive officer.

The survey has found that South Africa's funds under management (excluding undrawn commitments) relative to GDP of 3,2% were higher than 2007 and again greater than the global average of 2,7%.

This is the tenth year in which KPMG and SAVCA have produced the private equity survey.

Funds under management were R30,7bn in 1999, with R103,1bn reported in the current survey. This represents an impressive 14,4% compound annual growth rate.

South African private equity houses should be buoyed by the Survey results as Preqin, a global alternative investment



Warren Watkins

research firm released results for the global private equity industry that paint a far bleaker picture.

The private equity industry suffered its worst year on record in 2008, as its investments lost almost 30% of their value, according to Preqin.

One-year returns for the private equity industry fell 27,6% last year, far more than the 9,1% drop that the industry suffered in 2002 after the dotcom bubble burst, said Preqin.

The stark drop in performance, which contrasts with a one-year gain of 26% at the peak of the market in 2007, may also reflect a recent tightening up of accounting rules for private equity groups, forcing them to use fair market value for investments. ♦

**For the full survey visit  
[www.kpmg.com](http://www.kpmg.com) or  
[www.savca.co.za](http://www.savca.co.za).**



**As an industry blossoms so does the amount of attention it receives. That's what the private equity industry is busy finding out. The South African private equity industry is at an all time high with capital commitments to funds passing the R100bn mark<sup>1</sup>**

## Do uncertain times mean uncertain valuations?

### Rory Ord

This increase in industry profile has brought more than just asset inflows. This growth, combined with the international financial crisis, has brought increased scrutiny of actual fund investments, particularly their carrying values and leverage levels.

The very nature of private equity fund investments is that they are not, as the name implies, publicly traded. Unlike listed investments, the prices of unlisted investments generally made by private equity funds (PE funds) are not quoted on a stock exchange, making it difficult for investors to assess accurately the value of the portfolio companies.

**PE funds have historically valued their investments infrequently: at best quarterly and at worst annually for the fund's statutory audit**

At the time of entry into a new investment, PE funds devote considerable time and resources performing due diligence and assessing market conditions to determine a price they are willing to pay. Since this process is a market

transaction, and often competitive, with several funds bidding for the investment, entry price is generally considered to be a fair market price at transaction date.

However, after the entry date a PE fund will generally hold an investment for approximately three to seven years before exit, depending on the type of investment and market conditions. This leaves a long period between entry and exit where the PE fund manager must regularly determine a market value to report to investors. In South Africa, most PE funds subscribe to the International Private Equity and Venture Capital Valuation Guidelines (the Guidelines).

The Guidelines recommend several valuation methods, as well as the circumstances under which each method is appropriate. The Guidelines aim to establish a fair value for each investment at each reporting date, and therefore encourage the use of market-based methods.

Even in less uncertain times, the application of a valuation method is time-consuming and requires discretion from the expert assessing the PE fund's investments. As a result, PE funds have historically valued their investments infrequently: at best quarterly and at worst annually for the fund's statutory audit. The time-consuming process of valuation typically results in a two-month time lag from reporting date to the time when valuations are complete and reported to investors. PE fund managers must allocate significant resources away from sourcing new deals and managing the existing portfolio to the valuation

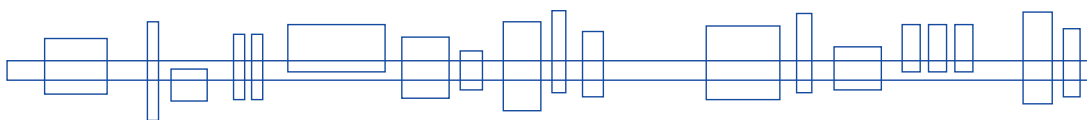


Ord

process each quarter.

Some fund managers are working to address this issue by outsourcing the valuation process to third party experts with the capability of running more frequent and objective fund valuations, and without being distracted by the need to manage the fund itself.

PE fund investors have varying levels of interest in the values reported to them by fund managers. High net worth individuals often take the view that the investment in the fund is illiquid and the only important values are those realised on exit. However, an institutional investor or pension fund must provide regular, accurate fund valuations to their own investors or unit holders to facilitate member entry and exit, and, therefore, need to rely on accurate and up-to-date valuations. If, for example, the valua-



tion recognised by a pension fund is too high, members exiting the pension fund will benefit, while the remaining members and new entrants will lose out. A regular fair value gives fair treatment to all members as the ultimate investors in private equity.

