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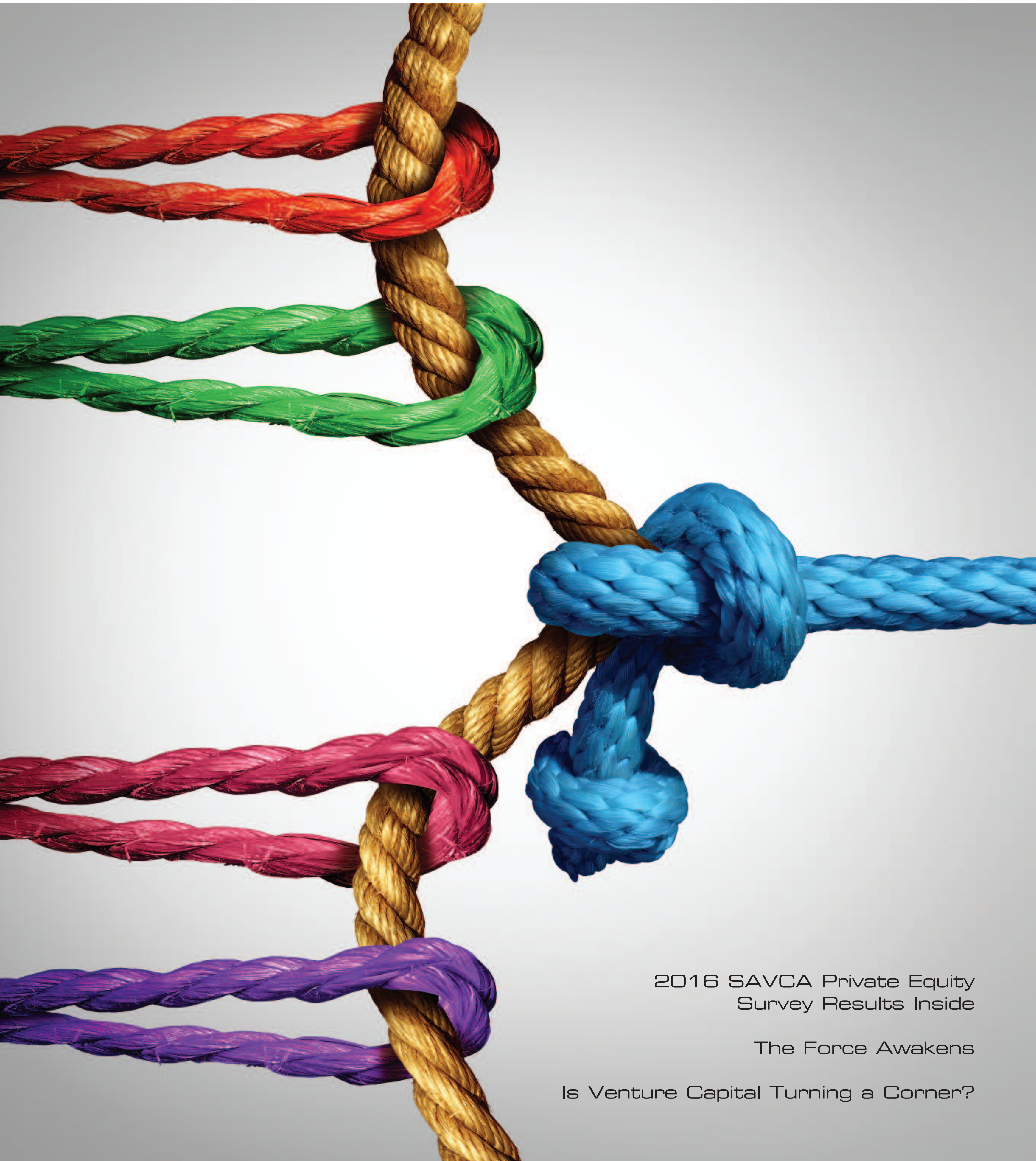

2016 SAVCA Private Equity
Survey Results Inside

The Force Awakens

Is Venture Capital Turning a Corner?

FROM THE EDITOR'S DESK

The second quarter ushered in one of the most unexpected global events of recent times, though not for being poorly visible. The Brexit was largely unpredicted because the market was backing the bookies and not the pollsters, who were calling a far tighter race. The theory doing the rounds now are that the bookies market was gamed to benefit a few hedge funds, which saw an opportunity to shift the trillion-dollar forex markets by using the far shallower bookies pool. It's an interesting theory that I don't fully have time to unravel here, suffice to say that investors will be weary of following the bookies again.

But what Brexit has done (ably assisted by the rise of Donald Trump and ISIS), is create an unexpected fillip for Africa and by extension private equity on the continent.

I attended a breakfast with some heavyweights in the private equity space hosted by KPMG recently and the consensus seems to be that developed market risk premia have shot up in light of these events. This means Africa, despite its lingering governance concerns, the impact of the slowdown in commodities and currency concerns, is now looking attractive again because of yield spread – the difference between rates, inflation and the rates foreign investors can borrow at – and the long-term growth potential which remains intact.

As the SAVCA industry survey reveals on page 1, funds raised during 2015 (prior to all this developed market uncertainty) were a record R29bn. The percentage raised offshore came down from 75% to 50% indicating that sentiment could have been turning against us – thanks in no small measure to the political governance issues, which seemed to accelerate in December around Nenegate.

Despite this, and pleas from the IMF recently to re-energize growth by seeking inclusion and job creation, a far more uncertain world means investors are forced to reconsider their options.

That said, I think the news out of Ethos in July that it is effectively creating its own limited partner that will invest in Ethos funds, called Ethos Capital, indicates just how much tougher it expects fund raising to become. As the deal was announced in July, I'll bring you a full breakdown of the Ethos transaction in the third quarter issue.

Another major challenge for SA-based GPs at the moment is how to access family-owned and/or managed businesses in Africa. It's increasingly clear that these are the midsize-cheque deals that offer compelling potential for private equity firms to partner with, grow to scale and exit.

The problem, according to one general partner I was chatting to, is that there is a trust deficit when it comes to SA firms entering these markets. This means GPs will have to spend more time developing networks - breaking bread at the dinner table so to speak - and accessing the networks of institutional advisors who already have access to high net worth families whom they service as clients.

Trust is hard earned. ◆

Michael Avery

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Gleason Publications

The private equity industry has been quite a resilient performer through various economic cycles and this was demonstrated at the launch of the SAVCA 2016 Private Equity Industry Survey, which covers the 2015 calendar year.

Record fundraising year masks offshore difficulties

Catalyst sat down with SAVCA CEO, Erika van der Merwe, to find out what the highlights of the year were for the asset class.

