BY HANNA BARRY

Private-equity investors are reaping the benefits that are currently being offered by African markets

A DONE DEAL

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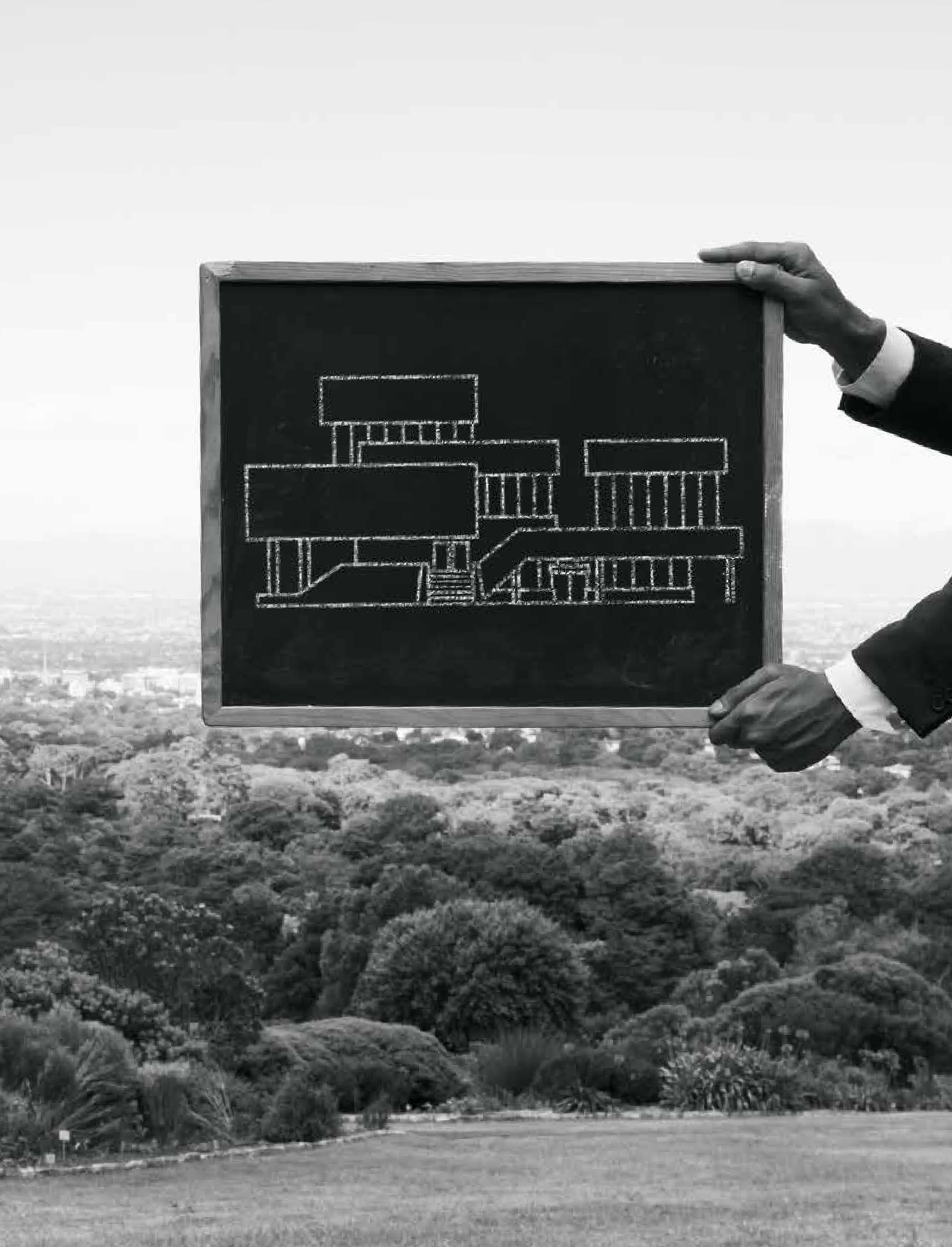

As a crucial source of financing for SMEs, private equity (PE) fund managers can help develop a sound culture of corporate governance within an organisation, according to the African Private Equity and Venture Capital Association (AVCA). This leads to more sustainable organisations in the long run.

'Private equity in its simplest form is an investment in a company, which allows it to grow so that more people can get hired and more children can go to schools,' states the AVCA. 'It puts more money into circulation, and that means more tax revenue for local governments.

'It improves the skills of the workforce and transfers knowledge from investors to local entrepreneurs and employees. It may be simplistic but it is really about developing economies.'

Erika van der Merwe, CEO of the Southern African Venture Capital and Private Equity Association (SAVCA) says: 'In economies where capital markets are underdeveloped, this inflow of capital is essential in supporting economic growth, in ensuring the transfer of skills and to help develop local financial, legal and business infrastructure.'

Playing a leading role in Africa's growth story, PE is no longer the preserve of the SA market. Once the dominant beneficiary of this form of investment on the continent, the country received just 20% of the overall PE investment in sub-Saharan Africa between 2011 and 2013, states professional services firm EY in its Private Equity Roundup Africa report. But the country remains the largest market for PE investment in the region.

Increasingly, PE companies are directing funds towards frontier markets such as Nigeria, Ghana, Kenya, Uganda and Côte d'Ivoire in their search for investment returns. In 2013, $3.2 billion was invested in 98 PE investments on the continent, states the firm.