This leads institutional investors to push PE funds to report valuations more regularly to reflect better the value of their portfolios for members. This is particularly important during times of greater market volatility when significant movements may occur in a short space of time.

For example, consider the events of last October, when the JSE All Share Index fell more than 11%. While the movement of the listed equity market does not mirror private equity returns, this fall would have been of concern to all investors. During the time lag between these types of events and the reporting of PE fund values, investors face the uncertainty of the effect of mar-

ket movements. Most PE funds reported their September 2008 quarter end valuations in November 2008, and it wasn't until February 2009 when PE fund investors were able to see the effects of the October movement on their PE investments.

At the PE fund's inception, investors contractually agree to the terms of the investment with the fund manager, which apply for the life of the fund. Investors must consider carefully valuation and reporting at this time to ensure their needs are met. Many institutions now insist that the PE fund manager contracts a third party valuation expert to give investors more comfort regarding reported values.

The industry is now reflecting a desire for more frequent valuations on other unlisted investments such as OTC traded derivatives or property. Investors in these asset classes are starting to view reported values with scepticism, and regularly request independent valuations to

give them more confidence in the valuation of the assets in their portfolios.

The devastating effect of the global financial crisis has highlighted the importance of asset valuation to investors worldwide, and private equity has not escaped attention. The crisis is likely to accelerate the development of a more investor-friendly private equity industry, with improved transparency, third party checks and communication. In particular, investors are demanding sight of valuation methods and assumptions, or that a third party valuation expert regularly performs valuations to ensure more reliable reporting.

The South African private equity industry has grown swiftly over the last decade and, by embracing investor concerns that have arisen over this period of uncertainty, it can continue to build on this base and scale new heights. ♦

**Ord is Head of Valuation and Pricing at RisCura Analytics**

<sup>1</sup> KPMG and SAVCA Venture Capital and Private Equity Industry Performance Survey of South Africa (May 2009)

## Catalyst recently caught wind of an electrifying blue sky project in the South African water and energy sector

# Ingenuity at the cusp of chaos

When a former mining engineer and an outspoken water scientist join up with a group of young successful entrepreneurs to share their intellectual capital and vision of a new future for energy and water utilisation, the old adage of necessity mothering invention springs to mind.

The projects in question are housed in newly formed TouchStone Resources, which is engaged in the venture capital dimension of prospecting for, and developing, "New Energy and New Water."

TouchStone is a partnership between CEO David Gadd-Claxton and director Anthony Turton, with the recent acquisition of a stake in Oasis water adding the youthful franchising flair to the business but more of that later. The unmistakable impression that bursts through is passion, lateral thinking and ambition.

Gadd-Claxton is a mining engineer with 35 years experience; he is the venture capital tactician driving TouchStone into a brave new world. "I started at Rand Mines where I completed my apprenticeship in deep level gold mining. I spent some time with Sasol's coal mining division and then joined De Beers where I worked for ten years and helped build Venetia, which is their flagship mine," recalls Gadd-Claxton. He credits being exposed to De Beers' thinking and the construction of its model mine as a career-defining experience.

"I left De Beers in the late 1990's and joined SouthernEra," the Canadian-listed junior diamond miner, which mined the Marsfontein pipe, which was described as the richest diamond pipe in the world, in a joint venture with De Beers.

"SouthernEra also took me into Angola, where we tried to establish Camafuca Diamond Mine – a very large 162 ha kimberlite diamond reserve which was the biggest in the world at the time. We presented an independent feasibility study to the Angolan government and they simply couldn't believe the numbers. Life of mine of 1 000 years with return on investment of 2 500%. An amazing project but Camafuca is still sitting in the ground in Angola."

After that Claxton joined Petra Diamonds with the Poroulis brothers and worked on a few more diamond mining projects before he decided to take a sabbatical during the middle of 2008.

"And it was during this time that, after realising that the resources sector would only swing back in roughly five years, I was

# Catalyst

drawn to the energy sector. However solar, wind and the rest of the alternative energy sectors didn't resonate with my mining skills, which lead me to geothermal energy and that is where I reconnected with Tony. We were old friends from our days in the army and he joined TouchStone Resources at the start of this year after leaving the CSIR."