The standout theme for 2015 was the success that fund managers have had when it comes to fund raising, so capital raising for new funds, for investments in South Africa and beyond.

"R29bn was raised in 2015 by fund managers. This capital was raised both in SA and outside SA in the US, UK and Europe, a very important source of foreign capital inflows into the local market," says van der Merwe.

The bulk of these funds are earmarked for late stage investment, generalist funds that will invest across industry sectors.

Of that R29bn, roughly three quarters was raised locally, whereas in years gone by that number has been closer to a fifty-fifty spread. Van der Merwe is quick to point out that the funds raised in 2015 are the end result of processes that started before the Nenegate scandal and other significant political headwinds, which means fund raising now into 2016 will be much more "interesting" for GPs.

"I do think that [the political headwinds] are temporary, because the overall appetite for SSA private equity remains strong, for growth and returns. Over time those concerns about currency are eliminated because currencies come and go and in diversified portfolios those concerns are minimised," says Van der Merwe

The decision by Ethos to basically open up alternative fund raising avenues by listing Ethos Capital (ostensibly creating its own LP that will draw from local investors) points to a far tougher offshore fundraising environment over the next few years.

The other side of that coin is that the largest source of these funds were from SA pension funds, which means these large institutional investors are starting to ascertain and commit to the value that the asset class offers – it is up from R1,9bn in 2014 to R2,5bn in 2015.

"The overall industry has R165bn in funds under management," says Van der Merwe.

Of that, R40bn remains undrawn or uncommitted (roughly a quarter) while just over half of that (R20bn) is earmarked for investments into SA, across industry sectors.

This is the 16th year of the Survey and over that period private equity has delivered roughly 12% compound annual growth.

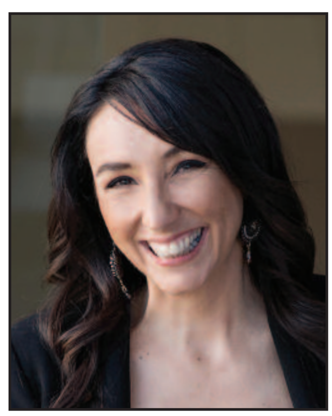
"Yes, there were some good years and not such good years as with all asset classes and all sectors and all markets, but what you do see is that when you stand back and review this asset class, it's one of steady growth, it's resilient, it's got the track record. Over the last ten years delivering CAGR of 18% and that's what investors are looking for," says Van der Merwe.

Turning to deal activity, 534 deals were announced (over 300 of these included Business Partner's, mom and pop, and lifestyle businesses) totalling some R10,5bn, demonstrating healthy activity levels. Van der Merwe adds that the split between new deals and follow-on transactions is roughly equal, which indicates that some confidence is seeping back into the market when compared with a few years ago.

Michael Rudnicki

Michael Rudnicki, Head of Private Equity at KPMG, observed that deal sizes have halved since the mega-deal peak of 2007.

"The variety of sectors has changed and we've seen trends in the form of infrastructure, in the form of energy, mining related services and retail picking up in the last couple of years.



Erika van der Merwe

Rudnicki points out that the so-called family managed or owned business has always been of interest to private equity. “They typically have the nuts and bolts of what PE wants, which is good track record, good management, typically low gearing. I think we'll see that trend playing out of deal activity in this space as some of these bigger retail type transactions have potential spin-offs in terms of investments into other countries in Africa. And if you look at the growth rates in Africa, they are double digit, and there is the opportunity of bringing services to people.”

When it comes to African entry the partnership model still appears to be route one and sourcing deals, getting to know the families and gain their trust is the real challenge.

“It's hard to go into countries in Africa on your own. We see that and we see clients and companies have failed,” Rudnicki says matter-of-factly. “Typically the approach to follow is either a good brand, which is marketable and which is easily accessible to the population. What typically works better is having good JV partners in those territories, who know the regulations, who know how to get cash out of those particular countries back into SA which is always an issue from a currency control perspective.”

Rudnicki references the fact that only 10% of transactions north of SA work and 90% fail, to further underline just how challenging Africa can be.

Despite this there is still a large volume of capital that appears to be chasing a relatively shallow pool of deals in Africa.

“It's an interesting conundrum. I think there's a lot of opportunity out there (in Africa). The difficulty is to find those deals. When we talk to our colleagues and our friends and investors overseas, they typically have large cheque books - so the small family owned business is not necessarily what they're looking for, but that in my opinion is where the real opportunity lies.

“The big cheque books are there and they'll find a small number of mega deals in Africa. The opportunity that exists is to find those family businesses, 10 to 100 million dollars and to find the right partnership and turn those onto mega deals in the coming years.”

On the exit front, the IPO window that was whistling wide open in the relatively calm breeze of market certainty at last year’s SAVCA conference has now been narrowed somewhat, as the gusts of volatility sweep through the markets making pricing difficult and leading to far more trade buyers or secondary exits.

"It's a question of exiting the deal to yield the proceeds for the investors,” says Rudnicki. “It’s far quicker typically to do a trade deal of PE-to-PE deal (secondary deal) and the volatility of the market make it not as comfortable, typically. The trade buyer play is really what’s happening.”

The trend of the public investment corporation as far more active player in the industry is on the rise. “We've seen a number of transactions over the past six to seven years where the PIC has had stake in a typical PE fund,” explains Rudnicki. “They've got a large balance sheet to deploy in the PE mould, they don’t necessarily need other partners to co-invest, they've got sufficient capital.”

But will that lead to the PIC’s bulk crowding out the private players in the space?

“There's certainly, in my opinion, a lot more conversations to be had between the industry and the PIC to work together,” answers Rudnicki. “They've got the capital and they've got the expertise as well. More conversations need to be had to work together and to deploy that money, because at the end of the day that's money that's invested for government workers who want a decent pension when they exit.”

Is that happening?