'Nigeria and then Ghana will be your big markets [in West Africa]. In East Africa, it's the whole East African Community. Kenya, particularly, is a hub and then Tanzania, Uganda and Rwanda,' says EY's Africa private-equity leader Graham Stokoe. 'Going forward, Ethiopia and Mozambique are becoming new and interesting markets for private equity.' The trade links between many of these economies is also particularly compelling.

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ERIKA VAN DER MERWE, CEO, SAVCA

For instance, the AVCA points out, the Economic Community of West African States creates an environment for portfolio companies to achieve significant growth, which PE investments can support. Similarly, the East African Community is attracting investor interest as PE companies value the benefits of regional trade links and governments implementing investment-friendly policies.

'North African countries like Tunisia, Egypt and Morocco continue to provide an allure to PE investors due to their long-held relationships with Europe and the Middle East,' states the AVCA.

The attraction to Nigeria and Ghana provides a good indication of the sectors towards which PE investing is shifting. Both countries have large middle-class populations, which bodes well for consumer-facing, service-driven businesses.

The move towards broad-based, service-driven economies is highlighted by the fact that 'from 2000 to 2011, in which [time] the size of Africa's GDP has trebled, the single greatest contributor to GDP was the services sector, accounting for close to 54% of growth over the period,' states EY.

A large and increasingly affluent consumer market is good news for the fast-moving consumer goods, retail and consumer services industry, particularly as urbanisation rapidly increases. Due to open in September 2015, Jabi Lake Mall in Abuja, Nigeria expects to create in excess of 2 000 jobs and attract more than 300 000 shoppers every month.

In 2011, emerging markets-focused Actis and Duval Properties invested $120 million to complete the 25 000 m^2 project.

VALUABLE ASSETS

PRIVATE EQUITY INVESTMENTS BY SECTOR IN SUB-SAHARAN AFRICA*

Media and telecoms infrastructure
$1.4 billion

Banking and financial services
$772 million

Consumer
$692 million

Energy and natural resources
$1.2 billion

*Source: EY *From 2010 to Q3 of 2013*

Boasting the bulk of the world's uncultivated arable land, Africa's agribusiness opportunities are also generating interest, especially since farming on the continent is mostly small-scale.

'Africa generates only 10% of global agricultural output and accounts for less than 5% of world agribusiness GDP,' says the AVCA. 'This creates a broad range of opportunities from a private equity perspective, including in the infrastructure that supports the sector.'

The association says the financial services sector currently accounts for the biggest share of PE investment deal activity in Africa, and will remain a focus for PE as a function of the increased need for these services.

Stokoe agrees, saying: 'Financial services is historically a big sector and will stay a big sector.' He notes that the sector's regulatory underpin has boosted investment. With new investments, Stokoe says PE investment is moving away from banking and more towards insurance and peripheral industries such as credit bureaus and collection firms.

The scalable nature of financial-services firms enables expansion across multiple regions, boosting their attractiveness to general partners (GPs) and limited partners (LPs) looking for long-term investments, states the AVCA. LPs are usually institutional or high net-worth investors looking for capital gains and diversification. GPs manage the investments within a PE fund, earning a management fee and a percentage of the fund's profits.

EY notes that 'growing interest from LPs resulted in a significant increase in funds raised in 2013. Funds raised by Ethos ($800 million) and Vital Capital's maiden vehicle ($350 million) contributed a third of the amount raised'.

Consumer demand for telecoms, technology and media infrastructure is also creating exciting opportunities for PE firms. 'In particular, financial technology serving the significant under-banked population and telecoms infrastructure supporting the growth of mobile and wireless communications continue to generate interest from PE firms,' says the AVCA.

In July 2014, Helios Towers Africa, one of the continent's leading independent telecoms towers firms, announced it had raised $630 million in new equity resources from existing and new shareholders.

THE FINANCIAL SERVICES SECTOR ACCOUNTS FOR THE BIGGEST SHARE OF PE INVESTMENT DEAL ACTIVITY IN AFRICA

'The deal showcased increased appetite for large-scale telecoms investment opportunities,' states the AVCA.

Not all deals are this size. In fact, the average size of transactions in 2013 was $60 million. These 'present a challenge to the larger PE firms looking to deploy larger funds across a smaller number of companies', states the EY report, adding that deal sizes will grow as the market matures.

As an indication of the direction PE investing is taking, EY points out that 'five years ago, emerging markets represented approximately 12% of total PE fund-raising. Now they account for more than 20%.

'While global investor interest has begun shifting back in favour of the growing developed economies in recent months and away from some emerging economies that have weaker economic or political environments, Africa's strong long-term growth fundamentals should continue to drive the development of the PE industry on the continent,' states the report.

Echoing these positive sentiments, the AVCA expects PE in Africa to become more competitive and compelling in the future, as perceived risks of investing on the continent fall and opportunities increase. AVCA's survey-based research reveals that all investors plan to increase their percentage exposure to emerging-market PE over the next few years.

Some 85% of institutional investors – including pension and sovereign wealth funds as well as development finance institutions – surveyed by the AVCA, SAVCA and RisCura last year, said they would increase their allocation to PE over the ensuing two years.

'African and global fund of funds will spearhead the increase in exposure, and expect to have roughly half of their portfolios in emerging market private equity in the next 24 months [up from the current 42%],' says the AVCA.

'In contrast, development finance institutions have expressed the least interest in increasing their emerging market private equity exposure [albeit still a reported 1% increase], suggesting that their current allocation [nearly 30%] may be nearing allocation limits.' ■