Dr Anthony Turton, a globally respected water scientist and self-confessed water geek, burst onto the public stage when he was controversially suspended from the CSIR last year for raising concerns about the safety and security of the country's water supply.

Turton's keynote presentation *A Clean South Africa* was due to be delivered at the CSIR's Science Real and Relevant conference in Pretoria last November, but he was instead charged with insubordination and bringing the Council into disrepute. He felt it was his moral responsibility to go public with the presentation warning that the country could be headed for a crisis in the water sector, which could fan social instability.

Turton points to the research contained in the business plan where it is evident that "in terms of water quantity there is a potential market for *New Water* in South Africa alone of 27 x 109m3yr1 water at the national level by 2035 with localized short-falls (and hence potential market demand) of 763 x 106m3yr1 in the Orange-Senqu river basin and 180 x 106m3yr1 in the Incomati river basin alone. In terms of water quality there is a very lucrative niche market in three distinct areas – sewage management by means of a franchising mode; the mitigation and treatment of acid mine drainage from both the gold and coal industry; and the provision of safe and affordable domestic water where public concerns exist about deteriorating local water quality."

"We needed to establish a footprint in both the energy and water sectors," explains Gadd-Claxton, "and that is where Oasis Water comes in. We looked at the business model and more importantly the human capital and loved what we saw. We've concluded a deal with Oasis, a straight share swap with each company taking a stake in the other."

Oasis Water CEO, Naas Du Preez, jokes that the tuft of grey now visible is a badge of honour obtained since taking over the company with his partners in 2006.

"At the time we had 32 branches but the company has shown phenomenal growth and currently we have 93 branches nationwide."

"We provide affordable water to the public using a retail platform and are distinguished from the other bottled water suppliers in the market by the fact that we encourage recycling through refilling. We refill our containers for 80 cents per litre at any of our 93 outlets that are situated in easily accessible retail centres nationwide, so instead of paying R20 for five litres the customer pays R4 and this creates a huge cost saving through stripping out the packaging and more importantly transport costs."

"At each of the retail outlets we have manufacturing plants where we take the municipal water and put it through a seven step filtering process."



Anthony Turton

"The bottled water business forms part of our small water strategy," says Gadd-Claxton. "That's not meant to be derogatory: it's just a question of scale. When we move up the chain we see ourselves getting involved in Municipal sewage treatment where we partner with local government to provide the services that, increasingly, the government is finding difficult to deliver. We will be targeting those Municipalities where the ratepayers have placed their money in an escrow account due to breakdown of the contract to deliver basic services. We can then rebuild that contract by providing the service and roll this out on a national scale using our newly acquired franchising skills housed in Oasis."



David Gadd-Claxton

"These young entrepreneurs have driven the business model forward enthusiastically," adds Gadd-Claxton, "and this human capital and their franchising skills are a critical component of what we are trying to achieve."

The TouchStone business model has been fashioned around noted financial guru Nassim Taleb's barbell investment strategy.

In his book, *The Black Swan* (TBS), Nassim Taleb recommends (pp. 205-26) an investment strategy in which one puts 85-90% of one's assets in "extremely safe assets, like Treasury bills" and the rest in "extremely speculative bets, as leveraged as possible (like options), preferably venture-style portfolio."

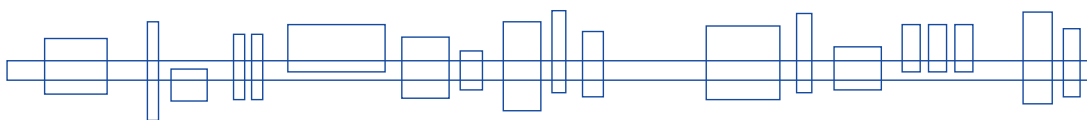
"The ten percent in the TouchStone business model is the high-risk high-gain geothermal and the ninety percent is the water which is operational and will provide operating income but the bounce is going to happen on the geothermal," says Gadd-Claxton. "As far as the investor is concerned we have created a suite of risk profiles."

TouchStone is aiming to list towards the end of 2010.