“I'm not aware of the conversations happening yet,” is Rudnicki’s short answer. ◆

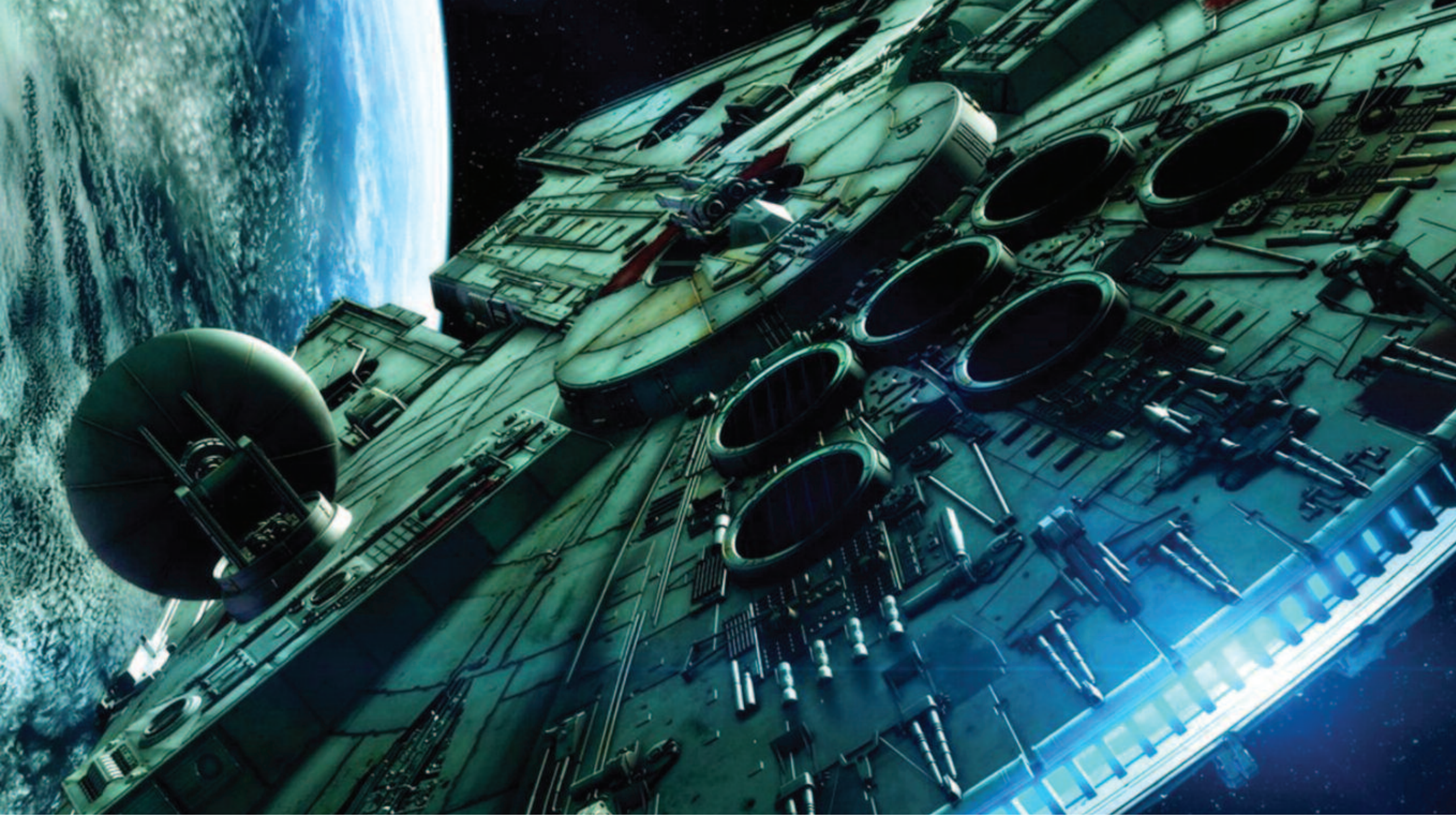
“What improves the circumstances of the greater part can never be regarded as an inconvenience to the whole. No society can surely be flourishing and happy, of which the far greater part of the members are poor and miserable.”
- Adam Smith, The Wealth of Nations

The Force is strong with PE

Adam Bennot

Although Adam Smith, often referred to as the father of modern capitalism, may have not have been a proponent of businesses pursuing charitable activities, he clearly believed in a society of shared value creation.

In order to address some of South Africa’s most pressing social and environmental challenges, a paradigm shift is taking place within the realm traditionally seen as driven by narrow profit maximization. By aligning purpose with profit, private



equity (PE) is emerging as a powerful tool that supports long-term financial sustainability, reduces business risk and focuses on value creation for a wider group of stakeholders.

According to the Bertha Centre for Social Innovation and Entrepreneurship's 2015 African Investing for Impact Barometer, an estimated 70% of funds managed in South Africa - representing $480bn - implement at least one or more investing for impact (IFI) strategies. These strategies include:

- Integrating Environmental, Social and Governance (ESG) factors into investment analysis, valuation and decision-making;
- Investor engagement which seeks to influence a company's behaviour through proxy voting and board participation;
- Negative or exclusionary screening;
- Thematic investments which focus on investments along the themes of environmental sustainability and inclusive socio-economic development; and
- Impact Investment which is an investment strategy intended to generate positive environmental and social impact alongside financial return.

According to the Bertha survey, ESG integration was the most popular strategy with 71% of assets being managed using this strategy. While Impact Investment only constituted 1% of total assets under management at $6bn, it has a greater level of impact; and private equity is leading the way within this strategy.

Although private equity firms managed relatively fewer assets than the listed asset managers, the survey found that they were generating more impact per unit of assets under management. Thanks to the efforts of DFIs, which have been a major contributor to funding PE mandates integrating ESG in South Africa, PE is now being used as a force for good.

Although private equity firms managed relatively fewer assets than the listed asset managers, the survey found that they were generating more impact per unit of assets under management.

Driving this investment philosophy is the belief that well-managed and well-governed private equity investments can be a powerful driver of improvements in the livelihoods of people living at the bottom of the economic pyramid (BoP). A joint report by SAVCA and the DBSA shows that investee companies increased the number of staff employed both within and outside of South Africa by around 40%.

Private equity is no longer just about growing the bottom line in the short-term; it is about contributing to real business growth, maximising value for society, and increasing returns over the longer term. Beyond job creation,

Bennot

PE is raising operational standards, improving corporate governance and putting South African businesses on par with their global counterparts.

This transformation couldn't happen at a more critical time. South Africa's current economic challenges seem almost unsurmountable. GDP growth of less than 1%, a looming credit ratings downgrade and rising unemployment, means that South Africa's economy is on the brink of a recession. Targeted investments are desperately needed in the education, infrastructure, healthcare and agriculture sectors. Unfortunately, the level of investment needed far outweighs the resources available from the public sector, private foundations and DFIs. Private sector resources are needed to bridge the gap; and private equity is paving the way.

SAVCA's Case Study Compendium showcases how PE investments are contributing to sustainable economic development in South Africa.

For example, in the food and agriculture sector, Musa Capital invested in African Frontier Holdings (AFH), an integrated FMCG group focused on the food industry with investments in farming, processing, manufacturing, distribution, logistics and retail. With the support of Musa, AFH established an Emerging Farmers Programme to provide internships for 50 aspiring black farmers. These farmers will be up-skilled to develop new co-operatives which will ultimately be phased into new farming units.

In the housing sector, Lereko Metier Capital Growth Fund invested in South Point Management, which was established in 2003 to redevelop and manage underutilised inner-city properties to provide affordable, quality accommodation for students. Since the fund's investment in 2007, South Point's property portfolio has grown from six buildings to 40, providing housing to approximately 10 000 students.

The renewable energy sector has attracted significant PE investment, which is providing much needed clean energy to the national grid. For example, Inspired Evolution invested in Red Cap, which is developing two onshore wind energy projects in the Eastern Cape. The two projects include the Kouga Wind Farm (KWF) and Gibson Bay Wind Farm (Gibson Bay). The KWF project will generate approximately 305GWh of clean energy per annum, mitigating approximately 220 tons of CO2 greenhouse gas emissions each year.

In education, Milpark Education and Management received an investment from Leaf Capital, which has helped the company grow into a prominent higher education institution with two campuses and over 14,500 students enrolled countrywide.

Even in healthcare, PE is having a significant impact. For example, Medu Capital invested in Medipost Pharmacy, which is the largest courier pharmacy for chronic medicine in the country. The resulting deal enabled Medipost to improve its BBBEE rating from Level 4 to Level 2. It also helped the company establish an additional hub in Cape Town and increase the number of jobs from 408 at investment to 1 300 in 2014, at exit.

The above examples highlight some of the tangible value-enhancing socio-economic impacts of private equity investment across companies and industries. Clearly, PE has a vital role to play in driving inclusive growth and sustainable economic development in South Africa, as well as driving strong, long-term returns for investors. ◆

Bennot is a senior analyst, African Private Equity, RisCura.

Our intuition about the future is linear. But the reality of information technology is exponential, and that makes a profound difference. If I take 30 steps linearly, I get to 30. If I take 30 steps exponentially, I get to a billion.
~ Ray Kurzweil

Fintech momentum behind venture capital

The Venture Capital industry has been talking about the news that South African venture capital firm 4Di Capital raised almost a quarter of billion rand with the successful first closing of its new technology venture capital fund. When one considers that the total funds under management in the VC space are roughly R2bn, according to the SAVCA industry survey, this quantum of capital is news in its own right. But the real kicker was that the major investor in the fund is Exponential Ventures, the externally focused innovation unit of JSE listed insurance group MMI Holdings.

This is one of the first collaborations between a venture capital fund and a large institutional investor in this country, and Catalyst caught up with some of the major role-players in the transaction to find out what this signifies for the country's nascent VC sector.

Justin Stanford, co-founding General Partner of 4Di Capital, and one of the driving forces behind the Silicon Cape Initiative, which is geared at growing specifically technology focussed start-ups, is understandably upbeat.

"It's very good to see innovation-minded corporates in South Africa beginning to acknowledge the benefits of having a stake in the venture sector, as is common in the US, and we've been impressed by the constructive and enlightened engagement we've had with MMI management. We look forward to working together with them to leverage their strengths as well for our future portfolio companies' benefit," Stanford said.

"The depth and breadth of the venture market has grown substantially in South Africa since we first launched The Silicon Cape Initiative in 2009, and there is more opportunity than ever before to partner with great local talent and participate in this rapidly growing industry on a global scale."

The fund's mandate will include early- and growth-stage investments, focusing principally on scalable technology opportunities in the FinTech, InsurTech and HealthTech verticals, particularly those with ambitions to reach international markets.

"I met Justin and the team towards the back end of last year, and was very impressed with the entrepreneurial approach that they have there," enthuses Jonathan Stewart, managing partner, Africa Investments at Exponential Ventures. "Justin is a self-made tech success and entrepreneur. He left school before finishing his matric to make sure he didn't miss the internet boom. And with a few failures in between he finally struck a successful formula. And also in his team is a chap by the name of Laurie Olivier (Partner, 4Di capital) with a long 30-year track record in venture capital and he's had experience in corporate VC as well, at Anglo American, which was attractive to us. He knows how to bridge the gap between the start-up and the corporate and understands the perspective of both and that's important."

Venturing with big business

The approach to the looming fintech wave of disruption was carefully calculated inside MMI according to Stewart. "These rapid changes in technology which are reducing barriers to entry for young companies - it's really quite cheap now to start a tech company - and the business model that this uses, cloud, data analytics and so forth, makes it possible," he adds.

Stewart explains the rise in Fintech as one of the key drivers behind the formation of Exponential Ventures.

"In fact, it was identified in a 2014 board meeting that these emerging business models in other sectors were likely to become evident in insurance as well. We were seeing a huge explosion in fintech investment, overseas more than here, and nascent signs at that point of insurance becoming a theme - it's quite a big theme now - and we felt that better to get in front of the game and be proactive around future proofing MMI, which was our initial thought," elaborates Venter, "and maybe a little bit more defensive initially and then we started to realise that is also a huge opportunity as well.

"So we spent most of last year with some consultants to see how other businesses around the world have attacked this problem and ultimately took our proposal to the board at the end of last year and it was born then to really proactively embrace these disruptive trends and secure the future of MMI."

And so Exponential Ventures was born, officially, in December 2015 with a mandate to focuses on three key external innovation opportunities namely:

- Scaler opportunities: Technology-based businesses, which when combined with MMI's assets (e.g. brand, distribution, insurance skills), show meaningful potential to rapidly generate exponential growth in revenue and profit;

- Optimiser opportunities: Technology-based businesses that have the potential to deliver significant savings in expenses for MMI's existing business; and
- Venture developer opportunities: Identifying and developing brand new and disruptive ventures that reach new markets, meet new needs, leverage new business models and show the potential to fundamentally disrupt the insurance market space as we know it over slightly longer time horizons.

But why choose to go the LP route into a VC fund rather than go it alone?

Stewart explains that during the course of the last year, as the Exponential Ventures team formed its view of how they wanted to attack this, their first decision was whether they were going to invest in this process or just conduct research and then have an accelerator/incubator type approach.

The market will be following the outcome of the 4Di Exponential Ventures deal with more than passing interest, as it may pave the way for similar mutually beneficial wins in the future.

"When we settled on the fact that we were going to put money to work in the market we had to decide how," says Stewart.

"Of course it was still also a possibility to do it ourselves which is model that many businesses adopt. We chose not to for a number of reasons, but an important one being the testy trust relationship between the corporate world and the start-up community. Start-ups are fairly suspicious of corporates. And the school fees will be high, so we decided to partner."