Gadd-Claxton feels that venture capital investors would see significant returns on the 10% side of the business. That is the geothermal exploration (Big Energy), water storage and Acid Mine Drainage research and development (Big Water)

"I looked at the closing bell on CNN at the end of last year and they were whining and whining that US\$30trillion had evaporated from the stock exchange," recalls Gadd-Claxton, "and I don't believe that to





be entirely correct. I think the money has gone from public sector to private sector and the private equity players are sitting with large pools of capital to invest and they're looking for good projects."

"On the geothermal exploration side of the business we are looking for compartments below ground with hot rocks at the bottom of these compartments so we can pump the water down and convert it into steam to drive above ground turbines to generate power."

Turton says this exploration also provides an opportunity to look for storage spaces where compartments are found without the requisite hot rock. "By storing water underground, and therefore negating the effect of evaporation, one can guarantee the assurance of supply needed

for companies such as Eskom and Sasol," explains Turton.

This leads to the opportunity presented by the Acid Mine Drainage (AMD) problem. "The AMD problem is a technical issue that is not being tackled correctly because the main driving force behind the people developing the technology is the mining houses and their objectives are to avoid liabilities for environmental damages. So their incentive is not necessarily the right incentive, which means they're bumping their heads against the economic constraints of the problem," says Turton.

"The current attempts to treat AMD are being hampered by economies of scale, but if the problem is dealt with at a higher level of scale, then the processes start to become economically viable and

thus financially sustainable as solutions."

Turton sees a major prospect for AMD remediation opening up a global industry if the problem can be solved at a technical level. "Existing mine voids can be considered as potential future bulk storage. The mine void under the Witwatersrand gold-field alone is estimated to be eight times the volume of Lake Kariba."

Turton, with his disarming and infectious passion, says that "South Africa is a crucible of new ideas. It's an exciting place to be because even though so many things appear to be going wrong we are at our best at the eleventh hour." Quoting from one of his favourite authors, Thomas Homer-Dixon, Turton says that "ingenuity occurs at the cusp of chaos." ♦

**In the US, venture capital investment is down 61% in the first quarter of 2009, compared with the same period last year. This is a 12-year low for venture capital according to the National Venture Capital Association of America (NVCA).**

## Venture Capital falls in US but not locally

"The nature of venture capital is to invest in early-stage, rapidly-growing businesses – assisting them to grow and become more profitable – with a view to selling the investment to another partner within a three to five year period," says Julia Fourie, CEO of venture capital company Here Be Dragons (HBD).

According to Fourie, there has also been a considerable international slow-down in venture capital funds raised as venture capital companies focus on firstly assessing the impact of the economic turmoil on their existing portfolio companies before making any new investments.

"Globally, venture capital exists have also been virtually halted, as companies across the board experience slowdown in growth and increased cutting of expenses. NVCA's statistics show that companies that used to grow at 50-75% year-on-year are now growing at 10-15%," says Fourie.

In 2008, the biggest venture capital investment in the US was in biomedical compa-

nies, accounting for 34,5% of total funding. This was followed by investment into software companies, accounting for 20,4% of total investment.

"In South Africa, the venture capital trends mirror the international trends, but our country is unique in certain aspects," points out Fourie.

"The biggest similarity is in that the actual performance of the underlying companies is not as good as anticipated as a result of the tough economy. This is likely to result in longer holding periods before selling the companies, in order to deliver the returns required.

"Where South Africa differs from the US is in that we have a less stable venture capital market, so the number of venture capital players is not expected to diminish in the next year. There are many new entrants that have mostly unused funds that they are still looking to invest.

"Coupled with this, the crisis in the econ-

omy is not as severe in SA. Our banking industry has protected us to some extent and government has also stimulated the economy with new construction projects.

"As a result, we expect to see venture capital companies continuing to invest in the year ahead, as funds are available and the slow economy presents a window of opportunity to acquire companies at good value."

HBD is looking to make at least more investments of between R10m and R25m in local, early-stage businesses this year. The focus will be companies with innovative ideas with the potential to expand internationally.

"If we can partner with quality companies through tough times, there should be substantial rewards to be reaped in later years. As HBD takes a three-to-five year outlook on the business potential of an investment, we not only focus on this year's problems but also next year's opportunities," concludes Fourie. ♦

# International round-up

**The Wall Street Journal** reports that a London firm that buys secondhand private equity assets has tapped hedge funds for opportunities for the first time ever, as its alternative investment peers seek to offload their most illiquid investments after other avenues to sell them shut down last year.