Of course it's exactly that partnership approach that holds the promise of great reward but also great risk. There's no explicit legal agreement that guarantee's the investee companied in the 4Di fund will end up partnering with MMI in the long run but one can understand the implied relationship building that this model employs.

"It's a fairly boilerplate agreement and deliberately so," explains Stewart. "We found that VC has found a format and approach that has worked. It's proven in Silicon Valley, over 40 or 50 odd years, it's been honed and rehoned and the local industry has made a few little tweaks to suit this market and we didn't want to break the formula which has been proven. At the same time, naturally, there were specificities which were important to address around the fact that we were a major LP in this and not a spread but we have no specific claim on intellectual property."

Justin Stanford

Joshua Janks

Importantly the start-ups and investee companies have relationship with 4Di Capital through the VC fund managed on the normal principles.

"Of course, we aim to make available to these start-ups our skills sets and IP around insurance, health, wealth, and so forth in the wider MMI Group, to help them and support them in their growth endeavours. And through that hopefully build and earn a trust relationship with them so that we can voluntarily have partnership going forward so there's no force and obligation in it."

Joshua Janks, partner in the Bowman Gilfillan Africa Group's Private Equity Funds Practice, advised 4Di Capital on establishing the fund and believes the fact that a large corporate institutional investor has come into this market is "very interesting" and that it "might set a trend and for others to follow and take the lead from MMI to be looking for these disruptive opportunities."

"It might mean there's a lot more capital coming into the market," says Janks. "The other point is that it really provides a network and skills set that this market doesn't necessarily have access to."

Janks believes the South African VC sector might be poised for a real lift-off soon.

"We're a bit behind the likes of Israel, America with Silicon Valley, and China, but I think we have fantastic entrepreneurs and some of the social conditions in the country have forced people to go out and start businesses and be entrepreneurial. There is certainly a need for it and a growing trend for people to try and grow in the Fintech space."

The market will be following the outcome of the 4Di Exponential Ventures deal with more than passing interest, as it may pave the way for similar mutually beneficial wins in the future. Wins that ensure we create a far more conducive environment for start-ups and for the incumbents to protect their current shareholders by outsourcing the so called moat building to smaller nimbler operators. ◆

There's an African proverb that says one hand does not catch a buffalo. This proverb in the Ewe language is spoken in Southeast Ghana, Southern Togo, Benin and Southwest Nigeria. Its literal meaning is that there is no strength in isolated efforts. But collective efforts yield great things. And it finds expression in the way the venture capital (VC) industry in South Africa is starting to mature.

One hand does not catch a buffalo

The South African VC industry now represents almost R2bn in assets under management, with healthy confidence levels that are commensurate with reported rising deal activity, an encouraging exits record and a meaningful increase in VC fund managers and industry professionals.

These findings are encapsulated in the SAVCA 2015 VC Survey, which covers VC-type transactions that took place between January 2011 and July 2015, and follow two previous VC studies produced by the Southern African Venture Capital and Private Equity Association (SAVCA), in 2010 and 2012.

The most recent survey reveals that between 2011 and 2015, 21 public and private VC fund managers and angel investors completed 168 new deals amounting to a total value of R865m. As at July 2015, total VC assets under management were valued at R1,87bn, comprising 187 deals, with this now being boosted above the R2bn mark following the announcement of 4di Capital's successful first closing of its tech fund in June.

Samantha Pokroy sits on the SAVCA board, chairs the VC subcommittee, and founded private equity and late stage VC fund Sanari Capital in 2013. ***Catalyst*** sat down with her to find out more about Sanari Capital and to talk about the state of the VC industry.

Pokroy jokes that she was going for a feminine image with the name Sanari, which is a Tshivenda word meaning 'Like a buffalo'.

"It's all about strength and courage and community," she adds with a broad smile. "Our aim is to build businesses that are sustainable, scalable and saleable." Sanari Capital specialises in founder-run, owner-managed and family-owned businesses, bringing corporate best-practices to under-served entrepreneurial businesses, and a sense of ownership to overly-corporate environments. "Our private equity frameworks are similar to most in the market, but the conversations we have with founders differentiates us. This is reflected in the team composition, all of us come from top tier corporates but are entrepreneurs at heart and in practice".

Pokroy sees the key difference identifying the sort of private equity and VC that Sanari looks at from early stage VC investing as "the difference between market risk and execution risk. Our experience and expertise is more in how a company delivers and scales to the next level, and after it has proven out its idea and market".

"We are in later stage VC, growth equity, 'buy and builds' and in certain instances later stage private equity...but the common thread is that we are institutional investors and that's where we differ somewhat to your angel investors. We follow certain institutional practices in terms of how we evaluate, source and execute investments and then we sit on the boards and participate and ultimately grow the company, and then at some point exit."

Pokroy believes we actually have an industry of so called super-angels in South Africa, more so than a traditional institutional VC industry. "The reason for that is because a lot of the VC firms ultimately have been either seeded, or are supported in some way, by an angel investor who is usually a

highly successful businessperson who is now looking at what he or she can do with their wealth, and their friends' wealth, and deploying it," explains Pokroy.

"It definitely is riskier. It's less formal in many respects but I actually think that our angel investors, given their prevalence in the VC industry, bring quite a formal approach to things. You're not going to get off light going with an angel investor!"

Samantha Pokroy

Sanari Capital's investment size ranges from R40m to R200m, with a sweet spot between R75m to R125m.

And then in the smaller part of the market, Sanari's typical investment size, through its Sanari Growth Partners 12J Fund is between R10m to R40m, with a sweet spot of R20m to R30m.

How could we improve the VC ecosystem?

"In our SAVCA VC industry subcommittee we have actually got a big focus on how we move this forward.

The challenge," says Pokroy, "is that you have to move forward multiple pieces at the same time."

Everyone bemoans the state of the industry and says there's not enough capital to deploy behind these entrepreneurial ventures. But even if we had all the money we could possibly invest tomorrow, do we have enough VC capacity, skills and then what is the quality of the deals themselves? So the quality of the entrepreneurs and the volume of the deals are some of the big challenges that we face when comparing SA with the likes of VC markets in the US, Israel or China, and this impacts on the model we can employ here."

Pokroy points to the size of the market as a key constraint to simply adopting models that work in far larger markets.

"We have a smaller volume of deals which means we can't play a numbers game as much as you can in certain other markets, which means you have to manage risk differently here."

So the major question the market is grappling with is how to increase the number of high quality deals and then how the regulatory environment impacts on this ecosystem as whole.

"And it's not just about incentives," says Pokroy, "it's also about how you remove obstacles. There are incentives and things that are happening and progressing but some of the fundamental obstacles remain which actually keeps all of those parts from moving forward at the same time."

One of the incentives introduced held much hope for market participants: the Section 12 J tax incentives, which first came into effect from July 1, 2009. This meant that investors (any taxpayer) can claim income tax deductions in respect of the expenditure incurred in exchange for VCC shares.

The VCC regime is subject to a 12-year sunset clause, which will see it end on June 20, 2021. This will allow for review of the efficacy of regime and a decision will then be made as to whether it should be continued.

Pokroy adds though at it's not necessarily an incentive for VC, though it does help, it is actually used as an incentive to direct capital towards the smaller part of the market, to SMEs.

It does seem like the VC and growth equity market is making progress, and its firms like Sanari Capital, and passionate advocates for the sector such as Samantha Pokroy, that epitomise a newfound bullishness for the future. ◆

"Exacerbating the position in respect of foreign fund managers is the FSB's reluctance (read: refusal) to grant a Category II FSP licence to an offshore applicant that has no local presence (and also no desire to establish such a presence)."

Contradictory laws

Bright Tibane & Francisco Khoza

From a Financial Advisory and Intermediary Services Act, 2002 (**FAIS**) perspective, foreign fund/asset managers looking to offer discretionary financial services to South African-resident investors are only required to obtain a Category I financial services provider (**FSP**) licence, provided that the discretion in question is exercised (i.e. the investment decision is taken) offshore. Under these circumstances, the Category I FSP licence then covers the foreign manager's proactive engagement and marketing activities in relation to South African-resident investors, and a Category II (discretionary) FSP licence is unnecessary given that the discretionary service is not being performed in South Africa. This is a position long-held by the FAIS Department of the Financial Services Board (**FSB**).

Investments by South African pension funds, however, as institutional investors, are subject to the prescripts of the Pension Funds Act, 1956 (**PFA**) and are specifically regulated by Regulation 28 of the Regulations to the PFA (**Regulation 28**). Regulation 28 significantly limits the extent to which a pension fund may invest in certain categories of assets, including private equity funds. Regulation 28 defines a "*private equity fund*" as:

"a managed pool of capital that-

…

(c) *is managed by a person licensed as a discretionary Financial Services Provider as defined in the Code of Conduct for Administrative and Discretionary Financial Service Providers, 2003, or if a foreign private equity fund, managed by a person licensed as a Category I Financial Services Provider that is authorized to render financial services on securities and instruments as defined in the Determination Of Fit And Proper Requirements For Financial Services Providers, 2008; and*

(d) *is subject to conditions as may be prescribed".* (emphasis added)

From the definition of a "*private equity fund*", it is apparent that in order for a South African pension fund to invest in a foreign private equity fund, that fund must be managed by a person who holds a Category I FSP licence. This position is in line with the long-held position of the FSB, as outlined above.

However, subsequent to the coming into effect of Regulation 28, the Registrar of Pension Funds published Board Notice 1 of 2012, entitled "*Conditions for Investment in Private Equity Funds*" (**Conditions**). These Conditions are those contemplated in paragraph (d) of the definition of a "*private equity fund*".

Contrary to Regulation 28, item 3 of the Conditions (**Condition 3**) provides that a pension fund may invest in a private equity fund only if the person rendering financial services, whether discretionary or otherwise, to that private equity fund, **whether local or foreign**, is a Category II FSP or a representative of a Category II FSP.

By stipulating the need for a Category II (discretionary) FSP licence under these circumstances, Condition 3 not only directly contradicts Regulation 28's definition of a "*private equity fund*" but also undermines the view long-held by the FSB.

While the clear contradiction between Regulation 28 and Condition 3 has been acknowledged by the FSB in the past, the matter remains unresolved to date and, in the meantime, Condition 3 is binding on and enforceable against South African pension funds.

The lack of resolution places local pension funds in a dilemma, with most insisting on compliance with Condition 3's Category II FSP licence requirement.

Exacerbating the position in respect of foreign fund managers is the FSB's reluctance (read: refusal) to grant a Category II FSP licence to an offshore applicant that has no local presence (and also no desire to establish such a presence). This position, against the backdrop of Condition 3, effectively

In general, a foreign fund/asset manager rendering financial services to a foreign private equity fund (in which a local pension fund may seek to invest) will not render such services to the private equity fund in South Africa, but solely offshore.

Tibane

Khoza

excludes foreign private equity fund managers, who operate on a cross-border basis, from securing investment from local pension funds.

In general, a foreign fund/asset manager rendering financial services to a foreign private equity fund (in which a local pension fund may seek to invest) will not render such services to the private equity fund in *South Africa*, but solely offshore.

The South African legislature does not have general jurisdiction over foreign legal subjects and what those subjects do outside of South Africa's borders, as this would offend against the 'doctrine of effectiveness' (ie the ability to enforce or give effect to an order in relation to such conduct). This is a well-developed principle of our common law and it highlights the need for resolution of this issue. ◆

Tibane is a senior associate, overseen by Khoza, a partner and head of Bowman Gilfillan Africa Group's Banking & Finance Department.

Local and International news

National news

The SA private Equity and Venture Capital Association will host its 2016 AGM on September 21, 2016 from 4:30 pm – 6:30 pm at Webber Wentzel, 90 Rivonia Rd, Sandton. ◆

Metier Capital Growth Fund II completed further closings to June 2016, raising in excess of R2,5bn, with further commitments expected by final closing.

The fund is the successor fund to the Capital Growth Fund of 2006/7 which invested in eight portfolio companies, the majority in value now realised.

The fund will focus on private equity investment in buy out and growth capital transactions in South, Southern and Sub-Saharan Africa. Investments are targeted in sectors set to benefit from demographic trends such as population growth and increased urbanisation, and the accompanying consumer spend from the emerging middle class. The fund will also target investments in sectors which are advantageously exposed to increasing intra-regional and international trade, and also where strong management teams are able to lead regional expansion of their businesses. The fund strategy targets exposure of 50% to sub-Saharan Africa, excluding South Africa.

The fund has already concluded four investments in the retail, out of home dining, healthcare and industrial services sectors. ◆

Vantage Capital, Africa's largest mezzanine fund manager, disbursed the second and final tranche of a R250m ($17m) expansion capital facility to Vumatel in June. The funds will be used for the on-going expansion of Vumatel's fibre-to-the-home ("FTTH") network in a growing number of Johannesburg and Cape Town suburbs.

The Vantage mezzanine facility was structured in two equal tranches of R125m ($8,5m), to be drawn by Vumatel upon the achievement of certain operational and financial milestones by the company. Since concluding the transaction in April this year, Vumatel has rapidly expanded its network and has exceeded the milestones required to drawdown both tranches of the R250m facility from Vantage.