Coller Capital, an US\$8.5bn investor in private equity interests, has sealed deals to buy illiquid assets from two hedge funds so far, and is in discussions with many more to do so.

The British Private Equity and Venture Capital Association threw its weight behind damning criticism of the European Commission's plans to regulate the industry according to *Dow Jones Newswires*.

Welcoming recent comments from industry leaders and financial experts, the BVCA said that private equity should be excluded from the EU Directive.

A tough year seems to have brought reality home to the buy-out barons at Kohlberg Kravis Roberts reports *The New York Times*. The firm's latest step toward a full stock market listing looks more practical than last year's overambitious plan.

Private equity groups will take more minority stakes in companies as they face up to the shortage of bank debt available to finance full takeovers, according to the head of one of Europe's biggest buy-out groups.

Martin Halusa, chief executive of Apax Partners, told the *Financial Times* that he expected more companies to be interested in selling minority stakes to private equity groups as they seek to repair their over-indebted balance sheets.

We've seen securities fraud, hedge fund fraud, now private equity fraud? Prosecutors have charged Danny Pang who ran Private Equity Management Group in California with fraud expected to reach \$654m. *The Wall Street Journal* reported that Pang allegedly extracted at least \$83m in inflated fees. The Pang case is the first high profile private equity fraud publicly reported.

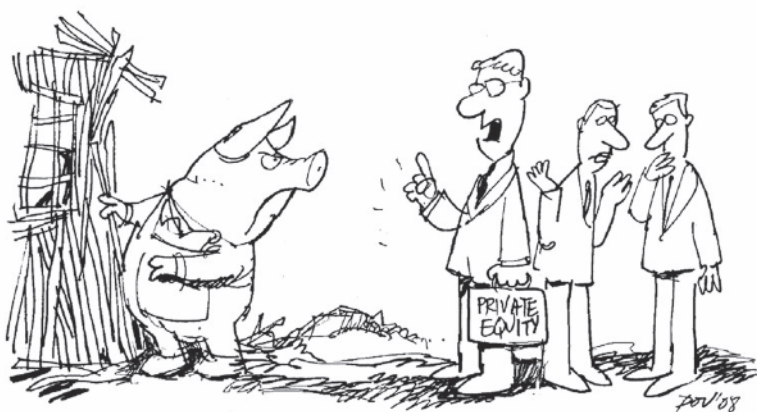
In July, KKR wanted to buy and delist its Amsterdam-listed investment vehicle, KKR Private Equity Investors, also known as KPE. Shortly afterward, it intended to list the enlarged KKR on the New York Stock Exchange. But the deal seemed too complicated even before the market turmoil reports the *Times*.

Last year, KKR hinted at a market cap in its pre-deal form of up to \$15bn, when about \$10bn seemed more reasonable.

Now, everything appears to fit a little better. KPE's shares trade at around \$6 apiece, for a market cap of \$1.2bn. They have risen lately, but being closely held and not very liquid, probably do not reflect the full value of KKR's offer.

The underlying net asset value of KKR Private Equity Investors' holdings is \$2.6bn. Split the difference, and the 30% of KKR that KPE will get could be worth around \$1.9bn.

That means the other 70% — essentially, KKR — would be worth about \$4.5bn. *The Times* speculates that the second stage of KKR's plan, a New York listing of the enlarged firm next year, could raise that valuation somewhat.



*Our recommendation is bricks but if you're going to huff and puff about this, that's your problem*

## SOUTH AFRICA PRIVATE EQUITY DEALS Q2 2009

NATURE	PARTIES	ASSET	ADVISERS	VALUE	DATE
Acquisition by	Investec Private Equity (Investec Bank) from Stella Hospitality Group	33% stake in Protea Hotels		not disclosed	Apr 15
Sale by	Mediscor to Pan-African Capital	25% of Mediscor		not disclosed	Apr 23
Acquisition by	Cost2Coast Private Equity	stake in St Pie		R30m	Apr 24
Acquisition by	Medu Capital	40% stake in Medipost Courier Pharmacy and 40% stake in Kawari Wholesaler		not disclosed	May 11
Acquisition by	Management, private equity and BEE partners	Masslift Africa	Nodus Capital; Tugendhaft Wapnick Banchetti	not disclosed	May 12