Vumatel was established in 2014 to supply affordable high-speed fibre optic network connectivity to homes in South Africa. Vumatel began deploying its open access FTTH network in October 2014 in Parkhurst, a Johannesburg suburb. Since then, the company has rapidly expanded its network to cover 22 suburbs, reaching more than 33 000 homes. Driven by strong customer demand for reliable high speed internet, Vumatel has a robust pipeline of additional suburbs for further network deployment. ◆

International

How Wall Street made an absolute killing from Twinkies

Reuters reported in May that Hostess Brands, the maker of Twinkies, is going public in a deal that is great news for private equity.

Apollo Global Management and the family-owned private equity firm C. Dean Metropoulos & Company, which together bought Hostess out of bankruptcy in 2013, have sold the company to Gores Holdings, a special-purpose acquisition company, for some $675m.

In the process, they've made a ton of money.

Much of it comes from a $905m dividend recapitalization last year, in which Hostess sold $1,23bn of term loans to pay dividends to shareholders, according to Bloomberg.

Here are the details:

- Apollo and Metropoulos bid $410m for Hostess in 2013.
- They also committed $250m to rehabilitating the company and about $20m for additional costs like lawyer fees.
- That was financed by a $140m equity investment from Apollo, a $40m equity investment from Metropoulos, and a $500m debt offering.
- Apollo has earned about $522m to date in realised proceeds and expects to earn another $200m from Tuesday's deal. It will continue to hold a stake in the company worth about $220m. ◆

PRIVATE EQUITY DEALS H1 2016 – SOUTH AFRICA

NATURE	PARTIES	ASSET	ADVISERS	ESTIMATED VALUE	DATE
Disposal by	Vantage Capital and African Woman Chartered Accountants Investment to Kleoss Capital	entire stake in TrenStar		undisclosed	Jan 12
Acquisition by	Old Mutual Fund IV (Old Mutual)	significant minority stake in In2Food	Merrill Lynch; Nedbank CIB; Webber Wentzel; Cliffe Dekker Hofmeyr	undisclosed	Jan 14
Acquisition by	Ethos	65% stake in The Eazi Group	Webber Wentzel	R1,6bn	Jan 25
Acquisition by	Amadeus and MTN	stake in Travelstart		$40m	Feb 3
Acquisition by	Amadeus Capital Partners	stake in Hepstar		undisclosed	Feb 24
Acquisition by	Nodus Equity	undisclosed stake in Hair City	Webber Wentzel	undisclosed	Mar 1
Acquisition by	Nodus Equity	undisclosed stake in Big Save	Webber Wentzel	undisclosed	Mar 1
Acquisition by	Medu Capital	increased stake from 27% to 100% in Elite Truck Hire		R450m	Mar 9
Acquisition by	Medu Capital	Universal Coatings	Hogan Lovells (SA)	incl above	Mar 9
Acquisition by	Convergence Partners	stake in inQuba		undisclosed	Mar 9
Acquisition by	Stanlib	a partnership stake in Exeo Capital		undisclosed	Mar 15
Disposal by ■	Anglo American to consortium led by Taurus Fund Management	70% stake in Foxleigh metallurgical coal mine, Queensland Australia	Rand Merchant Bank	undisclosed	Apr 5
Acquisition by	Convergence Partners and Stockdale Street	100% of e4		undisclosed	Apr 13
Acquisition by	Investec Equity Partners from management	24 034 409 Assupol shares, taking it's stake from 30.8% to 36,6%	Investec Specialist Bank; BDO; Cliffe Dekker Hofmeyr	R132m	Apr 22
Acquisition by	Investec Equity Partners from minorities	63,4% of Assupol	Investec Specialist Bank; BDO; Cliffe Dekker Hofmeyr	to be advised	Apr 22
Disposal by	Masonite (Africa) through Business Resuce Proceedings to Warhorse Private Equity	plant and equipment	Investec Bank; Nedbank CIB; Norton Rose Fulbright (SA)	R 100	May 5
Disposal by	WG Wearne to a consortium led by Jade Industrial Holdings	Wearne Precast	Exchange Sponsors; Cliffe Dekker Hofmeyr	R21,2m	May 10
Acquisition by	Harith General Partners (through its Pan African Development Fund II)	a significant stake in NOVO Energy		undisclosed	May 22
Acquisition by	Fairtree Capital	The Rosevine in Cornwell, UK		undisclosed	May 31
Acquisition by	Convergence Partners	stake in Snapt		$1m	Jun 1
Acquisition by	Yellowwoods Capital	stake in DataProphet		undisclosed	Jun 14
Acquisition by	Invenfin (Remgro) from major shareholder	significant minority stake in DV Artisan Chocolate		undisclosed	Jun 14
Acquisition by	Bidvest from Ethos Private Equity and management	Brandcorp	Standard Bank; Rand Merchant Bank; Investec Bank; Werksmans; Webber Wentzel	not publicly disclosed	Jun 17
Disposal by	Torre International (Torre Industries) to African Agriculture Fund and a management consortium	45% stake in Torre Equipment Africa (40%:5%)	Rand Merchant Bank; Bowman Gilfillan	$15,7m	Jun 20
Acquisition by	Nedbank Private Equity	25% stake in Comsol Networks		undisclosed	Jun 28
Acquisition by	Marlin Brands (Coast2Coast Capital)	Albi		undisclosed	Jun 29
Acquisition by	Acorn Agri	an additional 14,7% of Grassroots (total stake now 59,3%)		undisclosed	not announced Q2
Acquisition by	Kleoss Capital GP Trust	a stake in Real Foods	Bowman Gilfillan; Werksmans	not publicly disclosed	not announced Q2

PRIVATE EQUITY DEALS H1 2016 – REST OF AFRICA

COUNTRY	NATURE OF DEAL	DETAILS	ADVISERS	ESTIMATED VALUE	DATE
Africa	Strategic Partnership	Denham Capital and GreenWish Partners : to develop, build and finance a 600MW renewable-energy portfolio across Sub-Saharan Africa by 2020		undisclosed	Feb 22
Africa	Disposal by	Actis of Emerging Markets Payments to Network International	Morgan Stanley; Perella Weinberg Partners; Clifford Chance; Webber Wentzel; Freshfields Bruckhaus Deringer	$340m	Mar 2
Africa	Acquisition by	Abraaj Group of Themis		undisclosed	Mar 16
Africa	Joint Venture	Africa Finance Corporation's interests in Cenpower and Harith General Partners' assets in the Pan Africa Infrastructure Development Fund(PAIDF) : new energy entity	Standard Bank; KPMG; Allen & Overy	$3,3bn	Jun 22
East Africa	Acquisition by	AfricInvest of a stake in Silafrica Plastics and Packaging International	Clyde & Co; Bowman Gilfillan Africa Group	undisclosed	Mar 11
North Africa	Acquisition by	Mediterrania Capital Partners and Euromena III of a minority stake in BS Invest (Tunisia), CAP Retail (Morocco) and Investex Alegérie (Algeria)		undisclosed	Apr 7
Algeria	Disposal by	Mediterrania Capital Partners of its stake in Cellulose Processing to The Abraaj Group		undisclosed	Jan 11
Algeria	Acquisition by	Mediterrania Capital Partners of a 43% stake in Cieptal Cars		undisclosed	Apr 4
Cape Verde	Acquisition by	Africa Finance Corporation of InfraCo Africa's remaining stake in the Cabeólice Wind Farm		undisclosed	Feb 19
Cote d'Ivoire	Acquisition by	Amethis Finance and West Africa Emerging Markets Growth Fund of an additional stake in Pétro Ivoire		undisclosed	Feb 28
DRC	Investment by	XSML in Institut Aurora		undisclosed	May 9
DRC	Investment by	XSML in Laboratoire BIS		undisclosed	May 9
Egypt	Disposal by	Abraaj Group of its remaining stake in Integrated Diagnostics Group		undisclosed	Jan 17
Egypt	Disposal by	Amwal AlKhaleej of its investment in Sarwa Capital to the Egyptian-American Enterprise Fund		undisclosed	Feb 1
Egypt	Acquisition by	EFG Hermes of a 76.7% stake in Tanmeyah Microenterprise Services from Qalaa (70%) and Tanmeyah management (6.7%)	EFG Hermes Investment Banking; Arab Legal Consultants; KPMG	EGP345m	Feb 24
Egypt	Disposal by	MENA Infrastructure of its 30.33% stake in Alexandria International Container Terminals to Hutchison Port		undisclosed	Mar 7
Egypt	Disposal by	Actis of a 7% stake in Edita Food Industries		EGP905,8m	May 31
Egypt	Acquisition by	Emerging Investment Partners of General Cable Egypt		undisclosed	Jun 22
Ethiopia	Acquisition by	54 Capital of an undisclosed stake in Addis Pharmaceutical Factory		$30m	Jan 6
Ethiopia	Acquisition by	Schulze Global Investments of a 45% stake in MB Plc, the producer of Family Milk		undisclosed	Jan 22
Ethiopia	Acquisition by	8 Miles of a significant minority stake in Verde Beef Processing	KPMG; Clifford Chance; Armbrust & Brown; Harbottle & Lewis	undisclosed	Apr 26
Ghana	Acquisition by	PCM Capital Partners of a stake in Surfline Communications		€5m	Apr 12
Ghana	Investment by	Injaro Agricultural Capital in Gold Coast Fruits		undisclosed	Jun 22
Kenya	Acquisition by	The Norwegian Investment Fund for Developing Countries (Norfund) of a minority stake in Freight-in-Time		$10m	Feb 12
Kenya	Acquisition by	Andreessen Horowitz of a stake in Branch International (Branch.co)		$9,2m	Mar 30
Kenya	Acquisition by	Equator Capital Partners and Progression Capital Africa on a stake in Jamii Bora Bank	Bowman Gilfillan Africa Group	Ksh1,2bn	Apr 11
Kenya	Investment by	Kibo Capital Partners in partnership with Velogic in General Cargo Services		undisclosed	Apr 18
Kenya	Investment by	Catalyst Principal Partners in Orbit Chemical Industries	Bowman Gilfillan Africa Group	undisclosed	Apr 25
Kenya	Investment by	CDC group in ARM Cement	Tradeways; Bowman Gilfillan Africa Group	$140m	Apr 30
Madagascar	Investment by	Adenia Partners in Opham		undisclosed	May 3
Mauritius	Acquisition by	Vantage Mezzanine Fund III USD of a 4.33% stake in Worldwide Landmark Holding Company	Investment One Financial Services; Werksmans; Adepetun Caxton-Martins Agbor & Segun	undisclosed	Apr 12
Mauritius	Disposal by	MCB Equity Fund of 100% of Speedy France to Bridgestone EMEA	MCB Capital Markets	undisclosed	May 30
Mauritius	Disposal by	Torre International (Torre Industries) to African Agriculture Fund and a management consortium of a 45% stake in Torre Equipment Africa (40%:5%)	Rand Merchant Bank; Bowman Gilfillan	$15,7m	Jun 20
Morocco	Acquisition by	AfricInvest of a stake in Outsourcia Group		undisclosed	Mar 29
Morocco	Investment by	Actis in Mundiapolis University		undisclosed	May 22
Morocco	Acquisition by	Mediterrania Capitl Partners of a stake in MedTech Group		undisclosed	Jun 7
Mozambique	Acquisition by	S2 Africa (Satya Capital and Sonae Distribuição) of Extra supermarket chain from Africom Delta Corporation		undisclosed	Feb 7
Namibia	Acquisition by	Eos Capital of a mjority stake in Elso Holdings		undisclosed	May 24
Nigeria	Acquisition by	Synergy Capital of a stake in Africa Terminals		undisclosed	Feb 18
Nigeria	Acquisition by	Synergy Capital of a stake in Suburban Fiber Company		undisclosed	Mar 24
Nigeria	Financing by	Vantage Mezzanine Fund III USD to Worldwide Landmark Holding Company : iro Landmark Village	Investment One Financial Services; Werksmans; Adepetun Caxton-Martins Agbor & Segun	$20m	Apr 12
Nigeria	Investment by	Singularity Investments in Sliide Airtime		undisclosed	May 13
Senegal	Acquisition by	Lekela Power of codevelopment rights and sole rights to invest in the 158MW Taiba Ndiaye Wind Project	Clifford Chance	undisclosed	Jun 22
Tunisia	Acquisition by	The Abraaj Group of a 49% stake in JM Holding, the majority shareholder of Société d'Articles Hygiéniques		undisclosed	Jan 18
Tunisia	Disposal by	Abraaj Group of its stake in Unité de fabrication de médicaments (Unimed) via IPO		undisclosed	May 4
Tunisia	Investment by	The Carlyle Group in Mazarine Energy		undisclosed	May 16
Zambia	Acquisition by	QG Africa Hotel (QG Investments Africa Management) of 100% of the Intercontinental Hotel Lusaka from Kingdom Hotel Investments		$35,9m	Apr 12
Zambia	Acquisition by	Inqo Investments of a stake in Bee Sweet Honey		$60 000	May 24